Class Action Watch

MARCH 2008

Cy Pres Settlements

by Theodore H. Frank

The idea of *cy pres* (pronounced "see pray" or "sigh pray," from the French *cy pres comme possible*—"as near as possible") originated in the trust context, where courts would reinterpret the terms of a charitable trust when literal application of those terms resulted in the dissolution of the trust because of impossibility or illegality.[1] In a classic nineteenth century example, a court repurposed a trust that had been created to abolish slavery in the United States to instead provide charity to poor African-Americans.[2] The California Supreme Court endorsed the use of cy pres or "fluid recovery" mechanism in class action settlements in 1986, to distribute proceeds to a "next best" class of consumers, and many other courts have gradually adopted the procedure.[3] Cy pres settlements arise in one of three circumstances:

- There is a fixed settlement fund that exceeds the amount paid out because only a few class members have registered to be claimants;
- The court (often at the parties' behest) decides that administering a settlement by paying class members directly would be too expensive;
- The parties otherwise agree that a case shall be settled by paying a third party.

While original cy pres class action settlements provided that left-over money be distributed to a different set of consumers who may or may not coincide with the class, in recent years, left-over or specifically earmarked funds are typically given directly to a third-party charity.

Plaintiffs' lawyers have recently shown renewed interest in the cy pres mechanism in class action settlements.[4] The interest of the class attorney in a class action settlement does not entirely coincide with the interests of the class members. A defendant may be willing to spend a certain amount of money to settle a class action to avoid the expense and risk of litigation, but that money must be divided between the class and their attorneys. At the same time, a class action settlement must be approved by the court. One mechanism often used to maximize attorneys' fees are "coupons," which, if structured improperly, act to exaggerate the size of class recovery to maximize the return to plaintiffs' lawyers at a lower cost to defendants. The parties represent to the court that the value of the settlement to the class is the nominal value of the coupons; in fact, both parties expect the coupons to have a low redemption rate because

continued page 21

The Supreme Court Rejects "Scheme Liability" in Securities Class Actions

by Larry Obhof

On January 15, 2008, the Supreme Court issued its decision in *Stoneridge Investment Partners LLC v. Scientific-Atlanta, Inc.*, a case heralded by commentators as the "most important securities case in decades."[1] The five-to-three *Stoneridge* majority rejected a theory of "scheme liability" that would have greatly expanded the universe of potential class action defendants.

What makes *Stoneridge* so important? In simple terms, the plaintiff sought to expand the scope of Section 10(b) actions beyond the securities markets and into the realm of ordinary

continued page 9

INSIDE

63 *Id.* at 1194.

64 *Id.*

65 *Id.* (quoting *Watson*, 487 U.S. 977, 990, 999 (1988)).

66 *Id.*

67 *Id.* (quoting *Watson*, 487 U.S. at 992).

68 *Id.* at 1194-95.

69 *Id.* at 1195-96.

70 *Id.* at 1196.

71 *Id.*

72 *Id.*

73 *Id.*

74 *Id.*

75 *Id.*

76 *Id.* at 1197.

77 *Id.*

78 *Id.*

79 *Id.*

80 *Id.*

81 *Id.* at 1198.

82 *Id.*

83 *Id.* at 1199 (quoting Califano v. Yamasaki, 442 US 682, 700-01 (1979)).

84 *Id.*

85 *Id.*

86 *Id.*

87 *Id.*

88 *Id.*

89 *See, e.g.*, Gen. Tel. Co. of the Southwest v. Falcon, 457 U.S. 147, 151 (single facility), 159 n. 15 (wholly subjective decisionmaking process).

90 *Dukes I*, 222 F.R.D. at 155.

91 *Watson*, 487 U.S. at 992 (plurality op.) (internal quotation marks omitted).

92 *Id.*

93 *Id.* at 992-93 (internal quotation marks and citations omitted).

94 *Id.*

95 Int'l Bhd. of Teamsters v. United States, 431 U.S. 324, 362 (1977); *see also* Reeves v. Sanderson Plumbing Prods. Inc., 530 U.S. 133, 148 (2000).

96 *Dukes II*, 509 F.3d at 1193.

97 *See, e.g.*, Philip Morris USA v. Williams, 127 S. Ct. 1057, 1063 (2007) (due process requires that a defendant have "an opportunity to present every available defense").

Cy Pres Settlements

Continued from page 1

for many class members, "the right to receive a discount [or coupon] will be worthless."[5] The class attorneys then capture the lion's share of the actual settlement. There are countless examples where the nominal or even the predicted values of the coupons that justified a huge attorneys' fee far outstripped the actual redemption rate.[6] In a recent settlement (a nationwide Sears class action in Cook County, Illinois), plaintiffs' attorneys received about $1 million, while the 1.5-million member class redeemed claims at under a 0.1% rate for a total of $2,402.[7] Such settlements benefit defendants in the short run by permitting them to pay off class action attorneys cheaply, but hurt defendants in the long run by creating a mechanism by which class action attorneys can profitably bring weak cases.

The Class Action Fairness Act (CAFA), passed in 2005, has drawn de jure[8] and de facto[9] scrutiny to the issue of coupon settlements by requiring attorneys' fees in coupon settlements to be tied to the actual value of the redeemed coupons. But CAFA does not provide the same scrutiny to cy pres settlements and trial lawyers are shifting to that mechanism to accomplish the same task of maximizing return from weak cases.

Judge Richard Posner has argued that cy pres is a misnomer in the class action context:

> [Cy pres] doctrine is based on the idea that the settlor would have preferred a modest alteration in the terms of the trust to having the corpus revert to his residuary legatees. So there is an indirect benefit to the settlor. In the class action context the reason for appealing to cy pres is to prevent the defendant from walking away from the litigation scot-free because of the infeasibility of distributing the proceeds of the settlement (or the judgment, in the rare case in which a class action goes to judgment) to the class members. There is no indirect benefit to the class from the defendant's giving the money to someone else. In such a case the "cy pres" remedy (badly misnamed, but the alternative term—"fluid recovery"—is no less misleading) is purely punitive.[10]

But sometimes cy pres is less a matter of being punitive and more a matter of disguising the true cost of a settlement to the defendant to maximize the share of the actual recovery received by the plaintiffs' attorneys. If the beneficiary is related to the defendant, or the defendant otherwise benefits from the payout, then the contingent attorneys' fee can be exaggerated by claiming that the value to the class is equal to nominal value of the payment

to the beneficiary; as in the coupon scenario, the defendant is willing to make a larger nominal contribution to settle the case than the actual cost to the defendant. For example, a California state court settlement of a derivative action against Larry Ellison, alleging insider trading, settled when Ellison agreed to pay $100 million to a charity chosen by Oracle—even though the billionaire has previously stated that his fortune would go to charity.[11] The only real expense to Ellison was the $22 million attorneys' fee.

