Legal Backgrounder

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TARGETED POLICIES CAN END CLASS ACTION FORUM SHOPPING

by

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As the debate over class action reform comes to a head in Congress, the Circuit Court of Madison County, Illinois, continues to make headlines as the poster child of what's wrong with the current class action system. Most recently, in a bench trial, a Madison County judge awarded a class of smokers $10.1 billion in damages ($7.1 billion compensatory, $3 billion punitive), based on their allegations that Philip Morris misleadingly promotes light cigarettes as less dangerous than regular cigarettes — reportedly just months after he accepted $10,000 in campaign contributions from the plaintiffs' lawyer in that case. Robert Lenzner and Matthew Miller, *Buying Justice*, FORBES, July 21, 2003, at 64.

The Philip Morris verdict highlights some of the key problems with the current class action system: the ability of plaintiffs' lawyers to freely forum shop for plaintiff-friendly judges, particularly those who are elected with their contributions; the willingness of certain judges to make their courts "magnets" for major class actions by freely certifying class actions without carefully examining whether the claims at issue can fairly be adjudicated on a classwide basis; and the looming threat of runaway jury awards that frequently pressure companies into settling cases lest they be faced with a $10 billion verdict.

Congress is currently considering legislation that seeks to put Madison County and other "magnet" state courts out of the mass production class action business. Under the Class Action Fairness Act — H.R. 1115 (which passed the House by a wide margin earlier this year) and S. 274 (which likely will receive Senate floor action later this year) — the current parameters of diversity jurisdiction would be expanded to include class actions in which: (1) the aggregate amount in controversy exceeds $5 million; and (2) at least one plaintiff is diverse from one defendant. S. 274, 108th Cong. § 4(a) (2003); H.R. 1115, 108th Cong. § 4(a) (2003). However, the bill does not grant federal jurisdiction over class actions filed in the defendants' home state, so long as two-thirds or more of the class members are from that state. Moreover, if between one-third and two-thirds of the class members are from the defendant's home state, the bill instructs federal courts to perform a balancing test (if a party seeks to remove the case) to determine whether the case is a

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local dispute that should more properly be adjudicated in state court, or whether it raises substantial interstate issues, making it more appropriately litigated in federal court. *Id.* In addition, the bill's jurisdictional provisions do not apply to securities cases, suits with fewer than 100 class members, or suits against state governmental entities that might be entitled to sovereign immunity if the suit were litigated in federal court. *Id.*

The purpose of the legislation is two-fold — to correct an anomaly in the diversity jurisdiction statute and, at the same time, to diminish class action abuse by moving more class actions to federal courts, which are less likely to tolerate the type of mischief that is taking place in Madison County and a selected number of class action "mills" around the country. Current jurisdictional laws allow federal courts to hear interstate disputes between individuals as long as the amount in controversy exceeds $75,000. *Zahn v. International Paper Co.*, 414 U.S. at 301 ("Each *plaintiff* in a Rule 23(b)(3) class action must satisfy the jurisdictional amount, and any plaintiff who does not must be dismissed from the case – 'one plaintiff may not ride in on another's coattails.'"). At the same time, however, federal courts cannot hear most large, interstate class actions because there is frequently one plaintiff and one defendant from the same state (more often that not as a result of plaintiffs' counsel's manipulation to keep a case in state court), and because courts require each individual class member to meet the $75,000 minimum rather than looking at the total relief sought by the class. This bizarre state of affairs, which allows relatively minor slip-and-fall cases into federal court, while excluding billion dollar class actions like the recent Madison County tobacco case, is directly contrary to the intention of the Framers who established diversity jurisdiction. Their goal was to protect interstate commerce by diminishing the likelihood that local state courts would discriminate against businesses. *See generally* John P. Frank, *Historical Bases of the Federal Judicial System,* 13 LAW & CONTEMP. PROBS. 3, 22-28 (1948); H. J. Friendly, *The Historic Basis of Diversity Jurisdiction,* 41 HARV. L. REV. 483 (1928). It is hard to imagine a type of lawsuit that has resulted in more discrimination and had a more deleterious effect on interstate commerce than class actions.

Despite the substantial amount-in-controversy threshold and the carve-outs for small and local class actions, one criticism of the bill has been that its jurisdictional provisions are over-inclusive — *i.e.*, that the legislation would clog federal courts with class actions that are local in nature. In order to address these criticisms, the authors recently completed a limited study intended to assess the bill's effects in the courts of states that do not have reputations as class action havens versus the effects on courts (like those in Madison County) that have become notorious for class action abuses. To that end, the study looked at all class actions for which there were reported decisions on the Lexis or Westlaw legal databases between January 1, 1997 and June 30, 2003, in the state courts of Connecticut, Delaware, Maine, Massachusetts, New York and Rhode Island, to see how those cases would have been affected by the bill.[1] The survey then reviewed class action complaints filed between 1998 and 2001 in Madison County, Illinois, to examine the effects on the class action cases filed there.[2]

The study indicates that the Class Action Fairness Act is a targeted solution to class action abuses that potentially will result in moving to federal court a substantial percentage of the nationwide or multi-state

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[1]The study focused on the state courts of these jurisdictions because they are among the very few for which a substantial body of trial court decisions is available on-line. (For the vast majority of states, the only legal decisions available on-line are those issued by appellate courts.) The survey does not purport to be an exhaustive review of all cases filed in these states during a specified period. Rather, by looking at five years of judicial decisions involving class actions in these states, the survey provides insights about the types of class actions filed in these states and how they would be affected by the pending legislation.

