Defeating Class Certification through Superior Out-of-Court Settlement Programs

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In seeking to certify a class in federal court, a plaintiff bears the burden of establishing the four well-known requirements of Rule 23(a) of the Federal Rules of Civil Procedure: (1) numerosity; (2) commonality; (3) typicality; and (4) adequacy of representation. If damages are sought under Rule 23(b)(3), the plaintiff must further demonstrate that common questions of law or fact predominate over issues affecting individual plaintiffs and that "a class action is superior to other available methods for the fair and efficient adjudication of the controversy."1 While the strategy to defend a Rule 23(b)(3) class action often entails showing that individual issues predominate, under certain circumstances, defendants may want to focus on the superiority requirement of Rule 23(b)(3). In particular, where liability to a class of persons (e.g., customers) is highly probable and it has been decided that a remedy will be voluntarily extended to the affected persons, a defendant might put into place a private, out-of-court program—either at the outset of litigation or, if litigation is anticipated, even before it begins—that sufficiently addresses and resolves the claims of putative class members. By doing so, a defendant may persuade the court that a class action suit is not the superior mechanism for addressing class members' claims. In the past several years, a number of district courts have reached that conclusion.

The Growing Trend in the District Courts

The seminal case of Berley v. Dreyfus & Co.2 is an early example of a district court refusing to certify a class action where the defendant was already offering an effective out-of-court remedy for putative class members. There, the defendant broker had sold investors stock which turned out to be unregistered. The U.S. Securities and Exchange Commission suspended trading in the stock after discovering that it was not registered. Defendant offered to refund the purchase price of the stock when its trading was suspended. Most of the investors accepted the refund; however, the plaintiffs and putative class members chose not to take advantage of the refund offer, choosing instead to bring a class action lawsuit. The court declined to certify the proposed class because class certification under the circumstances "would needlessly replace a simple, amicable settlement procedure with complicated, protracted litigation."3 The court acknowledged that the language of Rule 23 did not explicitly contemplate nonjudicial alternatives to a class action, but nonetheless denied certification based on a broad view of the policy of economy underlying the rule: "Although Dreyfus & Co.'s offer to refund the purchase price to its customers is not quite 'another method for the fair and efficient adjudication of the controversy,' we think that subparagraph (b)(3) read
as a whole reflects a broad policy of economy in the
use of society's difference-settling machinery.”
Since refunds were already readily available,
certifying the class would be "creating lawsuits
where none previously existed." Creation of such a
lawsuit would be anathema to the rule's "broad
policy of economy" in its inefficient use of court
resources.

More recently, a number of district courts have
adopted the reasoning in Berley. For example, in
Chin v. Chrysler Corp., plaintiffs sought
compensatory damages and restitution for
defective anti-lock brake systems (ABS) that had
been installed in their vehicles. The putative class
consisted of all owners and lessees of Chrysler
vehicles with defective ABS systems and all those
who previously owned such vehicles and incurred
expenses arising out of the repair or replacement of
the defective ABS systems. Chrysler instituted a
voluntary recall and reimbursed all prior and
current owners of vehicles with the defective ABS
systems for necessary repairs. Chrysler also offered
to replace all defective ABS systems free of charge
and extended the warranties of the replaced ABS
systems under the voluntary recall. The court held
that a class action was not superior to the
reimbursement and replacement program. The
court noted that "it is unclear if there is any useful
remedy this Court could fashion" which would offer
plaintiffs any redress not available through the
reimbursement program.7

In In re Phenylpropanolamine (PPA) Products
Liability Litigation, a district court again held that
class certification was precluded by a superiorly
effective recall and refund program. After the U.S.
Food and Drug Administration (FDA) issued a health
advisory and request for recall of all products
containing PPA, plaintiffs sought relief in a class
action based on theories of unjust enrichment.
Defendant voluntarily recalled its products
containing PPA and instituted a refund program for
purchasers of the recalled products. Holding that
the existing refund programs were superior to a
class action lawsuit, the court noted, "it makes little
sense to certify a class where a class mechanism is
unnecessary to afford the class members redress."9