Further ethical problems arise if the beneficiary is related to the judge. The *New York Times* recently documented the problem of charities soliciting judges for leftover settlement money.[12] In a mass-tort inventory settlement of fen-phen cases in Kentucky, tens of millions of dollars intended for plaintiffs was diverted to a newly created charity where the judge who approved the settlement and three of the plaintiffs' attorneys sat as board members, each receiving tens of thousands of dollars for their service. The settlement also provided a million dollars to the alma mater of one of the trial lawyers, which then hired the attorney for a $100,000/year no-show job. (Three of the attorneys are under indictment, and the judge was removed from office.)[13] While this is obviously an extreme case, it does illustrate the ethical problems associated with judges choosing or approving charitable destinations for settlement money.

More frequently, if the beneficiary is related to the plaintiffs' attorneys, or the plaintiffs' attorneys otherwise benefit from the payout, the award rewards trial lawyers twice: first by providing *cy pres* recovery to an organization that supports the agenda or causes of the trial lawyers bringing the case, and then a second time by basing attorneys fees on the first amount. Cy pres donations to law schools certainly provide further incentive for those institutions to support continued expansion of class action law; cy pres awards also regularly go to "public interest" law firms that provide litigation support for the trial bar.

In July 2007, Judge Colleen Kollar-Kotelly granted a motion to award $5.1 million of unclaimed antitrust settlement funds to George Washington University to create a "Center for Competition Law" on the grounds that it would "benefit the plaintiff class and similarly situated parties by creating a Center that will help protect them from future antitrust violations and violations of other competition laws."[14] The lead plaintiffs' attorney, Michael Hausfeld, was a GWU Law alumnus.[15] Other beneficiaries included the Naderite Public Citizen[16] and the Impact Fund, a trial lawyer organization that expressly lobbies for such awards.[17] In a Madison County, Illinois settlement where only $20 million of the $60 million award was left unclaimed, plaintiffs' lawyers Korein Tillery negotiated with Pfizer over the distribution of the remaining $20 million: $5 million each to the Illinois Institute of Technology (for its law school and biomedical research program), University of Chicago Hospitals and the Centers for Disease Control; $3 million to the United Way of Metropolitan Chicago; and $2 million to Lubavitch Chabad of Illinois. Korein Tillery took no discount on its $20 million attorneys' fee.[18] Such problems go beyond trial lawyers and civil lawsuits; Richard Epstein has criticized a government settlement with Bristol-Myers Squibb requiring them to endow a chair of ethics at the District of New Jersey U.S. Attorney's alma mater, Seton Hall Law School.[19]

There are several possible responses to the issue of unfettered cy pres awards, which frequently have too little scrutiny from courts, despite the clear conflicts of interest they present between class members and their attorneys. The American Law Institute's controversial Draft of the Principles of the Law of Aggregate Litigation proposes limiting cy pres to "circumstances in which direct distribution to individual class members is not economically feasible, or where funds remain after class members are given a full opportunity to make a claim."[20] This would imply that a settlement distribution should go to class members who have filed a claim, although some courts have rejected such a solution as a windfall to class members, especially when the number of class members filing claims is small relative to the size of the class.[21]

Illinois has passed legislation requiring at least half of any cy pres award to go to qualifying "nonprofit charitable organizations that have a principal purpose of promoting or providing access to justice for low income residents."[22] Such a resolution effectively taxes cy pres awards, reducing the incentive to divert settlement money into entirely self-serving charities. And while one may question the efficacy of Illinois's choice, better that the legislature be lobbied over the appropriate way to spend cy pres funds than the judicial branch.

There is another possible solution that has not received adequate attention, however. CAFA bases fee awards in coupon settlements on the actual redeemed value of the coupons; if coupons are donated to charity, those coupons cannot be used to calculate a fee award.[23] The same principle should apply when cash is involved. Contingent-fee attorneys should be rewarded only for benefits going directly to the class. Moreover, if a cy pres settlement benefits the plaintiffs' bar directly or indirectly, that settlement should offset the contingent fees. A $20 million cy pres award to Public Citizen or the Impact

Fund should count as part of the attorneys' fee award, not as a justification for additional attorneys' fees. Such a mechanism would give plaintiffs' attorneys the proper incentive to align their interests with those of the class when devising a settlement: if the class members do not get paid, the attorneys do not get paid.

Some might object that such limits would deter contingent-fee class actions when there is no identifiable class or when it is infeasible to distribute settlement funds in a lawsuit where damages are small. But that objection perhaps identifies an advantage, rather than a disadvantage, of tying fees to actual class recovery. A lawsuit where the cost of litigation is greater than the benefit to the class suggests that the social costs are greater than the social benefits. To the extent there is wrongdoing, it should be a job for public, rather than private, attorneys general. An elected official should at least hypothetically balance costs and benefits to society at large in deciding whether to bring suit and faces (at least potential) political consequences if taxpayer resources are wasted in meaningless suits. This is far from a guarantee of good behavior, but at least there would be checks in the political process; entrepreneurial plaintiffs' lawyers seeking rents through the class action mechanism have no such check, and thus act in the public interest only through occasional fits of serendipity.

** Theodore H. Frank is Director of the American Enterprise Institute's Legal Center for the Public Interest.*

Endnotes

1 Susan Beth Farmer, *More Lessons From the Laboratories: Cy Pres Distributions in Parens Patriae Antitrust Actions Brought by State Attorneys General,* 68 Fordham L. Rev. 361, 391-93 (1999); Richard Posner, Economic Analysis of Law 509-10 (4th ed. 1992); Bryan A. Garner, Black's Law Dictionary 392 (7th ed. 1999). "Justification for the use of the doctrine [in the middle ages] was laid on the shoulders of the donor, the idea being since the object of the testator in donating the money to charity was to obtain an advantageous position in the kingdom of heaven, he ought not to be frustrated in this desire because of an unexpected or unforeseen failure." *Id*. (quoting Edith L. Fisch, The Cy Pres Doctrine in the United States 4 (1950)).

