



U.S. CHAMBER
Institute for Legal Reform

Unstable Foundation

*Our Broken Class Action System
and How to Fix It*

.....
OCTOBER 2017





U.S. CHAMBER
Institute for Legal Reform

An Affiliate of the U.S. Chamber of Commerce

© U.S. Chamber Institute for Legal Reform, October 2017. All rights reserved.

This publication, or part thereof, may not be reproduced in any form without the written permission of the U.S. Chamber Institute for Legal Reform. Forward requests for permission to reprint to: Reprint Permission Office, U.S. Chamber Institute for Legal Reform, 1615 H Street, N.W., Washington, D.C. 20062-2000 (202.463.5724).

Table of Contents

Executive Summary and Introduction	1
Class Actions Do Not Benefit Class Members	3
Most Class Actions Provide Nothing to Absent Class Members	3
Settled Cases Deliver Benefits to Only a Handful of Class Members	4
Cases are Designed and Litigated to Benefit Plaintiffs’ Lawyers	6
Plaintiffs’ Lawyers Design Class Actions First, Find Plaintiffs Later	6
The Inherent Conflict Between Plaintiffs’ Lawyers and the Class, and Lack of Effective Oversight	8
Class Action Settlements Disproportionately Benefit Class Counsel and Demonstrate the Harmful Consequences of the System’s Flaws	10
The Class Action System Does Not Deter Future Wrongdoing	15
Injunctive Relief in Class Action Settlements Provides Little Specific Deterrence	15
The Class Action System is Not a Source of General Deterrence	17
Similar Abuses of Securities Class Actions Led Congress to Enact The PSLRA	22
The FICALA Legislation Before Congress Addresses Well-Documented Class Action Abuses	23
Protecting Class Members Against Abuse by Class Counsel	23
Combating Incentives to File Non-Meritorious Cases	26
Conclusion	29

Executive Summary and Introduction

Our current class action system was created more than half a century ago. It has drifted far from its intended purpose. Class actions are supposed to provide compensation to class members and deter wrongful conduct. But all too often, they fail at both tasks.

First, every recent study has found that the overwhelming majority of class members receive little or no benefit from these cases. Most class actions are dismissed by a court or dropped by plaintiffs without obtaining a class settlement. Even when class actions are settled, the percentage of class members who actually receive a benefit is miniscule. The reality is that very few potential class members ever see a dime from class actions supposedly brought on their behalf.

Second, class actions are poorly suited to achieve their stated aim of deterring wrongful conduct. Socially beneficial deterrence occurs when a decision maker believes that choosing lawful conduct will avoid significant costs and penalties—the decision maker then has an incentive to err on the side of acting lawfully. Because

virtually every class action in which the class is certified is settled with no judicial assessment of the underlying merits, however, the message to decision makers is that class action payments are simply an unavoidable cost of doing business, no matter what steps a company takes to comply with the law. Rather than having a beneficial effect, the class action device threatens to impose litigation costs and force settlement regardless of a company's choices, thereby harming society by deterring lawful, productive conduct.

Moreover, the class action system labors under an inherent conflict between the interests of the lawyers who bring these cases and the interests of class members. Too many cases are filed based on the ease with which a settlement may be extracted—with little or no focus on

“ [T]he class action system labors under an inherent conflict between the interests of the lawyers who bring these cases and the interests of class members. ”

whether there is serious consumer harm. And too many cases are settled with illusory benefits to class members and large fees for lawyers. Recent court challenges to proposed settlements have illuminated the prevalence of these abusive practices.

There are solutions. More than twenty years ago, Congress recognized and addressed many of these problems in the context

of securities class actions by enacting the Private Securities Litigation Reform Act.¹ Intervention by Congress in other substantive areas is now urgently needed to ensure that class actions fulfill their intended purposes rather than serving as vehicles for unjustified and abusive lawsuits.

“ Intervention by Congress in other substantive areas is now urgently needed to ensure that class actions fulfill their intended purposes rather than serving as vehicles for unjustified and abusive lawsuits. ”

Class Actions Do Not Benefit Class Members

Most Class Actions Provide Nothing to Absent Class Members

Clear evidence demonstrates that the vast majority of class actions today provide absolutely nothing to absent class members. In the very small percentage of class actions that settle on a class-wide basis, few class members file claims—and only small amounts are received by those who do file.

A number of recent studies have examined the outcomes of class actions and every one found that the overwhelming majority of cases filed as putative class actions provide no benefit at all to absent class members:

- The Consumer Financial Protection Bureau (CFPB) found that, of its sample of 562 cases, eighty-seven percent of resolved class actions resulted in no benefit to absent class members. These cases were either dismissed by the court or settled with the named plaintiff only.²
- A study conducted in 2013 by Mayer Brown on behalf of the U.S. Chamber Institute for Legal Reform (ILR) found that approximately sixty-six percent of resolved cases were dismissed on the merits or voluntarily terminated by the named plaintiff.³

- An empirical study conducted by a law school professor found that sixty to eighty percent of class actions under consumer protection statutes did not lead to any recovery for the class.⁴

Indeed, even a recent study portrayed as defending class actions reported that eighty percent of the cases yielded nothing for the absent class members.⁵

The lack of benefit to class members is only part of the story. Each of these cases imposes substantial costs on the parties sued, including the fees of defense lawyers and the costs of discovery if the lawsuit survives a motion to dismiss.⁶ These costs are inevitably passed on to customers, shareholders, or other innocent parties.

“ A number of recent studies have examined the outcomes of class actions and every one found that the overwhelming majority of cases filed as putative class actions provide no benefit at all to absent class members. ”

When a lawsuit is meritorious, imposing such costs can be justified by reference to the legal wrong suffered by the plaintiff. But the fact that the overwhelming majority of class action cases cost substantial amounts to litigate and consume significant judicial resources, but yield nothing for class members, must be considered in assessing the costs and benefits of the class action system.

That is especially true because other types of cases return benefits to plaintiffs at a much higher rate. For example, individual civil cases settle much more frequently than class actions—an average of sixty-seven percent settle according to one study⁷—or five times as frequently as class actions, based on the Consumer Financial Protection Bureau’s study.

Class actions thus impose huge, unjustified costs compared to other types of litigation, in a large proportion of cases that produce no benefits for class members. Those costs, which benefit no one other than lawyers, are a significant indicator of an unhealthy system.

Settled Cases Deliver Benefits to Only a Handful of Class Members

Virtually every class action case in which the class is certified ends in a settlement—final determinations on the merits are incredibly rare. The benefits to class members from these cases are largely illusory, as most class action settlements do not involve automatic distribution of settlement payments to absent class members. Settlements routinely require a class member to submit a claim form himself or herself to receive any settlement payment.

“ Publicly disclosing that few class members obtained the benefits of a settlement could undermine the settlement or cast doubt on the entire class action system. ”

Because class action settlements are implemented under court authority, one might expect that information about the distribution of these settlements would be filed with the court and available to the public. Yet that almost never happens. Once a settlement is agreed upon and approved, the plaintiffs’ counsel, the defendant, and even the court have an interest in keeping the settlement intact. Publicly disclosing that few class members obtained the benefits of a settlement could undermine the settlement or cast doubt on the entire class action system. The general rule is that settlement distribution results are rarely made public.

But the distribution information that has been disclosed all supports the same conclusion: the overwhelming majority of class members do not file claims to obtain payment from these settlement funds. For example:

- The Consumer Financial Protection Bureau’s study reported a “weighted average claims rate” of four percent for cases in which information was available.⁸

- ILR’s study, which found that (in the handful of cases where statistics were available, and excluding one outlier case involving individual claims worth, on average, over \$2.5 million) the claims rates were minuscule: 0.000006%, 0.33%, 1.5%, 9.66%, and 12%.⁹
- In one 2012 class action, a payment-card processor settled a lawsuit arising out of a breach of its computer systems. The class consisted of over 100 million cardholders, but despite what the court called “a vigorous notice campaign,” only eleven people filed valid claims—a claims rate of less than one millionth of one percent.¹⁰
- A video game maker settled a lawsuit brought by plaintiffs who purchased a video game that could be modified by third-party software to display sexual content. The class consisted of some 10 million purchasers of the game, but despite a notice campaign that led to more than 100,000 hits on the settlement fund’s website, only 2,676 class members filed claims—a minuscule claims rate of less than one thousandth of one percent.¹¹
- One federal court observed that “‘claims made’ settlements regularly yield response rates of 10 percent or less.”¹²
- A claims administrator filed a declaration in federal court stating that “consumer class action settlements with little or no direct mail notice will almost always have a claims rate of

less than one percent (1%).”¹³ Its analysis of such cases found that “[t]he claims rate ... ranged between .002% and 9.378%, with a median rate of .023%.”¹⁴

Indeed, one defender of class actions candidly acknowledges that “the class action is not known for its success at delivering compensation to class members: sometimes it does it well ... but, in the run-of-the-mill case, only a small percentage of victims are made whole.”¹⁵

The available evidence thus demonstrates that even in the small fraction of class actions that settle on a class-wide basis, most class members receive no benefit because they do not file claims to receive a settlement payment. A recent empirical study explains that “[a]lthough 60 percent of the total monetary award may be available to class members, in reality, they typically receive less than 9 percent of the total.” The author concluded that class actions “clearly do not achieve their compensatory goals ... Instead, the costs ... are passed on to consumers in the form of higher prices, lower product quality, and reduced innovation.”¹⁶

As one scholar put it, it is highly questionable whether the small compensatory awards that *some* class members *sometimes* receive “are worth the bother”¹⁷ of adjudicating these lengthy and massive cases (many of which will never lead to class-wide relief), paying plaintiffs’ lawyers a substantial cut of the recoveries, and going through the costly and laborious process of distributing settlement payments to the few class members that request them.

Cases are Designed and Litigated to Benefit Plaintiffs' Lawyers

The lack of compensation for consumers, even in cases that are settled, contrasts sharply with the benefits reaped by plaintiffs' lawyers. This dichotomy is no surprise: these cases are as a practical matter originated by plaintiffs' lawyers who then seek plaintiffs with standing to pursue the claims. The provisions for overseeing whether plaintiffs' lawyers are acting in the best interests of absent class members are limited, to say the least.

