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Class Actions and Legislative Proposals in the 109th Congress: Class Action Fairness Act of 2005

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Summary

S. 5, the Class Action Fairness Act of 2005 has three main sections: (1) an amendment to the federal diversity statute; (2) a provision regarding removal; and (3) a consumer class action "bill of rights." It would control and restrict class action lawsuits by shifting some of the suits from state to federal courts. This would be achieved by creating federal jurisdiction over class action suits when the total amount in dispute exceeds $5,000,000 and when any plaintiff lives in a state different from that of any defendant. The bill would treat certain "mass actions" with more than 100 plaintiffs as class actions for purposes of jurisdiction. S. 5 would require judges to review all settlements based on the issuance of coupons to plaintiffs and limit attorney's fees to the value of the coupon settlements actually received by class members. It would also require careful scrutiny of "net loss" settlements in which class members ultimately lose money. The legislation would ban settlements that award some class members a larger recovery because they live closer to the court. It would allow federal courts to maximize the benefits of class action settlements. Among other things, S. 5 would also require that a notice of proposed settlements be provided to the appropriate state and federal officials such as the state attorneys general. It was reported out of the Senate Judiciary Committee without amendment. On February 10, 2005, the Senate passed S. 5 (72-26) without amendment; the bill is now expected to be considered by the House of Representatives. On February 2, 2005, H.R. 516, the Class Action Fairness Act of 2005, was introduced in the House of Representatives.

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Article III, Section 2 of the United States Constitution provides that when a lawsuit involves citizens from different states or a foreigner, federal courts are given primary jurisdiction. This provision was added for the purpose of limiting discrimination against out-of-state litigants. However, under the doctrine of "complete diversity" current judicial rules provide that as long as at least one defendant and one plaintiff in a lawsuit are from the same state, they should proceed in that state's court system, even if the case involves millions of plaintiffs and is purely interstate or national in nature. In addition, even when "complete diversity" exists, the amount in controversy must be a minimum of $75,000 per plaintiff. Consequently, national class actions with plaintiffs from all 50 states and defendants from multiple states are rarely eligible for federal court jurisdiction.

It is generally agreed that class action lawsuits can facilitate the fair and efficient resolution of legitimate claims of numerous parties. For these reasons, the federal and state courts' rules of civil procedure are designed to enable the litigants to proceed on a class basis in appropriate cases.

In recent years, there have been allegations of abuses in class action suits: there are claims that some class action plaintiffs' attorneys have abused the class action procedures; there is distortion of the federalist system by the action of a few state courts; there is excessive compensation to attorneys at the expense of the injured plaintiffs; these suits create unprecedented costs to the national economy; and they (class action suits) have caused an overall decline in public respect for our nation's judicial system. Or so business groups and other supporters contend.[1]

Consumer groups and the plaintiffs bar associations such as the trial lawyers' groups oppose the legislation. They contend that it would unfairly help corporate defendants in class action suits by moving cases to federal court where damages awarded are generally smaller. As a result, they argue that the legislation would be inconsistent with the principles of federalism and it would create a clog in an already overburdened federal court system thereby slowing the pace of certifying class action cases.[2]

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[1] See Class Action Fairness Act of 2003: Hearing Before the House Comm. on the Judiciary, 108th Cong., 1st Sess. (2003); Class Action Litigation: Hearing Before the Senate Comm. on the Judiciary, 107th Cong., 2nd Sess. (2002).

[2] See Id.; CRS Report RL31859, Class Actions and Legislative Proposals in the 108th (continued...)

The 108th Congress was the fourth consecutive Congress which failed to enact this type of legislation. The House passed a class action bill (H.R. 1115; Class Action Fairness Act of 2003); however, due to a last minute attempt to attach non-germane amendments such as drug reimportation and the minimum wage to the companion bill (S. 2062) in the Senate, it was withdrawn from further consideration in the 108th Congress.

Senator Grassley reintroduced last year's stalled Senate class-action bill (S. 2062) as S. 5 on January 25, 2005, which was referred to the Senate Judiciary Committee.[3] On February 3, 2005, the Senate Judiciary Committee approved the overall bill on a 13-5 vote, without amendment, and referred it to the Senate.[4]

On February 10, 2005, S. 5 passed the Senate without amendment by a vote of 72-26.[5] The bill will now be considered in the House of Representatives where it is expected to pass.[6]

The Legislation

Section 1. Short Title. The act may be cited as the "Class Action Fairness Act of 2005." This section also states that it amends title 28 of the United States Code.