2 Jackson v. Phillips, 96 Mass. 539 (1867). *But see* Evans v. Abney, 396 U.S. 435 (1970) (upholding Georgia Supreme Court's dissolution of trust providing for segregated municipal park).

3 State v. Levi Strauss & Co., 41 Cal. 3d 460, 715 P.2d 564, 224 Cal. Rptr. 605 (1986).

4 *See, e.g.,* Remarks of Michael Hausfeld, "Class Action Fairness Act: Two Years Later," Federalist Society, Washington, D.C. (Feb. 14, 2007).

5 Geoffrey P. Miller & Lori S. Singer, *Nonpecuniary Class Action Settlements*, 60 L. & Contemp. Probs. 97, 108 (1997).

6 James Tharin & Brian Blockovich, *Coupons and the Class Action Fairness Act*, 18 Geo. J. Legal Ethics 1443 (2005).

7 Ted Frank, "Moody v Sears: Lawyers, $1M. Class, $2,402," Overlawyered weblog, http://www.overlawyered.com/2007/05/moody_v_sears_lawyers_1m_class.html (May 5, 2007).

8 28 U.S.C. § 1712.

9 E.g., Synfuel Technologies, Inc. v. DHL Express (USA), Inc., 463 F.3d 646 (7th Cir. 2006) (rejecting coupon settlement, though scrutiny under CAFA not required).

10 Mirfahisi v. Fleet Mortgage Corp., 356 F.3d 781, 784 (7th Cir. 2004).

11 Ted Frank, "Final update: Oracle settlement," Point of Law blog, http://www.pointoflaw.com/archives/001875.php (Nov. 23, 2005) ("That the plaintiffs are settling for pennies on the dollar with no benefit to the corporation on whose behalf they're ostensibly suing, as well as the fact that a Delaware court has already absolved Ellison of the same charges, suggests that even the plaintiffs recognize the suit as meritless."); Michael Paige, *"Judge OKs Ellison's $122M Settlement,"* Market Watch, Nov. 22, 2005; Peter Branton, *Wealth of Experience*, IT Weekly (Jul. 9, 2006) ("I think after a certain amount, I'm going to give almost everything I have to charity because what else can you do with it?").

12 Adam Liptak, *Doling Out Other People's Money*, N.Y. Times (Nov. 26, 2007).

13 Ted Frank, "Fen-Phen Zen," American.com (Apr. 4, 2007).

14 Diamond Chemical Co. v. Akzo Nobel Chemicals B.V., No. 01-2118 (May 14, 2007) ("Diamond I"); Diamond Chemical Co. v. Akzo Nobel Chemicals B.V., No. 01-2118 (Jul. 10, 2007); George Washington University press release, July 11, 2007.

15 Ashley Roberts, *Law School Gets $5.1 Million to Fund New Center*, GW Hatchet (Dec. 3, 2007).

16 Bruce Mohl, *Reilly Turns to Private Enforcement of Item Pricing*, Boston Globe (June 27, 2004) (settlement of consumer fraud litigation with $3.2 million to the private attorneys, $3.9 million to "an eclectic group of charitable, consumer, and nonprofit groups," and $425,000 to the Massachusetts Attorney General's Office).

17 *See* http://www.impactfund.org/New/pages/support/cypres.htm.

18 Ameet Sachdev, *Charities Reaping Lawsuit Dividends*, Chi. Tribune (Sep. 9, 2007).

19 Richard A. Epstein, *The Deferred Prosecution Racket*, Wall St. J. (Nov. 28, 2006).

20 § 3.08. *See also* Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423 (2d Cir. Jan. 4, 2007); Liptak, *supra* note 12.

21 Fears v. Wilhelmina Model Agency, Inc., No. 02 Civ 4911 (S.D.N.Y. Jul. 5, 2007).

22 Public Act 095-0479, codified at 735 ILCS 5/2-807 (2007).

23 28 U.S.C. § 1712(e).

Class Action Tolling in Mass Tort Personal Injury Litigation

Continued from page 4

plaintiffs on notice of their claims. One Pennsylvania court, for example, held that events giving rise to extensive media coverage of a medical device triggered discovery as a matter of law because the coverage would have put anyone exercising "due diligence" on notice of his or her claims.[6] In *Martin v. Dalkon Shield Claimants Trust*, the plaintiff brought a product liability lawsuit over an allegedly defective contraceptive device, and the defendant moved for summary judgment on the ground that the plaintiff's claim was time-barred. In granting the defendant's motion, the court observed that the plaintiff failed to make any inquiry regarding the cause of her injury in the face of, *inter alia*, "published news accounts, articles in medical journals and reports by the Food and Drug Administration" confirming a link between IUDs and spontaneous abortions.[7] Accordingly, the court refused to apply the discovery rule, reasoning that where "a plaintiff fails to obtain information which is readily available, she has not acted with reasonable diligence."[8]

Some courts have been careful to emphasize that the plaintiff need not have actually been aware of the news coverage. Because the discovery rule is an objective test, what is relevant is whether the coverage was so substantial as to put a *reasonable* plaintiff on notice.[9] Thus, the same media event that precipitates a mass tort might also trigger accrual for statute-of-limitations purposes. But the statute-of-limitations inquiry will usually not stop there. Once a plaintiff files the first class action in a nascent mass tort—an event that not uncommonly transpires within days of media coverage—a question of tolling arises. In mass-tort personal injury cases, such tolling should not be available. But in order to explain why this is so, it is first necessary to explain the origin and application of the *American Pipe* doctrine.

II. The *American Pipe* Doctrine as Originally Conceived

In *American Pipe & Construction Co. v. Utah*, the U.S. Supreme Court held that "the commencement of a class action suspends the applicable statute of limitations as to all asserted members of the class who would have been parties had the suit been permitted to continue as a class action."[10] Under the *American Pipe* rule, former members of a putative class can toll limitations periods to preserve their right to file suit in the event that their class is not certified.[11] The Court reached that conclusion after considering the purposes of statutes of limitations and of Rule 23, the federal class action rule.