Plaintiffs' Lawyers Design Class Actions First, Find Plaintiffs Later

Professor Martin Redish has recognized that “[u]nlike the overwhelming majority of traditional individualized or aggregative litigation, the attorneys representing a plaintiff class are invariably the starting and driving forces in the creation of the class and the bringing of the suit.”¹⁸ Most class actions today are created not by injured consumers seeking redress but by opportunistic plaintiffs' lawyers looking to recover substantial amounts in attorneys' fees.

Professor John Coffee has reached the same conclusion, explaining that in large damages class actions, “[r]ather than the ‘principal’ hiring the ‘agent,’ the reverse often occurs[,] with the attorney finding the client after the attorney first researches and prepares the action.”¹⁹

“Most class actions today are created not by injured consumers seeking redress but by opportunistic plaintiffs' lawyers looking to recover substantial amounts in attorneys' fees.”

A *New York Times* story, profiling one plaintiffs' law firm focused on suing technology companies, explains that the law firm maintains an “investigative team, which consists of three lawyers and a computer analyst. The group's job, to put it plainly, is to find ways to sue companies.”²⁰

An expert on the class action system observes that “no sooner does any product defect or consumer issue emerge than attorneys file multiple, repetitive class actions across the country.”²¹ In order to move with sufficient speed, plaintiffs’ lawyers frequently recruit plaintiffs for their class action, rather than waiting for potential class members to come to them.

For example, in one class action against 5-Hour Energy highlighted recently in *Forbes*, the lead plaintiff admitted in a deposition that “she had been recruited to serve as a plaintiff by her cousin, who worked for a Texas lawyer [whom plaintiffs’ counsel] knew; had purchased two bottles of 5-Hour Energy specifically to sue the manufacturer; had never complained to the company or sought a refund; and had signed a backdated retainer agreement with [plaintiffs’ counsel] the week before the deposition in order to comply with California law, months after she’d lent her name to his lawsuit.”²²

Plaintiffs’ lawyers may make improper payments to potential plaintiffs under the table in order to get them to serve as lead plaintiff.²³ Or they may work with “professional plaintiff[s]”—clients who have “appeared in literally hundreds of other [class] actions”—specifically for the purpose of ginning up claims.²⁴ (One such

plaintiff filed at least 31 Telephone Consumer Protection Act suits in New Jersey federal court).²⁵ And failing these options, plaintiffs’ lawyers may just recruit a relative or friend or even an employee of the law firm. In one consumer class action, for example, the lead plaintiff was the lead plaintiff’s attorney’s father-in-law—an arrangement that the court decried as marked by a “grave conflict of interest” and “palpable impropriety.”²⁶ In another case, a plaintiffs’ firm was disqualified from representing a putative class because the named plaintiff was a lawyer at the firm. The trial court had found that during a two-year period, the firm had filed ten class actions in which “an attorney from [the firm] or a relative of one of the attorneys was the named plaintiff.”²⁷

The huge percentage of class members who choose not to participate in settlements—even though funds are available for the taking—shows that consumers viewed the “injury” claimed in the class action as irrelevant or minor, or found the potential settlement payment not worth their time. Either indicates that the class action did not provide a benefit that consumers found valuable—which is perhaps the best evidence that consumers themselves do not view this litigation as advancing their interests, but rather that these cases are framed principally with lawyers’ interests in mind.

“ The huge percentage of class members who choose not to participate in settlements—even though funds are available for the taking—shows that consumers viewed the ‘injury’ claimed in the class action as irrelevant or minor, or found the potential settlement payment not worth their time. ”

In sum, plaintiffs' lawyers have taken control of the consumer class action mechanism and turned it into a big "business that uses the threat of expensive litigation and potentially ruinous damages to pry billions of dollars in settlements and hundreds of millions of dollars in legal fees from businesses each year."²⁸ Thus, as Judge Richard Posner has observed, in most class actions, "the lawyers for the class, rather than the clients, have all the initiative and are close to being the real parties in interest."²⁹

The Inherent Conflict Between Plaintiffs' Lawyers and the Class, and Lack of Effective Oversight

Professor Redish has cataloged the "stark differences in the attorney-client relationship between the modern class action and more traditional forms of litigation":

- "There will often exist potential conflicts of interest between class attorneys and their clients inherent in the class action procedure, which would never arise in the traditional attorney-client relationship."
- "As both practical and legal matters, class attorneys stand to gain more financially than any one of their clients. In the overwhelming majority of traditional situations..., this will never even be a possibility."

- "A class is capable of existing, and class attorneys may receive substantial fees, even though relatively few of the absent class members will ever be compensated when the class proceeding is successful. In the traditional attorney-client context, in contrast, it is all but inconceivable that this will occur."³⁰

Courts have recognized the "acute conflict of interest between class counsel, whose pecuniary interest is in their fees, and class members, whose pecuniary interest is in the award to the class."³¹ As another academic analyst has observed, "attorney fee incentives [in class actions] are so substantial as to invite unethical professional conduct or old-fashioned champerty."³²

For example, plaintiffs' lawyers may agree to settle a case early, before they invest too much time in the case—"even if the settlement is significantly less than what might be expected if counsel pursued the case more vigorously."³³ Class action plaintiffs' lawyers have an especially strong interest in seeking this kind of settlement because their business models are often based on taking on a high volume of cases and "achiev[ing] a less-than-optimal resolution for class members in each of these suits" rather than pursuing any one suit too aggressively.³⁴ In short, as one commentator bluntly puts it, in at least some situations "the class-action lawyer is not above dropping his case in exchange for a fee."³⁵

Plaintiffs' lawyers may also inflate the notional dollar amount of a settlement while agreeing to settlement terms that provide that any money left unclaimed is distributed to charities, often those selected by the plaintiffs' lawyers.³⁶ Class counsel's fees are based on the total amount distributed, so they have no incentive to oppose procedures that make it difficult for class members to submit claims.

Finally, plaintiffs' lawyers may seek to have defendants enter into "clear sailing" agreements, which commit defendants to not object to fee awards up to a certain ceiling. Plaintiffs' lawyers highly value these agreements because they provide assurance that the plaintiffs' lawyers will receive a hefty fee without opposition from defense counsel.³⁷ But as Judge Newman of the Second Circuit has noted, there is a great "likelihood that plaintiffs' counsel, in obtaining the [clear-sailing agreement], will *bargain away something of value to the plaintiff class.*"³⁸ The usual function of these agreements, therefore, is to enrich class counsel at the expense of their clients.

Because of these unique aspects of class actions, Professor Redish is correct in concluding that "there is no way to rely on the traditional ethical and personal bonds between attorney and client to avoid or deter the harms that an attorney can cause to her highly vulnerable clients." Therefore, "if the modern class action is to assure that those who represent the victims of legal harm do so fully, fairly, and adequately, we must conceptualize that procedure in some manner other than as a form of traditional litigation."³⁹

“ *Class counsel’s fees are based on the total amount distributed, so they have no incentive to oppose procedures that make it difficult for class members to submit claims.* ”

The class action system does not include mechanisms to prevent these abuses. Named plaintiffs and absent class members do very little to monitor or supervise class counsel once the lawsuit is underway, for two reasons:

FIRST

Class members generally do not expect a sufficient recovery to justify the cost of monitoring the litigation. If class members stand to gain, at most, a few dollars from a class action, it simply is not economically rational for them to spend time and energy trying to make sure that class counsel is acting in their best interests.⁴⁰

SECOND

"[E]ven if [class] plaintiffs wanted to monitor the litigation, they would experience severe difficulties in doing so because they are often entirely unaware that the litigation is pending until after a settlement has been reached."⁴¹

“ Named plaintiffs and absent class members do very little to monitor or supervise class counsel once the lawsuit is underway. ”

Nor do the procedural protections in the class action system succeed in preventing settlements that are unfair to class members. Rule 23 requires the judge to review any proposed class action settlement for fairness,⁴² and individual class members are permitted to file objections to settlements that they think are inequitable.⁴³ But in practice, these mechanisms may provide weak protection for class members—as Professor Redish has said, “it is easy to recognize how feeble these mechanisms are in preventing the abuses that plague” class actions.⁴⁴

One scholar explains that “the hydraulic pressure for courts to approve settlements routinely leads courts to rubber stamp ... class action settlement agreements.”⁴⁵ And “[t]his is especially true when the defendant and the class attorneys present a united front to the court as the result of a settlement class action. As a totally passive institution, the court counts on the litigants to provide all relevant information, and where both sides are already in agreement, neither party has the incentive to provide the counter to the pro-certification

argument.”⁴⁶ Although objectors have had some success in overturning dubious settlements, objectors are not present in many cases, and objections are also frequently dismissed by courts.⁴⁷

Class Action Settlements Disproportionately Benefit Class Counsel and Demonstrate the Harmful Consequences of the System’s Flaws

The structural flaws in the class action system have important and disturbing real world consequences. Settlement benefits often are skewed in favor of plaintiffs’ lawyers, with class members receiving illusory benefits.

LAWYERS RECEIVE MORE THAN THE CLASS

In many class actions the plaintiffs’ lawyers receive more than the class itself: a RAND Corporation study found that this happened in three out of ten class actions studied.⁴⁸ Examples of such class actions still remain commonplace:

- In a class action alleging that the defendants improperly interfered with the medical care of injured employees, the defendants (who denied wrongdoing) were required to make an \$8 million fund available to compensate more than 13,500 class members. But class counsel received over \$4.5 million out of the \$8 million—more than 55 percent of the fund.⁴⁹

- In a class action against the National Football League, retired players alleged that the League was using their names and likenesses without compensation. The class action was settled, but the named plaintiffs themselves opted to object to the settlement because it provided no direct payout to the retired players. Instead, money would be diverted to a new charitable group—while the class counsel received more than \$7.7 million in fees and expenses.⁵⁰
- In a class action against the makers of Duracell batteries alleging that they were misleadingly labeled “longest-lasting,” class members filed claims for just \$344,000 worth of coupons for new batteries, while the plaintiffs’ lawyers were awarded more than \$5.6 million in fees.⁵¹
- In a class action against a pizza company under the Telephone Consumer Protection Act, the settlement created a common fund of \$9.75 million, but at the time of the fairness hearing, only 770 claims had been filed on the settlement website, which was “less than one percent of the total class.”⁵² By contrast, the attorneys received \$2.535 million in fees and costs.⁵³
- In an antitrust class action against toy retailers and baby product manufacturers, the Third Circuit vacated the district court’s order approving a class action settlement consisting of a substantial cy pres award.⁵⁴ The defendant agreed to pay \$35.5 million into a settlement fund, with any unclaimed funds being paid to specified charities. The trial court approved the settlement, which included payment of \$14 million in attorneys’ fees and expenses. In the wake of the district court’s approval of the class settlement, it became clear that only \$3 million of the settlement fund was actually claimed by class members, leaving \$18.5 million to be paid to charities.⁵⁵ In other words, the attorneys received nearly five times the amount that actually ended up in the pockets of their clients. The Third Circuit reversed the class settlement.
- In a class action involving health clubs, the court granted final approval of a settlement despite the fact that only 617 class members had requested settlement checks totaling approximately \$7,200.⁵⁶ Class counsel collected \$200,000 in fees.⁵⁷
- In a class action alleging that certain Conair hair dryers were defective, the plaintiffs’ attorneys secured approval of a settlement that provided no direct notice of the class action to class members, making it unlikely that most would ever hear about the settlement. (Even the defendant called the notice plan “woefully insufficient” before the settlement was reached.) Those who did hear about the settlement would have to print out a claim form, fill it out and include two different serial numbers, and mail it in; no online claims were allowed. A claimant who actually managed to run this gantlet would receive only \$5 or a replacement hair dryer. Meanwhile, the plaintiffs’ lawyers collected more than \$1.1 million.⁵⁸

“ [I]n an increasing number of cases, ‘no effort [is] made to pay even a portion of the settlement fund to the absent class members’ before the cy pres distribution occurs.”

