GIBSON DUNN

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SECOND QUARTER 2018 UPDATE ON CLASS ACTIONS

To Our Clients and Friends:

This update provides an overview and summary of significant class action developments during the second quarter of 2018 (April through June), as well as a brief look ahead to some of the key class action issues anticipated later this year.

- **Part I** discusses the U.S. Supreme Court's decisions in two key cases, *Epic Systems Corp. v. Lewis*, and *China Agritech, Inc. v. Resh*.
- **Part II** looks forward to the Supreme Court's October 2018 Term and previews a new class action case on the Court's docket, *Nutraceutical Corp. v. Lambert*.
- **Part III** discusses two recent circuit-level cases involving class action settlements.

I. The U.S. Supreme Court Affirms Validity of Arbitration Clauses in Employment Agreements, and Limits *American Pipe* Tolling to Individual Suits

The Supreme Court issued two important opinions in the past quarter of significant relevance to class action defendants.

First, in the consolidated cases of *Epic Systems Corp. v. Lewis*, *Ernst & Young LLP v. Morris*, and *National Labor Relations Board v. Murphy Oil USA, Inc.*, 138 S. Ct. 1612 (2018), the Supreme Court held that arbitration agreements in which an employee waives his right to bring a claim against an employer on a class or collective basis are enforceable under the Federal Arbitration Act ("FAA") and do not violate the National Labor Relations Act ("NLRA"). The Court's ruling resolved a longstanding circuit split on this issue.

In a 5-4 decision written by Justice Gorsuch, the Court held that "Congress has instructed in the Arbitration Act that arbitration agreements providing for individualized proceedings must be enforced, and neither the Arbitration Act's saving clause nor the NLRA suggests otherwise." 138 S. Ct. at 1616, 1624–27. The Court rejected the employees' argument that the FAA's savings clause—which allows courts to refuse to enforce arbitration agreements "upon such grounds as exist at law or in equity for the revocation of any contract"—precludes enforcement of their arbitration agreements. Because the employees' argument was not applicable to "any" contract, and instead singled out "individualized arbitration proceedings" as invalid, the Court explained that the savings clause was not implicated, and there was no "generally applicable contract defense[]" to overcome the FAA's presumption of enforceability. *Id.* at 1622–23.

The Court also rejected the argument that enforcing an arbitration agreement's class action waiver would violate employees' right to engage in collective action under the NLRA. It disagreed with the suggestion that the later-passed NLRA had impliedly repealed portions of the FAA, emphasizing that "repeals by implication are 'disfavored,'" and "Congress 'does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions.'" *Id.* at 1624, 1626–27. Section 7 of the NLRA, moreover, "focuses on the right to organize unions and bargain collectively," "does not express approval or disapproval of arbitration," and "does not even hint at a wish to displace the Arbitration Act—let alone accomplish that much clearly and manifestly." *Id.* at 1624.

Finally, the Court declined to apply *Chevron* deference to the NLRB's contrary conclusions, noting that Congress had not given the NLRB any authority to interpret the FAA, a statute that the agency does not administer. The Court also observed that although *Chevron* deference is premised on the notion that "'policy choices' should be left to the Executive Branch," "here the Executive seems to be of two minds, for [the Court] received competing briefs from the [NLRB] and the United States (through the Solicitor General)," the latter of which had supported the employers. *Id.* at 1630.

Justice Ginsburg, joined by Justices Breyer, Sotomayor, and Kagan, dissented. They expressed concern that "underenforcement of federal and state" employment statutes will result from the majority's decision, because employees will be deterred by the relative expense and "slim relief obtainable" in individual suits. *Id.* at 1637, 1646–48 (Ginsburg, J., dissenting). In response, the majority observed that "the dissent retreats to policy arguments," and underscored that "[t]he respective merits of class actions and private arbitration as means of enforcing the law are questions constitutionally entrusted not to the courts to decide but to the policymakers in the political branches where those questions remain hotly contested." *Id.* at 1632.

Epic Systems confirms that courts will continue to enforce agreements between employers and employees to arbitrate their disputes on an individual—rather than class or collective—basis, and continues the Supreme Court's trend of enforcing the FAA's strong policy favoring arbitration.

In the second important class action case of the Term, *China Agritech, Inc. v. Resh*, 138 S. Ct. 1800, the Court declined to extend the rule of equitable tolling announced in *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974), to the filing of successive class actions.