First, the Court noted that Rule 23 was adopted to improve the efficiency of the class action device, in part "to avoid, rather than encourage"—as the old class-action rule had done—"unnecessary filing of repetitious papers and motions."[12] But because class certification decisions could often linger beyond the end of limitations periods—as had happened in the *American Pipe* case itself—this efficiency purpose of Rule 23 would be undermined unless plaintiffs could count on the pendency of the action to toll their claims. Otherwise, "class members would be induced to file protective motions to intervene or to join in the event that a class was later found unsuitable."[13]

Second, the Court found it important that the class members had acted reasonably in relying upon the pendency of the class action. It explained that certification had been denied (1) "'not for failure of the complaint to state a claim on behalf of the members of the class (the court recognized the probability of common issues of law and fact respecting the underlying conspiracy);'" (2) "'not for lack of standing of the representative;'" and (3) not "'for reasons of bad faith or frivolity.'"[14] Rather, class certification had been denied by the district court "solely because of failure to demonstrate that 'the class is so numerous that joinder of all members is impracticable.'"[15] "[A]t least where class action status has been denied" on these grounds, the Court held, tolling is appropriate.[16] Otherwise, in cases "where the determination to disallow the class action [is] made upon considerations that may vary with such subtle factors as experience with prior similar litigation or the current status of a court's docket, a rule requiring successful anticipation of the determination of the viability of the class would breed needless duplication of motions."[17]

Third, the Court noted that its tolling rule would not, as applied in *American Pipe*, disturb the purposes of the statutes of limitations. "The policies of ensuring essential fairness to defendants and barring a plaintiff who 'has slept on his rights'... are satisfied when" the class action is such that it "notifies the defendants not only of the substantive claims being brought against them, but also the number and generic identities of the potential plaintiffs who may participate in the judgment."[18] Thus, the Court was satisfied that such class actions provide defendants with "the essential information necessary to determine both the subject matter and size of the

prospective litigation," the primary concerns addressed by limitations rules.[19]

Justice Blackmun, joining the opinion and concurring in the judgment, nonetheless issued a word of caution. "Our decision... must not be regarded as an encouragement to lawyers in a case of this kind to frame their pleadings as a class action, intentionally, to attract and save members of the purported class who have slept on their rights."[20] He also noted that tolling would be limited to cases like the one before the Court, where the claims "invariably will concern the same evidence, memories, and witnesses as the subject matter of the original class suit,"[21] a sentiment that would later be echoed by other justices on the Court.[22]

III. American Pipe in Mass Tort Cases

Most courts have assumed that *American Pipe* tolling principles apply to any pending class action, regardless of the nature of the substantive claims raised. This reading of *American Pipe* is too uncritical. Savvy plaintiff lawyers are aware of the benefits of this approach to the doctrine, and have exploited it precisely to serve this purpose of extending limitations periods by filing class actions that in truth have no hope of certification.[23] The problem for both sides is that the oftentimes successful attempt to expand limitation periods delays resolution of mass torts, to the detriment of plaintiffs who did file their suits in a timely manner and defendants who seek to put a mass tort behind them.

The reasoning of the *American Pipe* decision does not translate well to the mass-tort context. First, because mass-tort cases are almost never certified, they are not the kinds of cases that present certification decisions that hinge on subtle distinctions. Parties on both sides can safely predict that certification will be denied; the only question is when. Reliance on a pending class is thus unreasonable in the mass tort context. The case in *American Pipe*, by contrast, was one of a genre of cases whose prospects for certification entailed "considerations that may vary with... subtle factors" and thus made difficult "successful anticipation of the determination of the viability of the class,"[24] making reliance on the possibility of certification reasonable.

Furthermore, the individualized nature of personal injury claims is such that a defendant is not fairly put on notice of all the claims against him by the filing of a class action. Such cases typically involve widely varying facts with respect to the nature of the injury, the character and duration of exposure to the harmful product, family and medical history, the content of any warning read by or available before or at the time of injury, and a host of other factors unique to each plaintiff. Not surprisingly, each case in a mass tort requires extensive individualized discovery, involving "evidence, memories, and witnesses" that are unique to each case, including, by way of example, family members, treating physicians, and other witnesses and documents to which defendants cannot possibly have access without knowing the actual identity of each plaintiff. Defendants have no way of knowing the number of claims that would be encompassed by such an action, let alone the identities of the witnesses or their evidence. Personal injury suits in the mass tort context are thus unlike the *American Pipe* case, in which the Court noted the "probability of common issues of law and fact,"[25] and in which there could be no doubt that individual claims "invariably will concern the same evidence, memories, and witnesses as the subject matter of the original class suit."[26]

In addition, as previously discussed, extending the doctrine to mass-tort personal injury cases has encouraged plaintiff lawyers to file class actions merely to achieve an illegitimate tolling benefit for unnamed members of the purported class. They are thus precisely the kinds of cases Justices Blackmun and Powell warned about in their concurring opinions in *American Pipe* and *Crown, Cork*. In mass tort personal injury cases, tolling serves no efficiency purpose—the solitary virtue of *American Pipe* tolling—because the vast majority of plaintiffs file individual complaints notwithstanding the hypothetical availability of class-action tolling. Indeed, in many cases *American Pipe* is all the more unnecessary in light of tolling agreements reached by parties which waive limitations defenses for those plaintiffs who sign up before the time on their claims has run out. By saving the courts from excess filings, plaintiffs who sign such agreements serve the purposes of *American Pipe*. It would thus be redundant at best and counterproductive at worst to apply *American Pipe* tolling to the mass tort context.

Finally, class action tolling in the context of mass tort proceedings also leads to injustice. If plaintiffs are allowed to slumber and not assert their claims while others have pursued their claims in mass litigation, the parties—plaintiffs and defendants alike—cannot get a grasp of the size or scope of the litigation until years after the deadlines contemplated by the applicable statutes of limitations. Without understanding the size or scope of the litigation, the parties are shackled in searching for ways to resolve the litigation, leaving the claims of individual plaintiffs—some of whom may be ill or elderly, languishing until the doors are deemed closed.