- In a class action against Subway alleging that its “Footlong” sandwiches were not really 12 inches long, the plaintiffs’ lawyers agreed to a settlement in which class members received nothing apart from Subway’s promising to take certain quality control measures, while the plaintiffs’ lawyers got more than \$500,000 in fees.⁵⁹ The Seventh Circuit threw out the settlement, finding the relief for consumers was “utterly worthless” because there was still the “same small chance” of a consumer receiving a sandwich shorter than 12 inches that there was before.⁶⁰ The court held that the class action “should have been dismissed out of hand” because it sought only “worthless benefits for the class” and “enriche[d] only class counsel.”⁶¹
- In a class action against a gym company for allegedly charging improper fees, class members ultimately received about \$1.6 million in cash, whereas the plaintiffs’ lawyers received \$2.39 million in fees and costs.⁶²

In the CFPB study, total attorneys’ fees add up to \$424 million for 419 cases, which equals an average of more than \$1 million per case.⁶³ Based on the Bureau’s study, the average fee paid to plaintiffs’ lawyers—as a percentage of the announced settlement (not the smaller amount actually distributed to class members)—was 41%, with a median of 46%. It is not possible, based on the data released by the Bureau, to calculate the legal fees’ relationship to the amounts actually distributed to class members, but it obviously is a much larger percentage.

CY PRES

Payments to charities—rather than class members—are used to inflate the value of settlements. These so-called “cy pres” settlements provide that the settlement fund is distributed not to injured class members but to a third party, such as a charity. Cy pres remedies originated as a means of distributing settlement money that “remain[ed] unclaimed following efforts to pay class members their respective shares”—the idea being to “serve the interests of the absent class members ‘as near’ as possible.”⁶⁴ But in an increasing number of cases, “no effort [is] made to pay even a portion of the settlement fund to the absent class members” before the cy pres distribution occurs.⁶⁵

A recent class action against Facebook illustrates the serious fairness issues raised by cy pres settlements. In 2008, plaintiffs brought a class action against Facebook under federal and state privacy laws seeking to represent millions of Facebook users, alleging that Facebook had violated their privacy by collecting information about users’ activity on other websites.⁶⁶ The case ultimately settled for \$9.5 million.⁶⁷

“ In other words, ‘the class attorneys’ financial interest will be wholly divorced from their efforts to compensate individual class members.’ ”

\$3 million went to pay the plaintiffs’ lawyers’ fees and the named plaintiffs’ incentive payments. Then, “because distributing the [remaining] \$6.5 million among the large number of class members would result in too small an award per person to bother,” that money was given to a new charitable foundation “that would help fund organizations dedicated to educating the public about online privacy.”⁶⁸

In dissent from the decision upholding this settlement on appeal, one appellate judge summed up the problems with this settlement perfectly, explaining that “class members get no compensation at all. They do not get one cent ... Their purported lawyers get millions of dollars ...”⁶⁹

The Supreme Court ultimately decided not to review the *Facebook* case, but Chief Justice Roberts wrote a statement on the denial of review noting that there are several “fundamental concerns surrounding the use of [cy pres] remedies in class action litigation, including *when, if ever*, such relief should be considered,” and suggesting that “[i]n a suitable case, [the] Court may need to clarify the limits on the use of such remedies.”⁷⁰

Plaintiffs’ lawyers are only too happy to agree to cy pres distributions rather than cash relief for class members because class counsel’s fee “is typically determined as a fraction of the settlement fund regardless of the portion that is actually claimed by absent class members”—which means that their “interest in maximizing fees is satisfied regardless of whether the settlement funds are paid to class members or distributed cy pres.”⁷¹ In other words, “the class attorneys’ financial interest will be wholly divorced from their efforts to compensate individual class members.”⁷²

Absent class members lose out, however, because as one court has put it, there is not even any “indirect benefit to the class from the defendant’s giving the [settlement] money to *someone else*.”⁷³ These class members’ claims are simply extinguished—without their receiving any benefit in exchange.

THE ILLUSION OF RELIEF

Class actions had been plagued by coupon settlements in which class members didn’t get cash, but rather coupons or vouchers toward the purchase of products or services from the very company that class members had been suing.

For example, in one class action, students who attended certain youth conferences around the 2009 presidential inauguration sued the company that organized the conferences, alleging that they did not receive all the services they were promised. When the class action settled, the student class members received only vouchers—to be used toward future conferences hosted by the same company they alleged had broken its promises. Meanwhile, the plaintiffs’ lawyers got nearly \$1.5 million in fees.⁷⁴

Similarly, in another class action involving claims that a brokerage company breached its fiduciary duty to its clients, the class members who were still account holders with the brokerage got no direct compensation in the settlement, receiving only vouchers toward future brokerage fees. Class counsel, however, got \$21 million in fees.⁷⁵

As a congressional report on the Class Action Fairness Act (CAFA) recognized, most coupon settlements are “valueless” to consumers; “the real winners in [a coupon] settlement are the lawyers who sued the company, who will be paid in cash, not coupons.”⁷⁶ Congress sought to correct the problem of coupon settlements when it enacted CAFA, by imposing additional restrictions to make it harder for coupon settlements to win federal court approval.⁷⁷

But as one commentator has observed, “parties have circumvented CAFA’s intent to eliminate notorious coupon settlements,” in part, “by creating surrogate remedies that mimic coupons but are not so designated.”⁷⁸ Thus, settlements that provide plaintiffs with only “the illusion of relief” remain alive and well despite Congress’s attempt at reform.

“As a congressional report on the Class Action Fairness Act (CAFA) recognized, most coupon settlements are ‘valueless’ to consumers; ‘the real winners in [a coupon] settlement are the lawyers who sued the company, who will be paid in cash, not coupons.’”

The Class Action System Does Not Deter Future Wrongdoing

Critics of the current class action system point to the absence of any substantial compensation for class members, the control by plaintiffs' lawyers of the class action process, and the unchecked conflict of interest between class members and class counsel. Defenders of the current system argue that these points should all be disregarded, because class actions supposedly deter unlawful conduct and provide potential defendants with a powerful incentive to act lawfully.

This deterrence argument may sound good, but there is a big difference between theory and practice. The reality of class actions shows that there is no credible basis for a deterrence justification. Deterrence-theory academics divide deterrence into two types—"specific" and "general" and class actions provide neither.

Injunctive Relief in Class Action Settlements Provides Little Specific Deterrence

Specific deterrence occurs when a lawsuit expressly prohibits future wrongdoing, typically through an injunction. Defenders of the current system argue that the injunctive relief included in class action settlements does just that, but their arguments fall short.

“ *The reality of class actions shows that there is no credible basis for a deterrence justification.* ”

To begin with, injunctive relief is rare. As already explained, eighty percent or more of class actions are dismissed or terminated with no relief for the class. One study found that one quarter of settled class actions provided injunctive relief—which means that only five percent of all class actions have any form of injunctive relief.⁸¹ That is a very small result for a large investment in litigation costs.

“ There is, accordingly, a strong likelihood that any injunctive relief included in a settlement will be window-dressing, neither necessary to stop wrongful conduct nor significantly altering the defendant’s practices.”

And, because these cases are settled, there has been no determination that the injunctive relief actually prevents illegal conduct. Indeed, in the real world of class action settlements, injunctive relief agreeable to the defendant is often included as a way to reduce the defendant’s monetary payment, to justify a “claims made” settlement in which unclaimed funds are returned to the defendant, and/or to enable the plaintiffs’ counsel to claim a larger attorneys’ fee award than that amount justified by the monetary settlement alone.

There is, accordingly, a strong likelihood that any injunctive relief included in a settlement will be window-dressing, neither necessary to stop wrongful conduct nor significantly altering the defendant’s practices.

The Seventh Circuit identified that problem in the settlement in the *Subway* case, concluding that the injunctive relief provisions “d[id] not benefit the class in any meaningful way.”⁸²

Professor Brian Fitzpatrick, a defender of the current system, acknowledged the argument that “the behavior-modification provisions in class action settlements are cosmetic and do not impose real restrictions on corporations.” But he claimed personal involvement in “dozens of class action cases” in which the provisions were not “toothless” and asserted that critics have failed to identify a sufficient number of cases with only “cosmetic” relief.⁸³

But his assertion runs right into the *Subway* case. And that example does not stand alone:

- In a class action involving nutritional supplements, the defendant agreed to minor changes to its labeling—and then only for a period of 30 months, after which it could use its old labels again. The Seventh Circuit rejected the proposed settlement, finding that the “trivial” changes to the label were “unlikely to influence or inform consumers,” and were too “meager” to justify class counsel’s nearly \$2 million fee.⁸⁴
- In a class action regarding allegations that Facebook scanned URLs included in Facebook messages, Facebook agreed to add a 22-word sentence to one of its help pages, while class counsel collected \$3.9 million in fees.⁸⁵
- A class action alleging that the Metropolitan Museum of Art misled patrons about whether its “recommended” price of admission was mandatory ended in a settlement requiring the museum to use the word “suggested” on signs and ticket kiosks instead. Class counsel pocketed \$350,000 in attorneys’ fees.⁸⁶

- In a class action alleging that Coca-Cola implied that its product “vitaminwater” was healthy, class counsel got \$1.2 million in fees, while the settlement only required tweaks to certain Coca-Cola marketing practices.⁸⁷
- In a class action against Pampers, the Sixth Circuit decried the behavioral relief in the settlement—adding a sentence to the defendant’s packaging—as “illusory” and insufficient to justify class counsel’s hefty \$2.73 million fee.⁸⁸

The argument that class action settlements provide a substantial amount of specific deterrence thus conflicts with the actual results in the overwhelming majority of class actions as well as the fundamental incentive structure governing class action settlements.