Section 2. Findings and Purposes of the Act. The act sets out Congress' findings describing in essentially these words the: (1) circumstances in which class actions are valuable to our legal system; (2) abuses of the class action process that have harmed class members with legitimate claims and defendants that have acted responsibly, adversely affected interstate commerce, and undermined public respect for our judicial system; (3) the manner by which class members have been harmed by a number of actions taken by plaintiffs' lawyers, which provide little or no benefit to class members as a whole, including (i) plaintiffs' lawyers receiving large fees, while class members are left with coupons or other awards of little or no value, (ii) unjustified rewards made to certain plaintiffs at the expense of other class members, and (iii) confusing published notices that prevent class members from being able to fully understand and effectively exercise their rights; (4) abuses in class actions which undermine the national judicial system, the free flow of interstate commerce, and the concept of diversity jurisdiction as intended by the framers of the

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[2] (...continued)
Congress: Class Action Fairness Acts of 2003 and 2004, at 9-10.

[3] 151 Cong. Rec. S450 (daily ed. Jan 25, 2005).

[4] 151 Cong. Rec. S978 (daily ed. Feb. 3, 2005).

[5] 151 Cong. Rec. S1259 (daily ed. Feb. 10, 2005).

[6] See *Class Action Debate Moves to the House* ...., CQ Today - The Week Ahead, Feb. 10, 2005. See also H.R. 516, the Class Action Fairness Act of 2005, which was introduced in the House of Representatives on February 2, 2005. H.R. 516 is similar to H.R. 1115 which passed in the House during the 108th Congress.

United States Constitution, in that State and local courts are (i) keeping cases of national importance out of federal court, (ii) sometimes acting in ways that demonstrate bias against out-of-state defendants, and (iii) making judgments that impose their view of the law on other states and bind the rights of the residents of those states.

The act's stated purposes are to (1) ensure prompt and fair recovery of legitimate class action claims; (2) reflect the purpose behind the Constitution's diversity jurisdiction clause; and (3) to encourage commercial innovation and consumer-friendly prices.

Section 3. Consumer Class Action Bill of Rights and Improved Procedures for Interstate Class Actions. S. 5 would add five new sections to 28 U.S.C. which are intended to provide greater protections for class members. In particular, section 3 would add the following:

- **Section 1711-Class action definitions**

(1) Class Action-The term is defined to include any civil action filed in federal district court under Rule 23 of the Federal Rules of Civil Procedure, as well as actions filed under similar rules in state court that have been removed to federal court.

(2) Class Counsel-The term is defined as "the persons who serve as the attorneys for the class members in a proposed or certified class action."

(3) Class Members-The term is defined as "the persons (named or unnamed) who fall within the definition of the proposed or certified class in a class action."

(4) Plaintiff Class Action-The term is defined as "a class action in which class members are plaintiffs."

(5) Proposed Settlement-The term is defined as "an agreement regarding a class action that is subject to court approval and that, if approved, would be binding on some or all class members."

- **Section 1712-Judicial scrutiny of coupon and other noncash settlements**

This provision is aimed at certain proposed settlements of class actions, in which the plaintiffs' lawyer and the defendant work out a settlement that provides class members with essentially valueless coupons while rewarding the lawyers with substantial attorneys' fees. To address this problem, this section provides that a judge may approve a proposed settlement under which the class would receive noncash benefits or would otherwise be required to expend funds in order to obtain part or all of the proposed benefits only after a hearing to determine whether, and making a written finding that, the settlement is fair, reasonable, and adequate for class members. In doing so, the judge on the motion of any party may receive expert testimony as to the coupons' value.

It would require that attorneys fees be based either (a) on the value of the coupons actually redeemed by class members in contingent fee cases; (b) on the hours reasonably billed in presenting the class action; or (c) on the value of the coupons redeemed and, to the extent a settlement provides, for equitable relief on a reasonable hourly rate and total. Attorneys fees coupon calculations could not be based on unredeemed coupons, although with court approval the value of unredeemed coupons could be distributed for charitable purposes specified in the settlement agreement.

- **Section 1713-Protection against loss by class members**

This provision provides that a judge may not approve a class action settlement in which the class member will be required to pay attorney's fees that would result in a net loss to a class member unless the court determines in a writing finding that the benefits to the class member substantially outweigh the monetary loss.

