Class Action Monitor

December 7, 2018

# Amendments to Rule 23 and New Procedural Guidance from N.D. Cal. May Impact Class Action Settlements

*By Jeffrey S. Klein*, David R. Singh and Bambo Obaro*

**In This Issue**

1 Amendments to Rule 23 and New Procedural Guidance from N.D. Cal. May Impact Class Action Settlements

5 Will Article III Standing Prevent the Supreme Court from Providing Clarity on Class Action *Cy Pres* Settlements?

9 The Supreme Court Revisits Class Arbitration Yet Again—*Varela v. Lamps Plus, Inc.* and *New Prime, Inc. v. Oliveira*

* Mr. Klein is Co-Head of Weil's Complex Commercial Litigation practice and Head of the Firm's Employment Litigation practice.

The dynamics inherent in class action settlements pose the risk of self-dealing by class counsel at the expense of class members. Indeed, rather than negotiate the best possible settlement, class counsel may be incentivized to broker a quick, low-value settlement, without significant investment of resources into a case, in exchange for the certainty and allure of an immediate fee award. Plaintiff counsel also has an incentive to oversell the benefit of the settlement to the class—even where participation will be low and the benefits minimal—because their fee award will be based, in part, on value generated for the class. Defendants, often motivated by the goal of obtaining a global release at the lowest possible price, are unlikely to curb the abuse. In theory, a court can endeavor to police such self-dealing because, pursuant to Fed. R. Civ. P. 23(e), a court may approve a class settlement only after a hearing and on determining that the proposed settlement is "fair, reasonable and adequate." But, given the information asymmetry between class counsel, on the one hand, and the court (and potential objectors), on the other hand, and the typically non-adversarial nature of the class settlement process, it is often difficult for a court to rigorously evaluate the bona fides of a proposed class settlement.

Recent amendments to Fed. R. Civ. P. 23, which were approved by the United States Supreme Court on April 26, 2018 and went into effect on December 1, 2018, and recent updates to procedural guidance for class action settlements, which were issued by the Northern District of California on November 1, 2018 (the "Guidelines"), could potentially alter this dynamic, discourage the filing of abusive class action settlements, and reduce information asymmetry, enabling courts and objectors to scrutinize more closely the terms of proposed class settlements. By way of example, the amendments to Rule 23 specifically identify factors that a court *must* consider in deciding whether a proposed settlement is "fair, reasonable, and adequate," including:

- whether the class representatives and class counsel have adequately represented the class;
- whether the settlement proposal was negotiated at arm's length;

- whether the relief provided for the class is adequate, taking into account: (i) the costs, risks, and delay of trial and appeal; (ii) the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims, if required; (iii) the terms of any proposed award of attorney's fees, including timing of payment; and (iv) any other agreement made in connection with the settlement agreement; and
- whether the settlement proposal treats class members equitably relative to each other.

The Guidelines go hand-in-hand with the amendments to Rule 23 as they require significant additional disclosures to a court when seeking preliminary or final approval of a class action settlement. The additional disclosures should help courts better evaluate the fairness, reasonableness, and adequacy of any proposed settlement, including under the factors enumerated in the new amendment to Fed. R. Civ. P. 23. The Guidelines also include a first-of-kind disclosure of post-distribution accounting, which could provide important data on the utility of class action settlements and whether further reform of our class action system is warranted.

Below is summary of the disclosures required by the Guidelines.

### Preliminary Approval

The Guidelines provide that the following information should be included in the parties' motion for preliminary approval of any proposed settlement:

- Any differences between the proposed class and proposed release of claims in the settlement agreement and (a) the class and claims in the operative complaint (if a class has not been certified) or (b) the claims certified for class treatment (if a class has been certified), including an explanation as to why the differences are appropriate.
- The anticipated class recovery under the settlement, the potential class recovery if plaintiffs had fully prevailed on each of their claims, and an explanation of the factors bearing on the amount of the compromise.
- The proposed allocation plan for the settlement fund.
- If there is a claim form, an estimate of the number and/or percentage of class members who are expected to submit a claim in light of the experience of the selected claims administrator and/or counsel from other recent settlements of similar cases, the identity of the examples used for the estimate, and the reason for the selection of those examples.
- Whether and under what circumstances money originally designated for class recovery will revert to any defendant, the potential amount or range of amounts of any such reversion, and an explanation as to why a reversion is appropriate.
- The identity of the proposed settlement administrator, the settlement administrator selection process, how many settlement administrators submitted proposals, what methods of notice and claims payment were proposed, and the lead class counsel's firms' history of engagements with the settlement administrator over the prior two years.
- The anticipated administrative costs, the reasonableness of those costs in relation to the value of the settlement, and who will pay those costs.
- Class notice and instructions for opt-outs or objections.
- The amount of attorneys' fees class counsel intends on requesting, the lodestar calculation (including the total number of hours billed and the requested multiplier, if any), whether and in what amounts they seek payment of costs and expenses, including expert fees, and, in a common fund case, the relationship between the award, the amount of the common fund, and the lodestar calculation. To the extent that counsel base their fee request on having obtained injunctive relief and/or other non-monetary relief for the class, the benefit conferred on the class.