The Class Action System is Not a Source of General Deterrence

The claim that the threat of class action liability generally deters wrongful conduct is just as flawed.

“An indisputable characteristic of the class action system, however, is that it does not sort cases based on their underlying merits. For that reason, it cannot provide general deterrence.”

The theory of general deterrence holds that when a decision maker believes that choosing lawful conduct will avoid significant costs and penalties that would attach to wrongful behavior, and make any wrongdoing uneconomic, the decision maker has an incentive to act lawfully.⁸⁹ Critical to socially beneficial deterrence, therefore, is the notion that the company is likely to pay if it acts wrongfully but not if it acts lawfully.

An indisputable characteristic of the class action system, however, is that it does not sort cases based on their underlying merits. For that reason, it cannot provide general deterrence. The threat of class action litigation instead harms society by deterring lawful, productive conduct.

Class actions that survive a motion to dismiss and class certification are virtually always settled.⁹⁰ The Supreme Court, lower courts, and commentators uniformly recognize that a defendant is likely to settle even non-meritorious class action claims.

For example, as Justice Ginsburg has put it, “[e]ven in the mine-run case, a class action can result in potentially ruinous liability. A court’s decision to certify a class accordingly places pressure on the defendant to settle even unmeritorious claims.”⁹¹ Chief Judge Wood of the Seventh Circuit Court of Appeals similarly characterizes class certification as “in effect, the whole case.”⁹² An academic expert agrees: class action defendants “may capitulate to meritless or unsubstantiated claims rather than incur substantial ongoing litigation expenses with the risk of an adverse jury decision.”⁹³

“The deterrence argument therefore ‘inadequately accounts for the realities of how class litigation evolves.’”

Given the paucity of class actions decided after a trial on the merits, the only reasonable conclusion is that these observations are correct, and that defendants in fact decide to settle without regard to whether the underlying claim is meritorious. That is why virtually every case that reaches this stage ends in a settlement.

Certainly there is no reason to believe that every class action filed is meritorious. As explained above, plaintiffs’ lawyers have no interest in enforcing consumer protection laws; their interest is in maximizing their own income. Thus, they do not choose which class actions to bring based on the merits of the class claims; they look for cases in which a complaint can be written that will survive a motion to dismiss and the class certification motion granted—with little regard to the outcome of a trial on the merits.

Moreover, the denial of a motion to dismiss and certification of a class do not mean that the underlying claim is meritorious. The former determines only that, assuming the allegations of the complaint are true, the plaintiffs can prevail. Critical questions—accuracy of statements, materiality, deception, negligence, etc.—remain to be determined at trial. And the class certification decision is wholly unrelated to the merits, turning instead on the presence or absence of common issues, manageability, the adequacy of class representatives and class counsel, and other similar questions relating to management of the proceeding.

Finally, there is no reason to believe that settled cases are necessarily meritorious. As already discussed, courts have long recognized that defendants agree to pay settlements in class actions even when they have a strong chance of prevailing on the merits—either because the costs of defense (which will not be recovered even if the defendant prevails) are higher than the costs of settling or because of the downside risk of a large adverse verdict (which would produce adverse publicity, brand damage, and additional litigation costs, including the costs of an appeal bond).

In sum, the class action system fails to distinguish between meritorious and non-meritorious claims—and results in settlements for all cases that survive a motion to dismiss and class certification.

For that reason, even a law-abiding company faces the very real possibility that it will be sued in a class action and be forced to pay millions of dollars to settle the case rather than seek vindication in a risky trial. The deterrence argument therefore “inadequately accounts for the realities of how class litigation evolves.” If the court certifies the class, “defendants usually bargain for the most financially advantageous settlement terms [T]he combination of ... settlement factors (cheap settlement funds, no punitive damages, no admission of liability, and reversionary or cy pres provisions), significantly undercut the deterrence rationale for class litigation.”⁹⁴

The threat of class action liability therefore is rationally viewed as unrelated to whether a company conformed its actions to governing law—and therefore unavoidable. And that means that class actions cannot deter wrongful actions: a decision maker cannot conclude that avoiding wrongful acts will avoid class action liability, because class action liability can result whether the company’s actions are lawful or unlawful.

Corporate defendants “view class judgments and settlements as a cost of doing business, subsidized by insurers or passed along to consumers.”⁹⁵ And they must take account of those costs even when they believe their actions comply fully with the relevant legal standards. The effect of the class action system, therefore, is to force decision makers to build into any plans an additional cost for a possible class action settlement, which has the harmful effect of deterring socially beneficial actions by making them more expensive.

Defenders of the current system, such as Professor Fitzpatrick, dispute this conclusion, but their arguments miss the mark.

Fitzpatrick describes deterrence theory generally—“that the threat of a lawsuit deters misbehavior.”⁹⁶ He adds that “[i]f the misbehavior benefits the corporation less than the harm it inflicts on others, then the corporation will rationally choose not to engage in the misconduct.”⁹⁷

In that way, Fitzpatrick avoids even mentioning the essential requirement for socially-beneficial deterrence: that the real-world operation of the litigation

system must single out wrongful conduct for greater costs than lawful conduct, and that decision makers must believe that it operates that way. Otherwise, wrongful conduct will not be deterred.

Fitzpatrick simply assumes that “the threat of a lawsuit deters misbehavior” without addressing the unique nature of class action litigation and the reasons why that is not in fact true, thus his entire analysis rests on a false premise. His claim that class actions can be justified on the basis of deterrence therefore must be rejected.⁹⁸

Fitzpatrick goes on to contend that several types of empirical evidence support his assertion that class actions deter wrongful conduct. But, this analysis is fatally flawed:

FIRST

Fitzpatrick relies first on a survey of executives at Fortune 500 companies, asserting it shows that “corporations can anticipate” the filing of class actions.⁹⁹ But that does not mean that corporations believe that they will be sued, or will have to pay, only if they do something wrong. In fact, the survey responses revealed that “a large margin of error exists for each of the relevant variables that inform the deterrence formula” and that, even when a prior suit has been filed involving the same claimed conduct, “optimal deterrence is unlikely to be achieved” because of companies’ inability to predict litigation or liability.¹⁰⁰

The survey data failed to confirm any of the author’s three hypotheses regarding the existence of litigation-based deterrence, and he acknowledges that “corporations are not successfully avoiding future litigation by

“ In sum, there is neither a theoretical rationale nor empirical evidence demonstrating that class actions have a beneficial deterrent effect. ”

relying on information learned from prior suits”—in other words, there is no proof of a beneficial deterrent effect.¹⁰¹ (It also is worth noting that, while Fitzpatrick says that “many” executives responded to the survey, in fact only 49 did—less than one-tenth of the sample solicited.¹⁰²)

SECOND

Fitzpatrick invokes a study of the deterrent effect of government enforcement actions targeting price fixing.¹⁰³ The study concluded that deterrence occurred when government enforcement actions were followed by the filing of private class actions targeting the same conduct. But that study says absolutely nothing about the deterrent effect of class actions standing alone. Indeed, the litigation calculus is completely different when class action plaintiffs can rely on a criminal conviction to establish the defendant’s liability—an extremely rare occurrence generally, and virtually unknown outside the price-fixing context.

The study notes that that private actions, moreover, were “possible” but “uncommon without a preceding criminal case”—

demonstrating that the deterrent effect flowed from the presence of the prior government enforcement action, not from the class action by itself.¹⁰⁴ That provides no evidence whatever about the deterrent effect of class actions *without* a prior, successful government enforcement action.

THIRD

Fitzpatrick cites a series of studies on disclosures by public companies,¹⁰⁵ which basically show that voluntary disclosure increases with higher litigation risk from securities class actions. Of course, the conclusion that additional disclosures might limit litigation risk does not mean that failing to make those disclosures violated the law—companies might be seeking to limit the risk of unjustified liability. In addition, securities class actions are an area where Congress instituted reforms to address class action abuse.¹⁰⁶ Even if there is a deterrent effect, that conclusion is not transferable to other types of class actions that have not been reformed by Congress.

FINALLY

Fitzpatrick cites studies relating to the deterrent effect of non-class action litigation.¹⁰⁷ But individual cases do not have the characteristics of class actions—in particular, the absence of determinations on the merits. Those studies accordingly are irrelevant in assessing the deterrent effects of class actions.

In sum, there is neither a theoretical rationale nor empirical evidence demonstrating that class actions have a beneficial deterrent effect.

