U.S. Supreme Court Rejects State’s Attempt To Limit Class Action Relief In Federal Court

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On March 31, 2010, the United States Supreme Court issued a significant decision, in which it rejected state law limitations on class actions heard in federal court. In *Shady Grove Orthopedic Assocs., PA v. Allstate Ins. Co.*, No. 08-1008, 559 U.S. __, 2010 WL 1222272 (Mar. 31, 2010), the Supreme Court addressed whether New York’s Civil Practice Law and Rule (“CPLR”) § 901(b) conflicts with Federal Rule of Civil Procedure 23.

By a five-four vote, the Court held that New York’s law – which bars class actions seeking penalties or statutory minimum charges – conflicts with Rule 23 and cannot be applied by a federal court sitting in diversity (click here to view opinion).

The majority applied a bright-line rule. It held that if Rule 23 answers the question as to whether a class could be certified, and Rule 23 does not exceed statutory authorization or Congress’s rulemaking power, Rule 23 controls notwithstanding the contrary New York law. The dissent urged that if the Court had instead considered New York’s legitimate interest in keeping class action awards “reasonably bounded,” it would not have found any conflict with Rule 23. The majority rejected the dissent’s plea “to interpret the Federal Rules with awareness of, and sensitivity to, important state regulatory policies.”

The Court’s approach signals a literal interpretation of Rule 23 to determine if the Rule governs an issue otherwise addressed by state law. This ruling has application beyond the particular New York law at issue. Many states have enacted other restrictions that affect the conduct of class actions. For example, certain state laws limit the parties who have standing to represent a class. *Shady Grove* may lead to challenges addressing the application in federal court of these and other state law limitations. The Court’s bright-line test also may apply in cases considering whether state laws must yield to other Rules of Federal Civil Procedure.

Justice Ginsburg noted in her dissent that, in enacting CAFA, Congress envisioned fewer, not more, class actions. It is ironic that the effect of *Shady Grove* may be to make certain restrictions that would have precluded class actions in state court inapplicable to those actions when filed in federal court. As a result, plaintiffs may engage in forum shopping by filing class action diversity suits in federal court that could not otherwise be brought in state court.

The Court issued three opinions, and only a portion of the lead opinion was endorsed by five Justices. The Court’s complicated opinions are described below.
Background

New York CPLR § 901(b) prohibits class actions in suits seeking penalties or statutory minimum damages. Plaintiff brought a class action diversity suit in federal court to recover unpaid statutory interest. Defendant Allstate contended that the statutory interest was a “penalty” and that New York law prohibited the recovery of such a penalty in a class action. If the cause of action was considered as an individual claim, the statute authorized $500 in relief. If the plaintiff’s claim was considered to be filed on behalf of a class, the amount at issue exceeded $5 million. The district court agreed with Allstate, and dismissed the case for lack of jurisdiction. The Second Circuit affirmed. The Supreme Court reversed, holding that the state law could not preclude a district court sitting in diversity from entertaining a class action under Rule 23.

Opinion for the Court

Justice Scalia announced the judgment and delivered the opinion of the Court. Chief Justice Roberts, and Justices Stevens, Thomas, and Sotomayor joined in the judgment and a portion of Justice Scalia's opinion. The Supreme Court began by asking whether Rule 23 answers the question in dispute. The Court observed that if Rule 23 answers the question, Rule 23 governs unless Rule 23 exceeds the statutory authorization or Congress's rule-making power. Thus, the Supreme Court did not treat the case as an “Erie question,” stating that “[w]e do not wade into Erie’s murky waters unless the federal rule is inapplicable or invalid.”

The Court then held that Rule 23 provides the answer by defining the circumstances in which a class may be certified in federal court. The Second Circuit had concluded that although Rule 23 defines the criteria for determining whether a class may be certified in federal court, the New York statute did not offend Rule 23 because it addresses the antecedent issue of whether the particular type of claim is eligible for class treatment. The Supreme Court rejected that distinction. It found the line between eligibility and certifiability to be “entirely artificial,” and held that the New York statute conflicted with Rule 23 because it attempted to define the circumstances in which a class could be certified in federal court.

The Supreme Court explicitly reserved the question of whether a state law that limits the remedies available in a class action would conflict with Rule 23.

Remainder of Scalia Opinion

The remainder of Justice Scalia’s opinion reflects divisions within the Court as to how to resolve the questions this case presented. Justice Scalia, joined by Chief Justice Roberts and Justices Thomas and Sotomayor (4 votes) stated that Rule 23 applies in federal court regardless of whether the application of that rule “frustrates a state substantive law (or a state procedural law enacted for a substantive purpose).” Justice Scalia stated that if a federal rule regulates procedure and is authorized by the Rules Enabling Act, it is “valid in all jurisdictions, with respect to all claims, regardless of its incidental effect upon state-created rights.” Justice Scalia further stated that a “federal rule governing procedure” is valid regardless of whether “it alters the outcome of the case in a way that induces forum shopping.”

Stevens’ Concurrence

Justice Stevens, who provided the fifth vote in support of the judgment, agreed that the New York law was a procedural rule, and therefore Rule 23 governed the dispute in federal court. Justice Stevens analyzed the statutory language and history of § 901(b) and agreed with Justice Scalia that it was not a substantive rule. However, Justice Stevens agreed with the dissent that some state procedural rules could apply in diversity cases if they “function as a part of the State’s definition of substantive rights and remedies.” Therefore, Justice Stevens’ disagreement with Justice Scalia and others stemmed from a larger dispute regarding the Erie doctrine.
Ginsburg’s Dissent

Justice Ginsburg, joined by Justices Kennedy, Breyer, and Alito, dissented. Justice Ginsburg stated there was no conflict between CPLR § 901(b) and Rule 23. She observed that the Court had previously granted “respectful consideration” to state interests – whether codified in statute or found in a procedural rule. Justice Ginsburg concluded that New York’s limitation on statutory damages reflected the state’s regulatory policy of preventing excessive damages.

Justice Ginsburg concluded there was no conflict between state and federal law because Rule 23 governs “procedural aspects of class litigation” while concurrently allowing “state law to control the size of a monetary award a class plaintiff may pursue.” Accordingly, the dissent noted that Rule 23 is focused on the efficient conduct of litigation, while CPLR § 901(b) is concerned with curbing exorbitant damages. Justice Ginsburg further concluded that no conflict existed in this dispute because plaintiffs in federal court could seek relief as a class if they “forgo statutory damages and instead seek actual damages or injunctive or declarative relief; any putative class member who objects can opt out and pursue actual damages, if available, and the statutory penalty in an individual action.” Justice Ginsburg stated that the CPLR § 901(b) bar on statutory damages in class action litigation served as a cap on damages, and as such, constituted a substantive rule under Erie. Therefore, Justice Ginsburg would have affirmed the Second Circuit’s judgment.