- The incentive awards class counsel intend to request on behalf of the named plaintiffs as well as any evidence supporting such awards.
- Any *cy pres* recipients, how *cy pres* recipients are related to the subject matter of the lawsuit and the class members, and any relationship the parties or their counsel have with the proposed *cy pres* recipients.
- Detailed information from class counsel regarding past distributions in a prior comparable class settlement, including the total settlement fund, the total number of class members to whom notice was sent, the method(s) of notice, the number and percentage of claims forms submitted, the average recovery per class member or claimant, the amount distributed to each *cy pres* recipient, the administrative costs, the attorneys' fees and costs.

### Final Approval

In addition to the more detailed disclosure required for preliminary approval of any proposed class settlement, the Guidelines also require that the motion for final approval include information about the class members' response rate, including the number of undeliverable class notices and claim packets, the number of class members who submitted valid claims, the number of class members who elected to opt out of the class, the number of class members who objected to or commented on the settlement, and a response to any objections. Moreover, any request for attorneys' fees must include detailed lodestar information, even if the requested amount is based on a percentage of the settlement fund.

### Post-Distribution Accounting

In an effort to more closely monitor the settlement distribution, the Guidelines provide that 21 days after the distribution of the settlement funds, the parties should file a "Post-Distribution Accounting" in an easy-to-read chart, which contains the following information:

- The total settlement fund.
- The total number of class members.
- The total number of class members whom notice was sent and not returned as undeliverable.
- The number and percentage of claim forms submitted.
- The number and percentage of opt-outs.
- The number and percentage of objections.
- The average and median recovery per claimant.
- The largest and smallest amounts paid to class members.
- Notice and payment methods.
- The number and value of checks not cashed.
- The amounts distributed to each *cy pres* recipient.
- The administrative costs.
- The attorneys' fees and costs, including as a percentage of the settlement fund, and the multiplier.
- Where class members are entitled to non-monetary relief, the number of class members availing themselves of such relief and the aggregate value redeemed by the class members and/or by any assignees or transferees of class members' interests.

### Potential Impact of the Recent Amendments to Rule 23 and the New Guidelines

The Guidelines, and amended Rule 23, require unprecedented disclosures by the parties in seeking preliminary and final approval of proposed class action settlements, and more in-depth analysis by the courts in granting such requests. Because most class actions that survive dispositive motions end in settlement, the Guidelines and amended Rule 23 could significantly affect how class action cases are litigated.

As an initial matter, while California will surely remain a popular venue for the plaintiff bar given its plaintiff-friendly consumer protection and employment laws and liberal jury pool, there may be some modest reduction in the filing of class actions in the Northern District of California, especially so-called "no injury" class actions that are unlikely to generate substantial recovery for the class (or justify large fee awards). However, if there is a reduction, it will likely be temporary, as other district courts (elsewhere in California and throughout the nation) adopt analogues to the Guidelines.

The requirement that all requests for approval of attorneys' fees must include detailed lodestar information, even if the requested amount is based on a percentage of the settlement fund, could also affect how class actions are litigated. A recent trend in the Northern District of California is that judges have used class counsels' lodestar to significantly reduce class counsels' fees when the judges believe that the percentage of settlement method provides a windfall to class counsel. The Guidelines' requirement that the lodestar information be provided follows this trend and could potentially lead to either overbilling by class counsel or the unnecessary prolonging of cases to increase a lodestar in an attempt to circumvent judges applying a lodestar calculation to reduce their fees. This would of course also have an impact on a class action defendant that may now see its class action cases go on for much longer and incur higher fees in defending against a more litigious plaintiff bar.

The Guidelines and new amendments to Rule 23 may also decrease the number of class action settlements. Concerned with the increased transparency required by the Guidelines (and the corresponding increase in judicial scrutiny of class settlements and proposed fee awards), Plaintiff counsel may insist on greater recoveries on behalf of the settlement class. Not all defendants will be willing to yield to the increased demands, fewer cases will settle, and there could be an uptick in more protracted class action proceedings.