Moreover, class actions cannot be defended on the theory that they uncover actual wrongdoing. Commentators have explained in detail that class actions rarely uncover wrongdoing that has not already come to light. Rather, “class action lawyers predominantly file ‘copycat’ or ‘coattail’ lawsuits that follow on the heels of government investigations.”¹⁰⁸ One commentator has called this a “recurring pattern ... under which [class actions] simply piggyback[] on the efforts of public agencies.”¹⁰⁹ Indeed, on some occasions, government agencies such as the FTC have filed *amicus* briefs arguing that class counsel’s fees should be reduced because the class action built off of an FTC investigation.¹¹⁰

The reason why “class action lawyers prefer to follow—rather than to lead,” as one study of this issue explained, is that “those lawyers prefer ‘no research’ lawsuits that appear likely (from the investigation itself) to yield lucrative settlements with only a minimal investment of time and money. In contrast, government lawyers, who by definition are not driven by profits, tend to be willing to spend more time doing the factual and legal research needed to decide what kinds of cases should be brought, not simply to increase revenue, but to further the public good.”¹¹¹

Similar Abuses of Securities Class Actions Led Congress to Enact The PSLRA

The documented abuses of class actions and the harmful consequences that result closely resemble the facts before Congress when it enacted the Private Securities Litigation Reform Act (PSLRA) in 1995. Congress then found:

- The securities class action system was controlled by lawyers, not class members. “Under the current system, the initiative for filing 10b–5 suits comes almost entirely from the lawyers, not from genuine investors. Lawyers typically rely on repeat, or ‘professional,’ plaintiffs who, because they own a token number of shares in many companies, regularly lend their names to lawsuits. Even worse, investors in the class usually have great difficulty exercising any meaningful direction over the case brought on their behalf. The lawyers can decide when to sue and when to settle, based largely on their own financial interests, not the interests of their purported clients.”¹¹²
- Class members recovered little, even in meritorious cases. “[P]laintiffs’ counsel in many instances litigate with a view toward ensuring payment for their services without sufficient regard

to whether their clients are receiving adequate compensation in light of evidence of wrongdoing” with the result that class members ended up receiving only “pennies on the dollar in damages” and “counsel in securities class actions receive a disproportionate share of the settlement award.”¹¹³

- “[T]he abuse of the discovery process to impose costs is so burdensome that it is often economical for the victimized party to settle.”¹¹⁴
- “The proliferation of ‘professional’ plaintiffs has made it particularly easy for lawyers to find individuals willing to play the role of wronged investor for purposes of filing a class action lawsuit. Professional plaintiffs often are motivated by the payment of a ‘bonus’ far in excess of their share of any recovery.”¹¹⁵

Congressional action is urgently needed to address the ongoing abuse of class actions outside the securities context, which is producing the very same adverse consequences that led Congress to enact the PSLRA in 1995.

The FICALA Legislation Before Congress Addresses Well-Documented Class Action Abuses

Congress is now considering legislation that would begin to address the problems in the class action system. The Fairness in Class Action Litigation Act (FICALA) was passed by the House of Representatives in March 2017 and is now pending before the Senate.¹¹⁶ Its provisions address a number of the problems discussed in this paper.

The House Judiciary Committee report accompanying the legislation found that “far too many” class actions are “initiated by opportunistic lawyers, and litigated primarily for the benefit of those lawyers, with any actual victims being used as a means of garnering vast fee awards.”¹¹⁷ The costs of these cases are borne in the first instance by “businesses—small and large—that are sued in these unjustified cases, forced to pay their own legal fees and, eventually, to pay settlements coerced even in meritless cases.”¹¹⁸ But, the Committee explained, ultimately these costs are paid by consumers, workers, and investors, throughout the

economy—because the diversion of hundreds of millions of dollars away from productive purposes, as well as the time and attention of entrepreneurs, means prices are higher, new products are not brought to market, and new jobs are not created.¹¹⁹

The Committee concluded that “[t]wo types of reforms are needed to fix our broken litigation system: protections against the abuse of consumers by unscrupulous lawyers, and protections against the filing of unjustified claims and other abusive litigation practices.”¹²⁰

Protecting Class Members Against Abuse by Class Counsel

A number of FICALA’s provisions are intended to prevent abusive practices by the lawyers who file class actions and to ensure that class actions are filed and litigated to further the interests of class members, not of lawyers.

“The Committee concluded that [t]wo types of reforms are needed to fix our broken litigation system: protections against the abuse of consumers by unscrupulous lawyers, and protections against the filing of unjustified claims and other abusive litigation practices.”

DETERMINING TYPE AND SCOPE OF INJURY

As the House Judiciary Committee explained, the class action system should be structured so that “those who are the most injured receive the most compensation” — “[n]o one should be forced into a class action with other uninjured or minimally injured members, only to see their own compensation reduced.”¹²¹ Today, however, “unscrupulous lawyers ... artificially inflate the size of a class to extort a larger settlement value for themselves, and in the process increase the prices of goods and services for everyone.”¹²²

These lawyers file lawsuits, for example, against a company that sells a washing machine. Some very small percentage of those washing machines do not work the way they are supposed to, but the vast majority of them do. The lawyers file a class action lawsuit that includes everyone who ever purchased a washing machine from the company, even the large number of people who are completely satisfied with their purchase. When these lawyers lump injured or non-comparably injured people into the same class action lawsuit, the limited resources of the parties are wastefully spent weeding through hundreds of thousands of class members in order to find and compensate those with actual or significant injuries.¹²³

To stop this practice, FICALA requires judges to determine, as part of the class certification process, that “each proposed class member suffered the same type and scope of injury as the named class representative or representatives”¹²⁴ — codifying in statute a requirement that should already be clear from existing court decisions.¹²⁵

“That is why few class members bother to collect settlement payments—‘they do not feel injured by the supposedly wrongful conduct in the first place.’”

COMBATING LAWYER-DRIVEN LITIGATION

“Lawsuits are supposed to be initiated by truly injured plaintiffs seeking redress, not invented by lawyers who hunt for a plaintiff to assert a supposed injury made up by the lawyer.”¹²⁶ The Judiciary Committee concluded that “[i]n too many cases, opportunistic lawyers come up with an idea for a lawsuit and then search for a person who has bought the product—or they send a relative or employee to buy the product—so they’ll have someone who can sue on behalf of a proposed class of all other buyers. No product purchaser has actually complained or feels cheated.”¹²⁷ That is why few class members bother to collect settlement payments—“they do not feel injured by the supposedly wrongful conduct in the first place.”¹²⁸

To combat lawyer-driven litigation, FICALA requires disclosure in the complaint of the way that the named plaintiffs became involved in the litigation and prohibits lawyers from representing the class when the named plaintiff is a relative of, employee of, or otherwise has a preexisting relationship with the plaintiffs’ counsel.¹²⁹

IDENTIFYING CLASS MEMBERS

The purpose of class actions is to provide class members with a way to redress meritorious claims. The ability to identify class members and deliver to them any compensation awarded in the class action is therefore a critical requirement for every class action. Cases that do nothing more than get lawyers lots of money—“without delivering relief to class members”—are not consistent with the legitimate purposes of class actions.”¹³⁰

Too often today there is no administrable method for identifying class members and reaching them to deliver compensation. While many courts apply this requirement today,¹³¹ some do not.

FICALA therefore requires that a court determine, as part of the class certification process, that there is an administratively feasible mechanism for identifying who is in the class and “for distributing directly to a substantial majority of class members any monetary relief secured for the class.”¹³²

BASING FEES ON ACTUAL DISTRIBUTION

FICALA addresses the pervasive problem that fee awards to plaintiffs’ lawyers are not based on benefits actually delivered to class members and often exceed the total amount received by class members. As already discussed,¹³³ these lawyers rely on cy pres and other techniques to inflate the settlement “benefits” and justify a higher fee. The House Judiciary Committee concluded, “[t]he class action system is supposed to primarily benefit victims, not lawyers. Class action lawyers should only get paid after the victims get paid” and lawyers should not get more than class members.¹³⁴

“ ‘Class action lawyers should only get paid after the victims get paid’ and lawyers should not get more than class members. ”

FICALA therefore limits lawyers’ fee awards to “a reasonable percentage of any payments directly distributed to and received by class members” or a reasonable percentage of the value of the equitable relief benefiting class members.¹³⁵

REPORTING SETTLEMENT DISTRIBUTION

As explained above, little information is available about the distribution of class action settlements—the number of class members that file claims and how much money they receive, and the number of class members that don’t bother to seek part of the settlement.¹³⁶ “Because lawyers and federal courts are not required to make public exactly how class action settlement funds are distributed, to whom, and in what amounts, the public and Congress are largely in the dark regarding the extent of potential abuses.”¹³⁷

FICALA requires submission of this information to the Federal Judicial Center and Administrative Office of the U.S. Courts, which are required to compile the information into annual reports.¹³⁸ As the Judiciary Committee explained, “[T]his would let the public and Congress know what comes out of its class action litigation

system. Transparency in this regard would be particularly helpful in exposing the extent of the abuse of so-called cy pres awards.”¹³⁹

DISCLOSING THIRD-PARTY LITIGATION FUNDING

Another important development in class actions is the increasing frequency with which the filing and litigation of class actions is supported financially by third-party litigation funders. The House Judiciary Committee identified a number of instances in which agreements between plaintiffs’ counsel and a third-party funder “inappropriately vest the funder with substantial control over key litigation decisions, undermining the primacy of the attorney-client relationship.”¹⁴⁰ For example, contractual provisions that promise the funder a percentage of the total recovery and give the funder a veto over class counsel. But third-party funders “do not represent the interests of the class members. They’re in the lawsuits solely to make money for themselves, possibly including taking money away from the victims’ own recovery.”¹⁴¹

The U.S. District Court for the Northern District of California has responded to these developments by requiring automatic disclosure of third-party funding of cases filed as class actions.¹⁴² FICALA extends that requirement nationwide,¹⁴³ which would “allow the district court to take appropriate steps to protect class members’ interests.”¹⁴⁴

Combating Incentives to File Non-Meritorious Cases

Today, as discussed above, defendants have an economic incentive to settle even unjustified class action claims because of the costs and potential downside risks of

litigation.¹⁴⁵ Plaintiffs’ lawyers therefore have little incentive to focus their efforts on meritorious claims: any claim that could survive a motion to dismiss and class certification will yield a settlement and a large attorneys’ fee. FICALA addresses this problem by enacting reforms that will deter the filing of unjustified claims by reducing the incentives to settle such cases.

AUTHORIZING APPEAL OF CERTIFICATION DECISIONS

The class certification decision is the critical stage of a class action. As already discussed, courts, commentators and participants in the class action system all recognize that cases virtually always settle if certification is granted.¹⁴⁶ Correct class certification determinations are therefore critical to the proper functioning of the system.

Recognizing that fact, the Federal Rules of Civil Procedure permit appeals of decisions to grant or deny class certification, but only if the court of appeals allows the appeal to go forward.¹⁴⁷ Unfortunately, courts are increasingly reluctant to permit these appeals. Moreover, the various federal courts of appeals appear to be applying different standards: the rates for granting appeals varies from 5.4% to 46.4%.

“ [T]he various federal courts of appeals appear to be applying different standards: the rates for granting appeals varies from 5.4% to 46.4% .”

When an appeal is allowed, however, one third of district court rulings are reversed, indicating that appeals are correcting a significant number of erroneous decisions.