Not every court has been blind to the disconnect between the policy underpinnings of *American Pipe* and the realities of mass tort litigation. Several jurisdictions have held that *American Pipe* tolling is simply unavailable for mass-tort personal injury cases. These courts have looked to the purposes of *American Pipe* and found them to be ill-served by applying the doctrine to such cases, because mass tort personal injury cases are widely recognized as uncertifiable and because the varying nature of personal injury claims are such that the details of one plaintiff's case do not generally put a defendant on notice of the claims of nameless class members. On the basis of these considerations, the more carefully reasoned opinions on the issue have uniformly rejected tolling.[27]

Other courts have limited the application of *American Pipe,* but have thus far refused to discard it fully in the mass-tort context. In New Jersey, for example, an appellate court held that *American Pipe* should be available in mass-tort litigation, but strongly suggested that such tolling should be available only where a plaintiff seeking to avail himself of its tolling benefit could prove that he actually relied upon a pending class action.[28] Other states have limited *American Pipe* tolling to class actions that were filed in courts within the same state, refusing to allow "cross-jurisdictional" tolling.[29] These rulings constrain the application of *American Pipe* tolling in the mass tort context, but they all proceed from the premise that such tolling should be available in the first place. Courts that have not already addressed the issue should go further and bar or substantially limit the application of *American Pipe* tolling in mass tort personal injury cases.

CONCLUSION

The *American Pipe* doctrine is an ill-suited transplant for mass tort personal injury litigation. Although a parallel exists at the most general level between the facts of *American Pipe* and the average mass tort plaintiff defending the timeliness of his or her claim by pointing to a pending personal injury class action—both address the intersection between class actions and statutes of limitations—the reasoning of *American Pipe* simply does not translate in this foreign context. Neither of the purposes served by tolling in *American Pipe*—efficiency of the litigation and fair notice to defendants of the number and nature of claims against them—is served by tolling in the mass tort context. To the contrary, it is the potential abuses warned of, but not present, in *American Pipe* that are facilitated by the application of its tolling rule in the mass tort setting. For these reasons, courts should carefully analyze claims for tolling in mass tort cases and decline the invitation to follow *American Pipe* as a universal rule.

** Jessica Miller is a Partner and Geoffrey Wyatt is an Associate in the Washington, D.C. office of O'Melveny & Myers, LLP.*

Endnotes

1 414 U.S. 538 (1974).

2 *See, e.g.*, Foster v. Harris, 633 S.W.2d 304, 305 (Tenn. 1982).

3 *Id.* Some states observe a stricter rule, under which a claim accrues upon discovery of injury, even if the identity of a tortfeasor is unknown. *E.g.*, Robinson v. Graves, 456 So. 2d 793, 794-95 (Ala. 1984) (holding that tolling of statute of limitations in absence of a known defendant is only possible by filing a claim against a fictional defendant). A shrinking minority of states observe no general discovery rule at all. *E.g.*, Johnston v. Dow & Coulombe Inc., 686 A.2d 1064, 1065-66 (Me. 1996) (explaining discovery rule is recognized only in "three discrete areas: legal malpractice, foreign object, and negligent medical malpractice and asbestosis"); *see also* Griffin v. Unocal Corp., No. 1061214, --- So. 2d ---- (Ala. Jan. 25, 2008) (adopting discovery rule for period during which a plaintiff is unaware of latent injury).

4 Burnett v. N.Y. Cent. R. Co., 380 U.S. 424, 428 (1965) (quoting Order of Railroad Telegraphers v. Railway Express Agency, Inc., 321 U.S. 342, 348-49 (1944)).

5 *Id.*

6 *See* Martin v. Dalkon Shield Claimants Trust, No. 93-2652, 1994 U.S. Dist. LEXIS 16395, at *11-12 (E.D. Pa. Nov. 20, 1994).

7 *Id.*

8 *Id.* at *11.

9 *E.g.*, Miller v. A.H Robins Co., Inc., 766 F.2d 1102, 1106 (7th Cir. 1985).

10 414 U.S. 538, 554 (1974).

11 Originally, *American Pipe*'s rule applied only to "purported members of the class who make timely motions to intervene after the court has found the suit inappropriate for class action status," *id.* at 553, but the rule was later extended. *See* Crown, Cork & Seal Co. v. Parker, 462 U.S. 345, 350 (1983) ("[t]he filing of a class action tolls the statute of limitations 'as to all asserted members of the class,' not just as to intervenors" (quoting *American Pipe*, 414 U.S. at 554)).

12 *Id.* at 550.

13 *Id.* at 553.

14 *Id.* (quoting State v. Am. Pipe & Constr., 473 F.2d 580, 584 (1973)) (omitting footnote).

15 *Id.* at n.9.

16 *Id.* at 552.

17 *Id.* at 553-54.

18 *Id.* at 554-55 (quoting Burnett v. New York Central Railroad Co., 380 U.S. 424, 428 (1965)).

19 *Id.* at 555.

20 *Id.* at 561 (Blackmun, J., concurring).

21 *Id.* at 562.

22 *See* Crown, Cork & Seal Co. v. Parker, 462 U.S. 345, 355 (1983) (Powell, J., concurring) ("[W]hen a plaintiff invokes *American Pipe* in support of a separate lawsuit, the district court should take care to ensure that the suit raises claims that 'concern the same evidence, memories, and witness as the subject matter of the original class suit,' so that 'the defendant will not be prejudiced.'" (quoting *American Pipe*, 414 U.S. at 562 (Blackmun, J., concurring))).

23 *See* Mitchell A. Lowenthal & Norman Menachem Feder, *The Impropriety of Class Action Tolling for Mass Tort Statutes of Limitations*, 64 Geo. Wash. L. Rev. 532, 573 (1996) ("The message, at least to cynics, is that by filing a class action on behalf of the client you found today you may be able to represent the client you only find tomorrow.").

24 414 U.S. at 553-54,

25 *Id.* at 553.

26 *Id.* at 562 (Blackmun, J., concurring).

27 *See, e.g.*, Jolly v. Eli Lilly & Co., 751 P.2d 923, 937-38 (Cal. 1988) (admonishing that personal injury plaintiffs "would be ill advised to rely on the mere filing of a class action complaint to toll their individual statute of limitations. *The presumption, rather, should be to the contrary*...." (emphasis added)); *see also* Philip Morris USA, Inc. v. Christensen, 905 A.2d 340, 358-60 (Md. 2006) (expressing support for *Jolly*'s presumption against tolling in the mass tort context); *In re* Rezulin Prods. Liab. Litig., MDL No. 1348, 2005 WL 26867, at *3 (S.D.N.Y. Jan. 5, 2005) (noting that the "wisdom of adopting the *American Pipe* rule in mass tort cases is, to say the least, highly debatable"); Barela v. Showa Denko K.K., No. 93-1469 LH/RLP, 1996 U.S. Dist. LEXIS 7830, at *16 (D.N.M. Feb. 28, 1996) (expressing doubt whether a federal court should adopt *American Pipe* tolling for a state that had not adopted the doctrine in a mass-tort personal injury case in light of the fact that "most federal courts... refuse to permit the use of the class-action device in mass-tort cases" (citation and internal quotation marks omitted)).

