NO. 17-662

IN THE

Supreme Court of the United States

AMY YANG,

Petitioner,

v.

DONALD WORTMAN, ON BEHALF OF HIMSELF AND ALL OTHERS SIMILARLY SITUATED, ET AL.,

Respondents.

On Petition for a Writ of Certiorari to the U.S. Court of Appeals for the Ninth Circuit

Brief of the Cato Institute as *Amicus Curiae* in Support of Petitioner

Ilya Shapiro
Counsel of Record
Trevor Burrus
Cato Institute
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org
tburrus@cato.org

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QUESTION PRESENTED

May a court approve a class-action settlement that dilutes the bona fide claims of actually injured class members by including, on equal terms and without separate representation, those without bona fide claims?

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INTEREST OF *AMICUS CURIAE*[1]

The Cato Institute is a nonpartisan public policy research foundation dedicated to individual liberty, free markets, and limited government. Cato's Robert A. Levy Center for Constitutional Studies helps restore the principles of constitutional government that are the foundation of liberty. To those ends, Cato publishes books, studies, and the annual *Cato Supreme Court Review*, conducts conferences and forums, and files *amicus* briefs.

This case concerns Cato because it involves a threat to the integrity of the adversarial legal system and thus to constitutional due process.

SUMMARY OF ARGUMENT

The Fifth Amendment's Due Process Clause protects class members' rights both to adequate representation and to pursue their legal claims against the defendant. While the nature of class action lawsuits may make it inevitable that some absent class members have their claims disposed of without compensation or consent, due process and the Federal Rules of Civil Procedure require rigorous judicial review to minimize the risks of that deprivation.

The settlement below aggregates together both valid and invalid claims to inflate the putative class size. Not surprisingly, class counsel want a large class to justify a large fee award. They thus treat strong claims on equal terms with weak ones, thereby

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[1] Rule 37 Statement: All parties were timely notified of and have consented to the filing of this brief. No party's counsel authored this brief in whole or in part and no person or entity other than *amicus* funded its preparation or submission.

diluting the recovery by valid claimants. Lax supervision by the class frees class counsel to engage in self-dealing and collusion with defendants' counsel—who just wants to settle the case for pennies on the dollar—selling valid claims at a steep discount to accrue higher fees. Since few if any claims are sufficient to justify litigation by themselves, few if any of the deprived class members holding valid claims will find it worth their time to object.

Class members' due-process rights are violated because such actions by class counsel fall short of constitutionally guaranteed adequate representation. *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 812 (1985). These rights are also implicated by the judiciary's complicity in the abrogation of legitimate legal claims without the compensation they could rightfully demand. To remedy this unfortunate dynamic, courts must apply a "rigorous analysis" under Rule 23 to forestall a wholesale deprivation of class members' due process rights. *Wal-Mart Stores, Inc. v. Dukes*, 564 U.S. 338, 351 (2011). In the context of the unitary *pro rata* settlement at issue here, that rigorous analysis must include an assessment of the internal conflicts within the class and whether such conflicts require bifurcated treatment to adequately represent the interests of all class members.

Above all, the deprivation of these rights will not be limited to this case—or even to the Ninth Circuit—but will be suffered by class members nationwide, as class counsel file national claims in those jurisdictions that exercise the least scrutiny over potential self-dealing.

ARGUMENT

Meaningful Judicial Oversight of Class-Action Settlements Is Needed to Ensure that Class Members Are Not Deprived of Their Claims without Due Process of Law

The Fifth Amendment's Due Process Clause protects individuals' liberty and property. Few forms of property are as crucial to a free society as the right to pursue legitimate legal claims seeking a redress of wrongs. While there is no right to counsel in civil litigation, the Court has said that due process includes the right of litigants to have their claims adequately represented by whatever counsel is bringing claims on their behalf. *Shutts*, 472 U.S. at 812.

Unitary treatment of class members with divergent interests raises serious due-process concerns and allows named plaintiffs, class counsel, and defendants to dispose of the legal claims of absent class members for their own ends. The only bulwark against this deprivation is the requirement that district courts approve "proposals [that] would bind class members" only after determining that the settlement is "fair, reasonable, and adequate." Fed. R. Civ. P. 23(e)(2). In making this determination the court must ensure that "the representative parties will fairly and adequately protect the interests of the class." Fed. R. Civ. P. 23(a)(4).