FICALA addresses this problem by authorizing appeals of all decisions granting or denying class certification.¹⁴⁸ As the Judiciary Committee explained, “[p]romoting correctness and uniformity of class certification decisions is essential given the critical role of certification in these lawsuits. And the differing treatment based on geographic location is something Congress should remedy.”¹⁴⁹

PRESERVING CLASS CERTIFICATION STANDARDS

The class action procedure is an exception to the usual rules of litigation, intended to be used only when issues common to all class members predominate over individualized issues that must be resolved on a plaintiff-by-plaintiff basis. Plaintiffs’ lawyers are increasingly attempting to circumvent class certification standards by—in the words of the Judiciary Committee—seeking “certification of so-called ‘issues classes’ in which a single legal or factual issue may be determined for the whole class even though the claims are dominated by individualized issues that require case-by-case evaluations.”¹⁵⁰

Federal Rule of Civil Procedure 23(c)(4) states that “[w]hen appropriate, an action may be brought or maintained as a class action with respect to particular issues,” but the U.S. Court of Appeals for the Fifth Circuit has properly rejected the argument that this provision overrides the detailed requirements for class certification—

“[r]eading [Rule] 23(c)(4) as allowing a court to sever issues ... would eviscerate the predominance requirement of [Rule] 23(b)(3); the result would be automatic certification in every case where there is a common issue, a result that could not have been intended.”¹⁵¹

Permitting this result provides little benefit for class members, each of whom is still obligated to prove his or her case individually. The real-world consequence would be to enable plaintiffs’ counsel to coerce a settlement by wielding a decision on one issue that could be erroneous or not determinative of the merits of the claims (because it relates to only a single issue), but that is sufficiently insulated from appellate review. This tactic forces the defendant to capitulate, even if the defendant retains strong arguments that the claims are meritless.

To prevent this unjustified and unfair result, which would provide new incentives to bring non-meritorious claims, FICALA provides that a class may only be certified if the entire claim satisfies the standards for class certification.¹⁵²

TOLLING DISCOVERY

Discovery costs are another major source of the pressure to settle unjustified cases. The price tag for discovery is extraordinarily large—it “imposes huge costs on litigants—particularly because of the astronomical costs associated with the discovery of electronic information, such as emails.”¹⁵³ Most importantly, “these costs are asymmetric: while defendants typically are subject to gigantic discovery costs, because

they are large organizations possessing large amounts of data, plaintiffs have little information in their possession and therefore are subject to a relatively small financial burden during the discovery process.”¹⁵⁴

The Judiciary Committee concluded that “[u]nscrupulous plaintiffs’ attorneys” can use the cost of discovery “as a weapon to coerce settlement of claims, regardless of their merit,” so defendants may decide to settle a case rather than incurring these huge costs.¹⁵⁵ The Supreme Court agrees: “the threat of discovery expense will push cost-conscious defendants to settle even anemic cases.”¹⁵⁶ For example, plaintiffs’ attorneys can serve massive discovery requests that force defendants to spend \$10 million to collect the requested documents. A rational decision for that defendant is to settle the case for millions of dollars, even if, four months later, the court grants the motion to dismiss, finding the class claims to be totally without merit. This result is inevitable because, without a stay

in discovery, the defendants will in the meantime have been required to spend all or part of the \$10 million complying with the discovery requests—ultimately, for no legitimate reason.¹⁵⁷

Congress recognized this problem in the Private Securities Litigation Reform Act, requiring that—in the absence of extraordinary circumstances—discovery should not be permitted until after the district court finds a complaint legally sufficient by denying the defendant’s motion to dismiss.¹⁵⁸ FICALA extends that rule to all types of class actions.¹⁵⁹

By taking significant steps to protect class members against overreaching plaintiffs’ lawyers and providing incentives for plaintiffs’ lawyers to focus their efforts on meritorious claims, FICALA would go a long way toward eliminating the flaws in today’s class action system.

Conclusion

A half-century after the birth of the modern class action, the evidence is clear: the current system suffers from pervasive, serious problems. The overwhelming majority of class actions deliver little or no benefit to the class members on whose behalf they are ostensibly filed. Class actions are almost never litigated on the merits. Only a miniscule percentage of class members receive payments from class action settlements, and those payments are often tiny. As a result, the class action system fails to provide compensation to allegedly aggrieved class members.

Moreover, the reality of class actions prevents these lawsuits from fulfilling their intended purpose of deterring wrongful corporate behavior. That is because companies have no reason to believe that they will be spared the heavy costs of class actions when they act lawfully. With virtually every case that survives a motion to dismiss and class certification ending in settlement—with no assessment of the underlying merits—the costs of class actions do not fall more heavily on wrongdoers.

In addition, these cases are largely lawyer-driven, and plaintiffs' lawyers are motivated to file class actions based on their perception of whether a lawsuit is likely to result in a settlement that offers a healthy attorneys' fee. Those incentives, of course, have little to do with whether the underlying

claims are meritorious. Accordingly, corporations correctly view class action lawsuits as a cost of doing business that is untethered to whether a company has in fact engaged in wrongful conduct.

FICALA would alleviate some of these abuses of the class action device. The legislation includes significant reforms to protect class members against overreaching by plaintiffs' lawyers and creates new incentives for plaintiffs' lawyers to focus their efforts on meritorious claims. It also calls for more information about class action settlements, so everyone will have the information needed to assess their utility. Enacting FICALA will take meaningful steps toward reducing or eliminating the flaws in today's class action system.

Endnotes

- 1 Congress addressed the problem of plaintiffs' lawyers filing nationwide cases in state court to circumvent the protections for class members provided by federal law, enacting the Securities Litigation Uniform Standards Act and the Class Action Fairness Act.
- 2 Consumer Fin. Protection Bureau, *Arbitration Study: Report to Congress 2015*, at section 6, page 37, <http://www.consumerfinance.gov/data-research/research-reports/arbitration-study-report-to-congress-2015/> ("*CFPB Study*").
- 3 Mayer Brown LLP, *Do Class Actions Benefit Class Members? An Empirical Analysis of Class Actions* (Dec. 11, 2013) ("*Chamber Study*"), <http://www.mayerbrown.com/files/uploads/Documents/PDFs/2013/December/DoClassActionsBenefitClassMembers.pdf>.
- 4 Jason Scott Johnston, *High Cost, Little Compensation, No Harm to Deter: New Evidence on Class Actions Under Federal Consumer Protection Statutes* Univ. of Va. Sch. of L., L. & Econ. Research Paper Series 2016-9, (May 2016), <http://ssrn.com/abstract=2777618>.
- 5 See Andrew Pincus, *Assessing 'The Value of Class Actions,'* Law360 (Aug. 22, 2017), <https://www.law360.com/foodbeverage/articles/956215/assessing-the-value-of-class-actions->, discussing Gary Mason, *The Proper Measure of the Value of Class Actions*, Law360 (Aug. 16, 2017), <https://www.law360.com/articles/954049/the-proper-measure-of-the-value-of-class-actions>.
- 6 See, e.g., Br. of Intel Corp. as Amicus Curiae at 8, *Wal-Mart Stores, Inc. v. Dukes*, 564 U.S. 338 (2011) (No. 10-277), 2011 WL 288897 (citing the "steep costs associated with litigating class action[s]" and explaining that "[p]retrial discovery . . . is especially costly in class actions, and tends to cost defendants far more than plaintiffs"); Linda Mullenix, *Ending Class Actions as We Know Them: Rethinking the American Class Action*, 64 Emory L.J. 399, 416 (2014) (discussing the "substantial ongoing litigation expenses" for class action defendants).
- 7 Theodore Eisenberg and Charlotte Lanvers, *What is the Settlement Rate and Why Should We Care?* 6 J. Empirical Legal Studies 111 (2009).
- 8 *CFPB Study* at section 8, page 30.
- 9 *Chamber Study* at 7 & n.20.
- 10 *In re Heartland Payment Sys., Inc. Customer Data Sec. Breach Litig.*, 851 F. Supp. 2d 1040, 1047 (S.D. Tex. 2012).
- 11 Defs.' Mem. In Support of Pls.' Mot. for Final Approval of Class Action Settlement at 3, *In re Grand Theft Auto Video Game Consumer Litigation (No. II)*, No. 06-md-1739 (S.D.N.Y. May 27, 2008), ECF No. 124.
- 12 *Sylvester v. CIGNA Corp.*, 369 F. Supp. 2d 34, 52 (D. Me. 2005).
- 13 Declaration of Deborah McComb at 2, *Poertner v. The Gillette Co.*, No. 6:12-CV-00803-GAP-DAB (M.D. Fla. Apr. 22, 2014) ECF No. 156.

- 14 *Id.*
- 15 Brian T. Fitzpatrick, *Do Class Actions Deter Wrongdoing?*, at 1 (Aug. 9, 2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3020282.
- 16 Joanna Shepherd, *An Empirical Study of No-Injury Class Actions* 5 (Emory Univ. Sch. of L. Legal Studies Research Paper Series No. 16-402 (Feb. 1, 2016), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2726905).
- 17 Mullenix, *supra* note 6, at 422.
- 18 Martin H. Redish, *Rethinking the Theory of the Class Action: The Risks and Rewards of Capitalistic Socialism in the Litigation Process*, 64 Emory L.J. 451, 460 (2014).
- 19 John C. Coffee, Jr., *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Class Action*, 54 U. Chi. L. Rev. 877, 885 (1987) (emphasis added).
- 20 Conor Dougherty, *Jay Edelson, the Class-Action Lawyer Who May Be Tech's Least Friended Man*, N.Y. Times (Apr. 4, 2015), https://www.nytimes.com/2015/04/05/technology/unpopular-in-silicon-valley.html?_r=0.
- 21 Mullenix, *supra* note 6, at 435.
- 22 Daniel Fisher, *Collapse Of 5-Hour Energy Case Reveals The Secrets Of Class Action Lawyers*, Forbes (Nov. 17, 2015), <http://www.forbes.com/sites/danielfisher/2015/11/17/collapse-of-5-hour-energy-case-reveals-secrets/#3ba849971aa4>.
- 23 Such payments continue to be made in non-security class actions; the Private Securities Litigation Reform Act (15 U.S.C. §§ 77z-1(a)(4), 78u-4(a)(4)) limits any such payments to reasonable costs and expenses, although there have been violations of that limitation. *E.g.*, *Swift v. First USA Bank*, 1999 WL 1212561, at *6 (N.D. Ill. Dec. 15, 1999) (refusing to certify class because plaintiffs' attorneys had initially agreed to pay lead plaintiff's husband a portion of their attorneys' fees as a "finders fee"); Press Release, United States Dep't of Justice, Milberg Weiss Law Firm, Two Senior Partners Indicted in Secret Kickback Scheme Involving Named Plaintiffs in Class-Action Lawsuits (May 18, 2006), <http://online.wsj.com/public/resources/documents/milbergpress05182006.pdf> (announcing 20-count indictment against Milberg Weiss and two of its senior partners).
- 24 John C. Coffee, Jr., *Rethinking the Class Action: A Policy Primer on Reform*, 62 Ind. L.J. 625, 632 (1987).
- 25 John O'Brien, *Phoney Lawsuits: Comcast Fighting for Access to 'Professional' Plaintiff's Prior Testimony*, Forbes, May 31, 2017, <https://www.forbes.com/sites/legalnewsline/2017/05/31/phoney-lawsuits-comcast-fighting-for-access-to-professional-plaintiffs-prior-testimony/#d6ba291727c7>.
- 26 *Eubank v. Pella Corp.*, 753 F.3d 718, 722, 724 (7th Cir. 2014).
- 27 *Apple Computer, Inc. v. Superior Court*, 126 Cal. App. 4th 1253, 1262 (2005).
- 28 Fisher, *supra* note 22.
- 29 *Mars Steel Corp. v. Cont'l Ill. Nat'l Bank & Tr. Co. of Chi.*, 834 F.2d 677, 678 (7th Cir. 1987).
- 30 Redish, *supra* note 18, at 460-61.