- **Section 1714-Protection against discrimination based on geographic location**

This provision provides that a settlement may not award some class members a larger recovery than others solely because the favored members of the class are located closer to the courthouse in which the settlement is filed.

- **Section 1715. Notifications to appropriate federal and state officials**

This provision requires defendants to notify the appropriate state and federal official of the particulars of any class action settlement and delays the effective date of the settlement until 90 days after they have done so. The appropriate federal officials include the Attorney General and in the case of financial institutions the federal regulatory authorities. State officials entitled to notice include the authorities with regulatory jurisdiction over a defendant in any state in which any member of the class resides. Should a defendant fail to comply with the notification requirements, any individual class member would be free to walk away from his obligations under the settlement agreement.

Section 4. Federal District Court Jurisdiction of Interstate Class Actions. Article III of the Constitution protects out-of-state litigants against the prejudice of local courts by allowing for federal diversity jurisdiction when the plaintiffs and defendants are citizens of different states. However, under current law, federal diversity jurisdiction for a class action does not exist unless every member of the class is a citizen of a different state from every defendant, and every member of the class is seeking damages in excess of $75,000.[7] This section would change the law by providing additional protection for out-of-state litigants by creating a minimal

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[7] 28 U.S.C. § 1332. See also *Zahn v. International Paper Co.*,414 U.S. 291, 301 (1973)(The Supreme Court decided that in class actions based on diversity of citizenship, every single class member must satisfy the "matter [amount] in controversy" requirement of section 1332).

diversity rule for class actions and by determining satisfaction of the amount-in-controversy requirement by looking at the total amount of damages at stake.

Under the proposal, federal district courts receive original jurisdiction over any class action in which the amount in controversy, exclusive of interest and costs, exceeds $5,000,000 and in which (A) "any member of a class of plaintiffs is a citizen of a State different from any defendant;" (B)"any member of a class of plaintiffs is a foreign state or a citizen or subject of a foreign state and any defendant is a citizen of a State;" or (C) "any member of a class of plaintiffs is a citizen of a State and any defendant is a foreign state or a citizen or subject of a foreign state." This rule holds true if less than one-third of the plaintiffs and the primary defendants come from the state where the suit is filed; has no application if two-thirds or more of the plaintiffs and a primary defendant come from the state where the suit is filed; and applies at the discretion of the federal court if more than one-third but less than two-thirds of the plaintiffs and the primary defendants come from the state where the suit is filed.[8]

In the exercise of their discretion, the federal courts must consider:

— "Whether the claims asserted involve matters of national or interstate interest"

— "Whether the claims asserted will be governed by laws of the State in which the action was originally filed"

— In the case of a class action originally filed in a State court, "whether the class action has been pleaded in a manner that seeks to avoid Federal jurisdiction"

— "Whether the action was brought in a forum with a distinct nexus with the class members, the alleged harm, or the defendants"

— "Whether the number of citizens of the State in which the action was originally filed in all proposed plaintiff classes in the aggregate is substantially larger than the number of citizens from any other State, and the citizenship of the other members of the proposed class is dispersed among a substantial number of States"

— "Whether ...1 or more class actions asserting the same or similar claims on behalf of the same or other persons have been filed."

This section contains a similar class action definition as section 3, defining a class action as (A) any civil action filed pursuant to rule 23 of the Federal Rules of Civil Procedure or a similar state statute or rule. It also deems to be class actions

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[8] H.R. 1115 in the 108th Congress would have provided for the removal of class actions to federal court if less than one-third of the plaintiffs are from the same state as the primary defendant and the suit involves more than $5,000,000.00. S. 2062 substantially broadened the "two thirds/one-third" analysis to eliminate consideration of a defendant's state or residence in determining whether to remove an action to federal district court.

certain other types of civil actions: (1) an action that asserts claims seeking monetary relief on behalf of 100 or more persons, in which the claims involve common questions of law or fact and are to be jointly tried; but not (2) an action on behalf of the general public pursuant to state statute.[9]

Again, in order that actions lacking national implications remain in state court, the minimal diversity rule does not apply in any action where "(A) two-thirds or more of the members of all proposed plaintiff classes in the aggregate and the primary defendants are citizens of the State in which the action was originally filed; (B) the primary defendants are States, State officials, or other governmental entities against whom the district court may be foreclosed from ordering relief; or (C) the number of members of all proposed plaintiff classes in the aggregate is less than 100."[10]