By design, the disclosure requirements in the Guidelines also will make it easier for courts and potential objectors to challenge the adequacy, reasonableness, or fairness of the proposed settlement. Indeed, access to information such as the number of class members the claims administrator/class counsel expect to submit a claim and the anticipated benefit to the class (compared against the potential recovery at trial); the proposed allocation plan for the settlement fund; the incentive awards class counsel intends to request on behalf of the named plaintiffs; and *cy pres* recipients and any relationship they or their counsel have with the proposed *cy pres* recipients would certainly serve as a treasure trove for objectors who are looking for a basis to object to the proposed settlement.

Attention to the differences between the settlement class and the proposed or certified class and differences between the original claims in the complaint and the claims to be released in the settlement, also raises concerns about whether district courts will limit the scope of a defendant's release if the settlement class and claims do not match the certified or alleged class and claims. Therefore, when negotiating a proposed settlement, defendants should seriously consider whether a requested change to the class definition is necessary to fully and finally buy their peace. Similarly, expansion of the claims to be released may garner the court's attention and the explanation for any expansion should be carefully thought out.

The Post-Distribution Accounting requirement also has the potential to have a lasting impact on class action litigation. Most judges do not monitor what happens to a class action settlement after granting final approval, and detailed information about actual claims distribution is rarely available. The data gathered from settlement distributions, which will be publicly available, should help in evaluating whether the class action system is working as intended. Depending on what the data shows, proponents of significant overhaul to the class action system might have additional evidence to support their position.

In sum, the newly updated Guidelines—which are consistent with, and expand upon, the new amendments to Rule 23—could have a significant impact on how class action cases are litigated and if they settle and on what terms. Although the Guidelines are directed specifically at parties litigating in the Northern District of California, they should be considered by parties litigating in other jurisdictions, as federal courts in all jurisdictions are now required to evaluate some of the same factors when deciding whether to approve a settlement proposal pursuant to the new amendment to Rule 23.

# Will Article III Standing Prevent the Supreme Court from Providing Clarity on Class Action *Cy Pres* Settlements?

*By David R. Singh and Jevechius D. Bernardoni*

Short for "*cy près comme possible*," or "as near as possible," the term *cy pres* typically refers to a court's power "to save testamentary charitable gifts that would otherwise fail." *Klier v. Elf Atochem N. Am., Inc.*, 658 F.3d 468, 473-74 (5th Cir. 2011). In trust law, *cy pres* permits the redirection of funds when the intent of a trust is no longer possible to fulfill (*e.g.*, the named charity no longer exists). More controversially, an approximation of the *cy pres* doctrine is sometimes invoked in support of class action settlements. In particular, where it is administratively infeasible or impractical to pay class members directly or the per-member award would be *de minimis*, parties to class actions sometimes agree for settlement funds to be paid to a charity or non-profit whose mission relates to the subject matter of the lawsuit, and courts sometimes approve such settlements by reference to the *cy pres* doctrine.

Although *cy pres* settlements are common, there is no uniform standard for evaluating whether they comport with Fed. R. Civ. P. Rule 23(e)(2), which requires that a settlement that would bind class members be "fair, reasonable, and adequate." The United States Supreme Court has never addressed this issue, but, in *Frank v. Gaos*, granted certiorari on the question whether *cy pres* settlements support class certification and comport with the requirement of Rule 23(e)(2), and if so, in what circumstances.

On October 31, 2018, the Court heard oral argument, but justices from across the ideological spectrum hinted that the Court may dismiss or remand the case on standing grounds, rather than evaluate the propriety of, and standards for evaluating, *cy pres* settlements.

### *Cy Pres* Settlement Criticisms and Benefits

Class action *cy pres* settlements have been the subject of considerable criticism. Class action *cy pres* is a judicially created remedy—it is not explicitly authorized by statute or rule, and the Supreme Court has never expressly affirmed its use. Moreover, *cy pres* class remedies pose fundamental concerns to the perceived or actual fairness of the class action process. For example:

