

To Certify or Not: A Modest Proposal For Evaluating “Superiority” In The Presence Of Government Enforcement

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D. Bruce Hoffman
Deputy Director, Bureau of Competition, Federal Trade Commission¹

Much of the discussion concerning overlapping governmental enforcement and class actions has focused on two issues: (1) the attorneys’ fees sought by class counsel; and (2) the type and value of relief sought by class counsel in settlements. These issues are very important, but arise late in the day in the typical class action. An issue that arises much earlier – indeed, before the case assumes the mantle of a class action, with all of the benefits and costs attendant on that status – also merits attention: whether a class should be certified at all when the subject matter of the proposed class action is the target of government law enforcement.

This paper addresses that question by proposing a modest idea: that courts considering the certification of a class under Rule 23, or its state law equivalents, consider carefully the full implications of a pending or completed government enforcement action. The result of that consideration cannot be predicted in advance, as it will necessarily depend on the facts of the case as they exist at the time of the decision on certification. It may often be true that the governmental remedies will not be “complete” and that there will be added value to the class action. However, there will also be cases where the results achieved by state or federal enforcers will either provide full relief or a “superior... method ... for the fair and efficient adjudication of the controversy,” and in those cases, in the interests of justice and faithful to the command of Rule 23, the court should refuse to certify the class.

The Legal Background: Rule 23

Section c of Rule 23 requires that the court “at an early practicable time” determine “whether to certify the action as a class action.” We know from many cases that the court may certify the class only if all the requirements of section (a) and at least one subsection of section (b) have been met. The Reporter for the 1966 amendments to Rule 23 stated: “The new provision invites a

¹The views expressed are mine alone, and do not necessarily represent the views of the Federal Trade Commission or any Commissioner. I thank Paul Karlsson of the Bureau’s Office of Policy and Coordination for his assistance with this paper.

close look at the case before it is accepted as a class action” and the Supreme Court in *Amchem*² confirmed that a close look is indeed required. That close look should include a focus on any government litigation that also involves the matters raised in the proposed class complaint.

The majority of class actions are certified under Rule 23(b)(3), which, among other things, provides that a class is appropriate if common questions of law or fact predominate and if “a class action is superior to other available methods for the fair and efficient adjudication of the controversy.” Thus, Rule 23(b)(3) provides an explicit command that courts consider alternative methods of adjudicating the controversy before certifying a class, a command that should easily encompass considering government actions. Rule 23(b)(3) provides a nonexhaustive list of factors to be considered in this “superiority” inquiry³, including “the extent and nature of any litigation concerning the controversy already commenced by or against members of the class.” The text does not expressly mention any government litigation that may have been filed or contemplated, but it is no stretch at all to realize that government enforcement action can have any number of effects on the success and conduct of the possible class action, as well as (and most importantly) the resolution of the controversy underlying the matter.

Though case law explicitly recognizing the relevance of government enforcement to the 23(b)(3) certification decision is somewhat sparse, some courts have recognized the issue. For example, in *Kamm v. California City Development Co.*,⁴ the Attorney General and the Real Estate Commissioner of California brought an action against a land developer that led to offers of restitution and the establishment of a fund for the settlement of future disputes. The trial court dismissed a class action involving the same matters, and was upheld on appeal even though the “superior” remedy was administrative not judicial. The appellate court cited *Katz v. Carte Blanche* for the factors to be considered when weighing superiority:

"Superiority must be looked at from the point of view (1) of the judicial system, (2) of the potential class members, (3) of the present plaintiff, (4) of the attorneys for the litigants, (5) of the public at large and (6) of the defendant. The listing is not necessarily in order of importance of the respective interests. Superiority must also be looked at from the point of view of the issues."⁵

² *Amchem Products, Inc. v. George Windsor*, 521 U.S. 591, 615-16 (1997).