Section 5. Removal of Interstate Class Actions to Federal District Court. Under existing federal law, civil actions filed in state court, which might have been filed in federal court, can be removed to federal court under some circumstances, see 28 U.S.C. 1441 et. seq. Section 5 would permit removal from state court of minimum diversity cases that section 4 would permit to have been filed originally in federal court. It would allow class action lawsuits to be removed from state court to federal court by any defendant without the consent of any of the other defendants.[11]

Section 6. Report on Class Action Settlements. This provision directs the Judicial Conference of the United States with the assistance of the Director of the Federal Judicial Center and the Director of the Administrative Officer of the United States Courts to report to the Judiciary Committees of the Senate and House of Representatives within 12 months of the enactment with recommendations on the best practices to further ensure fairness in class action settlements with regard to class members and attorneys' fees which should appropriately reflect the extent and success of the attorneys' efforts.

Section 7. Enactment of Judicial Conference Recommendations. This section, which perhaps survives through a scrivener's error, first appeared in bills introduced early in 2003 and was designed to accelerate the effective date of class action reform amendments to Rule 23 of the Federal Rules of Civil Procedure, see H.Rept. 108-144, at 45 (2003). Those amendments, then scheduled to become effective on December 1, 2003, did in fact become effective on that date. In its current form the section appears simply redundant, for it provides that those amendments to Rule 23 shall become effective on December 1, 2003, or upon enactment of S. 5, whichever comes first.

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[9] The House bill in the 108th Congress deviated from the Senate version with regards to two kinds of lawsuits that are not class actions: (1) "private attorney general" cases brought by a named plaintiff other than a state attorney general and (2) non-class action cases involving 100 or more plaintiffs, known as "mass tort" cases. 149 Cong. Rec. at H5295. H.R. 1115 would have imposed the new class action rules on both cases.

[10] See, S. 5, proposed 28 U.S.C. 1332(d)(4), (5).

[11] Under H.R. 1115, any defendant, named plaintiff or unnamed member of a plaintiff class would have been able to seek removal at any time.

Section 8. Rulemaking Authority of Supreme Court and Judicial Conference. This section provides that nothing in this act shall restrict the authority for the Judicial Conference and the Supreme Court to propose and prescribe the general rules of practice and procedure for the federal courts.

Section 9. Effective Date. This section provides that the legislation applies to any civil action commenced on or after the date of enactment.

Pro/Con

Although balanced by the enhanced class member protection features, the jurisdictional and removal components of S. 5 are much like its antecedents in the 106th, 107th, and 108th Congresses. Proponents argue:

- Class action process has been manipulated in recent years;[12]
- U.S. companies have been flooded with labor and employment litigation, much of which has been entirely without merit;[13]
- Proposed changes in the law will increase sanctions against lawyers who bring frivolous claims to court.[14]

Opponents object that they:

- Would clog an already overburdened federal court system and slow the pace of certifying class action cases;[15]
- Are inconsistent with the principles of federalism;[16]
- Would make consumer and public interest litigation more difficult to bring, more expensive, and more burdensome.[17]

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[12] H.Rept. 108-144, at 8. See also statements on the introduction of S. 5, 151 Cong. Rec. S450 (daily ed. Jan. 25, 2005) ("Consumers are too often getting the short end of the stick in class action cases, recovering coupons or pocket change, while their lawyers reap millions.")

[13] *Id.* at 13-14.

[14] *Id.* at 8 and 46-47.

[15] H.Rept. 107-370, at 125-26 (Dissenting views of Reps. Conyers, Berman, Nadler, Scott, Watt, Lofgren, Jackson-Lee, Waters, Meehan, Delahunt, and Baldwin).

[16] *Id.* at 126-29.

[17] *Id.* at 129-34. The legislation, they argue, would create numerous barriers to participating in class actions by permitting defendants to remove most state class action suits to federal court. The removal from state court to federal court would leave consumers shuttling back and forth between state and federal court because while a consumers' class could meet state law class certification requirements, it could fail to meet the class certification requirements set forth in federal law. The result, they contend, will be the federal courts' denial of class certification and dismissal of the case. See also, S.Rept. 106-420, at 51-60 (2000) (Minority views of Sens. Leahy, Kennedy, Biden, Feingold and Torricelli).