28 *See* Staub v. Eastman Kodak Co., 726 A.2d 955, 967 (N.J. Supr. Ct. App. Div. 1989).

29 *See, e.g.*, Portwood v. Ford Motor Co., 701 N.E.2d 1102, 1103, 1105 (Ill. 1998).

FACTA Truncation:
Applicable to the Digital World?

Continued from page 5

customer selects the item(s) for purchase and begins the checkout process. The process varies to some extent between retailers, but generally speaking the first step will be to provide identification and contact information such as your name, address, the shipping address (if different than the billing address), an email address for confirming emails, and a retyping of your email address to confirm it and other non-financial information. Often, that non-financial identification information is confirmed with the next screen, identifying either that the information has been input correctly or—as many online shoppers are all too familiar—that the highlighted boxes where the customer has failed to provide the information or input it incorrectly.

Once the name, address, and contact information are conveyed the customer is asked to provide financial information to begin the process of making the purchase. That information includes the type of credit or debit card you are using (VISA, MasterCard, Discover), your credit card number, your expiration date, and your CVV code number (often referring you to the three digits on the back of your card or four digits on the front.)[7] Typically, after inputting the financial information, that information, along with your order, are confirmed on the next screen. Once the order is placed, you may receive any combination of (1) an order confirmation email, (2) an order shipped email, and/or (3) a receipt email. Sometimes, rather than a receipt sent by email, the receipt is shipped with the product.

Comparatively, the online transaction is more complex and contains multiple steps, unlike the simple and routine credit or debit transaction at a brick and mortar retailer. Consequently, the online transaction does not lend itself cleanly and easily to a FACTA analysis—but that has not deterred plaintiffs from seeking its application and courts from wrestling with FACTA's scope.

The Courts Begin to Weigh-In

Three cases in particular have begun to shape the landscape for internet transaction FACTA cases—*Stubhub,*[8] *MovieTickets.com,*[9] and *Bose.*[10]

Stubhub. The *Stubhub* case, decided July 2, 2007, was the first to comment on one of the key issues unique to FACTA internet cases: can the requirement that the

defendant "electronically print" the receipt be satisfied by an electronic email receipt sent to the plaintiff?

Stubhub is an online ticket broker for concerts and sporting events and, according to its website, "[t]he largest ticket marketplace in the world, based on sales."[11] According to the plaintiff, Stubhub violated FACTA by "provid[ing] Plaintiff with one or more electronically printed receipts on each of which Defendants printed... the expiration [date] of Plaintiff's credit or debit card."[12] These alleged "electronically printed receipts" were emails sent to the plaintiff. Stubhub moved to dismiss the plaintiff's complaint, arguing that it "does not and indeed cannot state a claim for relief under [15 U.S.C. §] 1681c(g) because [Defendant] did not 'print' the [receipt] within any reasonable interpretation of the word."[13]

The court correctly noted that the term "print" is not defined in the statute.[14] The court further stated that "the statute should be construed to give the term its ordinary meaning,"[15] and that "[d]ictionary definitions are commonly consulted to 'clarify'... ordinary meanings."[16]

With that, the court seemed poised to entertain the battle of competing definitions. *Webster's Third New Int'l Dictionary* provides that "print" means "to make an impression in or upon."[17] But the court noted that, for example, the *Merriam-Webster's Collegiate Dictionary*, 10th ed., defines "print" as "to display on a surface (as a computer screen) for viewing." It seemed like a fair fight until the court held that even the definition cited by Stubhub supports the plaintiff's position. Without any elaboration, it held that "Plaintiff's [Complaint] is consistent with the claim that Defendant 'made an impression' on Plaintiff's computer screen including credit or debit card information in violation of 15 U.S.C. § 1681c(g)."[18] Concluding that an email is sufficient to meet the print requirement, the motion to dismiss was denied.[19]

Interestingly, however, although the motion was denied and the court had made no finding that the statute was ambiguous on its face, the court went on, in dicta, to address the "intent of Congress" in enacting FACTA. The court stated, "had Congress desired [to exclude online transactions], they would have explicitly done so, as they did for 'transactions in which the sole means of recording a credit card or debit card account number is by handwriting or by and imprint or copy of the card.... Failure to do so supports Plaintiff's interpretation of 'print' as being facially reasonable."[20] But in *MovieTickets.com* the same "language of the statute" analysis was considered—with a quite different result.

MovieTickets.com. On February 13, 2008, Judge Gold of the United States District Court, Southern District of Florida, expressly declined to follow *Stubhub* and *1-800-Flowers.com*, "because neither considered the plain meaning of the word 'printed,' within the context of the entire § 1681c(g)...."[21] On that basis, the court granted defendant MovieTicket.com's motion to dismiss.

In that decision, it noted that "[a]lthough the word 'print' in § 1681c(g) is not defined in the statute, the meaning of 'print' in § 1681c(g) is crucial to this case."[22] In attempting to determine the meaning of "print," the court said that several canons of statutory construction guided its analysis of these issues.[23] In applying the canons of statutory construction, the court stated:

> [C]ourts always begin the interpretation of a statute by looking at the plain language of the statute itself[24].... Court's 'read the statute using the normal meanings of its words,' while considering the entire context of the statute[25].... To this end, canons of construction are tools which assist courts in focusing on the context of the entire statute, as opposed to looking at one word in isolation[26].... Applying these canons of statutory construction, I conclude that the plain meaning is evident from the language of the statute.[27]

To that end, the court held that, "[b]y emailing Plaintiff an 'Order Confirmation,' Defendant has not printed a receipt under 1681c(g)."[28] The court, in so holding, stated that "Plaintiff does not allege that Defendant ever sent Plaintiff physical, paper copy of the emails at issue."[29] Here, the court also relied upon a dictionary definition of "print," this time turning to *Webster's New World Dictionary*, 2d College Ed.:

