

San Diego Daily Transcript

MAY 5, 2005

New Law Deters Abuse of Class Action Suits

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Saying that it would be "good for our system, and it's good for our economy," President Bush signed into law the Class Action Fairness Act of 2005 (CAFA) on Feb. 18.

CAFA, which went into effect immediately, provides some comfort to businesses concerned about being sued in a massive class action lawsuit in a distant state.

Before CAFA, it was possible that a medium-sized to larger business could be sued in virtually any court across the nation. The only real requirement was that the defendant be subject to personal jurisdiction in the state in which the case is filed.

For most businesses, this was an easy requirement to satisfy. Selling products or providing services to customers in other states can meet the test for jurisdiction. All that an enterprising class action lawyer would need is someone to agree to be the plaintiff. The attorney could then file a complaint on behalf of all persons "similarly situated," often times nationwide.

Defending these types of cases is extraordinarily expensive and

burdensome. The lawsuits were often far away (Alabama was a frequent host of nationwide class actions, due to its liberal laws governing these types of cases).

A defendant must then hire competent attorneys to defend the case, and many times a primary defense firm and a local firm were needed. These cases are also expensive due to all of the information exchange (called discovery) that is required.

Even if the risk of losing the case is slight, the cost of defense is so high, and the possible outcome so enormous, that many defendants find it easier to just settle.

CAFA's primary tool to help level the playing field in nationwide class actions is to allow many such cases to be heard in federal court, rather than state court.

In general, plaintiff's lawyers like to file cases in state courts, which tend to be more plaintiff friendly, in that the rules and procedures for class actions are generally more lax. Federal judges also tend to have more resources to allow them to scrutinize the case before them. Ask most

defense attorneys if they'd rather defend a case in state or federal court. The answer is almost universal -- federal court.

The location of the expected members of the class is a key factor under CAFA. If fewer than one-third live in the state where the lawsuit is filed, the federal court must hear the case if the defendant "removes" a state court claim to the federal court.

If more than one-third but less than two-thirds of the class members are found in the state, the federal court may, but does not have to, hear the case.

The federal court does not have to hear the case if more than two-thirds of the class members are found in the state where the suit is filed. These changes, along with a whole host of other provisions in CAFA, effectively limit an out-of-state defendant's exposure to



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nationwide class actions in other states' courts. It would be a rare case that a nationwide case could be brought where more than one-third of the class members are found in one single state.

CAFA also limits the ability of a plaintiff's lawyer to successfully bring a class action and collect a large fee, without providing much of a benefit to the class.

By way of example, before CAFA, a class action could be settled by the defendant issuing

"coupons" to all members of the class, and without paying much, or any, money.

CAFA requires a court to scrutinize and issue a written opinion on the fairness and adequacy of a settlement involving such coupons. It also prohibits plaintiff's lawyers from being paid money equal to a portion of such coupons, and instead requires their fees to be based upon either the amount of time actually spent on the case, or be set according to the value of coupons

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actually redeemed. The fact that a windfall to the plaintiff's lawyers effectively deters these abusive tactics.

These are just CAFA's highlights. It is a complex statute, and no doubt it will be interpreted by courts over the coming years. Regardless of how some of its more intricate provisions are interpreted, CAFA should allow some businesses peace of mind that the chance of a nationwide class action in a far away state is now much less likely.