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Second Circuit Clarifies the Analysis and Standard Governing Motions for Class Certification

By Neal D. Mollen, Allan S. Bloom, Stephen P. Sonnenberg and Jackie M. Ceurvels

In a decision that will be welcomed by employers that fear or face potential employment discrimination class actions, the United States Court of Appeals for the Second Circuit has reinforced the significant burden of proof putative class representatives face in attempting to secure class certification under Federal Rule of Civil Procedure 23 ("Rule 23"). In doing so, the court has expressly repudiated a far more relaxed certification standard that had existed under prior Second Circuit cases. *In re Initial Public Offering Securities Litigation*, ___ F.3d ___, 2006 WL 3499937 (2d Cir. Dec. 5, 2006) ("*IPO*").

The case, which dealt with alleged securities fraud, resolved a number of questions that are critical to employers defending employment law cases, and resolved them all in a way that makes class certification more difficult for the plaintiffs. The Second Circuit held: "(1) that a district judge may not certify a class without making a ruling that each Rule 23 requirement is met and that a lesser standard such as 'some showing' for satisfying each requirement will not suffice, (2) that all of the evidence must be assessed as with any other threshold issue [including evidence submitted by the defendant and its experts], [and] (3) that the fact that a Rule 23 requirement might overlap with an issue on the merits does not avoid the court's obligation to make a ruling as to whether the requirement is met, although such a circumstance might appropriately limit the scope of the court's inquiry at the class certification stage."

Prior to *IPO*, Little Scrutiny Was Given To The Record At Class Certification Stage

Courts in many circuits, including the Second Circuit, have historically applied a very forgiving standard to class certification motions. If the plaintiff can produce some evidence that might support a class, contrary evidence offered by the defendant is largely disregarded and the class is certified. This is particularly true with respect to evidence from the plaintiff's experts; courts often declare themselves unwilling to referee a "battle of the experts" at the class certification stage, and are content if the plaintiff's expert evidence is not "fatally flawed." Finally, stemming from broad language lifted out of context from the Supreme Court's decision in *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 177 (1974), the lower courts have often viewed themselves as prevented from considering evidence that is relevant to the Rule 23 class issues when it also overlaps the merits of the case the plaintiffs would have to prove at trial. That is almost always the case in employment discrimination class actions, where the Rule 23 questions of commonality and typicality largely parallel the question whether there has been a class-wide injury.

The district court's decision in *IPO* was a prime example. The district judge, Judge Scheindlin, had held that in order to get a class certified, the plaintiffs merely had to make "some showing" that the requirements of the Rule had been met. *In re Initial Public Offering Securities Litigation*, 227 F.R.D. *65*, 93 (S.D.N.Y 2004). She rejected a more muscular standard adopted by the Fourth and Seventh Circuits[1] — that Rule 23's requirements had been met by a preponderance of the evidence, even if resolving those issues requires a "preliminary inquiry into the merits," s*ee In re IPO*, 227 F.R.D. at 91-92 — first because that standard was seemingly irreconcilable with a much more forgiving "fatally flawed" standard articulated by the Second Circuit in *Caridad v. Metro-North Commuter Railroad*, 191 F.3d 283, 292 (2d Cir. 1999),[2] *Robinson v. Metro-North Commuter R.R. Co.*, 267 F.3d 147, 162 (2d Cir. 2001), and *In re Visa Check/MasterMoney Antitrust Litigation*, 280 F.3d 124, 134-35 (2d Cir. 2001),[3]

and second because using the more robust standard might "enmesh" the court in questions parallel to "the merits."

Under *IPO*, Findings Of Fact Are Required As To The Rule 23 Requirements

Reversing Judge Scheindlin's decision, the Second Circuit came full circle, adopting the higher standard of proof it had rejected in *Caridad, Robinson*, and *Visa Check*. First, it noted that the court had already begun to back away from the language of those earlier decisions in *Heerwagen v. Clear Channel Communications*, 435 F.3d 219 (2d Cir. 2006). While the court in *Heerwagen* had again admonished that the district court is not "to conduct a preliminary inquiry into the merits of plaintiff's case," the court also held that a district court must determine whether the requirements of Rule 23 had *actually been met*. *Heerwagen*, 435 F.3d at 231-33. The *Heerwagen* court also observed that "[s]ome overlap [between the Rule 23 class inquiry and] the ultimate review on the merits is an acceptable collateral consequence of the 'vigorous analysis' that courts must perform when determining whether Rule 23's requirements have been met . . . so long as it does not stem from a forbidden preliminary inquiry into the merits . . . ." *Id*. at 232.

Second, the court noted the significant amendments to Rule 23 that had been made in 2003, which "arguably combine to permit a more extensive inquiry into whether Rule 23 requirements [have been met]." *IPO, 2006 WL 3499937*, at *13. First, amended Rule 23 deleted the prior express statement that class certification "may be conditional." *Id*. Second, amended Rule 23 eliminated the earlier command that class certification decisions be made "as soon as practicable," replacing it with a provision requiring that the determination be made "at an early practicable time," suggesting that discovery and motions practice may well precede the class determination, thus allowing for a more confident factual finding on the Rule 23 question. *Id*. Finally, and most directly, the Advisory Committee notes to amended Rule 23 state that, "[a] court that is not satisfied that the requirements of Rule 23 have been met should refuse certification until they have been met." *See id*. (citing to Fed. R. Civ. P. 23(c)(1)(C) Adv. Comm. Notes 2003).

