

COMMENT

TO RESTORE A RELATIONSHIP BETWEEN CLASSES AND THEIR ACTIONS: A CALL FOR MEANINGFUL REFORM OF RULE 23

to
**THE CIVIL RULES ADVISORY COMMITTEE
and its
RULE 23 SUBCOMMITTEE**

**On Behalf of
LAWYERS FOR CIVIL JUSTICE
FEDERATION OF DEFENSE & CORPORATE COUNSEL
DRI – THE VOICE OF THE DEFENSE BAR
INTERNATIONAL ASSOCIATION OF DEFENSE COUNSEL**

August 9, 2013

Lawyers for Civil Justice (LCJ), the Federation of Defense & Corporate Counsel (FDCC), DRI – The Voice of the Defense Bar (DRI) and the International Association of Defense Counsel (IADC) respectfully write to urge the Advisory Committee on Federal Rules of Civil Procedure (“Committee”) and its Rule 23 Subcommittee to examine how the relationship between class members and their cases have changed since 1966, and to take much-needed action to reform Rule 23 in light of modern practices.

INTRODUCTION

Rule 23, and particularly subsection (b)(3), has become something that was not envisioned when adopted. The class action mechanism was intended to be a device for efficient litigation when the rights of the parties could be fully adjudicated in a single binding lawsuit, with representative members serving as the champions of the class members’ interests. Today, however, a significant fraction of class action cases demonstrates that the Rule has fostered a type of lawsuit that differs in fundamental ways from what existed in our legal culture prior to 1966. Some common features of today’s class action cases include: (1) very large classes whose members may not even know whether they have been injured; (2) class members who, despite receiving notice, have very little if any idea what is happening to their legal rights; (3) lawyers who make decisions about prosecuting and resolving cases without any meaningful input from any actual client; (4) lawyers whose focus is trained on the entrepreneurial aspects of their cases rather than on the objective of making their clients whole; (5) sparse and inconsistent judicial review (and therefore case law) concerning class certification decisions, which are often the most important legal determination in the case; (6) insufficient judicial scrutiny of settlements and fee requests to

protect the interests of the absent class members; and (7) settlements containing constitutionally suspect but feel-good transfer payments from defendants to non-party entities that have never been harmed by the defendants.

These elements, which are particularly common in cases involving mass torts and consumer-based claims, are symptoms of a more profound fact: Rule 23 has fostered a system in which class members lack any meaningful relationship to their cases. As the Rule 23 Subcommittee reviews possible reforms for its agenda, we urge it to keep this fundamental observation in mind and look for reforms that improve this situation while ruling out changes that would exacerbate it.

Some practitioners and commentators justify today's usage of Rule 23 as comprising a "private attorneys general" system that forces compliance with legal standards that would otherwise escape punishment. But our legal system already has public attorneys general and many other avenues for bringing about the outcomes that are preferred by those who justify Rule 23 in that way. More importantly, the Committee is bound to view the purpose of the Federal Rules of Civil Procedure to "secure the just, speedy, and inexpensive determination of every action and proceeding" as Rule 1 sets forth. The Rules Enabling Act does not provide the power to create new systems to impose punishment (as opposed to provide compensation) for alleged wrongdoing.

Comparing the history of Rule 23 to its meaning and usage today reveals some much-needed reforms to re-establish a relationship between class members and their cases. We propose four: (1) prohibiting or restricting cy pres payments to non-class members who have not been injured; (2) providing a right to interlocutory appeal of decisions to certify, modify or de-certify a class; (3) adopting an "opt-in" rule for Rule 23(b)(3) actions; and (4) clarifying that judicial estoppel does not apply to class action settlement negotiations.

I. Rule 23 Has Become Something Much Different than Originally Envisioned.

A. The History, Purpose and Adoption of Rule 23

From its inception, Rule 23, particularly with its adoption of categories of class actions, has created controversy.¹ The class action device, with its origins in equity, was intended to deal effectively with litigation involving large numbers of persons. It was characterized as a "bold and well-intentioned attempt to encourage more frequent use of class actions."² The original Rule 23, which had been adopted in 1938, created categories of class actions including "the so-called 'true' category [which] was defined as involving 'joint, common, or secondary rights'; the 'hybrid' category, as involving 'several' rights related to 'specific property'; and the 'spurious' category, as involving 'several' rights affected by a common question and related to common relief."³ The rule's divisions were based upon the character of the right to be asserted for or

¹ See Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure*, 81 HARV. L. REV. 356, 375-401 (1967).

² 7A CHARLES ALAN WRIGHT ET AL, FEDERAL PRACTICE AND PROCEDURE § 1752, at 15 (footnote omitted).

³ FED. R. CIV. P. 23 advisory committee's note; see also James William Moore, *Federal Rules of Civil Procedure: Some Problems Raised by the Preliminary Draft*, 25 GEO. L.J. 551, 57-576 (1937).

against a class. If it was “joint,” the class was characterized as “true.”⁴ If the right was “several,” but “the action was directed to the adjudication of claims affecting specific property,” it was deemed to be “hybrid.”⁵ If the right was “several,” but “a common question of law or fact” affected the right and “a common relief” was sought, then it was deemed to be “spurious.”⁶

These initial categories created confusion both in classification and in the determination of the proper scope of any judgment. In other words, it was unclear to what extent a judgment in these various categories would bind the participants. The “spurious” class, for example, was not supposed to amount to a class since any judgment was not supposed to bind absent class members who had not opted in or become a member of the litigation. The “judgment in true actions was conclusive on the class; in hybrid actions, conclusive upon the appearing parties and upon all claims whether or not presented insofar as they affected the property; and in spurious actions, conclusive only upon the appearing parties.”⁷ Eventually, it became clear that the doctrines purporting to apply and explain the rules were inadequate and reform was sought. Because the rule lacked a requirement to provide notice to class members in hybrid or spurious class actions, judgments from those actions were subject to attack and raised due process issues for litigants.

These and other problems prompted calls for reform. Professor Charles Wright, then a member of the Advisory Committee, argued that a new rule should be drafted, noting that “[a]n average of some ten class actions a year in federal court is not very many, and the bulk of these, I should imagine, have been integration suits where Rule 23 poses no real problem except for the aberrational case where it is held inapplicable.”⁸ The key question before the drafters was “whether a procedure could be developed to distinguish which actions were suitable for class treatment and whether proper safeguards could be fashioned to control its application.”⁹ At that time, the drafters were divided about the proper treatment of spurious class actions, with some members of the Rules Committee vigorously opposed to the use of class actions in tort cases because it interfered with the “principle that each person has a right to litigate his or her own case, that enforcing a judgment against an absent class member would be contrary to fundamental principles of fairness.”¹⁰

To address these problems, the rule was amended with the focus on the “well-agreed proposition that there is no basis for a class action unless the class is so numerous as to make individual joinder impracticable, questions of law or fact exist common to the class, and the representative parties are proper champions of the class.”¹¹ Out of this general focus, the current Federal Rule

⁴ Kaplan, *supra* note 1, at 377.

⁵ Kaplan, *supra* note 1, at 377.

⁶ Kaplan, *supra* note 1, at 377.

⁷ Kaplan, *supra* note 1, at 378.

⁸ Letter from Charles Alan Wright, Professor of Law, Univ. of Texas, to Benjamin Kaplan, Reporter to the Advisory Committee on Civil Rules & Professor of Law, Harvard Law Sch., 5 (Feb. 6, 1963) (on file with the Rules Committee Support Office, Administrative Office of the U.S. Courts).

⁹ John K. Rabiej, *The Making of Class Action Rule 23 – What Were We Thinking*, 24 MISS. C. L. REV. 323, 334 (Spring 2005).

¹⁰ *Id.* at 335 (citing Advisory Committee on Rules of Civil Procedure Meeting Minutes, Oct. 31 – Nov. 2, 1963 at 9-10 (on file with the Rules Committee Support Office, Administrative Office of the U.S. Courts)).

¹¹ Kaplan, *supra* note 1, at 378

of Civil Procedure 23, with its three categories of class actions, was born. But there is a rough correspondence between class actions described in today's Rule 23(b)(1) and true class actions, 23(b)(2) and hybrid class actions, and 23(b)(3) and spurious class actions. Strong debate occurred about whether spurious class actions, the (b)(3) category, should be continued or entirely abolished.