[2]The Madison County complaints had been gathered in connection with two earlier research projects sponsored by the Manhattan Institute. *See* John H. Beisner and Jessica Davidson Miller, *They're Making A Federal Case Out Of It . . . In State Court*, 25 HARV. J. L. & PUB. POL'Y 1 (Fall 2001); John H. Beisner and Jessica Davidson Miller, *Class Action Magnet Courts: The Allure Intensifies,* 4 BNA CLASS ACTION LITIG. R. 58 (Jan. 24, 2003).

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class actions filed in class action mill jurisdictions (like Madison County, Illinois), while allowing state courts that are not magnets for nationwide class actions to continue litigating the truly local class actions that they normally see on their dockets.

Most notably, the study found that in each of the six states surveyed, more than half of the class actions for which decisions were available on-line would remain in state court. In contrast, the vast majority of class actions brought in recent years in Madison County, Illinois would be subject to diversity jurisdiction and would thus become removable to federal court under the legislation. Specifically, *of the 113 class actions brought in Madison County between 1998 and early 2002, 98 (86.7 percent) would be removable to federal court under the bill.*

With regard to class actions filed in the six surveyed states, most of the cases were outside the scope of the bill. For example, in Connecticut, 24 of 40 (61 percent) of the class actions identified over the period would have remained in state court under the bill. Similarly, in Massachusetts, 30 of 49 (61 percent) of the reported class actions would have remained in state court. These cases typically involved: (1) suits by local consumers, homeowners, and employees against local businesses; (2) suits against state and local governmental entities; and (3) suits in which the amount in controversy was less than $5 million.[3] In other words, most of these cases would remain in state court under the bill because they involved truly local controversies.

In Madison County, the picture was totally different. First, it is striking that the study data suggest that the Circuit Court of Madison County, Illinois, sees more class actions than entire states with exponentially larger populations. Second, the nature of the Madison County class actions was completely different. There were no class actions by local homeowners or employees against a local company. There were no class actions against local governmental entities. Rather, most of the cases were brought on behalf of nationwide purported classes, 99 percent of whose members lived outside of Madison County, against corporations based outside of Illinois, concerning acts that did not occur in Madison County. And the few suits that were not nationwide class actions against out-of-state corporations involved either: (1) Illinois-only suits against out-of-state businesses (the very type of case that diversity jurisdiction was intended to address); or (2) multi-state or nationwide suits against Illinois corporations (all of which involve application of numerous states' laws). Moreover, none of the defendants in any of these cases was located in Madison County, Illinois. Thus, in contrast to the states surveyed, it was clear that the suits brought in Madison County — and particularly those that would be affected by the bill — arrived there as a result of forum shopping, not because of any legitimate nexus to the county.

Examples of suits brought in Madison County over the last several years that would be removable under the bill include:

- Numerous nationwide lawsuits against insurance companies challenging a variety of practices, from how insurance companies compute premiums to how they value vehicles that are totaled in car accidents;[4]

- A nationwide suit against a hotel chain (which has no hotels in Madison County) for

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[3]The cases identified in the survey were categorized in a conservative manner, erring on the side of presuming removal to federal court if the available facts were unclear. For example, in many cases, it was difficult to discern from the reported on-line opinions the aggregated amount in controversy in the case. In such cases, the survey simply assumed that the $5 million threshold was met.

[4]*See, e.g.,* Complaint, *Abalos v. Allstate Ins. Co.*, Case No. 01-L1005 (June 13, 2001); Complaint, *Phillips v. Union Fidelity Life Ins. Co.*, No. 01 L 1835 (Dec. 13, 2001); Complaint, *Mincey v. Auto. Prof'ls Inc.*, No. 01 L 1848 (Dec. 19, 2001).

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imposing an energy surcharge on guests;[5]

- A suit by residents of thirty-one states against a national plumbing franchise alleging that franchisees around the country send technicians out to do plumbing work instead of licensed plumbers;[6]

- Numerous nationwide suits against telephone companies and cellular phone companies regarding the ways they bill consumers;[7] and

- Several nationwide suits challenging extended warranties on vehicles.[8]

Not only do these suits have little (if any) nexus to Madison County, but they seek to resolve various issues on behalf of consumers nationwide. Thus, these suits highlight the basic premise of the Class Action Fairness Act: why should a judge in Madison County, Illinois, regularly be setting nationwide policies regarding numerous commercial practices that affect millions of consumers and companies each day?

In short, the survey demonstrates three important things about the Class Action Fairness Act. First, critics of the legislation are simply wrong when they say that the bill would move all — or even most — class actions to federal court. Second, for the most part, the legislation narrowly targets "problem" courts like Madison County, where class action abuse is most rampant. And third, the bill would not affect local disputes; rather, the legislation would move *most nationwide class actions* to federal court, while allowing local disputes to be litigated in the state court forums where they properly belong. Thus, the bill will indeed put the Madison County court out of the nationwide class action business, but at the same time, it will have only a modest impact on numerous other jurisdictions where most class actions would remain right where they are now — in state court.

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[5] *Nicoloff v. Wyndham Int'l, Inc.,* Complaint, No. 01L1165 (July 23, 2001).

[6] Complaint, *Garvey v. Roto-Rooter Services Co.*, No. 00-L-525 (June 13, 2000).

[7] *See, e.g.,* Complaint, *Donaldson v. Sprint Communications Co.*, No. 01L1660 (Nov. 3, 2001); Complaint, *Ragan v. AT&T Corp.*, No. 02L168 (Jan. 23, 2002).

[8] *See, e.g.*, Complaint, *Reynolds v. Gen. Motors Acceptance Corp.*, No. 01 L 1103 (July 5, 2001); *Hodge v. Firstar Bank*, No. 01 L 1079 (June 28, 2001).

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