> 1. to mark by pressing or stamping; make a print on or in 2. to press or stamp (a mark, letter, etc.) on or in a surface 3. to draw, trace, carve, or otherwise make a (a mark, letter, etc.) on a surface 4. to produce on the surface of (paper, etc.) the impression of ink type, plates, etc. by means of a printing press....[30]

The court stated that based on these dictionary definitions of "print," one draws the "common sense impression that a 'printed' item is something physical and tangible that can be impressed or marked upon, such as a printed paper."[31] Confirming his common sense impression, Judge Gold stated that "[w]hen § 1681c(g) is looked at as a whole, it is clear that this subsection focuses on paper receipts electronically printed by a cash register or other machine and provided to consumers at the point of sale or transaction."[32]

In contrast to *Stubhub*, where the court concluded that the statute was silent on excluding internet transactions from FACTA's scope, the *MovieTickets.com*

court found silence to have a different impact. "[T]he language of the statute only addresses printed receipts [meaning, according to this Court, physically printed on paper at the point of sale].... Congress included no language to specifically extend the statute's restrictions to email transmissions, and such silence is controlling."[33]

Bose. In *Ehrheart v. Bose Corporation,* the United States District Court for the Western District of Pennsylvania wrestled with a different issue. In *Bose* the issue was where (or when) the "point of the sale or transactions" lies in an internet FACTA case.[34]

The facts were simple and undisputed. The plaintiff—about one week after FACTA went into effect—telephoned the Bose Factory Store to purchase headphones with her credit card.[35] The headphones were shipped and there was a receipt in the package, exactly as she would have received in the store, containing her credit card's expiration date.[36] Although Ehrheart did not experience identity theft or any other harm as a result of the receipt containing her credit card's expiration date, she filed suit against Bose—one of several she filed against various defendants under FACTA—seeking statutory damages, and to certify a class of similarly situated individuals.[37]

Bose argued that because the order was taken over the phone, Ehrheart was not provided an electronically printed receipt at "the point of the sale or transaction."[38] Bose argued that the point of the sale or transaction "denotes a "precise location within a store."[39] Ehrheart responded that "the phrase [point of the sale] refers not to a place, but 'to an event in time, *i.e.*, when payment (or exchange) is being made with a merchant.'" [40]

The court, finding that this was a question of first impression, denied the underlying motion, concluding that FACTA could apply even though the transaction took place over a phone, and not face-to-face. In reaching that conclusion, the court also commented not that there is not a point of sale (a physical location) because it is a telephonic transaction, but rather, that the point of sale is a "time or event":

> The Plaintiff points out that although Congress has used the term "point of sale" to apply to a location, it has also used the phrase to identify a point in time. For example, Section 707(b)(5) of the National Oilheat Research Alliance Act of 2000, 42 U.S.C. § 6201, (repealed), addressed assessments on oil imported by the owner "after the point of sale". *See* § 707(b)(5). She also cites case law in which the term "point of sale" was used to refer to a foreclosure sale in a bankruptcy proceeding. *In re Lenton Brunson McGill*, 78 B.R. 777, 779 (Bankr.D.S.C.1986). According to Ehrheart, logic requires the court to find that the phrase "point of sale or transaction" is ... meant to refer to the sale or transaction itself, thereby excluding all other instances where a cardholder may, for legitimate reasons, request and be provided with a receipt bearing their [sic] credit/debit card information."
>
> * * *
>
> Having carefully reviewed the parties' submissions on this issue against the background of relevant law, the court is convinced that there is no definitive legal authority addressing the meaning to be assigned to the phrase "point of sale or transaction" as that phrase is used in FACTA. The words do not appear to have a fixed meaning, but have been defined instead by the context in which they are used. The term has been applied to denote a time or an event, as opposed to a location.[41]

With these three cases the courts have begun to wrestle with the question of whether FACTA applies to internet transactions and, if so, how it applies. The decisions reflect that the issue is far from settled. The vast differences between them raise yet another interesting question: if the courts cannot agree on whether FACTA applies to internet transactions, how can any retailer have acted willfully (knowingly or recklessly) in allegedly violating the statute?

** Shawn J. Organ, a partner in the Columbus, Ohio office of the international law firm of Jones Day, is a trial lawyer who focuses his practice in the areas of complex litigation, such as class action defense work, including several FACTA cases.*

Endnotes

1 Ted Frank, *Omission in FACTA Might Be Windfall for Plaintiff's Bar*, Class Action Watch, September 2007; Shawn J. Organ & Mark Herrmann, *If Your Company Accepts Credit Cards, You Need to Read This*, The Metropolitan Corporate Counsel, October 2007; Shawn J. Organ & Kasey Ingram, *FACTA Truncation – A Small Answer to Identity Theft or a Big Problem for Businesses?*, CCH Financial Privacy Law Guide, Oct. 17, 2007.

2 The Fair Credit Reporting Act ("FCRA"), 15 U.S.C § 1681c(g)(1).

3 There are cases alleging a violation of the truncated credit card number requirement, but they are relatively few.

4 In the suit against Cost Plus the court noted that the company's net worth is approximately $316 million, with net income for fiscal 2005 of approximately $20 million, yet plaintiffs were seeking between $340 million and $3.4 billion for alleged violations related to the truncation of the expiration date. Spikings v. Cost Plus, Inc., Case No. CV 06-8125-JFW (AJWx), 2007 U.S. Dist. LEXIS 44214, at *4 (C.D. Cal. May 25, 2007).

5 § 1681c(g):

(g) Truncation of credit card and debit card numbers

(1) In general

Except as otherwise provided in this subsection, no person that accepts credit cards or debit cards for the transaction of business

shall print more than the last 5 digits of the card number or the expiration date upon any receipt provided to the cardholder at the point of the sale or transactions.

(2) Limitation

This subsection shall apply only to receipts that are electronically printed, and shall not apply to transactions in which the sole means of recording a credit card or debit card account number is by handwriting or by an imprint or copy of the card.

(3) Effective date

This subsection shall become effective –

(A) 3 years after December 4, 2003, with respect to any cash register or other machine or device that electronically prints receipts for credit card or debit card transactions that is in use before January 1, 2005; and

B) 1 year after December 4, 2003, with respect to any cash register or other machine or device that electronically prints receipts for credit card or debit card transactions that is first put into use on or after January 1, 2005.