Concerns were expressed that this category of class actions “invites treating these mass accident and negligence cases as class actions’[,] a result surely to be avoided.”¹² Advocates for the (b)(3) category insisted that “a ‘mass accident’ situation resulting in injuries to numerous persons is on its face not appealing for a class action because of the likelihood that significant questions, not only of damages but of liability and defenses to liability, would be present, affecting the individual in different ways. In these circumstances, an action conducted nominally as a class action would degenerate in practice into multiple lawsuits separately tried.”¹³ Eventually, the rule adopted added more specific notice requirements and a series of threshold tests intended to divide those actions suitable for class treatment from the rest, and to assure adequate protections for the rights of class litigants. The idea was that “where the criteria are satisfied, fundamental safeguards are respected, and adequate representation is assured, the device of the class action should be used to the full extent.”¹⁴

According to John P. Frank, a well-known lawyer, legal commentator and member of the 1966 Advisory Committee, in adopting Rule 23, the Committee assumed the largest class would be about 100 people injured by an airplane crash or fire.¹⁵ The use of Rule 23 to include increasingly large class actions that cover thousands and thousands of people was beyond the anticipation of the Committee.¹⁶ To the extent there was any such concern, the Committee concluded that class notice and opt-out requirements would keep large classes from being certified and prevent class counsel from resolving cases in ways that favor counsel, but not the class members they represent.¹⁷ In the years since that 1966 modification, class sizes have grown exponentially, class members’ overwhelmingly common response to the distribution of class notice has been inaction, even when they receive and read it (which is often not the case).¹⁸

¹² Advisory Committee on Rules of Civil Procedure Meeting Minutes, Oct. 31-Nov. 2, 1963 (on file with the Rules Committee Support Office, Administrative Office of the U.S. Courts).

¹³ Memorandum from Benjamin Kaplan, Reporter to the Advisory Committee on Civil Rules & Professor of Law, Harvard Law Sch., to the Advisory Committee on Civil Rules, *Modification of Rule 23 on Class Actions*, at EE-18 (Feb. 21-23, 1963) (on file with the Rules Committee Support Office, Administrative Office of the U.S. Courts).

¹⁴ Tentative Proposal to Modify Provisions Governing Class Actions – Rule 23 EE-31 (May 28-30, 1962) (on file with the Rules Committee Support Office, Administrative Office of the U.S. Courts).

¹⁵ See Statement of John P. Frank to Courts Subcommittee on Senate S.B. 353, May 4, 1999, p. 52.

¹⁶ *Id.*

¹⁷ *Id.* at pp. 63-64, 70.

¹⁸ *Id.*; see also, e.g., Martin H. Redish, *Comments of Martin H. Redish* (submitted at the request of Lawyers for Civil Justice to The Federal Rules Advisory Committee), Feb. 15, 2002, at 9, 12-14 (class counsel, acting like bounty hunters, are enabled by the failure of Rule 23(b)(3) class members to respond to class notice by affirmatively filing an opt-out through inadvertence, rather than due to a conscious decision to participate in the class); MARTIN REDISH, *WHOLESALE JUSTICE: CONSTITUTIONAL DEMOCRACY AND THE PROBLEM OF THE CLASS ACTION LAWSUIT* (2009); Charlotte S. Alexander, *Would an Opt In Requirement Fix the Class Action Settlement? Evidence from the Fair Labor Standards Act*, 80 MISS. L.J. 443, 453 (Winter 2010) (studies reveal that opt out rates in class actions are exceedingly low); Theodore Eisenberg & Geoffrey Miller, *The Role of Opt-Outs and Objectors in Class Action Litigation: Theoretical and Empirical Issues*, 57 VAND. L. REV. 1529, 1532, 1546 (2004) (a study of 143 class

The change of the “spurious” action – binding only on those who appeared – into the current (b)(3) damages class – binding on all within the class definition but often remunerative only for class counsel and the small percentage of class members who make claims – has drawn less-than-laudatory comments from the U.S. Supreme Court:

Classes certified under (b)(1) and (b)(2) share the most traditional justifications for class treatment—that individual adjudications would be impossible or unworkable, as in a (b)(1) class, FN11 or that the relief sought must perforce affect the entire class at once, as in a (b)(2) class. For that reason these are also mandatory classes: The Rule provides no opportunity for (b)(1) or (b)(2) class members to opt out, and does not even oblige the District Court to afford them notice of the action. Rule 23(b)(3), by contrast, is an “adventuresome innovation” of the 1966 amendments, *Amchem*, 521 U.S., at 614, 117 S.Ct. 2231 (internal quotation marks omitted), framed for situations “in which ‘class-action treatment is not as clearly called for,’” *id.*, at 615, 117 S.Ct. 2231 (quoting Advisory Committee’s Notes, 28 U.S.C.App., p. 697 (1994 ed.)).

Wal-Mart Stores, Inc. v. Dukes, ___ U.S. ___, 131 S.Ct. 2541, 2558 (U.S. 2011) (emphasis added).

In 1991, the Advisory Committee began additional study of Rule 23 to determine whether to enact further reforms. During this process, the Committee became aware that the rule was being used for mass torts.¹⁹ Complaints were raised about the use of 23(b)(3) to provide plaintiffs with unfair leverage to coerce settlements in meritless class actions. Debate began to be heard about the propriety of using the class action device as a means of prosecuting actions to enforce various laws as opposed to its original purpose of serving as a procedural device to aggregate claims for judicial efficiency. Various amendments were published for comment in 1998 to control or eliminate inappropriate class actions, but the Committee deferred taking action on most of them. The only amendment actually approved after being published for comment in 1996 was the change adding Rule 23(f) to provide for a highly discretionary interlocutory appeal. Rule 23 was later amended in 2003 “to enhance judicial supervision of class counsel, the deliberateness of the certification decision, and the judicial review of settlements.”²⁰ Other reform came with the enactment of the Class Action Fairness Act (CAFA)²¹, which created special diversity jurisdiction and other reforms.

B. Lessons Learned Since 1966

The “adventuresome innovation” of 23(b)(3) is not working as planned. Instead of nine or ten class actions a year as Professor Wright envisioned, millions of persons each year who likely have no idea that they are part of a damages “class” have their rights preclusively adjudicated on no more notice than publications and mass mailings largely indistinguishable from junk mail.

action cases found the median percentage of class members opting out was a mere 0.1 percent).

¹⁹ Rabiej, *supra* note 9, at 349.

²⁰ Rabiej, *supra* note 9, 386.

²¹ Pub. L. No. 109-2, 119 Stat. 4 (codified as 28 U.S.C.A. § 1711).

They receive coupons, or the ability to obtain de minimis payments upon submission of time-consuming claim forms. The percentage of persons bound by settlements of (b)(3) classes who do not bother to claim payments is legendary; so much so that courts have developed constitutionally suspect methods for allocating unclaimed settlement funds to charities.²² It would seem that, particularly with respect to (b)(3), what is being “vindicated” is often something that very few people other than class counsel care very much about. Yet this is being done at great public and judicial expense. And all of this takes place within a setting that the Supreme Court has described as one in which “class action treatment is not as clearly called for.”

Rule 23(b)(3) in particular seems to be without economic justification. Typically, it escalates to justiciability damages claims that no individual would find worth making. The supposed theory is that aggregating many worthless claims together creates something worthwhile, but there is no judicial free lunch. Individual claimants find very little in this process worthy of the most minimal time expenditure in returning a claim form. Only class counsel receive anything of value in the process. This is often justified as employment of “private attorneys general” to coerce compliance with various legal norms, the violation of which would otherwise escape prosecution.²³ Yet – leaving aside for the moment the questionable public interest in vindicating claims on behalf of “victims” who take no notice of their supposed victimhood – this country has no shortage of actual, public attorneys general, all of whom are empowered by a wide variety of laws and regulations to enforce compliance with consumer protection legislation. The idea that what is vindicated in the typical (b)(3) class action would go unvindicated if not for (b)(3) is plainly wrong. Numerous tools exist for prosecuting violations of law and regulation if indeed those violations are actually causing harm. In this context, Rule 23(b)(3) does not provide a return that justifies its enormous expense. Indeed, it is inflicting a great cost on the judicial system, both in time and reputation, as well as effectively taxing entities that provide goods and services widely in the economy. The simplest test of Rule 23(b)(3) is this: look at the low rate at which persons whose claims are being adjudicated take advantage of settlements made on their behalf. More profoundly, look at the purpose behind cy pres awards – finding an uninjured non-party to receive funds as a means of justifying not only the lawsuit itself but also the failure to deliver compensation to the class members.

