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Litigation Update

A Brief Overview of the Class Action Fairness Act of 2005

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Nearly a year has passed since President Bush signed into law the Class Action Fairness Act of 2005, Pub. L. 109-2 (CAFA). Although CAFA's full impact remains to be seen, the law has already spawned considerable litigation, resulting in a number of published decisions.

CAFA, which applies to class actions "commenced" on or after February 18, 2005, grows out of Congressional concerns about the abuse and misuse of class actions nationwide. Correctly or incorrectly, Congress perceived that the rights of both defendants and plaintiff class members were being shortchanged while plaintiffs' class counsel were reaping enormous benefits.

CAFA addresses Congress' concerns in two fundamental ways. First, it dramatically expands federal court jurisdiction over class actions, with the presumption that all parties will receive a fairer shake in federal court. Second, it modifies procedures for settling class actions, in an effort to improve protections for class members.

CAFA Expands Federal Jurisdiction Over Class Actions

As noted throughout CAFA's legislative history, Congress believed that many of the problems with class actions stemmed from the fact that most cases were litigated in state courts, with many cases venued in a few troublesome jurisdictions. The worst of those state courts applied judicial procedures inconsistently and allowed class counsel to effectively run the show, with inadequate judicial involvement. To avoid that problem, Congress has tried to shift the primary class action forum from state court to federal court.

CAFA changes the requirements for federal jurisdiction over class actions. The standard jurisdictional rules requiring complete diversity and prohibiting aggregation of class members' damages no longer apply to *most* class actions. (CAFA does not apply to certain class actions, including ones involving governmental defendants, securities claims, or state-law claims regarding the internal affairs of a corporation.)

Instead, federal courts now *generally* have jurisdiction over all class actions where:

- The class includes 100 or more members;
- The class members seek aggregate damages in excess of $5 million; and
- At least one of those class members is diverse from at least one defendant.

Thus, if a class of 100 or more plaintiffs seeks more than $5 million in total damages and there is at least minimal diversity, the basic requirements for federal jurisdiction are met. 28 U.S.C. § 1332(d). Not all cases that meet these central requirements, however, qualify for federal jurisdiction. To determine whether federal jurisdiction exists, a more detailed analysis, regarding the citizenship of the various plaintiffs and the importance of the various defendants, is required.

There are basically three possibilities: a) the federal court will have mandatory jurisdiction; b) the federal court will not have jurisdiction; and c) the federal court will have discretionary jurisdiction. Attorneys involved in class actions will need to review CAFA's rules carefully to determine which category applies.

A. Mandatory Federal Jurisdiction – If 1/3 or fewer of all class members are citizens of the forum state, the federal court *must* exercise jurisdiction over the case.

B. No Federal Jurisdiction/Mandatory Remand – If 2/3 or more of all class members are citizens of the forum state, the federal court *must decline* jurisdiction if:

- the "primary defendants" are also citizens of the forum state; or
- at least one defendant from whom "significant relief is sought" and whose alleged actions form a "significant basis for the claims" are citizens of the forum state, and the "principal injuries" were suffered in that state.

Unfortunately, CAFA does not define any of these key terms, such as "primary defendants," "significant," or "principal injuries." Litigation surrounding the meaning of these terms is inevitable.

C. Discretionary Federal Jurisdiction – The analysis becomes even more complicated when between 1/3 and 2/3 of the plaintiffs are citizens of the forum state and the "primary defendants" are also citizens of that state. In that situation, the federal court has discretionary jurisdiction and must decide whether to exercise its jurisdiction based on six factors:

- 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 or by the laws of other states;
- whether the class action was 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; and
- whether, during the three-year period preceding the filing of that class action, one or more other class actions asserting the same or similar claims on behalf of the same or other persons have been filed.

> ***"...[C]ounsel should simply remember that the rules of the class action game have changed and that careful attention to those new rules is critical..."***

CAFA Alters the Rules Regarding Class Action Settlements

CAFA includes a number of new rules regarding class action settlements. These provisions seem designed to make sure that class members actually obtain something of value from a settlement. A few of the new settlement rules bear specific mention.

CAFA requires defendants to notify various federal and state officials (including the state Attorney General as well as reasonably pertinent state regulators and licensing authorities), of the settlement of a class action within 10 days after a proposed class action settlement is filed with the district court. The notice must contain a number of items, which are too numerous to discuss here. Notice must be sent to each state in which a class member resides. 28 U.S.C. § 1715(b). Thus, 50-state notification may be necessary if the class includes members of all 50 states.

Federal courts cannot approve any proposed settlement until 90 days after the last "appropriate" state or federal official receives the required notice. 28 U.S.C. § 1715(d). CAFA generally provides that class members will not be bound by any settlement if the required notices are not given.

CAFA also provides that in the event of a settlement resulting in "coupons" to class members, class counsel's attorney's fees can be calculated only on the basis of the coupons actually "redeemed," not all the coupons issued. 28 U.S.C. § 1712(a). This, of course, delays the payment of any attorneys' fees award until after the court reviews the redemption results.

The Early Case Law

The initial CAFA-related battles have involved two topics. First, does CAFA apply to actions pending in state court at the time of CAFA's enactment? Second, who bears the burden of proof in establishing federal jurisdiction on a motion to remand?

When Does a Case "Commence" Under CAFA?

