Class Actions: Understanding the Fundamentals as a First Step Toward Management and Avoidance

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If you have doubts about the prevalence and importance of class action litigation just scan the national newspapers on any given day and there is an excellent chance you will find a story involving a class action suit. Certainly, if you ask general counsel in many sectors of American business about the litigation that presents their enterprise with the greatest risk of loss, it is likely that class litigation will be among the finalists for that dubious distinction. Class litigation is a present and growing aspect of risk management and dispute resolution in the United States, and we believe that class litigation will become increasingly common in the healthcare industry, for the reasons discussed below. A clear understanding of what class litigation is and how it works is an essential first step in managing and avoiding class action risk.

The questions that follow are those that come up regularly, even from the most sophisticated clients.

Can You Give a Brief Description of What a Class Action Is, Exactly?

A class action is a lawsuit filed by a single plaintiff—the “named plaintiff”—who purports to represent not only his own interests but also the interests of all of those who are similarly situated with regard to the claimed wrong.1 The remedy sought is on behalf of the entire class. The lawsuit can seek injunctive relief, to change the defendant's conduct by court order, but most often the remedy sought is money damages. For example, if a hospital used a billing system that had a software error that resulted in all patient bills being overstated by 1%, then a single patient could sue in an individual action for the 1% overcharge on his bill. In a class action, he also would be suing to recover the 1% for every patient who had been overcharged by the hospital during the time period allowed by the applicable statute of limitations. In Illinois, for example, if the claim were for breach of contract, that period would be ten years prior to the date that the class action suit was filed.2 If the plaintiff invoked a statutory consumer fraud statute, damages for that alleged fraud in some jurisdictions may be multiplied by a prescribed factor, perhaps trebled.3

The damages sought by the plaintiff are almost always substantial because of the aggregating effect of the class. In our example, 1% of a single plaintiff’s bill may only be tens or hundreds of dollars. But the bills for one thousand patients over the period of a year may be hundreds of thousands of dollars. And over a multi-year period, the numbers can become much more substantial. Aggregating many claims, even small ones, can quickly create significant, and even intolerable, litigation risk.

Class actions can be found in both federal and state courts because both systems have rules that allow for class litigation. A class action is not, however, its own cause of action or wrong upon which to base a suit—it is only a procedural device. The class nature of a suit is administrative and procedural—there must still be a legitimate underlying claim that the defendant violated a law or breached a duty or agreement, as in any other lawsuit.

Recently, it has become possible to conduct class action disputes in an arbitration setting.4 Like all arbitrations, a class arbitration is a creature of contract and requires the parties’ consent. While a class action lawsuit can be commenced without permission or notice, class arbitration must be agreed upon by the parties.

When a Plaintiff Brings a Class Action Claim, Is There an Opportunity for the Defendant to Challenge the Existence of the Class?

The plaintiff begins the suit by alleging the existence of a class—sometimes called a “putative class”—and has the burden of demonstrating that a class action is appropriate under court rules. A judge must then determine whether to “certify” the class for the litigation to proceed as a class action. The class certification decision generally is made early in the case, but usually after at least some of the facts have been gathered in pre-trial discovery, and after the court has been briefed on the issues relevant to class certification.

As the litigation progresses, new facts may be discovered that could be used to challenge the class certification determination. If so, the defendant can go back to the court to ask that the certified class be “decertified.” Also, at least in federal court, the rules permit a defendant, in certain instances, to appeal a certification decision when that decision is made early in the case, rather than having to wait to appeal until the end of the case.5 The ability to appeal class certification early—on an “interlocutory” basis—can be extremely useful. A decision certifying a class can pressure the defendant to settle at that point in the litigation because the plaintiffs will have taken a major step forward in establishing the defendant’s risk of class-wide liability. An appeal at this juncture can correct clear errors in class certification and avoid placing the defendant unfairly in a position of great vulnerability.
What Does the Plaintiff Have to Show to Get a Class Certified?
The federal and state rules often are phrased somewhat differently, but the requirements for class certification in a damages action are usually fundamentally the same. Broadly stated, the court must determine whether all the class members have enough in common relating to the alleged wrongdoing so that treating all of the putative class members as a group makes sense for everyone, including the court. As part of its decision, the court will consider whether proceeding with the litigation as a class action would be fundamentally fair to both the plaintiffs and the defendant. The court also will consider whether a class action would be an efficient use of its resources, or whether a class action would be so unwieldy that it would not make sense. The court will determine whether the named plaintiff—the person listed as the actual plaintiff in the complaint—has conflicts of interest with the class and whether the named plaintiff will, in all respects, be a good representative of the class that she purports to represent."