C. Rule 23 Today – The Current Problems With Class Action Lawsuits

The problems with “damages” ((b)(3)) class actions became apparent early in the life of the “adventurous innovation.” Even commentators who enthusiastically endorsed the ostensible goals of “large-scale, small claim” litigation (i.e., “the private enforcement of law”), and who were willing to propose extremely non-traditional mechanisms for making (b)(3) deliver better results – such as auctioning off class claims to the highest-bidding consortium of lawyers and delivering the proceeds directly to the class at the outset, leaving the lawyers to keep any gain to the upside – nonetheless recognized that (b)(3) classes were plagued by: (1) lawyers acting without any meaningful monitoring by any real client; (2) lawyers serving their own interests at

²² See Jennifer Johnston, *Cy Pres Comme Possible to Anything is Possible: How Cy Pres Creates Improper Incentives in Class Action Settlements*, 9 J.L. ECON & POL’Y (forthcoming Winter 2013).

²³ William B. Rubenstein, *On What a “Private Attorney General” is – and Why it Matters*, 57 VAND. L. REV. 2129, 2150 (2004); John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not Working*, 42 MD. L. REV. 215, 223, 225 (1983).

the expense of those of the supposed client; (3) judicial review of settlements and fee requests that “is often haphazard, unreliable, and lacking in administrative standards”; (4) “lodestar” (based on hourly rate) fee awards for class counsel that remove any incentive for class counsel to maximize recovery for the ostensibly deserving class claimants; (5) named plaintiffs in class actions who often have little control over how the suit is conducted; and (6) the lure of large awards causing class counsel to circumvent applicable ethics rules, “with only the thinnest veer of compliance.”²⁴

These problems are not merely theoretical. Examples abound. Here are a few:

- In *In re: Nutella Mktg. & Sales Practice Litig.*, No. 11-086, 2012 U.S. Dist. LEXIS 181913 (D.N.J. July 30, 2012) (order approving class settlement and attorneys fees), class claims regarding labeling of sugar and oil content were settled by providing class members with ability to claim reimbursement for up to five jars of Nutella at \$4 per jar. Attorneys fees of \$1.2 million, plus administrative costs of up to \$498,000 were approved.
- In *Smith v. William Wrigley, Jr. Co.*, No. 09-60646, 2010 U.S. Dist. LEXIS 67832 (S.D. Fla. June 15, 2010) (order approving class settlement and attorneys fees), a minimum \$6 million settlement fund was created to address the claim that a gum manufacturer touted unproven, antibacterial characteristics of magnolia bark extract. The settlement entitled individual class members attesting to a gum purchase to submit a claim form for \$10.00. Any funds remaining in the settlement fund at end of the claims period go to a charity under the cy pres doctrine.
- In *In re: Dry Max Pampers Litig.*, No. 1:10-cv-00301 (S.D. Ohio June 7, 2011) (order approving class settlement), a settlement of an unsubstantiated claim of diaper rash resulting from gel in diapers contained attorney’s fees of \$2.7 million for achieving injunctive relief requiring the implementation of a 1-800 line to answer questions about diaper rash. A cy pres monetary award of \$250,000 was earmarked to fund pediatric residencies and a research program on skin care.
- In *Gamelas v. Dannon Co.*, No. 1:08 CV 236, 2010 U.S. Dist. LEXIS 99503 (N.D. Ohio Aug. 31, 2010) (order approving class settlement and attorney’s fees), a settlement of claims concerning the effectiveness of Activia and DanActive yogurt lines established a settlement fund of \$35 million. Claimants

²⁴ John R. Macey & Geoffrey R. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 3-6 (1991). See generally John C. Coffee, Jr., *Rethinking The Class Action: A Policy Primer on Reform*, 62 IND. L. J. 625 (1987); John C. Coffee, Jr., *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Class Action*, 54 U. CHI. L. REV. 877 (1987); John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 676 (1986); John C. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, 48 LAW & CONTEMP. PROBS. 5, 12 (Summer 1985); John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter Is Not Working*, 42 MD. L. REV. 215, 235-36 (1983).

with receipts for yogurt purchases during the class claim period could submit proof for up to \$100 in reimbursement. Claimants without receipts could attest under oath to purchasing yogurt and receive between \$15 and \$30. Claimants unwilling to attest under oath could receive \$15. The settlement provided attorneys fees of \$10 million plus expenses, and it directed the unclaimed settlement funds to charities to help feed the poor.

Rigorous empirical studies of the rate of occurrence of the above abuses are hard to come by: “No one has been able to compile a representative database of class actions that would enable the sort of objective cost-benefit analysis that ought to be the basis for public policy reform.”²⁵ But the 1966 amendments inadvertently altered public policy without any warrant and without any significant empirical evidence as a basis. The job of the federal courts when making rules of civil procedure is to ensure the just, speedy and inexpensive determination of every action, not to create new actions and then justify the outcome with new theories about the role of private litigation on public policy. It would be ironic indeed if the federal courts were to insist on “a representative database of class actions that would enable the sort of objective cost-benefit analysis that ought to be the basis for public policy reform” in order to address a past instance of public policy reform enacted without benefit of such evidence.

II. Rule 23 Should Be Amended to Prevent the Award of Cy Pres Funds to Non-Class Members.

Perhaps the most profound symptom of the often remote relationship between putative class members and the purported classes to which they belong is the rise of “cy pres” payments in lieu of awards of actual damages. “Cy pres” is a legal doctrine with roots in equity that is being employed in the class action context to allow awards to non-class members, almost always when actual class members have not been damaged in a reasonably calculable manner. Controversy has erupted about the use of cy pres because it has led a number of courts in recent years to discount the rights of absent class members and to permit class actions for damages to proceed despite the impossibility of contacting, or even identifying, those actually injured. Because this practice creates tension with Rule 23’s protections for class members and encourages pursuit of tenuous class actions, we respectfully suggest the Committee review how cy pres is employed today and amend Rule 23 to bar or at least restrict cy pres awards.

A. Background: The History of Cy Pres.

Cy pres (in full: “cy pres comme possible”) originated in cases involving testamentary bequests as a solution for bequests that no longer corresponded to changed circumstances, such as a

²⁵ Deborah R. Hensler, *Goldilocks and the Class Action* (Response to Margaret H. Lemos, *Aggregate Litigation Goes Public: Representative Suits by State Attorneys General*, 126 HARV. L. REV. 486 (2012) (posted on Harvard Law Review’s Online Forum), http://www.harvardlawreview.org/issues/126/december12/forum_984.php. Ms. Hensler is the author of numerous articles and books on class actions, including: DEBORAH R. HENSLER ET AL., CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAIN (Rand Corp. 2000); Deborah Hensler, *Has the Fat Lady Sung? The Future of Mass Toxic Torts*, 26 REV. LITIG. 883 (2007) (presenting data showing the use of MDL to resolve mass claims); Deborah R. Hensler, *The Future of Mass Litigation: Global Class Actions and Third-Party Litigation Funding*, 79 GEO. WASH. L. REV. 306, 309 (2011); and Deborah R. Hensler, *As Time Goes By: Asbestos Litigation After Amchem and Ortiz*, 80 TEX. L. REV. 1899, 1910 (2002).

donation to a charity that no longer exists. The concept was exported to the class action field in the 1970s, first proposed by a 1972 student comment in a law review.²⁶ Since that time, cy pres has become a mechanism for class counsel to pursue class action litigation on behalf of purported classes whose remotely situated members either cannot possibly be identified or whose identification would be more expensive than any potential recovery would warrant.²⁷

Cy pres has been invoked in federal court class actions with increasing frequency in recent years.²⁸ The doctrine dictates that where the best relief is not possible, the “second best” relief may be given. The doctrine has been invoked in class actions where it is impossible, for whatever reason, to reach a portion of an attenuated absent class in order to compensate them as the result of either a successful judgment or a settlement. In these situations, the court-awarded funds are donated to a charity deemed to be relevant in some way to the basis of the lawsuit. In certain instances, the relief is given in the form of what is known as “fluid class recovery,” where compensation is made in the form of either future reductions in costs or the provision of future benefits to those situated similarly to the injured victims. Both cy pres and fluid class recovery are linked by the fact that relief is given to individuals or institutions other than those who were allegedly injured by the defendant’s allegedly unlawful behavior. The class attorneys are compensated on the basis of the total amount awarded or agreed upon in settlement, regardless of whether a significant portion of that amount is given to recipients who were never injured by the defendants’ behavior.

