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Federal Judges Gain More Control Over Selection of Counsel in Class Actions—and Their Fees

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Our national news frequently includes headline stories regarding class action lawsuits. These cases are newsworthy not only for the fact that they uncover and (hopefully) curb alleged wrongdoing by large corporations against the unsuspecting public, but because these are “big ticket” items; both in terms of the amounts paid in settlement as well as the attorneys’ fees at stake for plaintiffs’ lawyers.

A notable example is the \$3 billion settlement in *In re Visa Check/Mastermoney Antitrust Litigation*, No. 96-CV-5238 (E.D.N.Y.) (“Visa”), an antitrust class action. Plaintiffs’ counsel sought a fee award in excess of \$600 million. The Court did not “rubber stamp” the request, and the actual amount awarded was appreciably less than the amount sought. Although no benefits will need to be held for Plaintiffs’ counsel, clearly they were disappointed at “only” being awarded \$220 million.

In December 2003, appreciable changes to Rule 23 of the Federal Rules of Civil Procedure were enacted and will have a significant impact on class actions. The changes are aimed at encouraging judges to exercise more control over selection of class counsel and attorney fee awards. The changes also give judges more discretion in the settlement process, and appear to be focused on protecting defendants and curbing class-action abuse. Time will be the best judge of whether these changes will achieve their desired effect, but clearly they are a step in the right direction. We discuss the key changes concerning: (i) class certi-

fication; (ii) appointment of class counsel; and (iii) attorney fees below.

Class Certification

Former Rule 23(c)(1) required district court judges to decide whether a lawsuit was suitable to be tried as a class action as early in the litigation process as possible. In particular, the former rule stated that the decision regarding class certification was to be made “[a]s soon as practicable after the commencement of an action.” In recognition of the fact that often it is difficult to make a sound decision regarding class certification early in the suit, the former rule gave judges discretion to conditionally certify a class action until they had enough information to make a final decision as to

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“The changes are aimed at encouraging judges to exercise more control over selection of class counsel and attorney’s fee awards.”

securities litigation

C O R N E R

Second Circuit Upholds Heightened Pleading Standard: In a case of first impression in the Circuit, the U.S. Court of Appeals for the Second Circuit held that a heightened pleading standard applies to securities fraud claims based on misstatements or omissions in prospectuses or registration statements. The claims were brought under sections 11 and 12(a)(2) of the Securities Act of 1933. As the Second Circuit noted, “[f]raud is not an element or a requisite to a claim” under those sections, “although such claims may be, and often are, based on fraudulent conduct. As such, the Court was asked to determine whether claims under sections 11 and 12(a)(2) were subject to the requirement that fraud be pled with particularity pursuant to Rule 9(b) of the Federal Rules of Civil Procedure. The Court concluded that, although a pleading of fraud was not required to state a claim under those sections, where the conduct at issue relies upon averments of fraud, they were subject to the heightened pleading requirements of Rule 9(b). As such, the plaintiff was required to plead with specificity not just that the statements at issue were false, but why and how they were false. *Rombach v. Chang*, (2d Cir. 2004).

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whether the putative class satisfied the requirements for a permissible class action.

District court judges often used their power to issue conditional certification orders when certification decisions were difficult because of their ability to modify the decisions later in the case. For example, in *Visa*, 192 F.R.D. 68 (E.D.N.Y. 2000), in certifying the class, the court stated that "[i]f factual or legal underpinnings of the plaintiffs' successful class certification motion are undermined...a modification of the order, or perhaps decertification, might be appropriate." *Id.*, 192 F.R.D. at 89.

On appeal, the Second Circuit affirmed the Eastern District's ruling. See *In re Visa Check/Mastermoney Antitrust Litigation*, 280 F.3d 124 (2d Cir. 2001). Despite the fact that the Second Circuit recognized certain weaknesses in the lower court's decision, the court affirmed the class certification decision precisely because the lower court recognized its ability to modify its class certification at a later date. *Id.* 280 F.3a at 141.

In a dissent, Judge Jacobs cautioned lower courts against using the conditional certification rule as a crutch. *Id.* at 150. He specifically stated that "[c]onditional certification [] is emphatically not an expedient by which a court may 'avoid deciding whether, at that time, the requirements of the Rule have been substantially met.'" *Id.* 280 F.3d at 150.

This Rule was amended in two significant ways. First, the Rule now provides that the certification decision be made "at an early practicable time," rather than "as soon as practicable." Second, a court's power to make a

conditional certification decision was eliminated. The changes recognize the fact that valid reasons may exist for delaying the certification decision, including the need for discovery, in order to get it right. Indeed, the Advisory Committee Notes acknowledge that discovery in aid of class certification decisions (including limited discovery on the merits) is often necessary to enable the court to make an "informed certification determination." The Advisory Committee Notes encourage courts to oversee discovery in aid of certification and caution that "active management may be necessary to ensure that the certification decision is not unjustifiably delayed."

Appointment of Class Counsel

Oddly enough, under former Rule 23, there was no provision that dealt expressly with appointment of class counsel. The practice, however, was that courts routinely made a determination concerning class counsel in connection with their evaluation of a motion to certify a class. To remedy this glaring void in the Rules, the drafters added a new section, Rule 23(g), which "responds to the reality that the selection and activity of class counsel are often critically important to the successful handling of a class action." See Fed. R. Civ. P. 23(g) Advisory Committee Note. The new rule codifies judicially created guidelines that traditionally governed the appointment process under the former Rule. See Fed. R. Civ. P. 23(g).

The new provision sets forth several factors that courts *must* consider when appointing counsel, including:

- (i) work done to identify and investigate potential claims;
- (ii) experience in handling class actions or other complex litigation;
- (iii) familiarity with the applicable law; and
- (iv) access to resources to aid in the proposed representation.

