The Class Action Fairness Act:

What's Fair About It?

By Lisa M. Bass

Citigroup just agreed to pay a $2 billion class action settlement due to its role in helping Enron with accounting fraud, becoming one of the largest corporate class action settlements in history.[1] This is in addition to the $2.58 billion that Citigroup agreed to settle due to its role in helping WorldCom last year. Just last year, plaintiffs won a $6.75 billion class action suit against ExxonMobil Corp. for the 1989 Exxon Valdez oil spill.[2] A few months earlier, in November, 2003, a verdict against Exxon granted the State of Alabama $11.9 billion for royalties on Exxon's extraction of natural gas in that state. These examples show some of the substantial, and possibly exorbitant, class action awards and settlements in recent years. Not all of these awards, however, go to the plaintiffs. Rather, a significant portion goes to attorneys for legal fees and towards the cost of litigation. Further, the costs that these businesses incur as a result of the class action awards are actually spread to the consumer through increasing the costs of products and services.

To protect consumers from losing entire awards and incurring the costs of class action suits through increased prices, and to protect businesses from state courts which give excess awards, Congress proposed the Class Action Fairness Act of 2005 (hereinafter "CAFA"). President Bush signed CAFA into law in February 2005. CAFA is designed to protect consumers from receiving paltry coupon awards while their attorneys receive exorbitant legal fees. It further prohibits settlements that result in a net loss for the plaintiffs, and requires judges to state the plain meaning of the settlement to class members, so that they may better understand their award and their rights associated with that award. This development of tort reform is also designed to help businesses avoid plaintiff-friendly state courts, decrease forum shopping, reduce corporate legal fees and insurance premiums, and stimulate overall economic growth. The idea is that, not only will businesses save money, but consumers will also save, since exorbitant litigation costs will not be passed on to them through the increased prices of products and services.

But is the Class Action Fairness Act really that fair? Personal injury awards from class action suits are supposed "to return the plaintiff as closely as possible to his or her condition before the accident,"[3] or to "make the plaintiff whole."[4] Although the monetary awards can be substantial, these awards are still unable to return a person to the exact condition they were in before the accident, considering only economic damages such as medical expenses and loss of earning capacity. Class action suits either result in excessive monetary awards, that hurt businesses and the economy, or end up with insufficient settlements for plaintiffs which allows businesses to avoid the costs associated with going to trial. The Act is designed to prevent forum shopping for large class action suits, but allows smaller class actions to be resolved in state court. CAFA is designed to help both businesses and consumers, but until the Act is put into action, it will be hard to determine whether it was worth Congress' time and energy.

The Class Action Fairness Act – Substantive Law or Procedural Rule?

CONGRESS' ABILITY TO ENACT CAFA is based on the concept of diversity jurisdiction - the federal courts' ability to hear claims usually based on state law if the claims are between citizens from different states[5] and Congress' power to regulate interstate commerce.[6] But, CAFA may undermine the Supreme

Court's decision in *Erie v. Tompkins*,[7] because it allows Congress to declare specific procedural rules of common law.[8] The question is whether CAFA is Congress' attempt to regulate procedure or to enact substantive law.

CAFA "supports the notion that state courts should handle predominantly state cases and federal courts should handle predominantly interstate cases."[9] Proponents of CAFA may argue that Congress' power to establish lower federal courts allows it to create procedures such as CAFA to run these lower federal courts.[10] Prior to CAFA, the concept of complete diversity prevented many class action cases from going to federal court, as plaintiff's attorneys would seek to join non-diverse parties to keep the case in state courts.[11] Federal courts usually had original jurisdiction over class actions if *each* named class member resided in a state different than that of the defendant.[12] Constitutionally, the diversity statute requires complete diversity. CAFA does not violate this constitutional requirement,[13] because CAFA only requires minimal diversity in class action cases heard in federal court, requiring that only one class member is from a state other than that of the defendant. Furthermore, CAFA eliminates the $75,000.00 amount in controversy requirement set out in *Snyder v. Harris*.[14]

Opponents argue that CAFA is substantive in nature because it may "unduly affect state law."[15] Opponents also maintain that CAFA violates equal protection, as individual plaintiffs who sue companies may get larger awards in state court and are able to forum shop, whereas class action groups must accept federal court jurisdiction, and are limited by the standards set out in CAFA.[16] The higher standard CAFA requires for certification of a class action also hurts class members, because both federal and state courts can automatically dismiss the case for failing to meet the class action prerequisites set out in Rule 23 of the *Federal Rules of Civil Procedure*. This prevents those cases that may otherwise be heard in a less stringent state court from going to trial.[17] Even if class action cases are able to be heard in state court, a defendant can automatically remove the case directly to federal court, even when the case is filed in their home state, and when other defendants do not consent to removal. This is a plus for businesses because they generally prefer litigating class action suits in federal courts.