Cy pres and fluid class recovery are controversial doctrines in the class action context.²⁹ They find no basis in the substantive laws enforced in the class action proceeding. “Rule 23(e) does not mention the district court’s discretion – or even its authority – to extinguish the right of recovery of identified class members through a later cy pres order.”³⁰ Courts resorting to cy pres do so either in reliance on vague “equitable” judicial powers or resort to the tautology that cy pres powers exist because the settling parties created them by contract, even though disadvantaged class members were not party to the negotiations that transferred their property to others. Cy pres is thus at least as much an unauthorized extension of judicial power as the procedures at issue in *Lexecon Inc. v. Milberg Weiss Bershad Hynes & Lerach*.³¹

B. Cy Pres Should Not Circumvent Rule 23 Class Certification Standards.

Use of cy pres distributions raises significant constitutional questions regarding Article III’s case-or-controversy requirement by compensating entities that have suffered no legally cognizable injury. The potential availability of a cy pres award invites certification of class action proceedings where the supposed class members are so remotely situated that all can recognize at the outset that meaningful relief to injured victims is impossible even if the action is

²⁶ Stewart R. Shepherd, Comment, *Damage Distribution in Class Actions: The Cy Pres Remedy*, 39 U. CHI. L. REV. 448 (1972).

²⁷ See generally, Martin H. Redish, et al., *Cy Pres Relief & the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 FLA. L. REV. 617 (2010).

²⁸ *Id.* at 620 (documenting the “dramatic turn in modern class actions toward the use of cy pres relief”).

²⁹ See concurring opinion of Chief Judge Jones in *Klier v. Atochem North America, Inc.*, 658 F.3d 468, 480 (5th Cir. 2011).

³⁰ *All Plaintiffs v. All Defendants*, 645 F.3d 329, 333-34 (5th Cir. 2011).

³¹ 523 U.S. 26 (1998) (previously common MDL practice of trying cases in transferee courts held ultra vires).

successful. Whenever a court resorts to “fluid recovery” or cy pres, it is a tacit admission that the suit, in class form, is incapable of achieving its goal of compensating actually injured victims. Cy pres is also an indicator that a damages class cannot be certified. For a class action seeking damages, common issues must “predominate” over case-specific ones, so cy pres is employed where it is impossible or too expensive to prove causation and damages as to the absent class members. By definition, such causation and damages cannot be proven on a class-wide basis with proof as to the class representatives serving as proof as to the rest of the class. In these circumstances, due to the expense or impossibility of proving causation and damages individually, those individualized issues necessarily predominate and preclude class certification. Cy pres should not be used as a stratagem for allowing attenuated class action litigation that Rule 23 otherwise prohibits. Such non-class member awards permit the class action device to relax the restrictions of substantive law in contravention of the Rules Enabling Act.³²

C. Cy Pres Raises Questions about Separation of Powers.

Cy pres raises foundational questions of separation of powers which were codified in the Rules Enabling Act, pursuant to which all of the Federal Rules of Civil Procedure, including Rule 23 authorizing class action proceedings, have been promulgated. When used to distribute funds from settlements involving the rights of class members to entities (including charities) who are not members of the class, cy pres is an exercise of undue judicial power without any check or balance from the other co-equal branches of government. Under our tripartite system of government, the legislature is supposed to enact the laws and the executive to enforce them. There are few, if any, statutes that permit a private entity to be liable to another private entity in the absence of injury or causation. The government can impose civil or criminal fines for illegal conduct, but such fines ordinarily are owed to the government. In the absence of statutory authorization, courts should have no power to redistribute money between private entities without proof of causation and damages. Such potentially boundless judicial power is inconsistent with our system of limited government.

In this fashion, cy pres poses a grave risk to the judiciary encouraging courts to transgress boundaries that are inherent in our system of checks and balances. By putting judges in the role of making policy judgments about how to allocate the funds of private parties without judicial standards, cy pres facilitates judges becoming what Justice Cardozo once called knights errant, believing that through litigation they can solve societal problems that neither the legislature nor the executive branch have seen fit to address in the manner selected by the court.³³

D. Cy Pres Should Not Be a Back Door to Punitive Damages.

Most civil litigation is based upon the notion of compensation for injury suffered. Some statutory claims add a legislatively authorized punitive element, such as an award of treble damages, but since these remedies require actual damages to be multiplied, they remain limited by the necessity of proving that the defendant actually harmed the plaintiff in some way. Cy pres

³² 28 U.S.C. § 2072. See Redish, *supra* note 57, at 664-67 (discussing substantive effects of cy pres on the underlying law).

³³ See BENJAMIN N. CARDOZO, NATURE OF THE JUDICIAL PROCESS, 141 (1921).

awards, however, are often justified not by compensation but by punishment.³⁴ They involve a judicial determination that the defendant allegedly acted illegally and should not be allowed to profit from that wrongdoing. In the absence of statutory authorization, imposing punishment for private wrongs is not a proper power of the judicial branch. Punishment is a creature of the criminal or administrative law, and such fines are paid to the government, not to uninjured private entities.

Cy pres payments, because they are made to persons who are not members of the class and because they are employed for punitive reasons, do not benefit class members. Thus they do not fall within the “common fund” rationale for awarding fees to class counsel. A cy pres payment cannot be a “common fund” that provides benefits to the class when it, by definition, is paid to other persons.

In civil litigation, to receive an award under a purely punitive rationale requires a plaintiff to meet strict standards for proof of punitive damages. Punitive damages are constrained, both constitutionally and as a matter of substantive law, by the requirement of a ratio to compensatory damages. Cy pres awards circumvent that requirement by allowing what can only be categorized as punishment, but in situations where plaintiffs cannot prove damages or causation.

E. Cy Pres Awards Risk Conflicts of Interest.

Cy pres awards pose a potential for conflicts of interest between class counsel and inaccessible class members.³⁵ For example, cy pres settlements have been proposed where identification of absent class members and calculation of their damages is possible, but expensive because of negligible ties to the litigation. A cy pres remedy in such a case could create financial incentives for class counsel not to incur the expense of proving causation and damages, but instead to assert that such proof is too difficult or to erect barriers to class members’ participation in settlement programs. The victims are the injured members of the class, the very people who are entitled to collect their damages.³⁶ Cy pres settlements thus run the risk of cheating unknown class members by paying settlement proceeds to entities who are not members of the class and who were not adversely affected by the conduct that was the subject matter of the litigation.³⁷ The availability of a cy pres remedy therefore causes tension with class counsel’s obligation to provide legal representation to the entire class.

³⁴ *E.g.*, *In re Baby Prods. Antitrust Litig.*, 708 F.3d 163, 172 (3d Cir. 2013) (excusing cy pres on the basis of “deterrent effect”); *Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 784 (7th Cir. 2004) (“There is no indirect benefit to the class from the defendant’s giving the money to someone else. In such a case the “cy pres” remedy . . . is purely punitive”).

³⁵ *Baby Prods.*, 708 F.3d at 173 (“inclusion of a cy pres distribution may increase a settlement fund, and with it attorneys’ fees, without increasing the direct benefit to the class”); *Id.* at 179 (“class counsel, and not their client, may be the foremost beneficiaries of the settlement”).

³⁶ *Mirfasihi*, 356 F.3d at 785 (cy pres settlement to avoid litigation expense and gain a fee “sold [the class] claimants down the river”).

³⁷ *Baby Prods.*, 708 F.3d at 169; *Dennis v. Kellogg Co.*, 697 F.3d 858, 863 (9th Cir. 2012) (8% of settlement to be paid to actual class members); *Mirfasihi*, 356 F.3d at 783-84 (none of settlement funds paid to members of one class).

Cy pres payments to non-class members also create potential conflict situations in the selection of the recipients of such payments. Courts have generally required that non-class member recipients of such payments have some logical nexus to the subject matter of the litigation, but the only current avenue for enforcing this limitation is the uncertain course of judicial review. Nothing in Rule 23 governs cy pres distributions, which invites questionable or improper behavior on the part of both lawyers and judges encouraging lawyers to find charities of special interest to themselves or the judge in charge of the class action proceeding.³⁸ Thus, there are currently no mandatory conflict-of-interest provisions concerning the selection of non-class-member recipients, and thus no institutional impediments to the misuse of such awards as a form of patronage. The Committee should consider reforming Rule 23 to prohibit awards to any entity affiliated with any party to the litigation, with counsel, or with the court itself.

Finally, some court decisions permitting non-class member payments have allowed, or even required, such payments to be made to organizations that encourage additional litigation, that pursue “research” intended for use in future litigation, or, even, for political advocacy purposes.³⁹ The class action mechanism should not be used as transfer payments for public policy purposes absent congressional action.