³ *Id.*

⁴ 509 F.2d 205 (9th Cir. 1975)

⁵ 509 F.2d at 212, *citing Katz v. Carte Blanche*, 496 F. 2d 747, 760 (3d Cir.1974)

Similarly, in *Patillo v. Schlesinger*⁶ a class action was held to be not superior when administrative proceedings were ongoing and would provide equal and perhaps greater relief. *Accord, Chin v. Chrysler Corp.*⁷

Under Rule 23(b)(3), the contrast between government and private enforcement perhaps most likely to present “superiority” issues is compensation. In the usual case, at the federal level at least, the government will have obtained or be seeking prospective relief and perhaps civil or criminal penalties. It is very rare for an FTC remedy to include monetary relief,⁸ although that result may be more likely at the state level. It is probably also the usual case that the private litigation will include or focus on a demand for monetary damages; indeed, that focus is a defining characteristic of Rule 23(b)(3) classes. Will that request for money damages mean that a 23(b)(3) class mechanism will inevitably be deemed a “superior” means of resolving the controversy, at least relative to government enforcement? Perhaps, but not necessarily.

For example, if the actual damages of class members are de minimis or unascertainable and likely to be substantially diminished by the normal litigation and settlement process,⁹ each class member’s pro rata share of the class attorney’s fees, and the costs of administering the distribution of the fund that remains, it is very possible that a court, keeping also in mind the costs to the judicial system of administering the case and to the defendants in litigating it, could conclude that there would not be sufficient value added to justify certification, given that the government would be prospectively remedying the harm. Similarly, a government disgorgement remedy that made all or most of the class members whole might counsel against the “superiority” of a class. On the other hand, of course, the presence of monetary damages likely to survive the litigation and settlement process, and not likely to be largely addressed by government action, may well counsel in favor of 23(b)(3) certification. The proper resolution of the issue will be case-specific; the important point is that the issue be addressed.

Rules 23(b)(2) and (b)(1)

⁶ 625 F.2d 262 (9th Cir. 1980)

⁷ 182 F.R.D. 448 (D.C.N.J. 1998)

⁸In a handful of cases the FTC has pursued monetary remedies in antitrust cases and the Commission has issued a Policy Statement that sets out in general terms when it will consider disgorgement or restitution and what factors will guide its decision. The full text of the “Policy Statement on Monetary Equitable Remedies in Competition Cases” is available at <http://www.ftc.gov/os/2003/07/disgorgementfrn.htm>.

⁹This may be especially relevant where the case is likely to be resolved by a low value coupon settlement of the sort discussed extensively in this workshop and in prior FTC amicus filings.

The second most popular vehicle for class certification appears to be Rule 23(b)(2), which allows certification when the requirements of (b)(1) are met and “the party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole.” In significant contrast to Rule 23(b)(3), Rule 23(b)(2) does not require that a class action, to be certified, be “superior to other available methods for the fair and efficient adjudication of the controversy.” On what basis, then, should a court consider the presence of government enforcement actions when determining whether to certify a 23(b)(2) class?

The answer to this question lies in the very nature of 23(b)(2) classes. Certification under this rule is available only where injunctive or declaratory relief is the heart of the action and monetary damages, if sought at all, are merely incidental to the request for injunctive relief.¹⁰ In order to determine whether the proposed class action will in fact focus on injunctive or declaratory relief, a court should plainly consider whether government law enforcement actions have achieved (or are likely to achieve) injunctive or declaratory relief comparable to that sought in the class action. If so, the class action is unlikely to focus on the request for an injunction or declaration, or would add little by so doing, and so class certification should proceed under another rule, if at all.

23(b)(1)(A) and (B) classes are less frequent and present complex questions. In essence, (b)(1)(A) classes are available when individual actions could “establish incompatible standards of liability for the party opposing the class.” The rule is actually designed to protect the defendant rather than the class,¹¹ and is unlikely to be implicated if government action has already established or is likely to establish the standard of conduct applicable to the defendant. Classes under 23(b)(1)(B), on the other hand, are available if deciding individual class members’ claims would, as a practical matter, dispose of other prospective class members’ interests; for example, if the class claims involve title to indivisible property. The effect of pending government law enforcement in such a situation is difficult to predict, but worth considering in appropriate cases.

In summary, each of the rules under which classes may be certified provides room for courts to consider the effect of pending or completed government law enforcement actions. Given the potentially significant effects of such actions on the class action, the class, and the defendants, courts should clearly use the authority provided by the rules to measure those effects at one of the earliest practicable points – the class certification decision.