See Fed. R. Civ. P. 23(g)(1)(c)(i). In addition, the new Rule also gives district courts discretion to consider other unspecified factors that are reflective of the proposed class counsel's "ability to fairly and adequately represent the interests of the class." Fed. R. Civ. P. 23(g)(1)(c)(ii).

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antitrust/unfair competition C O R N E R

With the United States' recent accession to the Madrid Protocol, it is now a lot easier for trademark owners in the U.S. to enforce their trademarks around the globe. The rights that accrue from trademark registration are territorial in as much as these rights may be asserted only within the jurisdiction where the trademark has been registered. Prior to the U.S. becoming a party to the Madrid Protocol, U.S. businesses that operated on a multi-national scale were required to pursue trademark registrations in several countries. This was both costly and cumbersome. Now under the auspices of the Madrid Protocol, an applicant can file only a single application in a single place and simply designate its mark for registration in any number of countries that are members of the Protocol. As AKO has already seen, this method of seeking trademark registration is gaining wide acceptance because it can result in substantial savings over filing in individual countries.

The Advisory Committee Notes state that, “[n]o single factor should necessarily be determinative” of whether the proposed class counsel is appropriate in any given case, and cautions judges to deny class certification if none of the applicants for class counsel is qualified.

Attorney’s Fees

Some federal courts in New York have expressed an inherent skepticism of attorney’s fee requests, and recognize that attorney’s fees are often a sticking point during class action settlement negotiations. Indeed, one court stated that:

the principal impediment to assuring an untainted settlement process is the financial interest of counsel, who may be improperly influenced to accept certain settlement terms, or to accept a settlement at all, thereby ‘subordinating the interests of class members to the attorney’s own economic self-interest.

See In re Holocaust Victim Assets Litig., 105 F. Supp. 2d 139, 146 (E.D.N.Y. 2000). Accordingly, in New York, courts have encouraged moderation when it comes to attorney fees, and have cautioned against awarding “windfall fees” to class counsel. *See In re Holocaust Victim Assets Litig.*, 270 F. Supp. 2d 313, 321 (E.D.N.Y. 2002)(citations omitted).

Recent changes in the provisions governing attorneys fee awards may represent a first step in avoiding such windfalls. First, Rule 23(g)(2)(c) gives courts discretion to include provisions for an award of attorneys fees in the order appointing class counsel. The purpose of this rule is to encourage the court “to adopt guidelines for fees . . . or to direct class counsel to report to the court at regular intervals on the efforts undertaken in the action, to facilitate the court’s later determination of a reasonable attorney fee.” *See Fed. R. Civ. P. 23(g) Advisory Committee Note.* The Rule also was drafted in an effort to motivate courts to begin monitoring counsels’ work starting at the inception of the case in order to facilitate a later determination of a reasonable fee award.

Additionally, the drafters enacted Rule 23(h), which provides that “the court may award reasonable attorney fees . . . authorized by law or by agreement of the parties,”

and sets forth the procedure that counsel must follow to request fees. The Advisory Committee Notes admonish judges to be actively involved in measuring fee awards, and explicitly state that such active involvement “is singularly important to the proper operation of the class action process.”

Significantly, the new Rule does not set forth the factors that judges should consider when assessing whether a proposed request for attorney’s fees is indeed reasonable. The Advisory Committee Notes nevertheless suggest certain factors that traditionally have guided courts in this determination, including: (i) the result achieved for class members; (ii) agreements between the parties concerning fees; and (iii) fees charged by class counsel or other attorneys when representing individual claimants. “Active judicial involvement” in measuring fee awards and “responsibility” to ensure that fee awards are fair and reasonable are the buzzwords of the day in the Advisory Committee Notes.

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“The new amendments broadcast loud and clear the message that the role of the federal courts in class actions will be heightened.”

real estate corner

Construction lenders beware—failure to file a Notice of Lending may result in diversion of trust funds. Under New York Lien Law, funds received by an owner under building loan contracts are deemed trust assets reserved for payment of specific “costs of improvement,” such as contractor, architect and subcontractor claims, as well as the discharge of any building loan mortgage. A recent New York Court of Appeals decision found that a lender, acting as owner-trustee after an assignment by the borrower, failed to satisfy notice requirements by not filing a *Notice of Lending* under New York Lien Law, despite filing all other notices normally sufficient to secure the priority of its lien. This failure rendered the lender’s repayment of its loan mortgage from trust funds a “non-trust use,” requiring disgorgement to the project subcontractors. *Aspro Mechanical Contracting, Inc. v. Fleet Bank, N.A.*

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The new amendments broadcast loud and clear the message that the role of the federal courts in class actions will be heightened. Decisions whether or not to certify a class will be made with a sharper focus; as will decisions concerning the appointment of class counsel and determinations of what is a fair and reasonable attorney fee award. Increased scrutiny can only be viewed as a good thing. ■

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product liability c o r n e r

In a significant victory for mass tort defendants, the First Department has affirmed Justice Helen Freedman's decision, which holds that in a personal-injury or wrongful death lawsuit, apportionment of liability among defendants pursuant to Article 16 of New York's Civil Practice Code and Rules should include companies that have filed for bankruptcy protection. In the past, defendants paid more than their share of non-economic damages by being forced to pay bankrupt joint tortfeasors' shares of liability. The *Tancredi* decision helps to avoid such an inequitable result by taking into account the various degrees of culpability of all tortfeasors-bankrupt or not—resulting in a more fair apportionment of non-economic damages. *Tancredi v. A.C. & S. et al.*, No. 04/03219, slip op. (1st Dep't April 29, 2004), aff'g No. 120136/00, slip op. (N.Y. Sup. Ct. Oct. 31, 2002).

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