

## Class Action Fairness Act of 2005

On February 18, 2005, President Bush signed the Class Action Fairness Act of 2005 (“CAFA”) into law. CAFA was enacted with the primary intent of reducing so-called “forum shopping” by plaintiffs searching for sympathetic state courts in which to file class actions, as well as enhancing the fairness of class action settlements to class members. To achieve these goals, CAFA expands federal jurisdiction over most inter-state class actions and mandates increased judicial scrutiny of class action settlements.

### Reducing Forum Shopping

CAFA is designed to reduce “forum shopping.” Forum shopping is a practice in which plaintiffs’ attorneys file class actions in the jurisdiction with the most beneficial legislation or in a jurisdiction whose citizens have a history of assessing large damage awards; rather than filing in the jurisdiction with the greatest connection to the controversy at issue. Such jurisdictions then become magnets for more class actions. Supporters of CAFA argue that this practice produces irrational verdicts and damage awards, which in turn promotes extortionate settlements by companies that do not want to risk litigating a case through trial.

Prior to CAFA, a class action defendant could not fight forum shopping by removing the case to federal court because removal required it to demonstrate complete diversity between the parties (meaning no defendant was a citizen of the same state as any class member), which is rare in

large class actions. Also, to obtain removal, a defendant had to show that the amount in controversy exceeded \$75,000, an amount which could not be established by aggregating class members’ claims. CAFA altered these requirements, thereby enabling the removal of most large, multi-state class actions from state to federal court.

### Expanding Federal Jurisdiction for Class Actions

CAFA expands the jurisdiction of federal courts to hear class actions and alters the rules governing removal of these cases to federal court. CAFA confers on federal district courts original jurisdiction over class actions in which (1) the aggregate value of the claims exceeds \$5,000,000, (2) there are at least 100 class members, and (3) any member of the plaintiff class is a citizen of a state different from any defendant.

However, several important exceptions apply. Most notably, a federal court would not have jurisdiction where two-thirds or more of the class members and the primary defendants are citizens of the state in which the action was originally filed. Also, CAFA does not alter the jurisdictional rules that currently apply to most securities claims, and does not apply to state law claims relating to a corporation’s internal affairs.

In addition to these limitations, CAFA also confers upon federal courts discretion to decline jurisdiction over a class action in which more than one-third but less than two-thirds of class members and the primary defendants are citizens of the state

in which the action is filed. In such a case, the federal court may decline jurisdiction based upon consideration of several factors designed to assess whether the dispute is more local or more national in nature.

### Increased Judicial Scrutiny of Class Action Settlements

The other primary purpose of CAFA is to increase judicial scrutiny of class action settlements to ensure they are fair and reasonable to class members.

**Coupon Settlements.** CAFA seeks to end what its proponents view as the abusive

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practice of class action settlements in which class counsel are awarded substantial fees, but class members receive only coupons of limited value. Under CAFA, a court may only approve a proposed coupon settlement after it holds a hearing and issues a written opinion finding that the settlement is reasonable, adequate, and fair to class members. Also, CAFA ends the practice of setting attorney's fees for a coupon settlement based upon the value of coupons issued, and instead mandates that such fees be based either upon the value of the coupons that are actually redeemed, or on the amount of time class counsel spent working on the case.

**Scrutiny of "Net Loss" Settlements.** Under CAFA, a proposed settlement requiring any class member to pay sums to class counsel resulting in a net loss to the class member will not be approved unless the court finds that the non-monetary benefits to the class member substantially outweigh any such loss.

**No Geographic Discrimination.** CAFA prevents courts from approving settlements that provide greater recovery to certain class members based solely upon their geographic proximity to the court.

### CAFA Does Not Apply Retroactively

CAFA applies only to class actions filed after February 18, 2005, the date of enactment.

### Other Provisions

**Notification Requirements for Settling Defendants.** CAFA requires defendants participating in a proposed class action settlement to make specified disclosures concerning the proposal to certain state and federal officials within 10 days after a proposed settlement is filed with the court. The statute seeks to limit the burden and expense involved in satisfying these notification requirements by mandating disclosure of materials defendants generally would already possess and allowing the use of the Internet in making such disclosures.

### Report Required by the Judicial Conference.

CAFA directs the Judicial Conference of the United States to prepare a report to Congress within one year making recommendations on the best practices that courts can use to ensure fairness in class action settlements.

### Implications

The most dramatic impact of CAFA will likely be a significant reduction in the number of class actions filed in so-called "magnet" state courts, those with reputations for being plaintiff-friendly venues. It is also likely that most multi-state class actions will now be heard in federal rather than state court. CAFA does not, however, strip state courts of jurisdiction for class actions altogether. Many commentators believe that the enactment of CAFA will result in fewer class actions being filed, as well as a higher rate of dismissal or denial of class certification for those that are filed. In part, this stems from a belief that federal procedural rules for granting class certification are more restrictive than those applied in many state courts. Critics argue that CAFA will effectively eliminate many types of consumer class actions because federal class certification will not be available in the face of widely varying state laws that provide the bases for such suits. But other commentators believe plaintiffs' lawyers will find ways around CAFA, by, for example, simultaneously filing duplicate class actions in separate state courts or carefully crafting complaints to fall within one of CAFA's exceptions. Only time will tell whether any of these predictions will prove accurate.

The other major impact of CAFA will be greater judicial scrutiny of class action settlements, and a reduction in the frequency of so-called "coupon settlements." ■