CAFA imposes procedural changes rather than creating substantive law. CAFA allows federal courts to hear most, but not all, class actions,[18] and imposes limits on how awards are divided between attorneys and class members. Procedural rules impact who prevails in legal disputes, and judges may interpret CAFA in different ways. CAFA restricts many class action suits to federal court and may prevent large awards for plaintiffs, which provides benefits for businesses. Thus, the enactment of CAFA does not undermine the Supreme Court's decision in *Erie*, as Congress utilized its power to regulate procedure, rather than to enact or change substantive law.

CAFA Benefits the Business Industry

CAFA MAY SEEM LIKE IT IS DESIGNED to protect businesses from excessive class action monetary awards and to prevent individual plaintiffs from obtaining large payments for non-economic damages. According to some, it is "more difficult to obtain a class-action certification in federal court, and the awards are usually less."[19] But others believe that federal courts are "generally kinder (or less tough) on defendants"[20] than some state courts such as Madison County, Illinois, where large damage awards and "cozy relationships"[21] between attorneys and judges provide a busy forum for class-action lawsuits.[22]

CAFA actually allows "businesses to focus their resources on serving customers"[23] and not "on defending themselves against frivolous lawsuits."[24] Defending a tort case can be expensive and the cost is ultimately spread to the consumer through increases in costs of products or services. The increased costs normally cover elevated insurance premiums, research and development of improved products, and overall litigation costs. The Bush administration believes excessive class action suits hinder the nation's economic growth as they are a drain on the economy,[25] and passing CAFA signifies a positive change in this country's overall economic outlook.

> **"CAFA is designed to help both businesses and consumers, but until the Act is put into action, it will be hard to determine whether it was worth Congress' time and energy."**

CAFA Benefits Consumers

CAFA BENEFITS CONSUMERS because "it ensures that consumers, not their attorneys, are compensated for the injuries they have suffered."[26] In a few class action suits, consumers lost money even though the plaintiffs won the case. When Martha Preston joined a class action against her mortgage company, her class won and her share was about $4. However, $95 was taken out of her escrow account to pay the $8.5 million in litigation fees.[27] CAFA would prevent a situation such as this by banning settlements that result in a net loss for class members.[28]

Monetary settlement awards may also include "coupons," which should be redeemable for a discount off certain merchandise made or sold by the defendant company. Prior to CAFA, attorneys took the monetary awards and left the indi-

vidual plaintiffs with only the coupons. These coupons frequently were too difficult or too small to redeem.[29] CAFA now requires that attorney's fees in these cases include a proportionate amount of the coupon settlement.[30] This restricts the amount attorneys can receive for legal fees, limiting the amount to a proportion of what plaintiffs actually receive rather than the amount awarded to them.[31]

Some groups of lawsuits are already managed only on the federal level, including securities, antitrust, racketeering, occupational health and safety, pensions and age discrimination.[32] Friendly local venues do remain available for the individual accident, injury and medical malpractice cases that, depending on perspective, are either the "soul or the scourge of the American judicial system."[33] Further, attorneys may end up using the loophole in CAFA by filing separate actions in different state courts to avoid federal court jurisdiction.[34]

Conclusion

CLASS ACTION SETTLEMENTS AND AWARDS have grown exponentially over the last decade. Tort reform to curb excessive awards continues to be debated by politicians and the legal community. The significance of CAFA's jurisdictional effect on class action suits in the United States will unfold within the next few years. Already, the Supreme Court's recent decision in *Exxon Mobil Corp. v. Allapattah Services, Inc.* noted CAFA's broadened diversity requirements, but stated that this particular class action suit did not fall retroactively under CAFA, as CAFA only applies to cases filed after its enactment.[35] Thus far, CAFA's requirements seem to benefit both businesses and consumers, but application of and any future challenges against CAFA will determine whether these benefits are really "fair." BLB

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Endnotes: *Lisa M. Bass*

[1] Joe Bel Bruno, *Citigroup to Settle Enron Lawsuit for $2B*, DULUTH NEWS TRIBUNE, June 10, 2005, *available at* http://www.duluthsuperior.com/mld/duluthsuperior/business/11863320.htm.

[2] *See* Mike Lewis, *Exxon is Ordered to Pay $6.75 Billion, but Few Expect Money Soon*, Seattle Post-Intelligence, Jan. 29, 2004, *available at* http://seattlepi.nwsource.com/local/158525_exxonvaldez29.html.

[3] Joseph H. King, Jr., *Pain and Suffering, Noneconomic Damages and the Goals of Tort Law*, 57 SMU L. REV. 163, 165 (*citing* Marc A. Franklin & Robert L. Rabin, Tort Law and Alternatives: Cases and Materials 679 (7th ed. 2001)).

[4] *Id.* (*citing* Harry Kalven, Jr., The Jury, the Law, and the Personal Injury Damage Award, 19 OHIO ST. L.J. 158, 160 (1958)).

[5] U.S. CONST. art. III, § 2, cl. 1.

[6] *Id.* at art I, § 8, cl. 13.

[7] In *Erie*, the Court concluded that federal courts exercising jurisdiction in diversity of citizenship should apply state law except in "matters governed by the Federal Constitution or by Acts of Congress." 304 U.S. 64, 78 (1938). States were left with the task of deciding whether to address tort reform through case decisions.

