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IN PRACTICE

CIVIL PROCEDURE

Federal-Court Door Is Now Open

Class actions that cannot proceed in state courts are welcomed

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On March 31, the Supreme Court released its opinion in *Shady Grove Orthopedic Assoc., P.A. v. Allstate Insurance Co.*, No. 08-1008, a case involving a procedural issue that could have been lifted from a first-year civil procedure exam. Despite its academic underpinnings, however, the Court's decision could have broad, real world implications on class action practice in federal court. Perhaps as a testimony to its importance, the decision has already been heralded as a victory by consumer advocates and criticized by big business as opening up the federal courts to an avalanche of class action lawsuits. While the true impact of the decision undoubtedly lies somewhere between these extremes, it is now clear, as even Justice Scalia acknowledged in his opinion, that it will "produce forum shopping" by "keeping the federal-court door open to class actions that cannot proceed in state court."

At the outset, it is worth noting that the decision produced three opinions that include uncommon alliances and an unusual vote tally: Justice Scalia wrote for the Court, and was joined, in whole or in part, by Chief Justice Roberts, and Justices Stevens, Thomas, and Sotomayor; Justice Stevens wrote separately to concur in the judgment of the Court, but not its reasoning; Justice Ginsburg wrote for the dissent, and was joined by Justices Kennedy, Breyer and Alito. In the end, there were five votes for the Court's judgment, but only four votes for its reasoning. Thus, the lower federal courts are left with the task of unraveling the controlling test from what was essentially a 4-1-4 decision on how issues like those raised in *Shady Grove* should be resolved going forward.

The *Shady Grove* case began as a putative class action in the U.S. District Court for the Southern District of New York. Plaintiffs alleged that Allstate Insurance Company failed to pay statutory interest penalties on overdue insurance benefit payments in violation of New York's no-fault insurance law. Allstate argued that plaintiffs could not maintain the lawsuit as a class action because New York law prohibits class actions seeking to "recover a penalty" unless the relevant statute specifically permits the use of class actions. This set up an interesting question — to what extent, if any, could New York law effectively override Federal Rule 23 and dictate whether plaintiffs could pursue their claims as a class action in federal court. The District Court and the Second Circuit both ruled in favor of Allstate and refused to permit the lawsuit to proceed as a class action. Both courts held that Rule 23 was procedural, while New York's ban on class actions was substantive, and thus, under the *Erie* Doctrine, federal courts were obliged to enforce the statute's ban on class actions.

The Supreme Court disagreed. Justice Scalia, writing for the Court, rejected the procedural-substantive distinction made by the lower courts. Instead, he wrote that both the statute and Rule 23 attempt to answer the same procedural question — whether a plaintiff may pursue its claims as a class action — and are therefore irreconcilable. Accordingly, pursuant to the Rules Enabling Act, the federal rule controlled and plaintiffs should have been able to pursue the lawsuit in federal court provided that they satisfied the requirements of Rule 23. Calling Rule 23 a "one-size-fits-all formula for deciding the class-action question," the Court further held that it "unambiguously authorizes any plaintiff, in any federal civil proceeding, to maintain a class action if the Rules' prerequisites are met." Accordingly, laws like the New York statute that purport to dictate when a lawsuit "may not be maintained as a class action because of the relief it seeks," cannot apply in diversity suits in federal court.

As noted above, Justice Scalia was able to garner five votes in support of his conclusion, but could not hold onto

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this majority in support of his reasoning. Instead, Justice Stevens filed a separate opinion concurring in the Court's conclusion but refusing to endorse the manner in which it reached this conclusion. His disagreement with Justice Scalia centered on how the Court should interpret the Rules Enabling Act, which authorizes the Supreme Court to promulgate rules of procedure for the federal courts provided those rules do not "abridge, enlarge or modify any substantive right." For Justice Scalia, determining whether a federal rule violates these limits by encroaching on a "substantive right" requires the Court to focus exclusively on the federal rule: "What matters is what the rule itself regulates: If it governs only 'the manner and means' by which the litigant's rights are 'enforced,' it is valid; if it alters 'the rules of decision by which [the] court will adjudicate [those] rights,' it is not." In contrast, Justice Stevens urged a more "careful interpretation" of both the state law and the federal rule, and suggested that the Court must determine whether the state law at issue is "part of a state's framework of substantive rights or remedies." Predictably, Justice Scalia was critical of this approach, noting the burden it placed on the federal courts and the fact that it might result in the same federal rule having a different meaning in different states: "Instead of a single hard question of whether a Federal Rule regulates substance or procedure, that approach will present hundreds of hard questions, forcing federal courts to assess the substantive or procedural character of countless state rules that may conflict with a single Federal Rule."

Not persuaded by Justice Scalia's efforts to bring him into the plurality, and unwilling to join the dissent, Justice Stevens provided the fifth vote for the Court's judgment but stood alone on the test that should be applied in the future. Justice Stevens agreed with Justice Ginsburg's dissent that "there are some state procedural rules that federal courts must apply in diversity cases because they function as a part of the state's definition of substantive rights and remedies." Nonetheless, he acknowledged that it would be "rare" for a state procedural rule to be so intertwined with a state's framework of rights and remedies that it should rightly be considered substantive, and refused to go along with Justice Ginsburg's more sweeping conclusions regarding the "degree to which the meaning of federal rules may be contorted . . . to accommodate state policy goals."

In the case before the Court, both the plurality and Justice Stevens arrived at the same conclusion, albeit by different means. However, this might not always be the case, and it will likely be Justice Stevens's approach that lower federal courts will follow in the future. Under Supreme Court practice, when no one opinion garners a majority of votes, the controlling opinion is the narrowest opinion on which a majority of the Court agrees. As the Supreme Court noted more than 30 years ago in *Marks v. United States*: "When a fragmented Court decides a case and no single rationale explaining the result enjoys the assent of five Justices, the holding of the Court may be viewed as that position taken by those Members who concurred in the judgment on the narrowest grounds . . ." Thus, somewhat ironically, Justice Stevens's approach will endure even though he was unable to persuade any of his fellow Justices to join his opinion.

What makes this result even more intriguing is the fact that Justice Stevens recently announced his retirement from the Court. Thus, lower federal courts faced with determining whether a state statute that purports to prohibit class actions is reconcilable with Rule 23 will find themselves with the daunting test of determining how the Supreme Court might apply a test to which none of its current members subscribed. Moreover, the chances of this happening are not at all remote. In its brief to the Court, Allstate identified dozens of state statutes that contain class action bans that may have just been nullified by the Court's decision. Among the list was the New Jersey Home Ownership Security Act (N.J.S.A. 46:10B-29, et seq.), which was enacted to curb abusive and predatory lending practices, and requires that borrowers pursue claims only "in an individual capacity," not as class actions. Whether these otherwise procedural provisions are "part of a state's framework of substantive rights or remedies" such that they should be considered substantive remains unknown until each is challenged in the federal courts.

Ultimately, the one thing that is certain is that the "federal-court door" is now open to certain class action lawsuits that would otherwise be dismissed from state court. What this likely means in the short term is an increase in the filing of such lawsuits — and the accompanying costs and expenses associated with defending against them — as plaintiffs test the boundaries of Justice Stevens's test. In the long term, state legislatures seeking to craft class action bans that satisfy this test, and thus apply in both state and federal courts, would be wise to yoke such bans to the substantive framework of rights and remedies addressed in the relevant statute. ■