Plaintiffs argued that the refund programs were not
superior to a class action because the programs had
proof of purchase requirements, had resulted in the
vast majority of refunds going to retailers rather
than directly to consumers, and were not
publicized. In rejecting plaintiffs' proof of purchase
argument, the court reasoned that such
requirements were "extraordinarily commonplace"
amongst retailers and were "a necessary
requirement for class identification purposes" in
any case.10 The court went on to note that "the
distinction between the amount of refunds given to
retailers, rather than consumers, is likely due to the
fact that the retailers had readily available proof of
purchase in the form of the products themselves
and that retailers may be called upon by their
consumers to make refunds."11 The court rejected
plaintiffs' publicity argument by pointing to the
actual numbers of participants in the refund
programs. The court noted that the FDA advisory
and recall were widely publicized and stated, "a
significant number of people somehow heard about
these programs."12 Based on the existence of the
refund programs, the court, like the court in
Berley, was concerned that "certification of the proposed
class would merely serve to create lawsuits where
none previously existed."13

Yet another district court analyzed the superiority
of a recall and refund program in In re ConAgra
Peanut Butter Products Liability Litigation.14 The
case involved the widely publicized recall of
defendant's peanut butter following an FDA
warning that certain containers of the peanut
butter were contaminated with salmonella. Even
though later testing showed that the vast majority
of the recalled peanut butter was uncontaminated,
ConAgra immediately offered full refunds to
purchasers of the recalled peanut butter. The court
noted that "[t]he recall received a lot of publicity
and prompted widespread participation in the
refund program."15 Despite the availability and
widespread use of the refund program, the lead
plaintiffs filed suit seeking to recover economic
losses because their peanut butter was rendered unusable. Plaintiffs argued that a class action lawsuit was superior because "it solves the problem of cost-effective adjudication of these hundreds of thousands of small claims." The court concluded that because any putative class members could easily get their money back from ConAgra, "the important policy concern that individuals were not or will not be able to recover because of small individual recoveries [was] not heavily implicated." Plaintiffs further argued that "any notice the Defendant provided the public for its refund program would be inferior to class action notices" guided by the court. Noting that the public received "massive" notice of the contaminated peanut butter through ConAgra's press releases, information on its website, and general news coverage, the court held "the standard for sufficient notice for a company's voluntary refund program should not be that of a class action suit." Therefore, where news of the refund program had been widely disseminated to a public that was "notified of the program immediately after its inception," the court found no basis for the plaintiffs' fears of insufficient notice. Because the refund program provided adequate redress for each potential class member and the public was sufficiently notified of the availability of refunds, the refund program provided a better remedy to putative class members, in much less time, and without the expenditure of substantial judicial resources for no benefit. The refund program was simply superior to a class action.

Most recently, in a case involving a line of children's toys that induced comas when swallowed, a district court again declined to certify a class action because the already-in-place refund and exchange program was a superior means for resolving the controversy. The court in In re Aqua Dots Products Liability Litigation noted that the safety threat to children and the ensuing recall of the defective toys were widely publicized and resulted in a refund program that was widely utilized by the public without assistance of counsel. Plaintiffs argued that the refund program was inadequate because some customers received refunds of the "current store price" of the toys at the time they sought their refunds rather than the purchase price of the toys at their time of purchase. The court rejected this argument, reasoning that because "each class member would likely receive a uniform estimate of damages" through litigation of a class action, the class action would provide no better a remedy than the existing refund program through which customers received refunds that "varied from one store to the next and from one moment to the next." The court held, "since the defendants will provide a refund—without needless judicial intervention, lawyer's fees, or delay—to any purchaser who asks for one, there is no realistic sense in which putative class members would be better off coming to court." Therefore, the refund program was found to be superior to a class action, and the class was not certified.

One District Court Concludes Otherwise

This line of cases demonstrates that a growing number of district courts have concluded that their broad discretion in deciding class certification issues includes the discretion to deny certification where there is a fair and efficient out-of-court settlement program already in place. But one district court recently reached the opposition conclusion.

