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Taking Control In Class Actions

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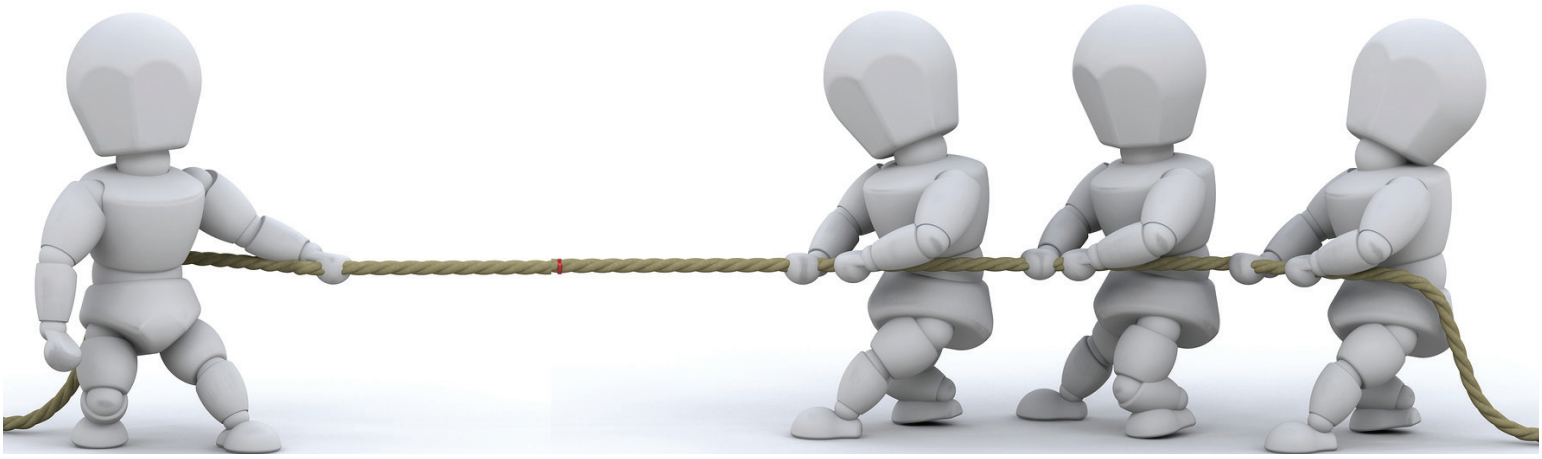

BY CHRISTINA GUEROLA SARCHIO

Class action lawsuits continue to pose substantial risks to corporate America, notwithstanding the passage of the Class Action Fairness Act and recent U.S. Supreme Court decisions, which should be reigning in these types of cases. In particular, there has been an explosion of consumer protection actions filed in the past few years. These will continue to grow since they have now begun to attract some of the more reputable members of the plaintiffs' class action bar. While plaintiffs' lawyers are seemingly quick to navigate around legal obstacles companies may place in their way, companies can implement a number of pre-litigation strategies, discussed below, to try to curtail the class action process. If and when a company does decide to settle, though, it has a vested interest in ensuring the settlement receives judicial approval. Given the recent trend of courts being critical of and rejecting class action settlement agreements, companies should consider retooling their approach to the settlement process to better protect their hard-fought negotiated agreements.

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Corrective Action

On occasion, courts reward companies for proactively identifying and resolving budding legal concerns, such as instituting a product recall or offering product refunds. For instance, just this January, Toyota prevailed against a class action in large part because it had initiated a voluntary safety recall of its vehicles to correct a defect in the anti-lock brake system.[1] Finding that car owners suffered no actual injury as a result of Toyota fixing the defect through the recall, the court denied class certification. It was not Toyota's first win of this kind, however, as a different court held last year that

another of Toyota's recalls rendered that lawsuit prudentially moot.[2]