The first wave of CAFA decisions has concerned the law's applicability to cases filed prior to its enactment. CAFA became effective on February 18, 2005 and specifically applies to all actions "commenced" on or after that date. A number of creative defendants have removed cases filed before February 18, 2005, arguing

that their cases "commenced" for purposes of CAFA on the date of removal to federal court, not on the date of initial filing in state court. Courts throughout the country have uniformly rejected these arguments and held that a case "commences," for purposes of CAFA, on the date that it is originally filed, not on the date that it is removed. *See Bush v. Cheaptickets, Inc.*, 425 F.3d 683 (Ninth Cir. 2005); *Natale v. Pfizer*, 424 F.3d 43 (First Cir. 2005); *Pritchett v. Office Depot, Inc.*, 420 F.3d 1090 (10th Cir. 2005); *Schorsch v. Hewlett-Packard Co.*, 417 F.3d 748 (Seventh Cir. 2005); *Pfizer, Inc. v. Lott*, 417 F.3d 725 (Seventh Cir. 2005); *Knudsen v. Liberty Mut. Ins. Co.*, 411 F.3d 805 (Seventh Cir. 2005). In addition to relying on the plain meaning of the statute, the courts considering this issue have found that CAFA's legislative history establishes that Congress did not intend the law to apply to currently pending cases.

Interestingly for counsel in this jurisdiction, however, the Seventh Circuit has held open the possibility that if a plaintiff adds a new defendant or claim for relief, or takes "any other step sufficiently distinct that courts would treat it as independent for limitations purposes," that action might "commence" a new piece of litigation, and thereby allow removal. *Knudsen*, 411 F.3d at 807. Thus, the possibility exists that certain class actions filed prior to CAFA's effective date could still end up in federal court under CAFA's new jurisdictional rules. Initial removal efforts relying on the rationale of *Knudsen* have failed in the Seventh Circuit, *see Schillinger v. Union Pacific Railroad Co.*, 425 F.3d 330 (Seventh Cir. 2005); *Schorsch*, 417 F.3d 748, but have succeeded elsewhere. *See Hall v. State Farm Mutual Automobile Ins. Co.*, No. 05-72164 (E.D. Mich. Aug. 19, 2005); *Adams v. Federal Materials Co., Inc.*, No. 5:05CV-90-R, 2005 WL 1862378 (W.D. Ky. July 28, 2005).

Who Bears the Burden of Proof?

While setting forth a bevy of new rules regarding federal jurisdiction over class actions, Congress did not address who bears the burden of proof regarding that jurisdiction. Do the standard rules apply, so that the removing party bears the burden of establishing federal jurisdiction? Or does CAFA, with its overriding purpose of shifting class actions into federal courts, alter that standard rule so that the party seeking remand bears the burden of establishing that federal jurisdiction *does not* exist?

Courts have gone both ways on this question. A number of courts have held that Congress intended to shift the burden of proof to the party arguing in favor of remand. *See, e.g., Berry v. Am. Express Pub'g Corp.*, 381 F. Supp. 2d 1118 (C.D. Cal. 2005); *Natale v. Pfizer Inc.*, 379 F. Supp. 2d 161 (D. Mass. 2005); *Harvey v. Blockbuster, Inc.*, 384 F. Supp. 2d 749 (D. N.J. 2005); *Heaphy v. State Farm Mut. Auto Ins. Co.*, No. C 05-5404, 2005 WL 1950244 (W.D. Wash. Aug. 15, 2005); *Waitt v. Merck & Co.*, No. C 05-0759L, 2005 WL 1799740 (W.D. Wash. July 27, 2005); *In re Textainer P'Ship Sec. Litig.*, No. C 05-0969, 2005 WL 1791559 (N.D. Cal. July 27, 2005); *Yeroushalmi v. Blockbuster, Inc.*, No. 2:05-CV-02550, 2005 WL 2083008 (C.D. Cal. July 11, 2005). The basic rationale behind these decisions is that because CAFA was intended to expand federal jurisdiction over class actions, it makes sense to require the party opposing federal jurisdiction to demonstrate why the case does not belong in federal court.

Taking the opposite approach, the courts in *Brill v. Countrywide Home Loans*, 427 F.3d 446 (Seventh Cir. 2005) and *Schwartz v. Comcast Corp.*, No. 05-2340, 2005 U.S. Dist. Lexis 15396 (E.D. Pa. July 28, 2005), have applied the well-established standard rule, placing the burden of proof on the proponent of federal jurisdiction. *See also Sneddon v. Hotwire, Inc.*, No. C 05-0951, 2005 WL 1593593 (N.D. Cal. June 29, 2005); *Aweida v. Pfizer, Inc.*, No. 5:05-CV-00425 (W.D. Okla. June 7, 2005). These courts have noted that Congress said nothing about changing the standard burden of proof rules and that, in the absence of such explicit direction, it would be inappropriate to presume that Congress intended to turn away from the standard approach.

Conclusion

CAFA has already influenced parties' behavior. For example, in Madison County, Ill., one of plaintiffs' counsel's favorite jurisdictions, the number of class actions filed in 2005 (45 cases) is about half of the number filed in 2004 (82 cases). Tellingly, plaintiffs have filed only nine class actions in Madison County since CAFA went into effect.

The full impact of CAFA, however, remains to be seen. Will it result in fewer class actions or just fewer class actions in state court? How will courts interpret CAFA's key terms and jurisdictional provisions? Time will tell. For now, counsel should simply remember that the rules of the class action game have changed and that careful attention to those new rules is critical for plaintiffs' and defendants' attorneys alike.

If you would like more information, please contact Kendall Harrison (kharrison@gklaw.com) or another Litigation Team member. ◆

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