- 31 *Pearson v. NBTY, Inc.*, 772 F.3d 778, 787 (7th Cir. 2014); *see also* Coffee, *supra* note 19, at 883.
- 32 Mullenix, *supra* note 6, at 434.
- 33 Michael E. Solimine & Christine Oliver Hines, *Deciding to Decide: Class Action Certification and Interlocutory Review by the United States Courts of Appeals under Rule 23(f)*, 41 Wm. & Mary L. Rev. 1531, 1545 (2000).
- 34 Deborah R. Hensler et al., *Class Action Dilemmas: Pursuing Public Goals for Private Gain* 79 (1999).
- 35 Daniel Fisher, *Study Shows Consumer Class-Action Lawyers Earn Millions, Clients Little*, Forbes, Dec. 11, 2013, <http://www.forbes.com/sites/danielfisher/2013/12/11/with-consumer-class-actions-lawyers-are-mostly-paid-to-do-nothing/>.
- 36 *See* pages 12-13, *supra*.
- 37 *See* William D. Henderson, *Clear Sailing Agreements: A Special Form of Collusion in Class Action Settlements*, 77 Tul. L. Rev. 813, 814, 827 (2003).
- 38 *Malchman v. Davis*, 761 F.2d 893, 908 (2d Cir. 1985) (emphasis added) (Newman, J., concurring).
- 39 Redish, *supra* note 18, at 461.
- 40 Coffee, *supra* note 24, at 633; *see also, e.g.*, Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. Chi. L. Rev. 1, 19-20 (1991).
- 41 Macey & Miller, *supra* note 40, at 20.
- 42 *See* Fed. R. Civ. P. 23(e)(2) ("If the [settlement] proposal would bind class members, the court may approve it only after a hearing and on finding that it is fair, reasonable, and adequate.").
- 43 *See id.* 23(e)(5).
- 44 Redish, *supra* note 18, at 466.
- 45 Mullenix, *supra* note 6, at 430.
- 46 Redish, *supra* note 18, at 466.
- 47 Mullenix, *supra* note 6, at 435.
- 48 Deborah R. Hensler et al., *Class Action Dilemmas: Pursuing Public Goals for Private Gain (Executive Summary)* 21 (1999), http://www.rand.org/content/dam/rand/pubs/monograph_reports/2005/MR969.1.pdf.
- 49 *See*, Plaintiffs' Unopposed Motion for Order Preliminarily Approving Class Action Settlement at 8, *Gianzero v. Wal-Mart Stores, Inc.*, No. 09-cv-00656 (D. Colo. Nov. 21, 2011), ECF No. 464 (settlement providing that plaintiffs' attorneys would receive more than \$4.5 million of the \$8 million settlement fund).
- 50 Alison Frankel, *Retired NFL stars reject settlement of their own licensing class action*, Reuters, Mar. 25, 2013, <http://blogs.reuters.com/alison-frankel/2013/03/25/retired-nfl-stars-reject-settlement-of-their-own-licensing-class-action/> (settlement awarding plaintiffs' lawyers \$7.7 million while class members received no direct compensation).
- 51 Pet. for a Writ of Certiorari at 16, *Frank v. Poertner*, No. 15-765 (U.S. Dec. 11, 2015), 2015 WL 8765974.

- 52 *Spillman v. RPM Pizza, LLC*, 2013 WL 2286076, at *2 (M.D. La. May 23, 2013).
- 53 Final Distribution Order ¶ 7, *Spillman v. RPM Pizza, LLC*, No. 3:10-cv-00349-BAJ-SCR (M.D. La. July 29, 2013), ECF No 245.
- 54 *In re Baby Prod. Antitrust Litig.*, 708 F.3d 163 (3d Cir. 2013).
- 55 *Id.* at 169-70.
- 56 *Martina v. L.A. Fitness Int'l, LLC*, 2013 WL 5567157, at *2 (D.N.J. Oct. 8, 2013).
- 57 *Id.* at *9.
- 58 Competitive Enter. Inst., *Conair Class Action Settlement Sets Our Hair on Fire*, Feb. 14, 2017, <https://cei.org/blog/conair-class-action-settlement-sets-our-hair-fire>.
- 59 Adam Schulman, *Subway Footlong Sandwich Settlement Now on Appeal*, Competitive Enter. Inst., Mar. 30, 2016, <https://cei.org/blog/subway-footlong-sandwich-settlement-now-appeal>.
- 60 *In re Subway Footlong Sandwich Mktg. & Sales Practices Litig.*, 869 F.3d 551, 557 (7th Cir. 2017).
- 61 *Id.*
- 62 *See Gascho v. Global Fitness Holdings, LLC*, 822 F.3d 269, 274 (6th Cir. 2016).
- 63 *CFPB Study* at section 8, page 33.
- 64 *See Rhonda Wasserman, Cy Pres in Class Action Settlements*, 88 S. Cal. L. Rev. 97, 100 (2014); *see also* Martin H. Redish et al., *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 Fla. L. Rev. 617, 631 (2010).
- 65 Wasserman, *supra* note 64, at 100.
- 66 *See Marek v. Lane*, 134 S. Ct. 8, 8 (2013) (Roberts, C.J., respecting the denial of certiorari).
- 67 This was only a fraction of the potential damages claimed, reflecting the weakness of the claims. In approving the settlement, the district judge noted that the class's claims rested on "novel legal theories" and that the class's "expectation of . . . recovery [was] speculative at best." *Lane v. Facebook, Inc.*, 2010 WL 9013059, at *4-5 (N.D. Cal. Mar. 17, 2010).
- 68 *Marek*, 134 S. Ct. at 9.
- 69 *Lane v. Facebook, Inc.*, 696 F.3d 811, 835 (9th Cir. 2012) (Kleinfeld, J., dissenting).
- 70 *Marek*, 134 S. Ct. at 9 (emphasis added).
- 71 Wasserman, *supra* note 64, at 101, 123.
- 72 Redish *et al.*, *supra* note 64, at 650.
- 73 *Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 784 (7th Cir. 2004) (emphasis added).
- 74 *See Radosti v. Envision EMI, LLC*, 717 F. Supp. 2d 37, 46-48 (D.D.C. 2010).
- 75 *See Bachman v. A.G. Edwards, Inc.*, 344 S.W.3d 260, 264-65 (Mo. Ct. App. 2011).
- 76 S. Rep. 109-14, at 30 (2005) (quotations omitted).
- 77 *See* 28 U.S.C. § 1711 note (criticizing class actions in which "counsel are awarded large fees, while leaving class members with coupons or other awards of little or no value"); *id.* § 1712 (measures addressing coupon settlements).

- 78 Mullenix, *supra* note 6, at 430 (collecting sources offering advice to defendants seeking to implement coupon settlements post-CAFA).
- 79 David Segal, *A Little Walmart Gift Card for You, a Big Payout for Lawyers*, N.Y. Times, Jan. 30, 2016, <http://www.nytimes.com/2016/01/31/your-money/a-little-walmart-gift-card-for-you-a-big-payout-for-lawyers.html>.
- 80 Rob Berger, *The CFPB Declares War on Arbitration*, Forbes, Oct. 18, 2015, <http://www.forbes.com/sites/robertberger/2015/10/18/the-cfpb-declares-war-on-arbitration>.
- 81 Fitzpatrick, *supra* note 15, at 2.
- 82 *Subway*, 869 F.3d at 557.
- 83 Fitzpatrick, *supra* note 15, at 3.
- 84 *Pearson*, 772 F.3d at 787.
- 85 Competitive Enter. Inst., *Campbell v. Facebook, Inc.*, <https://cei.org/litigation/campbell-v-facebook-inc>.
- 86 Competitive Enter. Inst., *Metropolitan Museum of Art Class Action Ends in Counter-Productive Settlement*, June 30, 2017, <https://cei.org/blog/metropolitan-museum-art-class-action-ends-counter-productive-settlement>.
- 87 See Final Approval Order and Judgment of Dismissal with Prejudice, *Volz v. Coca Cola Co.*, No. 1:10-cv-00879 (S.D. Ohio Mar. 30, 2015), ECF No. 70.
- 88 *In re Dry Max Pampers Litig.*, 724 F.3d 713, 721 (6th Cir. 2013).
- 89 For an analogous discussion of how a failure to distinguish adequately between the culpable and the innocent dilutes the deterrent effect of sanctions in the criminal-law context, see A. Mitchell Polinsky & Steven Shavell, *The Theory of Public Enforcement of Law*, in 1 Handbook of Law and Economics 403, 427-29 (A. Mitchell Polinsky & Steven Shavell eds., 2007).
- 90 See page 4, *supra*.
- 91 *Shady Grove Orthopedic Associates, P.A. v. Allstate Ins. Co.*, 559 U.S. 393, 445 n.3 (2010) (Ginsburg, J., dissenting) (citation omitted); see also *Coopers & Lybrand v. Livesay*, 437 U.S. 463, 476 (1978) (“Certification of a large class may so increase the defendant’s potential damages liability and litigation costs that he may find it economically prudent to settle and to abandon a meritorious defense.”); *In re Lorazepam & Clorazepate Antitrust Litig.*, 289 F.3d 98, 102 (D.C. Cir. 2002) (“[T]he grant of class status can put substantial pressure on the defendant to settle independent of the merits of the plaintiffs’ claims.”); *In re Rhone-Poulenc Rorer Inc.*, 51 F.3d 1293, 1298 (7th Cir. 1995) (noting that a defendant facing \$25 billion in potential liability “may not wish to roll these dice. That is putting it mildly. They will be under intense pressure to settle”).
- 92 Hon. Diane Wood, Circuit Judge, *Remarks at the FTC Workshop: Protecting Consumer Interests in Class Actions* (Sept. 13-14, 2004), in Panel 2: Tools for Ensuring that Settlements are “Fair, Reasonable, and Adequate,” 18 Geo. J. Legal Ethics 1197, 1213 (2005).
- 93 Mullenix, *supra* note 6, at 416; Robert E. Litan, U.S. Chamber Inst. for Legal Reform, *Through Their Eyes: How Foreign Investors View and React to the U.S. Legal System* 13 (Aug. 2007) (“[S]ome defendants can feel financially pressured to settle even if they have done nothing wrong, believing it not to be worth betting their companies on a subsequent mistaken jury verdict that can be difficult to overturn on an appeal.”); Henry J. Friendly, *Federal Jurisdiction: A General View* 120 (1973) (explaining the presence of “blackmail settlements” in class actions).