Under *American Pipe*, the timely filing of a class action tolls the applicable statute of limitations for "all persons encompassed by the class complaint" to intervene in the action or to file individual suits after the denial of class certification. *China Agritech*, 138 S. Ct. at 1804–05. The Ninth Circuit had extended that ruling to the successive filing of class actions, but the Supreme Court reversed, explaining that the concerns underlying *American Pipe* simply do not apply in the class action context. The rule announced in *American Pipe* serves to promote "the efficiency and economy of litigation" embodied in Rule 23, on the theory that plaintiffs "reasonably rel[y] on the class representative . . . to protect their interests in their individual claims," and without equitable tolling, potential class members "would be induced to file protective motions to intervene" (*id.* at 1806), or "a needless multiplicity of [separate] actions" to protect their interests in the event certification is denied (*id.* at 1810).

Extending *American Pipe* tolling to successive class actions, however, "would allow the statute of limitations to be extended time and again" and allow plaintiffs "limitless bites at the apple." *Id*. at 1808–09. The Court noted that in those circuits that had already declined to extend *American Pipe* to successive class actions, there had not been "a disproportionate number of duplicative, protective class action filings." *Id*. at 1810. The Court also reasoned that "efficiency favors early assertion of competing class representative claims" (*id*. at 1807), and early filing "may aid a district court in determining, early on, whether class treatment is warranted" (*id*. at 1811).

All of the justices joined the Court's opinion in *China Agritech* except for Justice Sotomayor, who wrote an opinion concurring in the judgment but expressing the view that the Court's holding should be limited to cases governed by the Private Securities Litigation Reform Act. *Id*. at 1811–15 (Sotomayor, J., concurring in the judgment).

China Agritech emphasizes the importance of timely filing putative class actions and reaffirms the class action defendant's reasonable expectation that class claims will not continue to emerge after the statute of limitations period has expired.

II. The U.S. Supreme Court Is Poised to Weigh In on the Timing of Rule 23(f) Petitions, Arbitration Issues, and the Validity of Cy Pres-Only Settlements

The Supreme Court's October 2018 Term promises to be another active one in the class action space, particularly on a number of bread-and-butter issues relating to class action procedure, settlement, and arbitration.

On June 25, 2018, the Supreme Court granted certiorari in *Nutraceutical Corp. v. Lambert* (No. 17-1094) to resolve whether equitable exceptions apply to non-jurisdictional claims-processing rules, and specifically, to decide if and when an appellate court may equitably toll the time to file a petition for permission to appeal the grant or denial of class certification under Federal Rule of Civil Procedure 23(f). Ordinarily, a Rule 23(f) petition must be filed within 14 days following the grant or denial of class certification or decertification, but the Ninth Circuit held that, under the particular circumstances of the case, the filing of a motion for reconsideration 20 days after the decertification order equitably tolled the 14-day deadline. The Ninth Circuit acknowledged, however, that its ruling conflicted with the other circuit courts that have considered the issue. (We covered the Ninth Circuit's decision in *Lambert* in our third quarter 2017 update.)

As noted in our first quarter 2018 update, the Supreme Court is also expected to resolve a series of other issues of interest to class action practitioners in the coming Term. In *New Prime Inc. v. Oliveira* (No. 17-340), the Court will decide whether (a) a dispute regarding the applicability of the FAA must be resolved by an arbitrator under a valid delegation clause, and (b) an exemption for contracts of employment for transportation workers in Section 1 of the FAA applies to independent contractors. Briefing is currently underway. (Gibson Dunn represents the petitioner, New Prime, Inc.) In *Lamps Plus, Inc. v. Varela* (No. 17-988), the Court will decide whether the FAA forecloses a state-law interpretation of an arbitration agreement that would authorize class arbitration based solely on general language commonly used in such agreements. And in *Frank v. Gaos* (No. 17-961), the Court

will consider the validity of *cy pres*-only settlements that provide no direct compensation to class members. Opening briefs were filed in both cases on July 9, 2018.

III. The Seventh and Eighth Circuits Issue Notable Class Action Settlement Decisions

The federal courts of appeals continue to closely scrutinize class action settlements, and this past quarter saw the issuance of two significant decisions (which both coincidentally involved Target Corp.).

In *Pearson v. Target Corp.*, No. 17-2275, — F.3d —, 2018 WL 3117848 (7th Cir. June 26, 2018), the Seventh Circuit examined a common tactic employed by professional objectors—filing baseless appeals from a settlement approval as a form of "blackmail," hoping that the parties will pay them to dismiss the appeals so that the settlement can become effective.