If this consideration amounts to a mere rubber-stamp rather than "rigorous analysis" that seriously values absent class members' interests, *Dukes*, 564 U.S. at 351, courts leave those interests at the mercy of class counsel and defendants, who have incentives to collude to the detriment of absent class members.

A. Class actions create conflicts of interest that courts must police.

The evolution of class actions in U.S. courts has yielded a system where litigation is controlled by class counsel and defendants, who bargain over class certification and settlement. Named plaintiffs may offer token input, as required by class counsel's professional obligations, but the vast majority of class members have no way of making their voices heard. *See* Christopher R. Leslie, *The Significance of Silence: Collective Action Problems and Class Action Settlements*, 59 Fla. L. Rev. 71, 77 (2007). This result is not surprising given the incentives faced by class counsel, but the typical lack of meaningful participation by absent class members suggests a systemic due-process problem.

Having suffered relatively small injuries, class members have little incentive to learn of the existence of class actions in which they may have legal interests. Class counsel, meanwhile, having already assembled their named plaintiffs, have no incentive to protect the interests of those not present beyond those imposed by the rules themselves. And the notice demanded by the rules is often observed in the breach, with "notice" amounting to a classified ad in the back of a newspaper, or (on a good day) a piece of junk mail quickly discarded by potential claimants perplexed by legalese. *See Sullivan v. DB Investments*, 667 F.3d 273, 329 n.60 (3d Cir. 2011) (*en banc*) (finding that response rates "rarely exceed seven percent"). Class counsel therefore pursue the case unencumbered by an informed and participating class that could object to the defenestration of their legal entitlements.

This Court has explained that "[t]he adequacy inquiry under Rule 23(a)(4) serves to uncover conflicts of interest between named parties and the class they seek to represent." *Amchem Prods. v. Windsor*, 521 U.S. 591, 625-26 (1997)(citing *General Telephone Co. of Sw.* v. *Falcon,* 457 U.S. 147, 157-158, n.13 (1982)). To ensure this, the "class representative must be part of the class and possess the same interest and suffer the same injury as the class members." *Id.* (quoting *E. Tex. Motor Freight System, Inc. v. Rodriguez,* 431 U.S. 395, 403 (1977)).

The reasons for this requirement are straightforward: just as an attorney representing a client in a matter in which he holds a personal interest may, even inadvertently, allow his own interest to undermine his professional duties, *see* Model Rules of Prof'l Conduct R. 1.7(a)(2) (2016), class representatives whose claims differ materially from absent class members will consider the balance of litigation risks and rewards in light of their own circumstances—which may differ dramatically from the circumstances of those they deign to represent. This reality is only exacerbated by the fact that these representatives are usually just vessels for counsel, who in turn possess their own set of incentives.

The instant case provides a good example: a minority of the class has actionable claims under the antitrust laws; a majority have negligible, if not frivolous, claims. Pet. at 7-8. Aggregating them together is great—if you're class counsel. It multiplies the number of potential class members, boosting the hypothetical recovery and therefore the total settlement value against which counsel can claim an allocation of attorney's fees. Great too for the majority

of the class with shaky claims: they can piggyback on the valid claims and recover more than their claim is probably worth. But all this bounty comes at the expense of the absent class members who see their claims diluted. Holding valid claims, a class of direct purchasers might well be in a position to negotiate more per-member, whereas indirect purchasers would likely have to settle for nuisance value, if anything. But we will never know, because class counsel was not incentivized to represent the interests of bona fide claims; for them, bigger is better.

The good news is that there is a ready answer to this dilemma: Rule 23(c)(5) provides that "a class may be divided into subclasses that are each treated as a class under this rule." Each subclass may then have its own counsel and named representative to shoulder responsibility for that subclass' particular interest. The intra-class conflict thus resolved, each subclass may negotiate on the merits (or lack thereof) of their common claims, with an appropriate settlement reached for each. That this may reduce the total dollar amount of the settlement—while increasing the distribution to those with legitimate claims—does not concern *amicus,* and should not concern this court.