6 There is active debate over what, if any, import the expiration date has related to identity theft. "Some credit industry watchers believe that, like the appendix, a credit card expiration date is one of those things that used to be a lot more practical than it is now." Dana Dratch, *Why Do Credit Cards Expire?*, www.bankrate.com/brm/news/cc/20050202a1.asp. While one credit card company and some banks acknowledge that the expiration date provides one more verification point for fraud protection *in manually processed transactions* (if expired, the card is rejected), in the United States that is of little significant because manually processes transactions are rare. *Id*. What all banks agree upon, however, is that having an expiration date allows: (1) the card to be replaced periodically, before the magnetic strip wears out; (2) updates to the magnetic strip, where information is stored, and (3) the bank a reason to be in communication with their consumer every so often to market other services. *Id*.

7 This is the Card Verification Value code ("CVV"). This is an authentication feature developed by the credit card companies to reduce fraud in internet transactions. It requires the cardholder to enter the information during the transaction to prove that the consumer has the card in their hand. It is a three or four digit code that provides a cryptographic check of the information embossed on the card. Each credit card company has its own name for the CVV code, but it works the same for each credit card company. Visa refers to the code as "CVV2"; MasterCard calls it "CVC2"; American Express and Discover refer to the code as the "Card ID" or "CID".

8 Vasquez-Torres v. Stubhub, Inc., Case No. CV 07-1328 (PSG) (SSx), 2007 U.S. Dist. LEXIS 63719 (C.D. Cal. July 2, 2007)

9 King v. MovieTickets.com, Case No. 07-22119-Civ-Gold/Turnoff, Order Granting Motion to Dismiss (S.D. Fla. Feb. 13, 2008) at 11 (MovieTickets.com Decision at __").

10 Ehrheart v. Bose Corp., Case No. 07-350, 2008 WL 64491 (W.D. Pa. Jan. 4, 2008).

11 Http://stubhub.com/about-us.

12 Vasquez-Torres v. Stubhub, 2007 U.S. Dist. LEXIS 63719 (C.D. Cal. July 2, 2007) at *1.

13 *Id.* at *2.

14 *Id*.

15 *Id.* at *6 (citing BP Am. Prod. Co. v. Burton, 127 S.Ct. 638, 643, 166 L. Ed. 2d 494, 502 (2006).

16 *Id.* at *6-*7 (citing U.S. v. Carter, 421 F.3d 909, 911 (9th Cir. 2005)).

17 *Id.* at *7.

18 *Id*.

19 In a similar case, *Grabein v. 1-800-Flowers.com, Inc*., Case No. 07-22235 (S.D. Fla. Jan 29, 2008)(Huck, J.), that Court also denied a motion to dismiss largely following the *Stubhub* analysis.

20 Vasquez-Torres v. Stubhub, 2007 U.S. Dist. LEXIS 63719 (C.D. Cal. July 2, 2007) at *9.

21 King v. MovieTickets.com, Case No. 07-22119-Civ-Gold/Turnoff, Order Granting Motion to Dismiss (S.D. Fla. Feb. 13, 2008) at 11 (MovieTickets.com Decision at __").

22 MovieTickets.com Decision at 6.

23 *Id.*

24 *Id.* at 6-7 (citing Snapp v. Unlimited Concepts, Inc., 208 F.3d 928, 934 (11th Cir. 2000).

25 *Id.* at 7 (citing Penn v. City of Montgomery, 381 F.3d 1059, 1062 (11th Cir. 2004)("We do not look at one word or term in isolation, but instead we look to the entire statutory text.").

26 *Id.* (citing CBS, Inc. v. Primetime 24 Joint Venture, 245 F.3d 1217, 1225 (11th Cir. 2001)).

27 *Id.* at 7-8.

28 *Id.* at 8.

29 *Id* at 10.

30 The court also noted that "Print," as defined in the online Merriam-Webster Dictionary (www.m-w.com), as of February 7, 2008, is (1)(a) "to impress something in or on" (b) "to stamp (as a mark) in or on something."

31 MovieTickets.com Decision at 9.

32 *Id.* at 10.

33 *Id*. (citing CBS, Inc. v. Primetime 24 Joint Venture, 245 F.3d 1217, 1226 (11th Cir. 2001)).

34 Ehrheart v. Bose Corp., Case No. 07-350, 2008 WL 64491 (W.D. Pa. Jan. 4, 2008).

35 *Id*. at *2.

36 *Id*.

37 *Id*.

38 *Id*. at *3.

39 *Id*.

40 *Id.*

41 *Id*. at *4 (citing *See e.g.,* Utica Mut. Ins. Co. v. Bancinsure, Inc., No: 4-06-cv664, 2007 WL 2860237 at * 11 (E.D.Missouri, September 25, 2007) (evaluating fraud after the point of sale when customers attempted to return purchases); Caremark, Inc. v. Goetz, 395 F.Supp.2d 683, 692 (D.Tenn.2005) (noting that insurer reimbursed at a lower rate for claim filed after the point of sale); Anderson v. Equitable Life Assur. Soc'y. of U.S., 248 F.Supp.2d 584, 592 (S.D.Miss.2003) (assessing whether there had been fraudulent concealment after the point of sale when plaintiffs were sent annual policy summaries); Ford Motor Co. v. Lloyd Design Corp., 184 F.Supp.2d 665, 676 (E.D.Mich.2002) (protecting trademarks required that court tolerate at least some confusion as to source or sponsorship after the point of sale).

The Federalist Society takes seriously its responsibility as a non-partisan institution engaged in fostering a serious dialogue about legal issues in the public square. We publish original scholarship on timely and contentious issues in the legal or public policy world in an effort to widen understanding of the facts and principles involved and to continue that dialogue. Positions taken on specific issues in publications, however, are those of the author and not necessarily reflective of an organization stance. **Class Action Watch** presents articles on a number of important issues, but these are contributions to larger ongoing conversations. We invite readers to submit opposing perspectives or views to be considered for publication and to share their general responses, thoughts and criticisms by writing to us at info@fed-soc.org. Additionally, we happily consider letters to the editor.

The Federalist Society
For Law and Public Policy Studies
1015 18th Street, N.W., Suite 425
Washington, DC 20036