- **Class Counsel's Interests and Class Members' Interests Are in Tension**: When class counsel's fee award is calculated using the size of a *cy pres* fund, class counsel lack a financial incentive to maximize class members' recovery because class counsel will receive a fee award regardless of whether class members receive any compensation for their injuries. These concerns are especially pronounced where *cy pres* is used to facilitate an early settlement with a sizable fee award. *See, e.g.*, *Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 785 (7th Cir. 2004) (characterizing a proposed *cy pres* settlement as selling the uncompensated class members "down the river" and observing "[w]ould it be too cynical to speculate that what may be going on here is that class counsel wanted a settlement that would give them a generous fee and [defendant] wanted a settlement that would extinguish 1.4 million claims against it at no cost to itself?").
- **Class Members Are Not Directly Compensated for Their Injuries**: A *cy pres* settlement typically waives class members' substantive legal rights in exchange for indirect benefits provided by the charity or non-profit *cy pres* recipient. Thus, *cy pres* remedies do not directly redress class members' injuries. Often, the indirect benefits are speculative, attenuated, or provide no meaningful recompense for class members' injuries. *See, e.g.*, *Pearson v. NBTY Inc.*, 772 F.3d 778, 784 (7th Cir. 2014) (observing that it was a "hopelessly speculative proposition" that a $1.13 million *cy pres* award to an orthopedic foundation in a joint-health supplements class action "may contribute to the discovery of new treatments for joint problems").
- ***Cy Pres* Settlements May Be Structured to Minimize Defendants' Liability or Benefit Defendants:** Defendants often have a say in

which charities or non-profits will receive the *cy pres* funds—through this negotiating power, defendants can direct funds to charities or non-profits that are supportive of defendants' commercial goals and/or controlled by defendants. *See, e.g.*, *S.E.C. v. Bear, Stearns & Co. Inc.*, 626 F. Supp. 2d 402, 415 (2009) ("In fact, *cy pres* distributions often stray even further from the 'next best use' to a use that actually benefits the defendant rather than the plaintiffs. In general, defendants reap goodwill from the donation of monies to a good cause. However, defendants may also channel money into causes and organizations in which they already have an interest."); *Schwartz v. Dallas Cowboys Football Club Ltd.*, 362 F. Supp. 2d 574, 577 (E.D. Pa. 2005) (distributing *cy pres* funds to an institution which was already funded in part by a defendant). Similarly, defendants may seek to offset class action damages with already-promised charitable donations by directing *cy pres* funds to entities that are already within defendants' charitable funding stream, thereby minimizing or even eliminating defendants' effective liability for class members' injuries. *See Dennis v. Kellogg Co.*, 697 F.3d 858, 868 (9th Cir. 2012) (characterizing a proposed settlement as a "paper tiger" where it was unclear whether *cy pres* funds would be allocated in addition to or in lieu of already-promised donations).

- ***Cy Pres* Settlements May Present Conflicts of Interest for the Judiciary**: *Cy pres* awards negotiated by the parties can put judges in the uncomfortable position of approving or rejecting settlements that would direct funds away from injured class members and to a judge's own favored charity, non-profit, or *alma mater*. Such decisions create the appearance, if not reality, of judicial conflicts of interest.
- **The Existence of *Cy Pres* Remedies May Incentivize Class Counsel to Initiate Class Actions They Would Not Otherwise File**: Because *cy pres* remedies present an opportunity for class counsel to obtain a fee award regardless of the administrability of the proposed class, the mere existence of *cy pres* remedies may incentivize class counsel to initiate lawsuits that would be infeasible to litigate or of questionable merit. Thus, *cy pres* remedies may encourage non-meritorious class action filings.

*Cy pres* settlement proponents respond to these concerns by asserting that the use of *cy pres* is an appropriate use of courts' equitable powers. Thus, *cy pres* is a "pragmatic and sensible" solution to the problem of class compensation in low-value class settlements involving a high number of potential class members. *New York ex rel. Koppell v. Keds Corp.*, No. 93 Civ. 6708 (CSH), 1994 WL 97201, at *3 (S.D.N.Y. Mar. 21, 1994). In such cases, *cy pres* proponents argue that requiring direct monetary payments—as *cy pres* critics would—wastes most or all of the settlement fund on administrative costs in order to confer trivial direct monetary benefits to the class; indeed, in those circumstances, the exclusive beneficiary of a class action settlement effectively would be class counsel, and not the injured class members.

### Justice Roberts Hints at Future Limits to *Cy Pres* Settlements

Five years ago, the United States Supreme Court declined an opportunity to impose limits on or an analytical framework for reviewing class action *cy pres* settlements when it denied the petition for writ of certiorari in *Marek v. Lane*. *See* 571 U.S. 1003 (2013).