Offering refunds has also curried favor in some jurisdictions as long as the putative class members are properly informed and made whole through the refund. A company that implemented a liberal refund program without requiring proof of purchase and provided wide-spread notification to consumers through press releases, information on its website, and general news coverage did not have to face a class action that emanated from a large-scale salmonella outbreak in its peanut butter.[3] Other class actions have met the same fate even where proof of purchase was required.[4]

And in 2011, the Seventh Circuit provided companies offering refunds with yet another defense by deeming "inadequate" the class representative who chose to pursue litigation and incur high transaction costs, such as attorney fees and costs related to class notices, at the class members' expense to obtain a refund that was already available to affected consumers.[5]

The decision whether to take corrective action is not one to make lightly. In circumstances where no lawsuit has yet been filed, recalling products may hasten litigation. And, in circumstances where litigation is pending, providing a refund may deprive the company of a remedy it can later offer as part of a negotiated settlement. Nevertheless, particularly in jurisdictions that have already rejected class actions on these grounds, resolving the problem in the short term may yield long-term cost savings.

Contract Clauses Precluding Class Actions

Contracts that either (1) contain explicit and clear provisions requiring individual arbitration, (2) specifically preclude class arbitrations, or (3) are silent on permitting class arbitrations have succeeded in preventing either a class action or class arbitration from going forward. In 2011, the Supreme Court permitted AT&T to enforce a mandatory arbitration clause in its sales contract that also required that any claim by a consumer of its wireless service be brought in an individual capacity and not as a plaintiff or class member in any class proceeding.[6]

Courts have applied the Supreme Court's holding to a variety of cases, including employment class actions where employees had agreed to arbitration in their employment contracts and personal injury suits.[7] Most recently, various courts have held that class action waivers are enforceable in sales contracts, notwithstanding a statutory right to a class action.[8]

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Several companies, including Sony, Microsoft, Netflix and now PayPal, have taken the next step of adding terms to their user agreements requiring consumers to waive the right to participate in class action lawsuits. Others, like auto manufacturers, have inserted arbitration provisions in their consumer product warranties.[9] But these provisions are not practical in all situations, such as in the sale of retail goods, where there is no contract between the manufacturer and consumer.

Moreover, despite such waivers, certain types of class actions will still proceed, particularly where the arbitration provision is overly one-sided or confusing to the consumer. Companies should also evaluate the potential downside of requiring arbitration since the ability to seek judicial review of awards is limited. But a well-drafted, consumer-friendly arbitration provision in a sales or service contract could prove advantageous in defending against class actions.

Protecting Settlements

While most companies initially shun the idea of settling what they perceive to be frivolous class action lawsuits, the burden of defending these cases might soon outweigh the cost of settlement. Once the decision to settle is made, whether because of limited financial resources, the strain on employees and business operations, or the uncertainty of litigation, negotiating favorable terms with class counsel is only half the battle. A number of settlements have recently come under attack by parties other than the usual professional objectors. In order to avoid having to go back to the drawing board, companies need to pay attention to the terms of the agreement and implement procedures to thwart meritless objections that may derail a settlement.

First, the parties need to consider what to do with unclaimed funds. Reversion of unclaimed funds to companies will invite objections, appeals, and likely reversal of the settlement if it is even initially approved. Cy pres distributions to charities with no connection to the class or the claims have met with increasing judicial scrutiny and resistance, particularly after the U.S. Chamber of Commerce petitioned Congress last year to eliminate these awards in class actions.[10] While few options remain, additional pro rata distributions to class members tend to pass judicial muster, even if criticized for creating windfalls.[11] Moreover, cy pres donations may be approved as long as the parties have provided ample justification for the selection of the charity and persuasively described the nexus to the lawsuit.[12] Finally, in some instances, contributions to a state or the federal government's coffers have been deemed acceptable.[13] For example, concerned with the "feeding frenzy of competing interests" over more than $79 million designated for a cy pres distribution in a class action settlement, a New York federal court ordered the entire amount turned over to the U.S. Treasury.[14]

Second, while the need to justify the amount of the attorney fee requested should fall on class counsel, courts have criticized and even rejected settlements that contain a disproportionately high attorney fee award out of a concern of collusion and the possibility that class counsel might have bargained away a benefit to the class in exchange for a

handsome fee.[15] Companies, therefore, need to distance themselves from fee requests, to include resisting efforts to condition a settlement on a specified amount for fees. The safest practice is to enable a court to rule on the fairness of the fee request independent from the fairness of the settlement to class members. While class counsel runs the risk that the fee award will be reduced, this practice best ensures that the settlement will be approved and upheld.

