

Calif. High Court Ruling Changes Class Action Landscape

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"There are three kinds of lies: lies, damned lies and statistics." The California Supreme Court could have been channeling Mark Twain when it rejected, emphatically, the unbridled use of statistical sampling to prove liability in a class action wage and hour case. In a unanimous decision, California's high court in *Duran v. U.S. Bank National Association* gave the heave-ho to the kind of "trial by formula" that has become a feature of modern-day wage and hour litigation.

At the same time, the state high court restored some sanity to class action litigation more generally. While it might be tempting to view *Duran* as strictly an employment case, the far-reaching implications for class actions across the board cannot be overstated. Practitioners should review their existing California state and federal class actions and evaluate whether *Duran* can be used to their advantage.



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Facts of *Duran*

This class action was filed against U.S. Bank on behalf of 260 business banking officers ("BBOs") who claimed they were denied overtime pay and meal and rest breaks in violation of California's unfair competition law. Liability turned on whether the bank misclassified the BBOs as exempt under the "outside salesperson" exemption, which applies to someone who spends more than 50 percent of the workday on sales activities outside the branch. U.S. Bank asserted the outside salesperson exemption as an affirmative defense.

Phase One: Liability

How would plaintiffs prove that all 260 were misclassified? The trial court turned to statistics. It took testimony from 21 "sampled" class members, which included two named plaintiffs and additional class members the court directed the clerk to select "from the proverbial hat." U.S. Bank objected at a case management conference that the court's plan to take a sample of class members and then extrapolate findings on liability to the rest of the class violates due process. The 21 sampled class members said they spent less than 50 percent of their time outside the branch and the court concluded, by extrapolation, based on testimony from plaintiffs' statistical expert, that all 260 BBOs had been misclassified and all were owed overtime in amounts to be determined in phase two. There was just one small problem: 75

class members — at least 28 percent of the class — filed sworn declarations saying they had not been misclassified. The trial court rejected that evidence and found the bank liable.

Phase Two: Damages

At the damages phase, the trial court again denied U.S. Bank's request to introduce any of the 75 declarations. Plaintiff's statistics expert testified that based on extrapolation from the 21 "sampled" class members — a small sample size and not entirely random — as much as 13 percent of the entire class was properly classified as exempt. U.S. Bank's expert identified several flaws in the court's phase one methodology, for example, small sample size, "non-response" error caused by a member of the original sample who failed to appear at trial and selection bias from including the two named plaintiffs in the sample group. The court disregarded these objections and, instead, took testimony about the average number of hours worked by the "21" employees, reasoned that the same was true for all, and awarded the class \$15 million — including \$6 million awarded to the 75 BBOs who admitted under oath they had no claim.

Judgment Reversed

In 2012, the Court of Appeal reversed the judgment, concluding that the trial court's flawed trial plan amounted to an improper "trial by formula" that deprived the employer of its due process rights because the employer could not raise individual challenges to absent class members' claims. The Court of Appeal also ordered the class decertified.

Why Duran Matters

The California Supreme Court opened with a stout denunciation of the trial court's plan, calling it "profoundly flawed." The court affirmed the appellate court's reversal, and in doing so it imposed new substantive and procedural hurdles. Those hurdles have reordered how class actions will proceed in all California class actions, not just employment class actions.

Substance: Statistical Sampling Generally

A due process right to prove defenses: Regardless of the kind of class action, employment or otherwise, and regardless of whether statistical sampling is used, a defendant has a due process right to litigate its individual affirmative defenses. This is fundamental. (Duran, slip opn. at 38; see also id. at 29 ("any trial must allow for the litigation of affirmative defenses ...").) "These principles derive from both class action rules and principles of due process." (Id., at 31.)

Statistical sampling to prove liability: As for statistical sampling to prove liability, it is not banned altogether. However, it has to be carefully controlled. The Duran court stated:

We need not reach a sweeping conclusion as to whether or when sampling should be available as a tool for proving liability in a class action. It suffices to note that any class action trial plan, including those involving statistical methods of proof, must allow the defendant to litigate its affirmative defenses. If a defense depends upon questions individual to each class member, the statistical model must be designed to accommodate these case-specific deviations. If statistical methods are ultimately incompatible with the nature of the plaintiffs' claims or the defendant's defenses, resort to statistical proof may not be appropriate. Procedural innovation must conform to the substantive rights of the parties. (Id., slip opn, at 38.)

Statistics can't be the only "glue." Moreover, evidence of liability common to each class member other than through statistics must come first. It cannot be created through, or replaced by, statistics: "Statistical methods cannot entirely substitute for common proof, however. There must be some glue that binds class members together apart from statistical evidence." (Id., at 26.) As the Duran court said: "Class actions do not create a requirement of common evidence. Instead, class litigation may be appropriate if the circumstances of a particular case demonstrate that there is common evidence." (Id. at 33.)