F. Proposed Alternative Amendments to Reform Cy Pres.

Rule 23 is an appropriate mechanism for reforming cy pres distribution of settlement funds because Rule 23 should embody the jurisprudential limitations inherent in the Rules Enabling Act and other limits on judicial authority. The proposed amendments to Rule 23 attached as Exhibit 1 seek to reform cy pres either by prohibiting, or in the alternative restricting, the use of cy pres relief or fluid recovery in a class action proceeding in federal court, in the form of either an award or settlement approved by the court, except where the substantive legislation enforced in the class proceeding expressly provides for the possibility of such relief. The first alternative would, consistently with enumerated grants of judicial authority by the Constitution and by Congress, recognize that there is no authority to transfer funds belonging to remote members of a putative class action to persons who are not members of the class. It would prohibit settlements that would distribute funds to non-class members. As enforcement, class counsel proposing transfer of class members’ property to non-class members would be deemed inadequate representatives of the class and would be replaced. An exception allowing cy pres payments where specifically provided by statute would recognize the possibility that Congress or state legislatures might grant cy pres authority to the courts in particular instances.

³⁸ See *Kentucky Bar Ass’n v. Chesley*, 393 S.W.3d 584, 598 (Ky. 2013) (disbarring attorney in part for diverting class settlement funds to phony cy pres charity controlled by attorney); *Nachshin v. AOL, LLC*, 663 F.3d 1034, 1040 (9th Cir. 2011) (cy pres distribution to Federal Judicial Center Foundation reversed as unrelated to litigation); cf. *In re Pharm. Indus. Average Wholesale Price Litig.*, 588 F.3d 24, 36 (1st Cir. 2009) (allowing cy pres distribution despite class counsel sitting on the board of the recipient charity).

³⁹ See *In re Agent Orange Prod. Liab. Litig.*, 818 F.2d 179, 186 (2d Cir. 1987) (reversing cy pres arrangement that would have allowed use of cy pres funds for “political advocacy”); *Jones v. Nat’l Distillers*, 56 F. Supp.2d 355, 359 (S.D.N.Y. 1999) (donating cy pres funds to legal aid to “help[] those needing legal assistance”); *In re Wells Fargo Sec. Litig.*, 991 F. Supp. 1193, 1198 (N.D. Cal. 1998) (distributing cy pres funds to a “clearinghouse” for publicizing securities litigation).

The second alternative addresses the controversy over cy pres settlements by ensuring judicial attention to the issues that could pose the most danger. Such settlements would be available only in cases of impossibility, not merely impracticability due to cost. Recognizing that funds transferred to non-class members are not “common funds” that benefit the class, the second alternative precludes consideration of cy pres payments in the calculation of attorneys’ fees under Rule 23(h).⁴⁰ Because governments acting in their formal *parens patriae* capacity are typically recognized as acting on behalf of the public, such as members of a putative class, an exception is provided for payments to such governmental entities. Finally, the second alternative incorporates conflict-of-interest provisions to ensure that entities chosen to receive cy pres payments are not selected due to their ties to the parties or to the court and that cy pres funds are not diverted to the facilitation of future litigation. We respectfully suggest the Committee review these proposals.

III. Rule 23(f) Should Be Amended to Provide a Right to Interlocutory Appeal of Decisions to Certify, Modify or De-Certify a Class.

The current Rule 23(f) was adopted in 1998 to provide increased opportunity for an immediate appeal to supplement the previously existing mechanisms (mainly mandamus) for obtaining appellate review of the all-important decision to certify a class action.⁴¹ Rule 23(f) has now been in existence long enough that it would be appropriate for the Committee to consider whether it has achieved its intended goal of increasing uniformity of district court practice regarding certification decisions.

Analytical data indicates that the number of petitions filed is relatively modest and that the number of actual written opinions is very small.⁴² For instance, one study indicates that only 476 petitions required decision over the almost seven years of data (thus an average of 5.2 petitions per Circuit per year).⁴³ Only a fraction of those petitions accepted for review ultimately result in opinions (a total of 47 opinions over almost 7 years – or, on average, less than a single opinion per Circuit). Notably these numbers indicate that only 28 percent of those petitions actually accepted result in an opinion (47 opinions out of 169 petitions granted over all Circuits over the nearly 7 year time period). These data demonstrate not only how little judicial review is occurring, but also indicate why there is a paucity of meaningful case law being developed to provide clear and uniform standards.

⁴⁰ See *Baby Prods.*, 708 F.3d at 178 (“awarding attorneys’ fees based on the entire settlement amount rather than individual distributions creates a potential conflict of interest between absent class members and their counsel”).

⁴¹ Certification decisions, although vitally important, are not subject to immediate appellate review. The courts have deemed “final” only a slim set of “collateral orders” that share these characteristics: They “are conclusive, [they] resolve important questions separate from the merits, and [they] are effectively unreviewable on appeal from the final judgment in the underlying action.” *Mohawk Indus., Inc. v. Carpenter*, 130 S. Ct. 599, 601 (2009) (quoting *Swint v. Chambers Cnty Comm’n*, 514 U.S. 35, 42 (1995)). “[O]rders relating to class certification” in federal court, it is settled, do not fit that bill. *Coopers & Lybrand v. Livesay*, 437 U.S. 463, 470 (1978).

⁴² Barry Sullivan & Amy Kobelski Trueblood, *Rule 23(1): A Note on Law and Discretion in the Courts of Appeal*, 246 F.R.D. 277, 290 (2008).

⁴³ *Id.*

A. The Committee’s Purpose in Drafting Rule 23(f) Was to Provide Greater Uniformity in Certification Decisions.

During the early 1990s, the Advisory Committee proposed reform to permit interlocutory appeals because it recognized that the certification ruling is often the crucial ruling in a case filed as a class action.⁴⁴ According to the Committee Note submitted with the proposed rule change to the Standing Committee in May of 1993, the severe consequences to be expected from a certification decision “justify a special procedure allowing early review of this critical ruling.”⁴⁵ The Committee’s proposal was limited because of concern over “the disruption that can be caused by piecemeal reviews.”⁴⁶ But the initial proposal required certification by the trial court, as well as agreement to hear the case by the appellate court.

In 1995, after further discussion and study, the Advisory Committee revised the initial proposal to eliminate the requirement that the district court certify the request for an immediate appeal. The Partial Draft Advisory Committee Note of December 12, 1995, noted that the expansion of “appeal opportunities affected by subdivision (f) is indeed modest.”⁴⁷ The note further mentioned the drafters’ view that the most suitable questions for immediate appeal would be those turning on “novel or unsettled” questions of law.⁴⁸ And in the drafters’ view, “[s]uch questions are most likely to arise during the early years of experience with new class-action provisions as they may be adopted within Rule 23 or enacted by legislation.”⁴⁹ The drafters also thought that permission would likely be denied when “certification decisions turn on case-specific matters of fact and district court discretion.”⁵⁰

In a 1997 report of the Advisory Committee, Chair Niemayer noted that the proposed Rule 23(f) “has persisted virtually unchanged through the many alternative Rule 23 drafts that have been prepared by the Advisory Committee over the last six years.”⁵¹ Chair Niemayer explained that the rule was intended to address the “widespread observations that it is difficult to secure

⁴⁴ Scholars and courts have regularly characterized the decision whether to certify a class as a key turning point in litigation. Such rulings “have enormous practical impact; a grant may impel the defendant to settle and a denial leaves only the named plaintiff’s claim which often saps the plaintiff’s lawyer of incentive to proceed.” Richard D. Freer, *Interlocutory Review of Class Action Certification Decisions: A Preliminary Empirical Study of Federal and State Experience*, 35 W. ST. U. L. REV. 13, 13 (2007-2008). Few decisions are more significant to the litigants than a district court decision granting or denying class certification.

⁴⁵ Letter (and attachments) from Sam C. Pointer, Jr., Chairman, Advisory Committee on Civil Rules, to Honorable Robert E. Keeton, Chairman, Standing Committee on Rules of Practice and Procedure (May 17, 1993) (citing (attached) Proposed Amendments to the Federal Rules of Civil Procedure, at 11 (May 1993)), available at <http://www.uscourts.gov/RulesAndPolicies/rules/archives/advisory-committee-reports/advisory-committee-rules-civil-procedure.aspx>.