In *IPO*, the Second Circuit made several significant determinations regarding Rule 23 class certification analysis. The Second Circuit concluded that:

(i) a district judge may certify a class only after making determinations that each of the Rule 23 requirements has been met;

(ii) such determinations can be made only if the judge resolves factual disputes relevant to each Rule 23 requirement and finds that whatever underlying facts are relevant to a particular Rule 23 requirement have been established and is persuaded to rule, based on the relevant facts and the applicable legal standard;

(iii) the obligation to make determinations is not lessened by overlap between a Rule 23 requirement and a merits issue that is identical with a Rule 23 requirement;

(iv) in making such determinations, a district judge should not assess any aspect of the merits unrelated to a Rule 23 requirement; and

(v) a district judge has ample discretion to circumscribe both the extent of discovery concerning Rule 23 requirements and the extent of a hearing to determine whether such requirements are met in order to assure that a class certification motion does not become a pretext for a partial trial on the merits.

IPO, 2006 WL 3499937, at *15.

Summarizing its sweeping repudiation of its own prior case law, the Second Circuit concluded that "it would seem to be beyond dispute that a district court may not grant class certification without making a determination that all of the Rule 23 requirements are met . . . . [T]here is no reason to lessen a district court's obligation to make a determination that every Rule 23 requirement is met before certifying a class just because of some or even full overlap of that requirement with a merits issue." *Id*. at *14-15.

Practical Consequences of *In re IPO*

The practical consequences of the *IPO* decision will be significant. The most immediate impact, of course, will be to reduce the likelihood of certified classes in pending class actions in the Second Circuit. For those cases in which classes have already been certified, employers would be well-advised to seek reconsideration, and

where class motions have not yet been decided, they will want to shape their arguments around the new circuit law. Because the *IPO* decision will almost certainly result in a petition for *en banc* review and perhaps a *certiorari* petition, time is of the essence.

Second, the Second Circuit — which had been, with the Ninth Circuit, a favorite venue for discrimination class actions because of *Caridad, Robinson*, and *Visa Check* — is no longer as hospitable a locale as it once was for plaintiffs. We can expect to see fewer class counsel choosing the Second Circuit as the situs for nationwide class cases.

More broadly, employers facing class actions outside of the Second Circuit will benefit enormously from the elimination of the *Caridad, Robinson*, and *Visa Check* line of cases, which are cited repeatedly in, and often have been adopted by, courts in other circuits.[4] By repudiating these cases — among the most important cases on which class counsel around the country have been relying in employment discrimination cases — the Second Circuit has made it far more difficult for make-weight arguments to result in class certification.

In addition, *IPO* will liberate employers in their use of expert testimony at the class certification stage. Previously, defendants had been reluctant to rely too heavily on expert work that merely contradicted the conclusions reached by the plaintiffs' experts for fear that the district judge would see the competition as a "battle of the experts" appropriately reserved for trial. *IPO* makes it clear that the district judge is obliged to enter into the fray and make findings of fact as to which expert presentation is more reliable. Defendants need no longer be content, then, simply to argue that the work of the plaintiffs' experts was "fatally flawed."

In sum, the decision in *IPO* is likely to give employers a better chance of having their evidence heard at the class certification stage, and thereby make it less likely that classes will be certified. This will come as welcome news to employers around the country, and most particularly in the Second Circuit.

For further information, please contact:

New York

Allan S. Bloom
212-318-6377
allanbloom@paulhastings.com

Stephen P. Sonnenberg
212-318-6414
stephensonnenberg@paulhastings.com

Washington, D.C.

Neal D. Mollen
202-551-1738
nealmollen@paulhastings.com

[1] *Gariety v. Grant Thornton, LLP*, 368 F.3d 356, 366 (4th Cir. 2004), *Szabo v. Bridgeport Machines, Inc.*, 249 F.3d 672, 676 (7th Cir. 2001).

[2] In *Caridad*, the Second Circuit considered whether the plaintiffs, appealing from a denial of class certification at the district court level, had in fact presented evidence sufficient to warrant class treatment under Rule 23. The Court of Appeals reversed the district court's denial of class certification, but observed that, "[o]f course, class certification would not be warranted absent some showing that the challenged practice is causally related to a pattern of disparate treatment or has a disparate impact on African-American employees at Metro-North." *Caridad*, 191 F.3d at 292 (emphasis added).

[3] In *Visa Check,* the Court of Appeals noted that a district court is obliged only to determine "whether [the plaintiffs] had shown, based on methodology that was not fatally flawed, that the requirements of Rule 23 were met." *Visa Check*, 280 F.3d at 135.

[4] Westlaw searches indicate that *Robinson* and *Caridad* have been cited in more than 500 other published decisions.