Procedure: A Manageable Trial Plan at the Class Certification Stage

A plaintiff who seeks to use statistical evidence to prove liability must meet a set of new criteria. If the trial plan will include statistical evidence, the court should consider at the certification stage whether a trial plan has been developed to address its use.

For one thing, a plaintiff must now prove manageability. This was optional pre-Duran.

Also, the bar has been raised. The trial court must conduct a preliminary assessment "to determine the level of variability in the class. If the variability is too great, individual issues are more likely to swamp common ones and render the class action unmanageable." (Id. at 28.)

What did the California Supreme Court mean by variability? "[A] defense in which liability itself is predicated on factual questions specific to individual claimants poses a much greater challenge to manageability" than individual questions regarding the calculation of damages. (Id. at 25.) "[T]he trial court could not abridge [the bank's] presentation of an exemption defense simply because that defense was cumbersome to litigate in a class action." (Id. at 31.) And "[i]f a defense depends upon questions individual to each class member, the statistical model must be designed to accommodate these case-specific deviations." (Id. at 38) In other words, a court's trial plan must allow a defendant to litigate its affirmative defenses, even if the process would be difficult; a plaintiff's procedural choices should not deprive a defendant of substantive rights.

All Misclassification Cases Now in Doubt

The Duran court went further. It not only called into question a tool commonly used by the class action bar to bring wage and hour cases, it cast doubt on the future of misclassification cases themselves — even those that do not rely on sampling. The court stated: "[A]n employer's liability for misclassification under most Labor Code exemptions will depend on employees' individual circumstances." (Id., at 33 (*italics added*)). By that, the Duran court seems to be saying that misclassification cases invariably raise inherently individual issues, no matter which Labor Code exemption is used.

Importantly, the Duran court also reaffirmed the correct reading of the wage order overtime exemptions. As the order's plain language states, the trial court must inquire "first and foremost" how the employee actually spends his or her time. "Ancillary" to this inquiry, as Duran made clear, are questions about the employer's realistic expectations of the job, which plaintiffs often claim is a basis for class certification under *Sav-On Drug Stores Inc. v. Superior Court*. To the contrary, "California's uniquely quantitative approach" to overtime exemptions requires proof about how individual employees actually use their time to accurately determine an employer's overtime liability. The Duran court recognized that this has the potential to raise several individualized questions that may be impossible to litigate on a classwide basis.

No, it Can't be Sorted Out Later

The Duran court took a stroll through the neighborhood of class action law that has been roiling with controversy: The “overbroad class.”

Class action plaintiffs always contend that everyone in the class was harmed, and will calculate classwide damages by multiplying the number of all class members times the average damage per class member. This leads to the “overbroad class,” where persons are included in the class simply by virtue of the broad definition (e.g., all persons who bought a certain product, worked at an employer during a certain time period, clicked on a webpage, etc.,). In such cases, the damage figure is wildly inflated by the inclusion of persons who have no claim.

“No matter,” says the class action bar, “this can be sorted out in the claims process,” or in “Phase II, the damages phase, after liability is decided.” “By the way,” class counsel will say, “the damages phase is also where the defendant can assert its now-meaningless due process right to bring individual defenses.” In other words, the plaintiff gets to assemble his damages case by multiplication. But defendant has to disassemble that figure by subtraction. That is an impossible task and effectively creates a presumption of classwide harm.

To date, no California appellate court has directly addressed this nonsensical argument — until now. The Duran court said: “Only in an extraordinary situation would a class action be justified where, subsequent to the class judgment, the members would be required to individually prove not only damages but also liability.” (Id., at 25.) Further, the court rejected a damages model in which plaintiff’s expert calculated damages by multiplying the average hours of overtime worked per class member times all class members, when some of those persons had no claim. People who have no claim and are unharmed must be subtracted and cannot be included in the multiplier for damages.

Duran’s Application in Federal Court

An open question is to what extent Duran applies in federal court. The substantive holdings discussed above should apply in federal court because they “derive from both class action rules and principles of due process.” (Id., at 31.) That means they supply the rule of decision that must be followed by a federal court. Under *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938), a federal court must apply state substantive law, as was decided in *Alaska Rent-A-Car Inc. v. Avis Budget Grp. Inc.* However, it is less clear whether Duran’s procedural holding — requiring trial courts to review plaintiff’s trial plan and make “manageability” findings — applies in federal court.

Conclusion

Duran will affect every California class action, both employment and otherwise, whether on file now or still just a glimmer in class counsel’s eye. And if the claim is brought under California’s Labor Code or unfair competition law, Duran could affect class actions pending in federal court.

Practical Tips in Light of Duran

- Businesses facing class action exposure should review their portfolio of cases and ask, “How has Duran changed each case?”

- Recognize that Duran is a paradigm-shifting decision that has implications beyond the employment or wage and hour context.
- Be vigilant in unleashing the full power of Duran to challenge statistical methods proposed or used to prove liability.
- If statistical methods have been used, identify flaws addressed in Duran (e.g., issues regarding sampling errors, selection bias and reliability of results).

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