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Civil Procedure—Class Actions

Supreme Court Gives Rule 23 Primacy Over State Law Limiting Class Actions

A plaintiff meeting the criteria of Fed. R. Civ. P. 23 may maintain a class action in a federal diversity suit even if the forum state's law would bar such a class action in state court—at least when the state law is not ''intimately bound up in the scope of a substantive right or remedy,'' a splintered U.S. Supreme Court held March 31 (*Shady Grove Orthopedic Associates PA v. Allstate Insurance Co.*, U.S., No. 08-1008, 3/31/10).

The result was that a health care provider suing an insurance company for interest on late claims payments could maintain a class action in federal district court in New York, despite a New York law, N. Y. C. P. L. R. § 901(b), providing that a suit to recover a ''penalty . . . may not be maintained as a class action'' unless specifically authorized by law.

Experts told BNA that the ruling is likely to result in more displacement of state law by federal law, but that states have avenues available to limit that outcome.

Five Agree on Judgment, Not Entirely on Rationale. Five justices agreed that the state law here was on a collision course, in diversity suits, with Rule 23. ''Rule 23 unambiguously authorizes *any* plaintiff, in *any* federal civil proceeding, to maintain a class action if the Rule's prerequisites are met. We cannot contort its text, even to avert a collision with state law that might render it invalid,'' Justice Antonin Scalia wrote for the majority on that point.

Scalia then examined whether Rule 23 is valid under the Rules Enabling Act, 28 U.S.C. § 2072, which says that federal rules of procedure ''shall not abridge, enlarge or modify any substantive right.'' Joined by Chief Justice John G. Roberts Jr. and Justices Clarence Thomas and Sonia Sotomayor, Scalia wrote that the rule is valid, reasoning that ''compliance of a Federal Rule with the Enabling Act is to be assessed by consulting the Rule itself . . . . In sum, it is not the substantive or procedural nature or purpose of the affected state law that matters, but the substantive or procedural nature of the Federal Rule.''

Justice John Paul Stevens, who concurred fully with the first step of Scalia's analysis finding the state and federal class action rules in conflict, also agreed that Rule 23 does not violate the Rules Enabling Act. But he reached the latter conclusion by a different route than Scalia. Stevens said that the Rules Enabling Act's command that a federal procedural rule ''not abridge, enlarge or modify any substantive right'' requires courts to focus on the state law affected, not solely on the federal rule. The federal rule complies so long as it does not displace a state law that defines substantive rights, Stevens said. He concluded that Section 901(b) was procedural, and thus properly overridden by Rule 23.

The court reversed the ruling of the U.S. Court of Appeals for the Second Circuit that Section 901(b) concerned a different issue from Rule 23—a suit's eligibility for class treatment rather than the criteria for class certification—and thus did not conflict with it.

Justice Ruth Bader Ginsburg, in a dissent joined by Justices Anthony M. Kennedy, Stephen G. Breyer, and Samuel A. Alito Jr., said the Supreme Court should ''not have read Rule 23 to collide with New York's legitimate interest in keeping certain monetary awards reasonably bounded. I would continue to interpret Federal Rules with awareness of, and sensitivity to, important state regulatory policies.'' She argued that Section 901(b) is ''remedial'' and substantive, affecting how a class action ''must end,'' while Rule 23 ''prescribes the considerations relevant to class certification and postcertification proceedings—but it does not command that a particular remedy be available when a party sues in a representative capacity.''

'Delicious' Irony? ''The irony here is delicious,'' John C. Coffee Jr., a professor at Columbia Law School, New York, told BNA. ''We have Justice Scalia broadly authorizing a class action in federal court that New York State would not permit in state court, over the dissent of Justice Ginsburg who says such a class action results in overkill and New York State appropriately wanted to prevent that.''

Coffee cautioned that the majority implied ''that there would be a way for New York State to realize its interest and achieve its policy goals here. They could adopt a statutory limitation on the damages assessable in any one case for the violation of a New York state statute.'' Indeed, he said, ''The real message here for states is they're going to have to be subtler.''

State substantive rules retain some force because Stevens's opinion is controlling as the ''narrowest ground that a majority agrees upon,'' Erwin Chemerinsky, dean of the University of California, Irvine School of Law, told BNA in an e-mail April 1. He read Stevens's opinion as saying that ''if a federal procedural rule 'would displace a state law that is procedural in the ordinary use of the term but is so intertwined with a state right or remedy that it functions to define the scope of

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the state-created right,' then the procedural rule 'cannot govern' such a case.''

''So what is the bottom line? I think that this will mean that there are more instances in which federal law displaces state law,'' Chemerinsky said. ''The basic framework of [*Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938),] that in diversity cases state substantive law controls while federal procedural law controls remains true. But under Justice Stevens' opinion a federal court must determine whether in operation the rule is procedural or substantive. If the former, federal law controls and if the latter, state law controls.'' But the ''test is uncertain given the lack of a majority opinion and is likely to create a great deal of confusion,'' he added.

Scott Dodson, William & Mary Law School, Williamsburg, Va., who teaches civil procedure and federal courts, agreed with Chemerinsky that under *Marks v. United States*, 430 U.S. 188 (1977), Stevens's opinion is controlling. ''But the divisiveness of the Justices, and the fact that Stevens' position was joined by him alone, suggests that lower courts will continue to struggle with these questions,'' he said.

