KIRKLAND & ELLIS LLP

ALERT

March 2005

Class Action Reform Law Increases Federal Judges' Workload and Raises New Issues for Parties to Litigate

The "Class Action Fairness Act of 2005" (the "Act"), signed into law by President Bush on February 18, 2005, will dramatically change class action litigation in two fundamental ways. *First*, it expands federal court diversity jurisdiction to encompass many class actions previously filed and litigated in state court; it authorizes removal of other state court class actions; it curtails the ability to remand them; and it provides for accelerated appellate review of remand orders. *Second*, it regulates class action settlements involving coupons and the attorneys' fees associated with them, and it imposes on settling defendants the duty of immediately notifying state and federal officials — in potentially every state — of the settlement of any class action in federal court.

Key Changes

With a few limited exceptions, the Act confers original federal jurisdiction over any putative class action filed in state or federal court if (a) the claims of *all* class members, aggregated together, would exceed $5 million, *and* (b) at least one plaintiff is from a different state than at least one defendant.

The Act also makes it easier to remove class action cases from state court to federal court. If *one-third or fewer* of the putative class members are citizens of the state in which the case was filed, then the federal court must exercise jurisdiction over the class action. A federal court *may*, in its discretion, decline jurisdiction if (a) *between one-third and two thirds* of all putative class members are citizens of the state in which the action was filed, *and* (b) the "primary defendants" are also citizens of that state.

The court must consider six factors in making its decision on whether to remand such cases:

- Whether the claims involve matters of national or interstate interest;
- Whether the claims will be governed by laws of the state in which the case was originally filed;
- Whether the action was pleaded in an attempt to avoid federal jurisdiction;
- Whether the action was brought in a forum with a connection to the class members, the alleged harm, or the defendants;

- Whether the number of putative class members from the state of original filing is substantially larger than the number from any other state and those from other states is dispersed among a substantial number of states;

- Whether during the 3 years prior to the filing of the action, other class actions asserting the same or similar claims were filed on behalf of the same putative class members.

Finally, a federal court must decline jurisdiction if (a) two-thirds or more of all putative class members are citizens of the state in which the action was originally filed, and (b) the "primary defendants" are also citizens of the state of original filing.

Alternatively, a federal court must also decline jurisdiction if (i) *two-thirds or more* of all putative class members are citizens of the state in which the action was originally filed, (ii) at least one defendant from whom "significant relief is sought" and whose conduct forms "a significant basis for the claims" is also from that state, (iii) "principal injuries" were suffered in that state, *and* (iv) no other class action was filed in the prior three years that asserts the same or similar allegations against any of the same defendants.

The Act's removal provisions *do not* apply to securities or corporate governance cases, to cases where state officials are the primary defendants, or where there are fewer than 100 putative class members. The Act does apply, however, to most "mass action" cases where numerous plaintiffs bring their claims together in a single action under permissive joinder rules rather than under the class action rules.

With regard to settlements, the Act requires courts to closely examine class settlements involving coupons awarded to class members. Specifically, the Act requires that the court hold a hearing and make specific written findings as to the adequacy and fairness of a coupon settlement. The Act also requires courts to carefully scrutinize attorneys' fees associated with coupon settlements. In non-contingent attorneys' fee cases, the fees must be related to the amount of time the class attorneys actually spent working on the case. In contingent fee cases, the value of coupons actually redeemed (not issued, distributed, or available) must form the basis for the attorneys' fee award. Finally, the Act also precludes class settlements that favor certain class members over others solely on the basis of their geographic location.

Issues That Likely Will Provoke Litigation and Require Judicial Refinement

Because the Act was not drafted by the Advisory Committee on the Federal Rules of Civil Procedure, but by Congress itself, the Act does not mesh particularly well with the current system of class action, removal, and multi-district litigation rules and jurisprudence. Consequently, the Act will undoubtedly raise a number of new areas of potential disagreement and litigation between defendants and plaintiffs — particularly where new definitions are introduced into the class action legal lexecon. Some of those likely areas of new friction are discussed below.

Counting Plaintiffs: Counting class members for purposes of the one-third/two-thirds thresholds will not be easy for the courts. Consumers often buy indirectly or via intermediaries, or pick up their purchases in-store, or ship their purchases to addresses out of state. Conversely, corporations may not know precisely where their shareholders or former customers are located. The new rules will surely provoke creative class definitions as plaintiffs' counsel attempt to squeeze two-thirds of their class into their chosen forum state.

Primary vs. Significant Defendants: Courts will also frequently need to determine who are "primary" defendants for purposes of determining whether the federal court has jurisdiction. Without any guidance in the legislation or in other statutory law, courts will have significant discretion in defining which defendants are primary and which are not.

There is an additional issue lurking. To what extent do "primary" defendants differ from defendants from whom "significant relief is sought" or whose "alleged conduct forms a significant basis" for the claims — which is a key issue when a court is considering whether it must decline jurisdiction. Neither of these "significants" is defined in the Act. Logically, a defendant would have to be "significant" in order to obtain "primary" defendant status, but presumably that would not be a sufficient condition in and of itself. As a result of these new rules, counsel seeking to keep their class claims in their chosen state forum may need to excuse certain defendants from their complaints in order to avoid naming an out-of-state primary defendant that will result in their case being kicked up to federal court.