*Marek* involved a *cy pres* settlement related to Facebook's "Beacon" program. Pursuant to the settlement, Facebook agreed to pay approximately $9.5 million: class counsel were awarded nearly a quarter of the settlement fund in fees and costs, the named plaintiffs received modest incentive payments, and the unnamed class members received no damages. *Id.* at 1005. Instead, the remaining $6.5 million of the settlement fund was utilized to establish a new charitable foundation that would help fund organizations dedicated to educating the public about online privacy, and a Facebook representative would be one of the three members of the new foundation's board. *Id.* As characterized by Justice Roberts, "Facebook thus insulated itself from all class claims arising from the Beacon episode by paying plaintiffs' counsel and the named plaintiffs some $3 million and spending $6.5 million to set up a foundation in which it would play a major role." *Id.*

While the Court denied certiorari in *Marek*, Justice Roberts authored an intriguing statement, hinting that a closer look at class action *cy pres* practice was in the Court's near future:

> Granting review of this case might not have afforded the Court an opportunity to address ***more fundamental concerns surrounding the use of such remedies*** in class action litigation, ***including when, if ever, such relief should be considered; how to assess its fairness as a general matter; whether new entities may be established as part of such relief; if not, how existing entities should be selected; what the respective roles of the judge and parties are in shaping a cy pres remedy; how closely the goals of any enlisted organization must correspond to the interests of the class; and so on.*** This Court has not previously addressed any of these issues. *Cy pres* remedies, however, are a growing feature of class action settlements. ***In a suitable case, this Court may need to clarify the limits on the use of such remedies***.

*Id.* at 1006 (internal citations omitted, emphases added).

## Background of *Frank v. Gaos*

*Frank v. Gaos* may be just the "suitable" case Justice Roberts foresaw in his statement regarding denial of certiorari in *Marek*. The class action underlying *Frank* involves alleged privacy violations caused by Google web searches. Specifically, class plaintiffs alleged that Google violated the Stored Communications Act as well as committed privacy torts by disclosing the users' search terms to websites accessed through Google Search. *See Gaos v. Holyoak (In re Google Referrer Header Privacy Litig.)*, 869 F.3d 737 (9th Cir. 2017).

Following mediation, the parties reached an early settlement whereby Google would pay a total of $8.5 million in exchange for a release of the claims of approximately 129 million Google Search users in the United States between October 25, 2006 and April 25, 2014. *Id.* at 740. Of the $8.5 million settlement fund, about $3.2 million was set aside for attorneys' fees, administration costs, and incentive payments to the named plaintiffs; the remaining $5.3 million was allocated to six *cy pres* recipients, each of which agreed "to devote the funds to promote public awareness and education, and/or to support research, development, and initiatives, related to protecting privacy on the Internet." *Id.* Google had already donated to several of the proposed *cy pres* recipients, and three of the *cy pres* recipients were *alma maters* of the class attorneys who signed the settlement.

In the district court, Theodore Frank and Melissa Holyoak ("Petitioners")—attorneys with the Center for Class Action Fairness—objected to approval of the settlement, class certification, and class counsel's fee request. Among other contentions, Petitioners argued that (1) it was feasible to use a standard claims process to compensate class members, and if the district court were to find that distribution to class members was infeasible, then class certification was improper; (2) the parties' selection of the *cy pres* recipients was improper given their preexisting relationship with Google and class counsel; and (3) class counsel's fee request was excessive because it was based on *cy pres* funds that would not be distributed directly to class members. The district court overruled Petitioners' objections and approved the settlement. Petitioners appealed to the Ninth Circuit, which affirmed the district court's approval of the *cy pres* settlement. Petitioners then filed a writ of certiorari to the Supreme Court, which the Court granted on April 30, 2018. *Frank v. Gaos*, 138 S. Ct. 1697 (2018).

## October 31, 2018 Oral Argument in *Frank v. Gaos*

The Court's questions at oral argument regarding *cy pres* settlements generally fell along ideological lines.

Many of the Court's conservative members—continuing their tendency to view class actions with skepticism—expressed doubts about the real or perceived fairness of class action *cy pres* settlements.

For example, Chief Justice Roberts questioned whether a *cy pres* award to AARP would meaningfully redress the harm alleged in the underlying suits and stated that "it's just a little bit fishy that the [*cy pres*] money goes to a charity or a 501(c)(3) organization that Google had contributed to in the past." Chief Justice Roberts also asked Google's attorney whether he agreed that "the district court should never be the one suggesting possible recipients of the funds of a settlement he has to approve?" Justice Kavanaugh, on at least three occasions, inquired about "the appearance of favoritism and collusion" inherent in many class action *cy pres* settlements. And, after observing that in many *cy pres* settlements "[t]he attorneys get money, and a lot of it. The class members get no money whatsoever. And money is given to organizations that they may or may not like and that may or may not ever do anything that is of even indirect benefit to them," Justice Alito inquired how the *cy pres* system can "be regarded as a sensible system[.]"