The questions that a court asks in deciding whether to certify a class are fairly straightforward and are similar to the questions asked by clients, in one form or another. Do these class members really share a common experience that is at the core of this lawsuit? Are the legal issues the same for all class members, or will different arguments or laws apply to various class members? Does it make sense from the court’s perspective, and is it fair to the parties, to determine these claims collectively rather than individually? Can this plaintiff be trusted to act as the representative for this class of people? So, what does a class certification analysis actually look like in practice? Going back to the alleged 1% overcharge example, let’s assume that the defendant is a corporation with hospitals in several states but that it bills centrally from one location. Issues may arise regarding the application of different state laws governing what constitutes a consumer fraud or a breach of contract. Different statutes of limitations also may apply from state to state. That is, different laws may apply to different subgroups within the putative class—which is something the court will consider in deciding whether class certification is appropriate.

Let’s further assume that the alleged billing error was not so much a clear error as an ambiguity, and that, in some hospitals at certain times, bills were explained more clearly to patients than at other hospitals. Under this scenario, different factual defenses will be available regarding different members of the class. Again, this will be a factor for the court to consider in determining whether class certification is appropriate.

As a further complication of the class certification analysis, the named plaintiff is a resident of only one state, not all of the states where the hospitals and the class members are located. His legal case may, as a result, be stronger (or weaker) than that of the other class members, depending on state law. Thus, his incentive to settle early, or to not settle at all, may differ from that of other class members. Let’s also assume that the named plaintiff could not have any conflict of interest with the class or that her incentive to settle early, or to not settle at all, may differ from that of other class members. Let’s also assume that the defendant learns that the named plaintiff has a chronic illness that may impact his ability to act in the interests of the class for a variety of reasons. In sum, the named plaintiff is not positioned as are the other class members, and he may not be a typical or adequate class representative.

Will this class be certified? Can these problems be solved by creating subclasses? At what point does managing these differences create so many inefficiencies, for the court and the parties, that a class action no longer makes sense to the court? How and when do you evaluate these risks and opportunities as a party to the litigation? These are all issues that will need to be addressed in connection with class action litigation.

Is a Class Action Different from a Claim Under the False Claims Act?
Class actions and False Claims Act (FCA) cases, either state or federal, are cousins in certain respects, but they are not the same. In an FCA case, the plaintiff is suing in the shoes of the government to address an alleged wrong that may involve many individuals, but the recovery is in the name of the government, and to recover the government’s loss. The relator (the “named plaintiff” in an FCA suit) shares only a portion of that recovery. In a class action, by contrast, the suit is in the name of the individual plaintiff and the class members, and seeks to recover for their losses; it is not concerned with the government’s loss except to the extent that the government may be a member of the class. Despite these differences, however, the FCA suit and the class action do share an important feature—they are both sponsored and driven by a claimant on behalf of others, and these claims are virtually always litigated by plaintiffs lawyers working on a contingent fee basis.
Who Is in Charge on the Plaintiff’s Side of a Class Action, And Who Stands to Benefit?
Defendants must understand that class actions—particularly those that are in the aggregate seeking substantial damages but where the individual claims are small—are almost always contingent fee cases where the plaintiff’s lawyers will be paid only from a recovery following a settlement or judgment. Generally, the named plaintiff’s stake in the outcome is too small to warrant the plaintiff’s investment of funds in the litigation to cover fees or costs, so the plaintiff’s lawyer also is advancing the out-of-pocket expenses of the litigation, which can be substantial. As a result, and as a practical matter, the plaintiff’s lawyer usually is the single person on the plaintiff’s side of the litigation with the most meaningful economic interest in the outcome. While some named plaintiffs, and committees of class members, may be significantly involved in the substance and progress of a class action, more often, in the authors’ experience, the plaintiff’s lawyers are in some respects the driving force in the litigation. The subtleties of decision making in class actions, including litigation strategies and settlement decisions, are, we believe, often colored by this reality. These facts must be understood and taken in to close account on the defense side of a case.