¹⁰See, e.g., *Barnes v. American Tobacco Co.*, 161 F.3d 127, 142 (3d Cir. 1998), cert. denied, 526 U.S. 1114 (1999); *Allison v. Citgo Petroleum Corp.*, 151 F.3d 402, 413-16 (5th Cir. 1998); *Faulk v. Home Oil Co.*, 186 F.R.D. 660, 662 (M.D. Ala. 1999); *Powers v. Government Employees Ins. Co.*, 192 F.R.D. 313, 318 (S.D. Fla. 1998); *In re Arthur Treacher’s Franchise Litig.*, 93 F.R.D. 590, 594 (E.D. Pa. 1982).

¹¹See *Pruitt v. Allied Chem. Corp.*, 85 F.R.D. 100, 106-7 (E.D. Va. 1980).

A Practical Point: Finding Out About The Government Action

This proposal raises a practical question: how will a court considering certification know that relevant government law enforcement actions exist? While the parties are likely to know – almost certainly, the case of the defendant, and probably in the case of the plaintiffs – each may have incentives to avoid disclosure.¹² In most cases, those incentives will probably not be sufficient to prevent at least one set of parties from identifying the government action(s) to the court, but that may not always be the case. Also, in some cases government investigations that have not reached the enforcement stage are confidential.

In 2002 the FTC filed comments to the Committee on Rules of Practice that was considering amendments to Rule 23 and suggested that the Rule be further amended to include specific requirements that parties to a proposed class action a) notify the court of related actions by government agencies, and b) notify agencies when private class actions are filed in matters where it is known that government agencies have acted or are investigating.¹³ In that statement, the FTC opined that the notice of the government actions should be given no later than the time that certification is being considered and could aid the judge in understanding the nature of the disputes and the issues presented: “Such notice would ensure that the all district courts are adequately informed with respect to the full context of the case. Knowledge of the existence of a parallel or preceding government action can be important information to the Court as it undertakes to understand the issues in dispute, assess the overall fairness of a settlement, and determine the appropriate level of attorney fees.”

While the Committee did not incorporate that suggestion into the Rules, nothing precludes courts from requiring parties seeking or opposing certification to disclose any relevant pending or completed government law enforcement actions or investigations.

The “Follow-on” Question

As the foregoing references to pending or completed government law enforcement actions – even including non-public investigations – may suggest, in this context which action is the “follow on” is not particularly important. Sequence may be important when considering attorneys’ fees, and the issue of ‘who is the chicken; who is the egg?’ has been the subject of much discussion, including at this workshop. However, which action came first is not relevant to the certification inquiry proposed here. Whether the class action is superior (under Rule

¹²For example, defendants and plaintiffs alike may believe that pending or completed government enforcement actions will prejudice their position on the merits, or affect the remedies, or render settlement more difficult. Class counsel may also have some reason to be concerned that the presence of government enforcement may affect attorneys’ fees.

¹³ “Proposed Amendments to Rule 23 of the Federal Rules of Civil Procedure,” letter from Federal Trade Commission, available at <http://www.ftc.gov/os/2002/02/rule23letter.pdf>

23(b)(3)), or redundant (under Rules 23(b)(1) and (b)(2)) is a question that can be answered without regard to the dates on which the various actions were filed.

Other Possibilities

It is worth noting that a total denial of certification is not the only option and other possibilities exist. In *Wechsler v. Southeastern Properties, Inc.*,¹⁴ a securities case, after a public offering, the Attorney General of New York started an investigation. A few months later a class action was filed, followed in a further few months by a formal court action by the attorney general. When the class moved for certification of an action that had followed the state investigation, the district court held the request in abeyance until it could be determined if the state action would be adequate to protect the interests of the class. In the event, the court determined that the consent relief achieved in the state action was more than enough to satisfy the class, dismissed the case and denied attorney's fees.

Conclusion

Class actions can be important vehicles for protecting the rights of those injured by anticompetitive practices while, at least in theory, maximizing judicial efficiency and reducing the litigation burden faced by defendants. Class actions can, however, be inefficient, costly, and unnecessary, particularly if the problem putatively addressed by the proposed class has been or is likely to be solved by government law enforcement. Courts considering requests for class certification should therefore take a close look at pending or completed government law enforcement actions and investigations to determine their effect, if any, on the proposed class action.

¹⁴ 506 F. 2d 631 (2d Cir. 1974)