B. Overbroad class definitions exacerbate principal-agent problems and suggest self-dealing.

The attorney-client relationship is a classic example of the principal-agent relationship. As with all such relationships, the most difficult task is to constrain the agent's self-interest, especially where the agent has a significant informational advantage over the principal. Standards of professional ethics,

enforced by state bar associations, provide some constraint on lawyers' tendency to enrich themselves at the expense of their clients. Yet the disciplinary actions commenced each month in each jurisdiction remind us that these ethical codes are not, by themselves, enough. The situation becomes even more problematic when the agent (class counsel) is aware that the vast majority of the principals (class members) are not monitoring his actions. Indeed, most of these "principals" are unaware even of the *existence* of the "agent," let alone the fact that he is acting in their names and binding them. *See* Leslie, *Significance of Silence, supra*, at 78.

Because class counsel need not worry about class members involving themselves in the litigation, they are largely free to pursue their own interests, even when doing so prejudices the interests of absent class members. This Court has previously held that due process is violated when the named plaintiffs' interests are in line with those of the defendant, rather than the absent class members. *Hansberry v. Lee*, 311 U.S. 32, 45-46 (1940). Self-dealing by class counsel violates the due-process rights of absent class members in precisely the same way.

While self-dealing on the part of class counsel could take a number of forms, it most often materializes through the pursuit of larger attorney's fees. One way that class counsel can inflate fee awards is to be over-inclusive when defining the class. By including weak or even frivolous claims, counsel boosts the number of theoretical claimants, and therefore the theoretical recovery. A larger class means more aggregate damages and thus larger fees. This larger recovery need not even reflect the dollars

that would actually be paid out, only what *could* be paid out. It is a back-of-the envelope calculation: total possible class members multiplied by notional claim value. Since class-action settlements often have abysmally low claims rates the chasm between the real amount accruing to the class and that accruing to the attorneys grows even wider. *See Pearson v. NBTY, Inc.*, 772 F.3d 778, 781 (7th Cir. 2014).

The danger of self-dealing is greater when there is an opportunity for class counsel to collude with defendants in reaching a settlement. Class counsel are motivated by a desire to increase the size of their fee awards, while defendants want to minimize both the payout and future legal exposure. The incentives of class counsel and defendants align in increasing the size of the class, even though they operate to the detriment of those actually injured. *See Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 785 (7th Cir. 2004) ("Would it be too cynical to speculate that what may be going on here is that class counsel wanted a settlement that would give them a generous fee and Fleet wanted a settlement that would extinguish 1.4 million claims against it at no cost to itself?").

That incentives to engage in self-dealing exist does not mean that class counsel will do so. But there is plentiful evidence that class counsel engage in self-dealing, thereby failing to provide adequate representation to absent class members as required by due process. *Shutts*, 472 U.S. at 812. The Court has recently dealt with two such examples of self-dealing by class counsel. In *Dukes*, the Court rejected an attempt to limit damages to back-pay claims as a ploy to make the class action mandatory. *Dukes*, 564 U.S. at 398. It disapproved class counsel's self-interested

gimmick because it would have precluded class members' compensatory damages claims. In *Standard Fire Ins. Co. v. Knowles*, 568 U.S. 558, 592 (2013), class counsel attempted to stipulate to less than $5 million in damages to avoid federal jurisdiction under the Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (2005). While the Court decided the case on other grounds, it acknowledged that the attempted stipulation would have reduced the value of class members' claims. *Knowles*, 568 U.S. at 593. Lower courts have also rejected selective pleading, waiver, and abandonment of claims in order to achieve class certification, where doing so would later impair class members' ability to raise abandoned claims. *See*, *e.g.*, *Arch v. Am. Tobacco Corp., Inc.*, 175 F.R.D. 469, 479–80 (E.D. Pa. 1997); *Pearl v. Allied Corp.*, 102 F.R.D. 921, 922–23 (E.D. Pa. 1984); *Feinstein v. Firestone Tire & Rubber Co.*, 535 F. Supp. 595, 602 (S.D.N.Y. 1982); *Kreuger v. Wyeth, Inc.*, No. 03-cv-2496, 2008 WL 481956, at *2–4 (S.D. Cal. Feb. 19, 2008).