Dodson told BNA in a March 31 e-mail, ''This is an important ruling for the broader *Erie* doctrine. It sheds light on the tricky questions that arise when a Federal Rule potentially conflicts with a quasi-substantive state rule. It also exposes the divisions on the Court in these cases—divisions that create strange bedfellows among the Justices.''

The ruling's ''practical effect is that Federal Rules are more likely to trump arguably conflicting rules in federal court,'' Dodson said. ''But states have a relatively easy solution: rewrite the state rules so that they are not in conflict and so that they are strongly tied to the substantive state rights at issue. New York, for example, can obviate *Shady Grove*'s specific holding by reframing Section 901(b) as a remedies limitation rather than a class action bar,'' he said.

Brian Wolfman, a professor at Georgetown University Law Center, Washington, D.C., who is affiliated with the Public Citizen Litigation Group and represented the plaintiff, told BNA, ''I think it's a terrific result. The federal courts will remain open to state-law and federal-law class actions.'' He said the decision was important in light of the Class Action Fairness Act's effect of bringing more class actions into federal court. Speaking of CAFA's proponents, he said, ''if you want the supposed benefit [of federal court], you have to take the downside.''

Wolfman was not sure how many states had attempted to block class actions through laws like New York's. Even if they haven't enacted such laws, he said, the decision is ''a signal that they can't.'' He described the decision as ''a significant victory for people who think class actions are an important tool for justice.''

Allstate spokesman Mike Siemienas told BNA, ″The case before the United States Supreme Court involved the applicability of New York state law in federal court, not any issues pertaining to Allstate claims practices or insurance. We are disappointed and respectfully disagree with the ruling of the United States Supreme Court. We believe that New York law clearly specifies that court cases involving statutory penalties cannot be brought as a class action. The Supreme Court did not agree, and the case will now return to the U.S. District Court in New York. Today's ruling does not affect the merits of the actual case, and Allstate will continue to defend it accordingly.″

Time Is Money. Plaintiff Shady Grove Orthopedic Associates PA, a health care provider for Sonia E. Galvez, who was injured in a vehicle collision, alleged in the

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U.S. District Court for the Eastern District of New York that defendant Allstate Insurance Co. delayed a claims payment beyond the time limit allowed by New York insurance law. Shady Grove and Galvez sued Allstate for interest on the payment under the statute on behalf of a proposed class whose payments had been delayed.

Allstate argued that Section 901(b), blocking class actions for ''a penalty, or minimum measure of recovery'' unless specifically authorized in the statute, applies to class actions in federal court. The district court agreed and dismissed the case. The Second Circuit affirmed.

Argument before the Supreme Court focused largely on the substantive/procedural distinction for purposes of a federal court's obligations under *Erie* and *Hanna v. Plumer,* 380 U.S. 460 (1965).

But Scalia's opinion focused, first, on the language of Rule 23 and Section 901(b). He wrote for the court that the provisions were in conflict because they both set preconditions for whether a class action may be ''maintained.'' In the second step of his analysis, he focused on the substantive/procedural issues in the Rules Enabling Act and a court precedent. Looking to *Sibbach v. Wilson & Co.,* 312 U. S. 1 (1941), Scalia wrote, ''A Federal Rule of Procedure is not valid in some jurisdictions and invalid in others—or valid in some cases and invalid in others—depending upon whether its effect is to frustrate a state substantive law (or a state procedural law enacted for substantive purposes).'' Rather, under *Sibbach*, a federal rule complies with the Rules of Enabling Act if it ''really regulates procedure.''

Scalia acknowledged that ''*Sibbach*'s exclusive focus on the challenged Federal Rule—driven by the very real concern that Federal Rules which vary from State to State would be chaos, see 312 U.S. at 13–14—is hard to square with § 2072(b)'s terms,'' which refer to modification of substantive rights. But he said that *Sibbach* has been ''settled law'' for ''nearly seven decades,'' and that Allstate ''has not even asked us to overrule *Sibbach*, let alone carried its burden of persuading us to do so.'' Stevens's approach takes into account the language of Section 2072, but ''squarely conflicts with *Sibbach*,'' Scalia said; the dissent's approach, focusing on the ''subjective intentions'' of state legislatures, would condemn federal judges to the dreaded task of ''poring through state legislative history.''

Scalia acknowledged one effect of the decision could be forum-shopping. That result is ''unacceptable when it comes to the consequence of judge-made rules created to fill supposed 'gaps' in positive federal law,'' he said. ''But divergence from state law, with the attendant consequence of forum shopping, is the inevitable (indeed, one might say the intended) result of a uniform system of federal procedure,'' he added. Ginsburg drove the forum shopping point home, noting that Shady Grove would have been limited to a $500 interest recovery if it had filed in New York state court, while it seeks over $5 million in its federal court class action.

Scott L. Nelson, Public Citizen Litigation Group, Washington, D.C., argued for the plaintiffs. Christopher Landau, Kirkland & Ellis, Washington, D.C., argued for Allstate.

BY MARTINA BARASH AND THOMAS D. EDMONDSON

Full text at http://pub.bna.com/lw/081008.pdf and 78 U.S.L.W.