In Turner v. Murphy Oil USA, Inc., the Eastern District of Louisiana held that out-of-court, private settlement programs cannot be weighed by a court in analyzing the superiority of a potential class action. In a case arising out of Hurricane Katrina, homeowners and business owners filed actions against a defendant oil refinery alleging damages from a post-hurricane oil spill. The court held that a class action would be superior despite the existence of a private settlement program. Without describing any characteristics of the settlement program, the court held that "[t]he [superiority] analysis is whether the class action format is superior to other methods of adjudication, not whether a class action is superior to an out-of-court, private settlement program." The court placed great emphasis on a
textual interpretation of the word "adjudication" and reasoned that the word does not contemplate nonjudicial alternatives. However, this reasoning has been criticized by one commentator as "an overly restrictive reading of Rule 23(b)(3) [since] the purpose of the superiority requirement is to assure that the class action is the most efficient and effective means of resolving the controversy."26 Furthermore, the court in Aqua Dots explicitly chose not to follow the Turner court, stating that it "join[ed] the majority of district courts and prominent commentators" in evaluating the merits of out-of-court settlement programs to find that "when a defendant is already offering an effective remedy for putative class members through out-of-court channels, a class action threatens to consume substantial judicial resources to no good end."27

It appears that the decision in Turner may be an outlier from the recent trend among district courts. Still, a defendant facing possible class action litigation in the Eastern District of Louisiana may want to pursue a change of venue if seeking to reap the potential benefits of a fair and efficient settlement program. With that said, it bears noting that none of the U.S. Courts of Appeals have weighed in on the issue. An appeal was taken in the Aqua Dots litigation, but as of this writing, no decision has been rendered. Therefore, it remains to be seen whether the recent trend among the district courts will be upheld on appeal.

Common Characteristics of Approved Out-of-Court Settlement Programs

It is useful to note a few common characteristics of the refund programs that were found superior in these cases. First, in each case the out-of-court remedy is substantially equivalent to what putative class members could expect to recover through the class action suit. If the class members stand to gain more through class action litigation than they could receive through the settlement program, the court may find the class action superior. Purchase-price refunds were found adequate in the cases here. However, before establishing the amount of refund to be offered, the amount of potential damages putative class members stand to be awarded should be closely scrutinized. Offering a refund only to those individuals who can provide a proof of purchase will not necessarily make a refund program inferior.

Second, the more publicized and widely utilized a refund program is, the more likely a court will be to deem it superior to a class action in which the court itself will oversee the notice of potential class members. Although extensive publicity may not be necessary, refund programs that are widely publicized serve to allay fears a court may have that not all potential class members received notice of their out-of-court remedy. Where all potential class members are already aware of an available out-of-court remedy, the court will have no reason to find class action notice superior.

Lastly, in each case discussed above, the refund program was implemented as soon as possible after the circumstances arose that could have potentially led to a class action lawsuit. Any defendant who is aware that it may face a potential class action and seeks to fashion a superior out-of-court remedy would be wise to institute a settlement program as quickly as possible. Programs that are efficient in providing potential class members redress are also more likely to be found superior to a class action that can be dragged out over a period of years. In all, where it can be demonstrated that an existing program offers potential class members fair and efficient redress, a court will be less inclined to find that a class action is superior or necessary.

Implementing a program that meets these criteria may very well be expensive. However, under circumstances where liability appears likely and plaintiff has a strong argument that the requisites for class certification (other than superiority) are met, the costs of putting such a program in place may be well-justified. For example, once the program is in place, a defendant might preemptively move to deny class certification on the grounds that the class action cannot be shown
to be superior to the out-of-court remedy offered by the program. Doing so might avoid costly and protracted discovery that disrupts business operations. In addition, obtaining early dismissal of the class action might avoid lengthy negative publicity surrounding the lawsuit. And by offering customers an out-of-court remedy, as opposed to fighting it out in class action litigation, goodwill with customers might be restored quickly.

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3 Id. at 399.
4 Id. at 398.
5 Id.
7 Id. at 463.
9 Id. at 622.
10 Id.
11 Id.
12 Id.
13 Id.
15 Id. at 691.
16 Id. at 699.
17 Id. at 700.
18 Id.
19 Id.
20 Id.
21 270 F.R.D. 377 (N.D. Ill. 2010).
22 Id. at 384.
23 Id. at 385.
25 Id. at 610.

26 7AA Wright, Miller & Kane, Federal Practice & Procedure § 1779 [add edition and year].
27 Aqua Dots, 270 F.R.D. at 281, 282.
28 See, e.g., Vinole v. Countrywide Home Loans, Inc., 571 F.3d 935 (9th Cir. 2009) (finding that the language of Rule 23 does not preclude defendants from seeking resolution of the class certification issue early in the case).