⁴⁶ *Id.*

⁴⁷ Letter (and attachments) from Patrick E. Higginbotham to Members of the Standing Committee on Rules of Practice and Procedure (Dec. 13, 1995) (citing Partial Draft Advisory Committee Note Draft Rule 23 at 10), available at <http://www.uscourts.gov/RulesAndPolicies/rules/archives/advisory-committee-reports/advisory-committee-rules-civil-procedure.aspx>.

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ Memorandum from Paul V. Niemayer, Chair, Advisory Committee on Civil Rules, to Honorable Alicemarie H. Stotler, Chair, Standing Committee on Rules of Practice and Procedure (May 21, 1997).

effective appellate review of class certification decisions and that increased appellate review would increase the uniformity of district-court practice.”⁵²

B. Rule 23(f) Has Not Delivered Uniformity in Certification Decisions Because It Is Highly Discretionary.

Interlocutory review is available under Rule 23(f) in the “sole discretion of the court of appeals.”⁵³ The Committee Note characterizes the discretion vested in the courts of appeals about whether to hear the appeal as “unfettered.”⁵⁴ The Note suggests that the appellate courts would likely “develop standards for granting review that reflect the changing areas of uncertainty in class litigation.”⁵⁵ But no standards were included in the rule – the appellate courts could grant or deny petitions for leave to appeal on “any consideration that the court of appeals finds persuasive.”⁵⁶

The federal appellate courts have, as the drafters of Rule 23(f) anticipated, sought to cabin their completely free discretion by adopting lists of criteria for determining whether or not to grant certification appeals. But the criteria adopted continue to be so “flexible” as to allow for virtually “unfettered” decision-making as is evident from review of the following cases:

Blair v. Equifax Check Services, Inc., 181 F.3d 832, 834-35 (7th Cir. 1999) (Declining to adopt a bright-line approach, but instead focuses on whether an appeal is important because class certification is likely to be outcome-determinative or “may facilitate the development of the law. . . .”)

Waste Mgmt. Holdings, Inc. v. Mowbray, 208 F.3d 288, 293-94 (1st Cir. 2000) (Recognizing three categories of cases that warrant the exercise of discretionary appellate jurisdiction: (1) when a denial of class status effectively ends the case; (2) when the grant of class status raises the stakes of the litigation so substantially that the defendant likely will feel irresistible pressure to settle; (3) when granting class status will permit the resolution of an unsettled legal issue that is important to the particular litigation as well as important in itself and likely to escape effective review if left hanging until the end of the case.)

Prado-Steiman ex rel. Prado v. Bush, 221 F.3d 1266, 1274-76 (11th Cir. 2000) (In determining whether to grant interlocutory appellate review of class certification, a court should consider, (1) whether the district court’s ruling is likely dispositive of the litigation by creating a “death knell” for either plaintiff or defendant; (2) whether the petitioner has shown a substantial weakness in the class certification decision, such that the decision likely constitutes an abuse of discretion; (3) whether the appeal will permit the resolution of an unsettled legal issue that is important to the particular litigation as well as important in itself; (4) the nature and status of

⁵² *Id.*

⁵³ FED. R. CIV. P. 23(f) advisory committee’s note (1998).

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.*

litigation before the district court; and (5) the likelihood that future events may make appellate review more or less appropriate.)

Sumitomo Copper Litig. V. Credit Lyonnais Rouse, Ltd., 262 F.3d 134 (2d Cir.2001) (petitioners seeking leave to appeal pursuant to Rule 23(f) must demonstrate either (1) that the certification order will effectively terminate the litigation and there has been a substantial showing that the district court’s decision is questionable, or (2) that the certification order implicates a legal question about which there is a compelling need for immediate resolution.)

Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 259 F.3d 154, 164 (3d Cir. 2001) (although not entirely restricting grant of class status to these three categories, the Court cited “(1) when denial of certification effectively terminates the litigation because the value of each plaintiff’s claim is outweighed by the costs of stand-alone litigation; (2) when class certification places inordinate or hydraulic pressure on defendants to settle, avoiding the risk, however small, of potentially ruinous liability; and (3) when an appeal implicates novel or unsettled questions of law; in this situation, early resolution through interlocutory appeal may facilitate the orderly development of the law.”)

Lienhart v. Dryvit Sys., Inc., 255 F.3d 138, 145-46 (4th Cir. 2001) (The court adopted the five-factor of *Prado-Steima*, adding that “the ‘substantial weakness’ prong operates on a sliding scale to determine the strength of the necessary showing regarding the other factors.”)

In re Lorazepam & Clorazepate Antitrust Litig., 289 F.3d 98, 105 (D.C. Cir. 2002) (Interlocutory review of class certification decisions is appropriate when (1) when there is a death-knell situation for either the plaintiff or defendant that is independent of the merits of the underlying claims, coupled with a class certification decision by the district court that is questionable, taking into account the district court’s discretion over class certification; (2) when the certification decision presents an unsettled and fundamental issue of law relating to class actions, important both to the specific litigation and generally, that is likely to evade end-of-the-case review; and (3) when the district court’s class certification decision is manifestly erroneous.”); *In re Delta Air Lines*, 310 F.3d 953, 959 (6th Cir. 2002) (The Sixth Circuit “eschew[s] any hard-and-fast test in favor of a broad discretion,” but is guided by the relevant factors articulated in other circuits.)

Chamberlan v. Ford Motor Co., 402 F.3d 952, 959 (9th Cir. 2005) (“Review of class certification decisions will be most appropriate when: (1) there is a death-knell situation for either the plaintiff or defendant that is independent of the merits of the underlying claims, coupled with a class certification decision by the district court that is questionable; (2) the certification decision presents an unsettled and fundamental issue of law relating to class actions, important both to the specific litigation and generally, that is likely to evade end-of-the-case review; or (3) the district court’s class certification decision is manifestly erroneous.”)

Vallario v. Vandehey, 554 F.3d 1259 (10th Cir. 2009) (Interlocutory review of district court’s class certification order is generally appropriate: (1) in “death knell” cases, when questionable class certification order is likely to force either party to resolve case based on considerations independent of the merits; (2) certification decision involves unresolved issue of

law relating to class actions that is likely to evade end-of-case review, significant to instant case as well as class action cases generally; or (3) decision is manifestly erroneous.)⁵⁷

These cases demonstrate that the criteria applied in numerous appellate decisions continue to be so “flexible” as to allow for virtually “unfettered” decision-making.

C. Unfettered Decision-Making Has Resulted in Seemingly Arbitrary and Highly Inconsistent Results.

The empirical data on immediate appeals under Rule 23(f) raises grave concerns about how it is working. One scholar commented that “between the courts’ ‘unfettered discretion’ and their opaque decision-making processes, what happens behind the courts’ closed doors has been something of a mystery....”⁵⁸ After examining available data, Sullivan and Trueblood concluded that “[a]t best, the circuits may be described as inconsistent – in terms of petition volume, as to whether the court of appeals adheres to an articulated standard of review, the frequency with which the circuits publish their opinions explaining why they accept or deny Rule 23(f) petitions, and of course, the frequency with which Rule 23(f) petitions are granted.”⁵⁹ In fact, as of the date of their data (December, 1998 - October 2006), one Circuit had failed to grant even a single Rule 23(f) petition and another Circuit had granted only five. The grant percentages for the Circuits varied wildly from 0% to 86% even though the data covered almost seven total years. Further, there was not much middle ground – six Circuits were 28% or below and four Circuits were 54% or higher.⁶⁰

Even more troubling, available data suggested inconsistent success rates between plaintiffs’ petitions and those brought by defendants.⁶¹ These inconsistencies raise concern about whether litigants are being provided a process that conforms to traditional notions of due process and judicial decision-making. Those concerns are necessarily heightened by the staggering consequences that flow from the decision to certify or deny certification. The importance of this decision point was acknowledged when Rule 23(f) was enacted. But the reform made interlocutory appellate review so discretionary as to invite arbitrary decision-making. Unlike the Supreme Court’s certiorari discretion to which it has been analogized, Rule 23(f) does not empower a single national body to accept cases to establish national law; it empowers twelve circuits to decide complex, and often fact-based decisions about whether a case will proceed as a class or not. And further, unlike the Supreme Court’s certiorari discretion, Rule 23(f) considerations are not examining whether there is a circuit split to ensure a consistent national rule of law but are “at least as much concerned with deciding actual disputes as with clarifying the law....”⁶² These distinctions are important, and they underscore the necessity for appeals of certification decisions as a matter of right.