Principal Injuries: For a federal court to decline jurisdiction when more than two-thirds of the putative class members are citizens of the forum state and at least one significant defendant is also a citizen of that state, the court must also determine that "principal injuries resulting from the alleged conduct or any related conduct of each defendant" were incurred in the forum state. Unfortunately, "principal" is not defined in the Act. The issue becomes even more difficult when non-monetary relief, such as an injunction or an accounting, is at stake.

Removal at Any Time: The Act removes the one-year strict prohibition on removals to federal court. In sharp contrast to the former rule, a case *not* initially subject to removal to federal court could suddenly become removable under the new rules if, for example, summary judgment rulings eliminated a significant plaintiff subclass, or group of class members' claims,

thereby pushing the case below one of the "plaintiff count" thresholds. The judicial efficiency of having cases yanked out of state court based on even a slight reduction in the number of class members — even on the eve of trial — is questionable at best. The Act also removes the requirement of unanimity among defendants for removal, and allows any defendant to seek removal, thereby making removal even more likely.

Coupon Settlements: Prior to the Act, it was commonplace for class action attorneys' fee awards to be made at the time the settlement was approved. The new rule tying attorneys' fees to actual coupon settlement redemptions means that attorneys' fees associated with a coupon settlement cannot be accurately determined until the time for redemption of the coupons has expired. This may further limit the attractiveness of coupon settlements in the eyes of class plaintiffs' attorneys. The unintended consequence of these changes, at least from the defendants' standpoint, may be that a relatively painless form of settlement for certain defendants may disappear as class plaintiffs' counsel reject coupon settlements and insist on strictly monetary class relief.

Effect on Indirect Purchaser Antitrust Class Actions: The Act will also have a major impact on the way in which typical state court indirect purchaser antitrust class actions (and other types of large state class actions) are resolved. *First*, in all but the smallest of cases, the class damage claims will exceed $5 million and diversity with at least one defendant will exist, thereby conferring federal jurisdiction. As a result, the typical indirect purchaser antitrust class action previously filed and litigated in state court will now be removable to federal court — on the motion of *any* defendant at any time, rather than on the early motion of all served defendants.

Second, the typical case will likely stay in federal court unless two-thirds of the putative class members are from the state in which the case was originally filed *and* all of the "primary" defendants are from that state as well. A federal court must also send a "two-thirds or more" case back to state court if (a) at least one "significant" defendant is also from the original state, (b) the "principal injuries" were suffered in that state, *and* (c) no other similar antitrust class action was filed in the previous three years against *any* of the defendants. In those removed cases where between one-third and two-thirds of the plaintiffs are from the state of original filing as well as the primary defendants, the court retains the discretion to remand the case — but the factors the Act directs a court to consider weigh heavily in favor of the case remaining in federal court.

Consequently, the deck is clearly stacked against indirect purchaser antitrust class actions remaining in, or being remanded to, state court. Again using indirect purchaser antitrust cases as an example, in all but the most localized of price fixing conspiracies or monopolization cases, the action will remain in federal court once it arrives there.

When the typical state court indirect purchaser antitrust class action is successfully removed to federal court it will most likely be sent, along with similar cases removed to federal court in the dozens of other states that permit indirect purchaser antitrust suits, to the single federal court assigned by the Multidistrict Litigation Panel to control the case for coordinated pretrial (but not for trial) purposes. Thus, the putative indirect purchaser classes from numerous states will be lumped together in the same court along with direct purchaser class and opt out plaintiffs who filed Sherman Act claims based on the same alleged conspiracy or monopolization facts. This will introduce many issues not typically addressed in antitrust cases coordinated in federal court. Specifically, when considering class certification, the federal court may find the various purported indirect purchaser classes so hopelessly conflicted as a result of the different state indirect purchaser statutes (i.e., some states allow for recovery of the "full consideration paid by the purchaser") that a single indirect class, or several indirect classes, will be deemed "unmanageable" under Federal Rule of Civil Procedure 23. Indirect purchaser plaintiffs may also be unhappy in federal court where coordinated discovery will allow the defendants to obtain evidence from the direct purchaser plaintiffs as to whether the direct purchasers passed any overcharges along to the indirect purchaser plaintiffs — possibly scuttling or limiting indirect plaintiffs' damage claims.

Finally, although most antitrust class actions are resolved before trial by motion or settlement, those that are not resolved must be sent back for trial to the various federal courts from where they came under the U.S. Supreme Court's ruling in *Lexecon*. This raises the prospect that indirect purchaser class actions will be returned for trial to dozens of different federal courts, with potentially dozens of different results for similarly situated purchases depending, once again, in large part on where the case was originally filed. This is clearly contrary to the general intent of the Act to coordinate these cases in one federal court for overall objectively impartial and consistent resolution.

In sum, although the Class Action Fairness Act of 2005 will broadly alter the class action landscape, many of the implementing and clarifying details left out of the statute will need to be filled in by the courts in the coming years. It is in those areas that class action plaintiffs and defendants will direct much of their future litigation efforts.

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