In contrast, some of the Court's liberal members appeared to defend the fairness and practicality of class action *cy pres* settlements. Justice Ginsberg asked the very first question at oral argument, challenging Petitioners' assertion that *cy pres* settlements are abusive, stating "[w]hy is it an abuse? Because, practically, the class members would get nothing, nothing at all, and, here, at least they get an indirect benefit." Similarly, Justice Sotomayor observed that in the "potentially abusive" cases identified in Petitioners' briefs, the circuit court rejected the proposed *cy pres* award. Thus, Justice Sotomayor noted that "[i]t seems like the system is working . . . ."

However, one major concern appeared to cross the Court's ideological boundaries: Article III standing. The United States Department of Justice ("DOJ"), in an *amicus* brief, noted that the Article III standing theory employed by the district court was subsequently rejected by the Supreme Court in *Spokeo, Inc. v. Robins*, 136 S. Ct. 1540 (2016) and that it is uncertain whether any of the named plaintiffs alleged an injury that satisfies the injury-in-fact requirement as clarified by *Spokeo*. It is clear that the Court shares the DOJ's Article III concerns—the Court asked every single participant at oral argument to address standing. Justices Gorsuch, Alito, Kagan, and Breyer questioned whether the class plaintiffs had suffered Article III injury and whether standing was an appropriate question for the Supreme Court to address in the first instance (*i.e.*, instead of ruling on the standing issue, should the Court remand the case for further development or dismiss the appeal as improvidently granted). At oral argument, Justice Kavanaugh was the only member of the Court who appeared to have no problem with Article III standing, stating that it is "plain common sense" that disclosure of search terms to third parties constitutes an injury. Emphasizing the Court's unease regarding the standing question, following the October 31 oral argument, on November 6, 2018, the Court directed the parties and the Solicitor General to file supplemental briefs addressing whether any named plaintiff has Article III standing in this case.

Given the number of Justices expressing skepticism regarding standing—and the cross-ideological makeup of those Justices—it appears that the Court may dismiss or remand the case on Article III standing grounds rather than providing clarity regarding the limits of class action *cy pres* settlements or articulating a test for analyzing those settlements.

# The Supreme Court Revisits Class Arbitration Yet Again—*Varela v. Lamps Plus, Inc.* and *New Prime, Inc. v. Oliveira*

*By David R. Singh and Audrey Stano*

Eight years ago, in *Stolt-Nielsen, S.A. v. Animal Feeds International Corporation*, the United States Supreme Court held that a court may not order class arbitration unless there is a "contractual basis" to conclude that the parties "agreed to" class arbitration and may not "presume" such consent from "mere silence" on the issue of class arbitration. *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662, 685, 687, 130 S. Ct. 1758, 176 L.Ed.2d 605 (2010). Despite this seemingly clear holding, and the fact that the Supreme Court has devoted a tremendous amount of attention to arbitration and class-waiver provisions over the past decade, currently pending before the Supreme Court are yet two more cases posing important arbitration issues: *Varela v. Lamps Plus, Inc.* and *New Prime, Inc. v. Oliveira*. Below we discuss each case and its potential implications on the arbitration and class action landscape.

### *Varela v. Lamps Plus, Inc.*: When Can Class Arbitration Be Required?

Frank Varela filed a class action complaint against his employer, Lamps Plus, asserting claims for negligence, breach of implied contract, violation of the California Consumer Records Act, violation of the California Unfair Competition Law, invasion of privacy, and negligent violation of the Fair Credit Reporting Act related to a data breach compromising the security of over 1,000 Lamps Plus employees' sensitive personal information, including Varela's. *Varela v. Lamps Plus, Inc.*, No. CV 16-577-DMG (KSX), 2016 WL 9110161, at *1-2 (C.D. Cal. July 7, 2016), *aff'd*, 701 F. App'x 670 (9th Cir. 2017), *cert. granted*, 138 S. Ct. 1697, 200 L. Ed. 2d 948 (2018). As part of his employment contract with Lamps Plus, Varela signed an arbitration agreement. Lamps Plus moved to compel Varela to submit his claims to individual arbitration. *Id*. at *6-7. Judge Gee of the Central District of California granted Lamps Plus's motion to compel arbitration—however, the court ordered that the arbitration should proceed on a class, rather than individual, basis. Specifically, the court found the language of the arbitration agreement "at least ambiguous as to class claims" and, pursuant to California state law, construed the construction of the arbitration agreement against the drafter (which was Lamps Plus). *Id*.