In 2014, the parties in *Pearson* had agreed to a classwide settlement in response to allegations that the defendants had "violated consumer protection laws by making false claims about the efficacy of [a dietary] supplement." *Id.* at *1. Ted Frank, a frequent objector to class action settlements, objected to the awards to class counsel in the district court, and appealed the settlement approval order to the Seventh Circuit. The Seventh Circuit agreed with Frank's objections and reversed the district court, holding that "the settlement provided outsized benefits to class counsel." *Id.*

On remand, the parties reached a new settlement, which the district court approved. It then dismissed the case "'without prejudice' so as to allow the Court to supervise the implementation and administration of the Settlement." *Id.* Three different class members then objected and filed appeals. *Id.* at *2. All three subsequently dismissed their appeals, and the district court entered a new order dismissing the case with prejudice. *Id.* Frank then moved to intervene and disgorge any side settlements made with the other three objectors. His concern was "'objector blackmail'" in which an "absent class member objects to a settlement with no intention of improving the settlement for the class," "appeals, and pockets a side payment in exchange for voluntarily dismissing the appeal." *Id.* at *1. The district court refused to hear the motion, reasoning that the dismissal with prejudice had divested the court of jurisdiction. Frank then moved under Federal Rule of Civil Procedure 60(b) to vacate the dismissal with prejudice and restore the court's jurisdiction over the settlement. *Id.* at *2. The district court denied that motion as well, which led to Frank's second appeal and the subject of this decision. *Id.*

The Seventh Circuit again ruled in Frank's favor. Writing for a three-judge panel, Judge Wood explained that Frank could bring a Rule 60(b) motion because he had objected the settlement and thus qualified as a "party." *Id.* On the merits, the court held that the district court should have granted the Rule 60(b) motion because (1) the objectors voluntarily dismissed their appeals before briefing raised concerns that they had done so at the expense of the class; (2) the class was comprised of ordinary consumers rather than sophisticated financial institutions (and thus needed greater protection from the court); (3) Frank sought only to effectuate the limited ancillary jurisdiction contemplated by the settlement itself, so the interest in finality was less compelling that it would be had Frank sought to unwind the settlement and re-litigate merits issues; and (4) Rule 60(b)(6) exists as an "'equitable'" "safety valve" for precisely these types of situations. *Id.* at *3-4.

This decision continues the trend among the federal courts of appeals to carefully scrutinize class settlements, particularly when they involve "ordinary consumers." And, as the Seventh Circuit recognized, it also highlights the importance of "an amendment of Rule 23"—Rule 23(e)(5)(B)—which is "designed to prevent this problem from recurring." *Id.* at *5. That proposed rule would require district court approval, after a hearing, of any "'payment or other consideration' provided for 'forgoing or withdrawing an objection' or 'forgoing, dismissing, or abandoning an appeal.'" *Id.* If Congress allows this new rule to go into effect, observers will be keen to see whether it "solve[s] the problem" of "objector blackmail," or whether objectors will find new, creative ways to "leverage[]" the process "for a purely personal gain." *Id.* at *1, *5.

The second case, *In re Target Corporation Customer Data Security Breach Litigation*, 892 F.3d 968 (8th Cir. 2018), also involved the re-examination of a class action settlement, at the urging of an objector, after the Eighth Circuit had rejected an earlier settlement.

With the earlier settlement, the Eighth Circuit concluded the district court had "failed to conduct the appropriate pre-certification analysis." *Id.* at 972. On the second go-around, however, the Eighth Circuit affirmed the judgment of the district court, reasoning that the court had not "fundamentally misunderstood the structure of the settlement agreement" (*id.* at 973), nor was separate legal counsel required to protect the interests of the subclass of plaintiffs who had yet to suffer any material loss from the data breach that formed the basis for the suit (*id.* at 976). On the latter point, the Eighth Circuit maintained that the interests of those class members with "documented losses" and those without losses were "more congruent than disparate" because it was "hypothetically possible that a member" of either subclass could "suffer some future injury." *Id.* at 975-76.

The Eighth Circuit also affirmed the district court's approval of the settlement. Even though it noted the district court's analysis of the $6.75 million fee award may have been "perfunctory," it held the court's reasoning was sufficient and that the lodestar multiplier applied was "well within amounts [the court had] deemed reasonable in the past." *Id.* at 977. The court also held that the district court was within its discretion to approve the settlement despite the objectors' concerns about what arguably constituted a "clear-sailing" provision requiring defendants not to oppose the attorney's fees request, and a "kicker" provision that permitted unused settlement funds to be returned to defendants rather than distributed to the class. *Id.* at 979.

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