⁵⁷ Neither the Fifth Circuit, *see, e.g. Anderson v. U.S. Dept. of Hous. & Urban Dev.*, 554 F.3d 525, 527 (5th Cir. 2008), nor the Eighth Circuit, *Liles v. Del Campo*, 350 F.3d 742, 746 n. 5 (8th Cir. 2003), has adopted specific standards regarding when the court will hear an interlocutory appeal of a class certification order.

⁵⁸ Barry Sullivan & Amy Kobelski Trueblood, *supra* note 32, at 280-81.

⁵⁹ Barry Sullivan & Amy Kobelski Trueblood, *supra* note 32, at 284.

⁶⁰ Barry Sullivan & Amy Kobelski Trueblood, *supra* note 32, at 290.

⁶¹ Barry Sullivan & Amy Kobelski Trueblood, *supra* note 32, at 286.

⁶² Barry Sullivan & Amy Kobelski Trueblood, *supra* note 32, at 288.

D. Uncertainty About Class Certification Decision Standards Creates Difficulty for Bench and Bar, and It Undermines the Litigants' Faith in the Judicial System.

The inconsistency in certification decisions creates uncertainty for the parties, renders it difficult for lawyers representing the parties to properly advise their clients, and undermines respect for the judiciary as an institution adhering to the rule of the law. For many years, great jurists and scholars of the past criticized the equitable courts for equitable power resulting in rulings as uncertain as the length of the Chancellor's foot, which might be long, or short, or somewhere in between.⁶³ The lack of predictability that made equity a "roguish thing" exists today in class certification decisions.⁶⁴ When judges employ different standards for the right of appellate review – let alone the standards for such review – the process inevitably departs from what has traditionally been considered the rule of law. Like cases are not treated alike. Litigants find it impossible to navigate such unpredictability, and frustration feeds the pressure to settle a case, not because it is weak on the merits, but to avoid the costs and vagaries of judicial system.

E. Amending Rule 23(f) to Provide Immediate Appeal Would Remove Uncertainty.

Adoption of a rule allowing for an immediate appeal of decisions to certify, de-certify or modify a class would end the arbitrary "unfettered" decision-making about when an interlocutory appeal can be taken and would foster the development of more case law on certification standards. Many states have adopted legislation providing for an immediate right of appeal from the certification decision of the trial court.⁶⁵ Ample precedent exists for the Committee's power to provide exceptions to the "final-decision" rule.⁶⁶ For the parties, the certification decision can

⁶³ John Seldon's oft-quoted comment about the problems created by unfettered discretion in the courts of equity applies here with even more force. He said:

Equity is a roguish thing. For Law we have a measure, know what to trust to; Equity is according to the conscience of him that is Chancellor, and as that is larger or narrower, so is Equity. 'T is all one as if they should make the standard for the measure we call a "foot" a Chancellor's foot; what an uncertain measure would this be! One Chancellor has a long foot, another a short foot, a third an indifferent foot. 'T is the same thing in the Chancellor's conscience.

John Bartlett, *Familiar Quotations*, (10th ed, rev. and enl. by Nathan Haskell Dole. Boston: Little, Brown, 1919; Bartleby.com, 2000) (quoting John Seldon) available at <http://www.bartleby.com/100/155.html> .

⁶⁴ See generally, Freer, *supra* at 20-22 (showing that different circuits accept review at different rates and on appeal affirm or reverse certification decisions at different rates).

⁶⁵ See, e.g., ALA. CODE § 6-5-642 (1975) ("court's order certifying a class or refusing to certify a class action shall be appealable in the same manner as a final order to the appellate court which would otherwise have jurisdiction over the appeal from the final order in the action"); GA. CODE ANN. § 9-11-23 (g) (West 2012) ("court's order certifying a class or refusing to certify a call shall be appealable in the same manner as a final order to the appellate court which would otherwise have jurisdiction over the appeal from a final order in the action"). Some states have embodied this right of immediate appeal in court rules. See, e.g., N. D. R. CIV. P. 23; OHIO REV. CODE ANN. § 2505.02(B)(5) (West 2012); Pa. R. Civ. P. 1710; TEXAS INS. CODE ANN. Art. 541.259. Florida's appellate rules likewise permit an appeal as a matter of right by an aggrieved party of orders either granting or denying class certification. Fla. R. App. P. 9.130. See also I.C.A. Rule 1.264/1.264(3)(making an order certifying or refusing to certify an action as a class action as appealable); LSA-C.C.P. Art. 592 (Louisiana's provision allowing for an appeal to be taken as a matter of right from an order that an action should be maintained as a class action). Many other states provide for discretionary appeals of certification decisions.

⁶⁶ See FED. R. CIV. P. 23(f) (pursuant to § 1292(e), accords Courts of Appeals discretion to permit appeals from district court orders granting or denying class-action certification); FED. R. CIV. P. 54(b) (providing for "entry of a

mean the death knell of the litigation – either because a denial makes the lawsuit too expensive to pursue or because a grant threatens litigation costs or risks that will be ruinous to the defendant thus forcing settlement. In either case, under our current system, the party who has been unsuccessful at the certification stage of the lawsuit is relegated to an extraordinary discretionary process that does not offer sufficient safeguards to assure that the decision is correct. It is time to re-write the rule.

IV. The Committee Should Adopt an “Opt-In” Rule for Rule 23(b)(3) Class Actions to Ensure a Meaningful Connection Between Class Members and the Case.

Rule 23(b)(3) permits representative plaintiffs to seek damages on behalf of all plaintiffs who have been certified as class action members. Because Rule 23(b)(3) actions are governed by Rule 23(c)(2)(B)(v)’s “opt-out” mechanism, the legal rights and interests of millions of people are determined in Rule 23(b)(3) cases each year where they are represented, often without their knowledge or consent, by attorneys they do not choose. The dramatic expansion of classes and the resulting changing nature of class action cases has led to a widespread view that many class members are so unconnected to the action that they have no idea whether class attorneys are conducting the action and handling the terms and conditions of settlement in the best interests of the class members. To address these problems, the Committee should consider amending Rule 23 by replacing the “opt-out” provision found in Rule 23(c)(2)(B)(v) and (vi) and 23(c)(3)(B) with an “opt-in” provision to ensure that every individual that becomes a certified class member has a meaningful right to decide whether to join a class action and choose his or her own lawyer.

The 1966 amendments authorized courts to certify as a class all persons who received actual or constructive notice of a certain type of class action (a Rule 23(b)(3) class action) and failed to take affirmative steps to withdraw from the class upon receipt of class notice. Under this system, unless a person within that class takes affirmative action to “opt-out” of the class, they are deemed class members and are bound by the outcome of the case. This is true regardless of whether they received or understood the class notice, and regardless of whether they wanted to be a member of the class.

To recipients, a class notice can be a complex legal document whose implications are unclear. As a result of this uncertainty, the common response of doing nothing has the incongruous effect of converting the recipient of the notice into a class member, often unwittingly. The effect is the creation of massive classes comprised of many members who do not understand the implications of class membership. These class members often do not understand that they have consented to be represented by class counsel who will effectively make all key decisions in the case, including the terms and conditions of any settlement that, if approved by the court, will be binding on all class members.

Equally important, a class member who passively fails to “opt-out” often does not understand the relationship between his or her inclusion in the class and class counsel’s compensation. As a

final judgment as to one or more, but fewer than all, of the claims or parties”). Congress has authorized the promulgation of rules defining finality and allowing for immediate appeal. Prescriptions in point include 28 USC § 1292 (immediately appealable “[i]nterlocutory decisions”); 28 USC § 2072(c) (authorizing promulgation of rules defining when a district court ruling is final for purposes of appeal under § 1291).

general rule, compensation of class counsel is related to the size of the class. The larger the Rule 23(b)(3) class, the greater the potential damages that can be assessed against the defendants and, therefore, the greater the settlement and attorney's fees. (The relationship between the class members and the settlement is even more complicated by the ability of courts to order cy pres payments to non-class members – see II., above.)

Class members are often unaware that any settlement negotiated between class counsel and the defendants in a Rule 23(b)(3) class will include payment to class counsel, which can be in the millions of dollars or more. Class members frequently fail to understand that class counsel and the defendants have their own financial interests in any settlement, with class counsel benefiting from a settlement that maximizes counsel fees and defendants benefiting from one that minimizes their payout. While a court is required to approve the fairness of any class settlement, when its primary proponents are the class counsel and defendants that negotiated it, and the opposition, if any, comes from isolated class members seeking greater compensation for the class, the process can be weighted in favor of the proposed settlement. As commentators have noted, parties to a class action can frequently “find a variety of means by which to trade a low settlement for a high attorney's fee, once the client becomes only a distant bystander to the litigation.”