The Ninth Circuit affirmed. It inferred an agreement to arbitrate on a class-wide basis based on both standard language in the arbitration agreement and the canon of construction that ambiguity in an agreement should be construed against the drafter. *Varela v. Lamps Plus, Inc.*, 701 F. App'x 670, 671 (9th Cir. 2017), *cert. granted*, 138 S. Ct. 1697, 200 L. Ed. 2d 948 (2018). Although other Supreme Court precedent holds that "a party may not be compelled under the [Federal Arbitration Act] to submit to class arbitration unless there is a contractual basis for concluding that the party agreed to do so[,]" *Stolt-Nielsen*, 559 U.S. at 684, the Ninth Circuit determined that "the mere absence of language explicitly referring to class arbitration" does not always mean that an arbitration agreement prohibits class proceedings. *Varela*, 701 F. App'x at 672-73. Lamps Plus petitioned the Supreme Court for a writ of certiorari, which was granted on April 30, 2018.

The question for review presented to the Supreme Court is whether the Ninth Circuit erred in finding that the parties agreed to class arbitration solely through the application of state-law contractual interpretation principles despite the arbitration agreement's silence as to class arbitration. *Lamps Plus, Inc. v. Varela*, No. 17-988, 2018 WL 3374999, at *i (U.S. 2018) (question presented by Petitioner Lamps Plus is "[w]hether the Federal Arbitration Act forecloses a state-law interpretation of an arbitration agreement that would authorize class arbitration based solely on general language commonly used in arbitration agreements."). Notably, the arbitration agreement between the parties in *Lamps Plus* does not contain a single reference to class arbitration and incorporates standard language commonly used in arbitration agreements. *See Varela*, 701 F. App'x at 672 (waiver of "any right I may have to file a lawsuit or other civil action or proceeding relating to my employment with the Company"; waiver of "any right I may have to resolve employment disputes through trial by judge or jury"; "arbitration shall be in lieu of any and all lawsuits or other civil legal proceedings relating to my employment."). In seeking to overturn the Ninth Circuit, the petitioners contend that *Stolt-Nielsen* prohibits the presumption that "mere silence" on the question of class arbitration "constitutes consent to resolve their disputes in class proceedings." *Lamps Plus*, 2018 WL 3374999, at *2 (quoting *Stolt-Nielsen*, 559 U.S. at 687 (full citation omitted)).

The Supreme Court heard oral argument on the appeal on October 29, 2018. The justices appeared divided on predictably ideological lines, with the more liberal justices focusing on whether the language of the arbitration agreement is ambiguous (and Justices Sotomayor and Kagan also expressing skepticism about creating a large role for federal law in governing arbitration agreements). Transcript of Oral Argument at 13, 15, 17-18, *Lamps Plus, Inc. v. Varela*, No. 17-988 (9th Cir. Oct. 29, 2018), https://www.supremecourt.gov/oral_arguments/argument_transcripts/2018/17-988_o7jp.pdf. The more conservative justices, however, appeared to question whether the applicability of state law here was truly neutral and whether class arbitration presents due process problems to the extent it purports to bind absent class members who were not party to the arbitration provision and never consented to the jurisdiction of the arbitrator. *Id*. at 32-35, 37-38.

### *New Prime, Inc. v. Oliveira*: Who Decides Arbitrability?

Dominic Oliveira, an employee of and former independent contractor for trucking company New Prime, filed a class action complaint against New Prime, alleging violations of the Fair Labor Standards Act and Missouri and Maine labor laws. *Oliveira v. New Prime, Inc.*, 141 F. Supp. 3d 125, 127 (D. Mass. 2015), *aff'd in part, dismissed in part*, 857 F.3d 7 (1st Cir. 2017). New Prime moved to compel arbitration pursuant to Section 4 of the Federal Arbitration Act, which allows any party "aggrieved" by the failure of another party "to arbitrate under a written agreement for arbitration" to petition a district court for "an order directing that such arbitration proceed in the manner provided for in such agreement." *Id*. at 130. Oliveira opposed the motion to compel arbitration, arguing that his claims fell within the Federal Arbitration Act's Section 1 exemption, which exempts "contracts of employment of transportation workers" from the Federal Arbitration Act entirely. Oliveira also argued that the Court, and not the arbitrator, should decide the applicability of Section 1's exemption. *Id*. at 128-30. Following the Ninth Circuit (and expressly rejecting the Eighth Circuit's approach), Chief Judge Saris of the District of Massachusetts denied New Prime's motion to compel arbitration, finding that the question of arbitrability itself is one for judicial determination. *Id*. at 131-33; *compare In re Van Dusen*, 654 F.3d 838 (9th Cir. 2011) *with Green v. SuperShuttle Int'l, Inc.*, 653 F.3d 766 (8th Cir. 2011).