Not every principal-agent problem or conflict of interest that arises in the class action context is the result of class counsel's nefarious motives. For example, it is often impossible to effectively communicate with an entire class, so inevitably some class members may be disadvantaged. But courts should be aware of the strong potential for self-dealing by class counsel and should refuse to condone it by certifying classes and approving settlements that appear self-serving. By reviewing class-certification requests and settlements with a skeptical eye, courts will be better able to protect the rights of class members to adequate representation.

C. Rule 23's "rigorous analysis" provides a basic check on class-counsel abuses.

Our current class-action regime raises significant due-process concerns, but it also contains a safeguard against due process violations, by requiring the trial court to engage in a "rigorous analysis" of the plaintiffs' claims. *Dukes*, 564 U.S. at 352 ("Rule 23 does not set forth a mere pleading standard . . . certification is proper only if the trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied") (internal quotation marks omitted). While the *Dukes* Court only needed to address the due-process aspects of the certification process, due-process violations are possible at all stages of class-action litigation—and especially in the settlement context. The Court should thus apply its "rigorous analysis" standard to the entirety of Rule 23.

A trial court that ignores its responsibilities under Rule 23, engaging in no review—or only cursory review—of class counsel's actions will further erode any remaining incentives for counsel to consider and protect the due process rights of absent class members. A trial court that takes its responsibilities under Rule 23 seriously, on the other hand, will be alert for those areas where self-dealing by class counsel is likely. It will better protect the interests of those most vulnerable in this context: absent class members whose liberty and property interests are now in the hands of class counsel.

D. Courts should fulfill their Rule 23 duties to avoid due-process deprivations.

The court below, in its decision to uphold approval of the settlement agreement, barely acknowledged its

responsibilities under Rule 23, tossing aside the objection with a few hundred words of *ipse dixit*. Pet. App. at 2a–4a. This dismissiveness was more than unwarranted, since, as the dissent explained, "[w]ith such an apparent conflict within the class, it is *virtually impossible* for the class representatives to adequately represent a class that includes members who may be entitled to absolutely no recovery." *Id.* at 5a (emphasis added). There is no good reason for class counsel to sacrifice the legitimate claims of their ostensible clients in this way—except to sacrifice them on the altar of attorney's fees.

Indeed, fee awards are a primary motivation for class action settlement. *Eubank v. Pella Corp.*, 753 F.3d 718, 720 (7th Cir. 2014) ("From the selfish standpoint of class counsel and the defendant . . . the optimal settlement is one modest in overall amount but heavily tilted toward attorneys' fees"). Since these cases are nearly always conceived by the lawyer, managed by the lawyer, and ultimately settled by the lawyer, it should not surprise this Court that too often the real value is captured by the lawyer. Where the class size is artificially inflated, it is incumbent on lower courts to perform a more searching analysis than occurred below.

The lower court's errors appear to derive from both its refusal to acknowledge the due process risks of class actions generally and its willful blindness to the possibility of collusion between class counsel and defendants. That collusion indicates that class counsel was not adequately representing class interests, thereby violating their due-process rights. The Ninth Circuit approved this settlement for the same reason that so many other courts approve settlements that

enrich class counsel and defendants at the expense of class members: acting otherwise takes time and effort, and rubber-stamping settlements rarely brings consequences. That this Court has not enforced its rigorous-analysis requirement rigorously, so to speak, has emboldened such lower-court lawlessness.

If allowed to stand, this decision will lead to greater levels of self-dealing by class counsel and greater levels of collusion between class counsel and defendants. These deprivations of due process will not be limited to those living in the Ninth Circuit, however, because class counsel nationwide will choose to file claims in whichever forum exhibits the least desire to police self-dealing.

CONCLUSION

For the forgoing reasons, and those stated by the petitioner, the petition should be granted.

Respectfully submitted,

ILYA SHAPIRO
Counsel of Record
Trevor Burrus
Cato Institute
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org
tburrus@cato.org

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