To preserve the benefits of the class action while correcting these deficiencies, the Committee should amend the applicable rules to ensure that a person can become a class member only if, after a class is certified, he or she affirmatively seeks that status in writing after being fully informed of his or her rights and obligations and those of the class counsel, and to specifically select his or her attorney in the pending class action litigation. Among the rule changes the Committee might consider in implementing a change from an opt-out to an opt-in system for Rule 23(b)(3) class certifications are:

- a. requiring an attorney claiming to represent any certified class member in a Rule 23(b)(3) class action to provide to the federal court that potential class member's express written authorization to be so represented and to become a class member, stating that the person:
 - intends to retain a specifically named attorney or firm;
 - is aware of the legal consequences of joining that litigation, including the rights a class member will lose or waive by joining the action, the person's right to enter an appearance through his or her own counsel, and the person's right not to be included in the class action; and
 - was provided by the designated attorney a good faith estimate of the dollar amount of any attorneys' fee, an explanation of how any attorneys' fee will be calculated and funded, and an explanation of the relative recoveries that the attorney or firm and such person would receive if the claim is settled or decided favorably.

- b. permitting the federal court, in its discretion, to direct notice to potential Rule 23(b)(3) class members of information that would reasonably provide them with information sufficient to make an informed decision as to whether to join the class while protecting them from undue or inappropriate influence by a class action attorney or his or her agent or representative that could dilute the effect of the full disclosure provision in paragraph a. above.
- c. confirming that any person who did not affirmatively consent in writing to join any putative or certified class described in paragraph a. above is not bound by any settlement of that action or any decision or judgment of that court and remains free to file a separate action using counsel of his or her choice as to the same subject matter without having his or her rights affected by the prior class action.

Changes such as these will go a long way towards restoring a relationship between class members and their actions, as well as remedying many of the controversial problems with Rule 23(b)(3) actions.

V. The Committee Should Clarify that Judicial Estoppel Does Not Apply to Class Settlement Negotiation Positions.

Class action defendants have historically utilized settlement classes to reach global resolution of claims brought against them.⁶⁷ A controversial decision of the United States Court of Appeals for the Seventh Circuit, however, put a significant restriction on settlement class negotiations when it applied the doctrine of judicial estoppel to defendants whose agreed-upon class had been disapproved.⁶⁸ In an unprecedented decision, the Seventh Circuit judicially estopped the defendants from subsequently challenging the adequacy of a settlement class on the ground that earlier conflicting positions could lead to “fraud in the legal process.”⁶⁹ The Committee should draft a rule to avoid the harm that this holding could produce.

The doctrine of judicial estoppel traditionally has been limited to instances where a proposed argument or position of a party has been accepted by a court and the party subsequently benefited from the court’s decision.⁷⁰ Other courts have also applied the doctrine to instances where a party negotiated in less than good faith or played “fast and loose” with the court.⁷¹ But where a settlement class has not been approved, and the parties are operating in good faith, there is no risk of judicial fraud or any perception that a court has been misled. Nor is there any risk of inconsistent court determinations if the original proposed settlement has never been adopted.

The potential application of judicial estoppel to an unsuccessful class settlement may have a detrimental effect on negotiations to resolve class certification disputes. Defendants would be wary of seeking to resolve claims which, if rejected or reversed, could bind them in future proceedings. Application of judicial estoppel could encourage defendants instead to engage in

⁶⁷ See Jon B. Nelsen, Note, *Fast and Loose Litigants and Courts: Carnegie v. Household International, Inc. and the End of Settlement Classes*, 84 TEX. L. REV. 541 (2005).

⁶⁸ *Carnegie v. Household Int’l, Inc.*, 376 F.3d 656 (7th Cir. 2004) (Posner, J).

⁶⁹ *Id.* at 660.

⁷⁰ *New Hampshire v. Maine*, 552 U.S. 742, 750-51, 755, 121 S. Ct. 1808, 1815, 1817 (2001).

⁷¹ See Nelsen, *supra* note 71, at 549 and cases cited.

protracted litigation, “wars of attrition,” or to adopt more aggressive individual litigation strategies. Global settlements may also be viewed as too risky for defendants to seek if a disapproving court could judicially estop a defendant from arguing against certification of the class in the future. Accordingly, we propose the following rule:

If a proposed settlement class is not approved either by a trial court or on appeal, or if negotiations between the parties fail to reach agreement on a settlement class, then no statements, representations, or arguments made by the proponents of the settlement in the settlement context may be used against the proponent making the statement in any subsequent litigation of class certification or merit issues.

A rule such as this would make clear that positions taken during an ultimately unsuccessful settlement stage will not be used against a party in future class certification or merit proceedings.⁷² This proposed rule would not prohibit a court from imposing sanctions on any party if the proponents of a settlement have taken positions in bad faith or misrepresented to the court the benefits of the proposed settlement.

We respectfully suggest the Committee consider a rule to ensure that parties attempting to negotiate a final resolution of a dispute through the class process can do so without fear that their positions could be applied to their detriment if the class is not ultimately certified.

CONCLUSION

Rule 23, and particularly (b)(3), has become something that was not envisioned. Class action cases have grown significantly since the FRCP created them in 1938 and modified Rule 23 in 1966. They serve an important function in our judicial system, but their abuse poses great risks. The exponential increase in the size of classes – and the corresponding lack of any meaningful relationship between class members and their cases – is a fundamental cause of many of the issues that have created controversy. Accordingly, we respectfully suggest that the Committee and its Rule 23 Subcommittee take much-needed action to reform four key areas of class actions: prohibit or restrict cy pres payments to non-class members; provide a right to interlocutory appeal on class certification decisions; adopt an “opt-in” rule for Rule 23(b)(3) actions; and clarify that judicial estoppel does not apply to class action settlement negotiations.

Respectfully submitted,

Lawyers for Civil Justice
Federation of Defense & Corporate Counsel
DRI – The Voice of the Defense Bar
International Association of Defense Counsel

⁷² The proposed rule is adopted in part from Section 3.06 of the PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION as adopted by the American Law Institute in 2009.

EXHIBIT 1 – Cy Pres Amendments to Rule 23

Alternative Proposal #1 – Prohibition of Cy Pres

New section to be added to Fed. R. Civ. P. 23 (e)

(6) (A) Except as provided in Rule 23(h), no settlement under this Rule shall allow any payments to charitable organizations or to other persons who are not members of the class as defined in the final settlement. No settlement proposal providing for payments in violation of this subsection may be approved by the court.

(B) Notwithstanding subsection (6)(A), a settlement under this Rule may allow payments to governmental entities responsible for the enforcement of any statute or regulation that the settling defendant(s) allegedly violated.

New section to be added to Fed. R. Civ. P. 23 (g)

(5) ***Inadequacy of class counsel.*** Class counsel proposing a settlement in violation of Rule 23(e)(6) shall be deemed inadequate to represent the class under Rule 23(a) and shall be replaced. Pursuant to this subsection, the Court may replace counsel on its own motion, or upon motion by any party or by any member of the putative class. Replacement counsel shall not be a member of the same firm or contractual consortium as counsel who were thereby removed. Class counsel removed pursuant to this subsection shall have no right to receive any fee, or quantum meruit award.

Alternative Proposal #2 – Cy Pres As A Last Resort

New section to be added to Fed. R. Civ. P. 23(e)

(6) No settlement providing for payments to charitable organizations or to other persons who are not members of the class as defined in the final settlement order, excepting governments acting in their official capacity, including as *parens patriae*, may be approved by the court except upon written findings that: (1) it is impossible, and not merely impractically expensive, to direct all settlement funds to members of the class; (2) a direct relationship exists between all non-members of the class proposed to receive payment and the subject matter of the litigation; (3) no non-member of the class proposed to receive payment is in any way affiliated with any party to the litigation, with either class or defense counsel or their relatives, or with the court; and (4) no non-member of the class proposed to receive payment is involved in the maintenance of, research for, or encouragement of future litigation.

(7) The court may refer issues related to findings required by Rule 23(e)(6) to a special master or a magistrate judge, as provided in Rule 54(d)(2)(D)

New section to be added to Fed. R. Civ. P. 23(h)

(5) No claim for an award under this Rule shall take into account any payments made to charitable organizations or to other persons who are not members of the class as defined in the final settlement and provided by Rule 23(e)(6). Only payments made to members of the class, or to governments acting in their official capacity, including as *parens patriae*, shall be considered the award of attorney's fees under this Rule.