Third, it is important to provide sufficient notice to the class, irrespective of the size of the settlement. As a threshold issue, the notice must be clear and inform interested parties of the pendency of the action and afford them an opportunity to present their objections.[16] While parties may want to keep notice costs down, a single notice in a newspaper such as USA Today was found insufficient to preclude a second copy-cat lawsuit from being filed.[17] Concerned that class members were deprived of the due process right to adequate notice of the prior class settlement, courts have encouraged traditional forms of notice, such as through multiple publications and direct mail, as well as newer forms like email and internet postings, in order to later permit full release of class member claims. Moreover, Spanish-language notice may also be necessary depending on consumer demographics.

Lastly, requiring objectors to satisfy specific requirements before appealing a class action settlement can deter those who are not willing to invest time or money to pursue an appeal that may be unsuccessful. For instance, the parties can require non-named class members to intervene in the district court to have the right to appeal. The parties can also request the court require objectors to post a bond for appeal. Circuits are split as to what amount of bond is appropriate, with some jurisdictions imposing only court-specific costs while others include the parties' attorney fees to defend the appeal.[18] But any amount of bond might serve to discourage a meritless appeal. In addition, the parties can invoke Federal Appellate Rule 38, which permits an appellate court to "award just damages and single or double costs to the appellee," as a sanction for frivolous appeals and a way to discourage professional objectors from challenging settlements in the future.[19]

The New York Court of Appeals' decisions in 'Fischbarg' and 'Deutsche Bank Securities' remain the **seminal cases** in New York on whether electronic communications are **sufficient to exercise personal jurisdiction** over a non-domiciliary.

Conclusion

In summary, when actively litigating a class action, there are a number of tactical maneuvers a company can make to defend itself. But the importance of steps taken before a class action is filed, as well as the steps taken to see a class action settlement through to the end, should not be overlooked. Often, a proactive approach at these crucial junctures will ultimately better serve the company's interests.

1. *In re Toyota Motor Hybrid Brake Mktg., Sales Practices & Prods. Liab. Litig.*, No. SAML 10-2172-CJC, 2013 WL 150205 (C.D. Cal. Jan. 9, 2013) (denying class certification).

2. *Winzler v. Toyota Motor Sales USA*, 681 F.3d 1208 (10th Cir. 2012) (dismissing action for mootness after Toyota voluntarily recalled the vehicles that were the subject of the pending litigation).

3. *In re ConAgra Peanut Butter Prods. Liab. Litig.*, 251 F.R.D. 689 (N.D. Ga. 2008); see also *Webb v. Carter's*, 272 F.R.D. 489 (C.D. Cal. 2011) (rejecting a class action against the manufacturer of children's tagless clothes that was already offering the relief sought by the putative class members).

4. *In re Phenylpropanolamine (PPA) Prods. Liab. Litig.*, 214 F.R.D. 614 (W.D. Wash. 2003) (finding class certification not superior to defendants' already-existing refund and product replacement program, notwithstanding the proof of purchase limitation).

5. *In re Aqua Dots Prods. Liab. Litig.*, 654 F.3d 748 (7th Cir. 2011) (affirming on different grounds the district court's denial of class certification against a manufacturer that implemented procedures to reimburse purchasers of a defective toy).

6. *AT&T Mobility v. Concepcion*, 131 S. Ct. 1740 (2011).

7. *Marmet Health Care Ctr. v. Brown*, 132 S. Ct. 1201 (2012) (invalidating public policy prohibition against arbitration agreements as to personal injury and wrongful death claims against nursing homes).