The pressure on defendants to settle class actions is magnified further in class actions brought under one of the many statutes that allow plaintiffs to recover a fixed dollar amount of “statutory damages” per alleged violation of the law, even if the plaintiffs suffered no actual harm from the alleged violations. Most statutory damages provisions are civil penalty provisions designed to make *individual cases* more attractive to prosecute. But as one scholar has noted, “when combined with the procedural device of the class action, aggregated statutory damages can result in absurd liability exposure in the hundreds of millions—or even billions—of dollars on behalf of a class whose actual damages are often nonexistent.” Sheila B. Scheuerman, *Due Process Forgotten: The Problem of Statutory Damages and Class Actions*, 74 Mo. L. Rev. 103, 104 (2009). Thus, as Justice Ginsburg has observed, “[w]hen representative plaintiffs seek statutory damages, pressure to settle may be heightened because a class action poses the risk of massive liability unmoored to actual injury.” *Shady Grove Orthopedic Associates*, 559 U.S. at 445 n.3 (Ginsburg, J., dissenting).

Finally, defendants also face pressure to settle because they bear a much greater share of the expenses of litigation and discovery. In a class action, the defendant is frequently the party who possesses the bulk of the relevant, discoverable information and bears the cost of producing it to the plaintiffs. The Supreme Court has recognized that the threat of this discovery expense, which can be considerable, produces unjustified settlements. See *Stoneridge Inv. Partners, LLC v. ScientificAtlanta, Inc.*, 552 U.S. 148, 163 (2008) (“[E]xtensive discovery and the potential

for uncertainty and disruption in a lawsuit allow plaintiffs with weak claims to extort settlements from innocent companies.”); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 559 (2007) (“[T]he threat of discovery expense will push cost-conscious defendants to settle even anemic cases.”).

- 94 Mullenix, *supra* note 6, at 420-21.
- 95 *Id.* at 415.
- 96 Fitzpatrick, *supra* note 15, at 4.
- 97 *Id.* at 5.
- 98 Fitzpatrick does address a different question—the risk that a company might not be able to predict whether its conduct would be found legal or illegal. He says “[t]here is no doubt that there is uncertainty in our system of justice” and that it is sometimes hard to predict” whether a company will lose a lawsuit. *Id.* at 10. But, he asserts, the company can hire lawyers to assess its conduct. Again, Fitzpatrick equates “being sued” with engaging in wrongdoing. As discussed in the text, there is no such equivalence.
- 99 *Id.* at 11-12 (citing Linda Sandstrom Simard, *A View From Within the Fortune 500: An Empirical Study of Negative Value Class Actions and Deterrence*, 47 Indiana L. Rev. 739 (2014)).
- 100 Simard, *supra* note 99, at 758, 759.
- 101 *Id.* at 772.
- 102 *Id.* at 756 n 76.

- 103 Fitzpatrick, *supra* note 15, at 14-15 (citing Michael Kent Block, Frederick Carl Nold, and Joseph Gregory Sidak, *The Deterrent Effect of Antitrust Enforcement*, 89 J. of Political Economy 429 (1981)).
- 104 Block *et al.*, *supra* note 103, at 440 n.33.
- 105 Fitzpatrick, *supra* note 15, at 16-17.
- 106 See page 22, *infra*.
- 107 Fitzpatrick, *supra* note 15, at 16-17.
- 108 John H. Beisner et al., *Class Action “Cops”: Public Servants or Private Entrepreneurs?*, 57 Stan. L. Rev. 1441, 1453 (2005) (emphasis added); see also, e.g., Howard M. Erichson, *Coattail Class Actions: Reflections on Microsoft, Tobacco, and the Mixing of Public and Private Lawyering in Mass Litigation*, 34 U.C. Davis L. Rev. 1, 2 (2000).
- 109 John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter Is Not Working*, 42 Md. L. Rev. 215, 222 (1983).
- 110 Beisner *et al.*, *supra* note 108, at 1453 n. 64 (citing Brief of Amicus Curiae The Federal Trade Commission, *In re First Databank Antitrust Litig.*, 209 F. Supp. 2d 96 (D.D.C. 2002) (No. 1:01CV00870), https://www.ftc.gov/sites/default/files/documents/amicus_briefs/re-first-databank-antitrust-litigation/firstdatabank.pdf; Brief of Amicus Curiae The Federal Trade Commission, *In re Buspirone Patent Litig.*, 185 F. Supp. 2d 340 (S.D.N.Y. 2002), https://www.ftc.gov/sites/default/files/documents/amicus_briefs/re-buspirone-antitrust-litigation/buspirone.pdf).
- 111 Beisner *et al.*, *supra* note 108, at 1453-54.
- Of course, some class actions are filed in the absence of government enforcement actions. But many class actions piggyback on *private* disclosures of wrongdoing, such as news reports. Once the wrongdoing is disclosed by reporters or others, the class action performs no disclosure function.
- And “[m]any class actions . . . are filed precisely *because* a state or federal regulatory agency has investigated an alleged problem and concluded that no punishment or remedial action is called for under the circumstances.” *Id.* at 1454 (emphasis added). Class action lawyers’ incentives, after all, differ from those of government agencies: they do not have “any concern about overdeterrence.” *Id.* Just “[t]he opposite is true: so long as the lawsuit appears likely to generate a settlement and accompanying attorneys’ fees, the class action lawyer’s incentive is to file it.” *Id.* Thus, it is unsurprising that there are many cases in which no government enforcement action is filed and yet a private class action was brought.
- 112 S. Rep. 104-98, at 6 (1995).
- 113 *Id.* at 6, 9, 12.
- 114 H. Rep.104-369, at 31 (1995); see also S. Rep. 104-98, at 14.
- 115 S. Rep. 104-98, at 10; see also H. Rep.104-369, at 32-33 (“Professional plaintiffs who own a nominal number of shares in a wide array of public companies permit lawyers readily to file abusive securities class action lawsuits. Floor debate in the Senate highlighted that many of the ‘world’s unluckiest investors’

- repeatedly appear as lead plaintiffs in securities class action lawsuits. These lead plaintiffs often receive compensation in the form of bounty payments or bonuses. The Conference Committee believes these practices have encouraged the filing of abusive cases.”).
- 116 See H.R. 985, 115th Cong., 1st Sess. (2017), <https://www.congress.gov/bill/115th-congress/house-bill/985>.
- 117 H.R. Rep. 115-25, at 3 (2017).
- 118 *Id.* at 3-4.
- 119 *Id.* at 4.
- 120 *Id.* at 4.
- 121 *Id.* at 16.
- 122 *Id.*
- 123 *Id.*
- 124 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1716).
- 125 H.R. Rep.115-25, at 17 & n.11.
- 126 *Id.* at 18.
- 127 *Id.*
- 128 *Id.*
- 129 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1717).
- 130 H.R. Rep.115-25, at 20.
- 131 *Carrera v. Bayer Corp.*, 727 F. 3d 300, 305, 306 (3d Cir. 2013) (“Many courts and commentators have recognized that an essential prerequisite of a class action, at least with respect to actions under Rule 23(b)(3), is that the class must be currently and readily ascertainable based on objective criteria.”).
- 132 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1718(a)).
- 133 See pages 12-13, *supra*.
- 134 H.R. Rep. 115-25, at 22.
- 135 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1718(b)).
- 136 See page 7, *supra*.
- 137 H.R. Rep.115-25, at 24.
- 138 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1719).
- 139 H.R. Rep.115-25, at 24.
- 140 *Id.* at 28.
- 141 *Id.* at 29.
- 142 Standing Order for All Judges of the U.S. District Court for the Northern District of California, ¶ 19 (Jan. 17, 2017), <https://www.cand.uscourts.gov/news/210>.
- 143 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1722).
- 144 H.R. Rep.115-25, at 29.
- 145 See page 3, *supra*.

- 146 See pages 17-18, *supra*.
- 147 Federal Rule of Civil Procedure 23(f).
- 148 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1723).
- 149 H.R. Rep.115-25, at 29.
- 150 *Id.* at 25.
- 151 *Castano v. American Tobacco Co.*, 84 F.3d 734, 745 n. 21 (5th Cir. 1996).
- 152 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1720).
- 153 H.R. Rep.115-25, at 26.
- 154 *Id.*
- 155 *Id.*
- 156 *Twombly*, 550 U.S. at 559.
- 157 H.R. Rep.115-25, at 27.
- 158 15 U.S.C. §§ 77z-1(b), 78u-4(b)(3(B & C)).
- 159 H.R. 985, § 103(a) (enacting 28 U.S.C. § 1720).



U.S. CHAMBER
Institute for Legal Reform

202.463.5724 main
202.463.5302 fax

1615 H Street, NW
Washington, DC 20062

instituteforlegalreform.com