[8] *See id.* at 78 (declaring that "Congress has no power to declare substantive rules of common law applicable in a State . . . be they commercial law or the law of torts").

[9] *Legislation makes suits more orderly; Law on class-action misrepresented by both sides*, Spokesman Review (Spokane, WA), Feb. 24, 2005 at B6.

[10] *See* U.S. CONST. art. III, § 1 (giving Congress the power to establish lower federal courts); *See also* U.S. CONST. art. 1, § 8, cl. 18 (allowing Congress to make all laws "necessary and proper" to execute their vested powers).

[11] JoEllen Lind, *"Procedural Swift": Complex Litigation Reform, State Tort Law, and Democratic Values*, 37 AKRON L. REV. 717, 745-46 (2004).

[12] As long as the class action suit meets CAFA standards, class actions will still be heard in state court if the defendant and at least two-thirds of the plaintiffs are from that state. Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (2005) [Hereinafter *CAFA*].

[13] *See* Strawbridge v. Curtiss, 7 U.S. 267 (1806) (requiring complete diversity, but acknowledging that it is merely a statutory requirement and not a constitutional limitation on Congress).

[14] *See* Snyder v. Harris, 394 U.S. 332, 336 (1969) (demanding that each class member in a class action suit satisfy the requisite jurisdictional amount in controversy, which at the time was only $10,000.00).

[15] *See* Paul Carrington, *"Substance" and "Procedure" in the Rules Enabling Act*, 1989 DUKE L.J. 281, 308 (1989) (implying that a law such as CAFA may be substantive in nature, as it may provoke the "organized political attention of a group of litigations or prospective litigants who claim to be specially and adversely affected by the rule").

[16] *See* Kevin J. Gfell, Comment, *The Constitutional and Economic Implications of a National Cap on Non-Economic Damages in Medical Malpractice Actions*, 37 IND. L. REV. 773, 790 (2004) (discussing equal protection implications of possible medical malpractice award caps); *See also* CAFA, *supra* note 12 at §1712 (requiring greater scrutiny of settlements, by requiring the court to approve settlement awards after giving notice and an opportunity for a hearing to class members).

[17] *See* Lind, *supra* note 11 at 749 (stating that cases may be certified class actions under state law, but may fail to meet the federal criterion for certification).

[18] Jim Peterson, *Trying for fairness; Balance Sheet*, THE INTERNATIONAL HERALD TRIBUNE, Feb. 26, 2005 at 21.

[19] Brian Lazenby, *Class Action Fairness Act Changes Stir Debate*, CHATTANOOGA TIMES FREE PRESS, Feb. 27, 2005 at B11 (quoting Stuart James).

[20] *Skewering the Lawyers; Tort Reform*, THE ECONOMIST, Feb. 19, 2005.

[21] *Id.*

[22] *Id.*

[23] Paul Barton, *Effects of Litigation Shift on Consumers Debated 4 Arkansans Voted for Class-Action Change*, ARKANSAS DEMOCRAT-GAZETTE, Feb. 21, 2005 (quoting Edward Yingling, executive vice-president of the American Bankers Association).

[24] *Id.*

[25] *See White House Trying to Squelch Consumer Protection by Limiting Court Access, Says Coalition to Preserve Access to Justice*, PR NEWSWIRE ASSOCIATION, Jan. 6, 2005 (stating that the President blames consumers filing frivolous class action lawsuits for hindering economic growth).

[26] Paul Barton, *Effects of Litigation Shift on Consumers Debated 4 Arkansans Voted for Class-Action Change*, ARKANSAS DEMOCRAT-GAZETTE, Feb. 21, 2005 (quoting Senator Blanche Lincoln, Democrat).

[27] Sen. Chuck Grassley, *Class Action Reform*, CONGRESSIONAL PRESS RELEASES, Feb. 24, 2005.

[28] CAFA, *supra* note 12 at § 1713.

[29] *Skewering the Lawyers; Tort Reform*, *supra* note 20.

[30] *See* CAFA, *supra* note 12 at § 1712 (linking attorney's fees directly to the coupon's redemption rate or the actual hours spent working on the case).

[31] *Skewering the Lawyers; Tort Reform*, *supra* note 20.

[32] Peterson, *supra* note 18.

[33] *Id.*

[34] *See Skewering the Lawyers; Tort Reform*, *supra* note 20 (quoting George Priest, Yale Law School, who believes that trial attorneys will merely file simultaneous individual actions in state court if they are barred from filing class actions in state court).

[35] Instead, the Court had to use supplemental jurisdiction analysis under 28 U.S.C. § 1367 to reach the same result had it been under CAFA, providing federal courts with supplemental jurisdiction over cases with at least one plaintiff meeting the amount in controversy requirement, with all other jurisdictional requirements met. *See* Exxon Mobil Corp. v. Allapattah Services, Inc., 125 S. Ct. 2611 (2005).