Don’t Most Cases, Including Class Actions, Settle Though?
The vast majority of civil litigation settles before trial, and this is especially true of class litigation. But that does not mean that settlement in class litigation is easy. Both sides in class litigation recognize the economic stakes, and the plaintiff will certainly take in to account the substantial litigation risk to the defendant when formulating his settlement demand. In other words, settlement in class litigation can often be expensive and present difficult risk analysis and economic decision making.

Further, settling a class action is procedurally different from settlement in other litigation. Unlike in other litigation, in a class action the judge must review and approve the proposed settlement before it can be finalized. Also, once settlement terms have been agreed upon, notice must go out to all class members advising them of the settlement terms and giving each putative class member an opportunity to take himself out of the class (“opt out”), or object to the terms of the class settlement. If a putative class member chooses to opt out of the class, his individual claims are preserved. He can leave the class litigation and bring his own individual lawsuit. If too many putative class members opt out and retain the threat of their individual claims against the defendant, the defendant may choose to not proceed with the class settlement at all, if the defendant has reserved that right for itself.

A class member may also choose to stay in the class but file an objection to the settlement terms. That objection will be heard by the court, or may be withdrawn by the objector.

The questions that a court asks in deciding whether to certify a class are fairly straightforward and are similar to the questions asked by clients, in one form or another.

What Factors Suggest That Class Litigation Is on the Uptick in the Healthcare Industry?
Class actions, by rule and by case law, are designed to function best, and be most commonly used, where large numbers of people have had a similar or identical experience in a transactional setting. That is, class actions are more likely where, if an error has been made once, then it is likely to have been made many times.

Class actions also are more prevalent when the subject transactions are governed by complicated or ambiguous regulations and rules, contract based or government imposed. Put simply, when there is a complicated set of rules to follow, there is a greater chance of error, and a greater opportunity for disagreement over what constitutes error. When those regulations or rules govern transactions that occur over and over, the consequence of an error is magnified many fold. Even when an error is only alleged and is only arguable, the stakes of class litigation and even the risk of loss can be enormous.

Finally, in our experience, the plaintiff’s class action bar seems to focus as a group on a particular industry. If class litigation in a particular industry has been productive from a plaintiff’s point of view, then more class actions in that industry will likely follow.

We believe that all of these factors describe many aspects of the healthcare industry and have noticed an increase in class litigation here.

From a defendant’s perspective, there are steps to help anticipate and manage the risks presented by an increased level of class action activity. For example, the U.S. Supreme Court recently has spoken to the validity of class action waiver provisions in certain consumer contracts. Also, there are document management considerations that may anticipate and reduce costs in the event of litigation. And many industries also have actively engaged in legislative affairs activities to address these risks and cost issues.

Class litigation is a fact of life in American business. The first step in managing this risk effectively is to understand it.
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Endnotes

1 Sometimes there are a small number of individuals who serve as named plaintiffs, rather than only one person. There are treatises written on the rules and variations in class litigation. See, e.g., Thomas A. Dickerson, Class Actions: The Law of 50 States (2011); David Herr, Manual for Complex Litigation (2011); William Rubenstein, et al., Newberg on Class Actions (2011). This article is intended only as an overview.


4 The American Arbitration Association, for example, now has a separate set of rules for class actions. See American Arbitration Ass’n, Supplementary Rules for Class Litigation, available at http://www.adr.org/sp.asp?id=21936.


7 In order for a class action suit to be maintained, the plaintiff must establish that the four requirements of Fed. R. Civ. P. 23(a) have been met: (a) numerosity; (b) commonality; (c) typicality; and (d) adequacy of representation. In addition, one or more of the class categories found in Rule 23(b) also must be satisfied.