8. *Flores v. West Covina Auto Grp.*, B238265, 2013 WL 139200 (Cal. Ct. App. Jan. 11, 2013) (granting auto dealer's motion to compel arbitration pursuant to class action waiver contained in a form contract widely used by dealerships throughout the state, finding preempted California's Consumers Legal Remedies Act, which contained an anti-waiver provision); *Ayzenberg v. Bronx House Emanuel Campus*, 93 A.D.3d 607, 941 N.Y.S.2d 106 (N.Y. App. Div. 2012) (in action for personal injuries, state statute against arbitration clauses in contracts for the sale of services preempted).

9. Only one circuit had initially deviated from the holdings of other circuits post-*Concepcion* that the federal Magnuson-Moss Warranty Act does not preclude mandatory arbitration provisions in consumer warranty contracts, but subsequently withdrew its opinion without explanation. See *Kolev v. Euromotors West/The Auto Gallery*, 676 F. 3d 867 (9th Cir. 2012), withdrawing 658 F.3d 1024 (9th Cir. 2011).

10. See *Dennis v. Kellogg*, 697 F. 3d 858 (9th Cir. 2012) (rejecting settlement where, inter alia, the proposed cy pres distribution of funds and food items to charities that feed the indigent had "little or nothing to do" with combating allegedly false advertising).

11. See *Klier v. Elf Atochem N. Am.*, 658 F.3d 468 (5th Cir. 2011) (holding that, in the absence of an express provision in the settlement agreement to the contrary, unclaimed funds should be distributed pro rata to class members who participated in the settlement as opposed to being given to charity as a cy pres distribution).

12. See *In re Lupron Mkt'g. & Sales Practices Litig.*, 677 F.3d 21 (1st Cir. 2012) (approving settlement that included cy pres award after adopting a "reasonable approximation test" as to whether cy pres distributions reasonably approximate the interests of the class members).

13. See *All Plaintiffs v. All Defendants*, 645 F.3d 329 (5th Cir. 2011) (reversed the award of unclaimed settlement funds in an antitrust class action because the district court had failed to follow state law governing fund distribution—the Texas Unclaimed Property Act—which required unclaimed class action funds to escheat to the state of Texas); *Nachshin v. AOL*, 663 F.3d 1034 (9th Cir. 2011) (reversed approval of a settlement, remanded for reconsideration and directed the district court to consider escheating the funds to the U.S. Treasury if a suitable cy pres beneficiary could not be located).

14. *SEC v. Bear Stearns*, 626 F. Supp. 2d 402 (S.D.N.Y. 2009).

15. *In re Bluetooth Headset Prod. Liab. Litig.*, 654 F.3d 935 (9th Cir. 2011).

16. *Kaufman v. Am. Express Travel Related Servs.*, 283 F.R.D. 404 (N.D. Ill. 2012) (requiring notice to be reissued instead of rejecting settlement in its entirety where notice was inadequate).

17. *Hecht v. United Collection Bureau*, 691 F.3d 218 (2d Cir. Aug. 17, 2012).

18. *Compare Azizian v. Federated Dept. Stores*, 499 F.3d 950 (9th Cir. 2007) (holding that the "costs on appeal" that may be included in an appeal bond under Federal Rule of Appellate Procedure 7 include attorneys' fees permitted by the applicable fee shifting statute), *Blessing v. Sirius XM Radio*, No. 09 CV 10035(HB), 2011 WL 5873383 (S.D.N.Y. Nov. 22, 2011) (holding that district courts in the Second Circuit may include attorneys' fees in an appeal bond when authorized by the substantive statute but not merely because the court deems the appeal frivolous), with *Cobell v. Salazar*, Civ. 816 F. Supp. 2d 10 (D.D.C. 2011) (noting that, in the D.C. Circuit, an appeal bond is limited to the costs taxable pursuant to Federal Rule of Appellate Procedure 39).

19. Fed. R. App. P. 38.