The First Circuit affirmed, also following the Ninth Circuit, holding that the district court (and not an arbitrator) properly determined whether Section 1 of the Federal Arbitration Act applied to Oliveira and dismissed for lack of appellate jurisdiction. *Oliveira v. New Prime, Inc.*, 857 F.3d 7, 13-15 (1st Cir. 2017), *cert. granted*, 138 S. Ct. 1164, 200 L. Ed. 2d 313 (2018). Additionally, the Court held that "contracts of employment"—the language used in Section 1's exemption—encompasses agreements with both employees and independent contractors. *Id*. at 16-24.

New Prime petitioned for certiorari, which the Supreme Court granted on February 26, 2018, raising two questions for the Supreme Court's review: (1) whether a dispute over the applicability of the Federal Arbitration Act's Section 1 exemption must be resolved by an arbitrator or a court when a contract delegates the question of arbitrability to the arbitrator; and (2) whether the Federal Arbitration Act's Section 1 exemption is inapplicable to independent contractor agreements. *New Prime, Inc. v. Oliveira*, No. 17-3402018, WL 2278112 (U.S. 2018), at *i. The Court heard oral argument in *New Prime* on October 3, 2018. While the actual outcome of the appeal remains to be seen, based on leanings expressed during the oral argument, it appears as though the first question (of who should determine arbitrability) may be resolved in Oliveira's favor, as even New Prime's counsel stated that he would be “happy” for the district court to decide whether the contract is arbitrable. Transcript of Oral Argument at 19, *New Prime, Inc. v. Oliveira*, No. 17-340 (1st Cir. Oct. 3, 2018), https://www.supremecourt.gov/oral_arguments/argument_transcripts/2018/17-340_2c8f.pdf. With respect to the second question presented, however, justices of both ideologies—including Justices Sotomayor and Gorsuch and Chief Justice Roberts—seemed reluctant to enforce arbitration agreements for transportation workers. *Id*. at 4 (Justice Sotomayor), 8 (Chief Justice Roberts), 9-10 (Justice Gorsuch).

### Conclusion

Over the past decade, the Supreme Court has shown great interest in Federal Arbitration Act issues, repeatedly weighing in on the enforceability of arbitration provisions/class action waivers and the propriety of ordering class arbitration. *See, e.g.*, *Stolt-Nielsen*, 559 U.S. 662 (holding that parties could not be compelled to submit claims to class arbitration absent a clear contractual basis to conclude that the parties agreed to class arbitration); *AT&T Mobility, LLC v. Concepcion*, 563 U.S. 333, 131 S. Ct. 1740, 179 L. Ed. 2d 742 (2011) (holding that the Federal Arbitration Act preempted a state law rule that discriminated against arbitration provisions with class action waivers); *Am. Express v. Italian Colors Rests.*, 570 U.S. 228, 133 S. Ct. 2304, 186 L. Ed. 2d 417 (2013) (enforcing an arbitration agreement that contained a class action waiver and rejecting an exception for antitrust claims); *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463, 193 L. Ed. 2d 365 (2015) (holding that the Federal Arbitration Act preempted a state-law contractual interpretation that deemed a class action arbitration waiver unenforceable); *Epic Sys. v Lewis*, 138 S. Ct. 1612, 200 L. Ed. 2d 889 (2018) (holding that arbitration agreements must be enforced as written and class and collective action waivers in employment arbitration agreements are not prohibited by the National Labor Relations Act). *Lamps Plus* and *New Prime* will be the latest in this growing line of cases.

We will continue to monitor these cases and update you on any developments.

***Class Action Monitor*** is published by the Litigation Department of Weil, Gotshal & Manges LLP, 767 Fifth Avenue, New York, NY 10153, +1 212 310 8000, www.weil.com.

If you have questions concerning the contents of this issue of *Class Action Monitor*, or would like more information about Weil's Class Action practice, please speak to your regular contact at Weil, or to the editors or authors listed below:

**Editor:**

| | | | |
|---|---|---|---|
| David Singh (SV) | View Bio | david.singh@weil.com | +1 650 802 3010 |

**Contributing Authors:**

| | | | |
|---|---|---|---|
| Jeffrey S. Klein (NY) | View Bio | jeffrey.klein@weil.com | +1 212 310 8790 |
| David Singh (SV) | View Bio | david.singh@weil.com | +1 650 802 3010 |
| Bambo Obaro (SV) | View Bio | bambo.obarp@weil.com | +1 650 802 3083 |
| Jevechius Bernardoni (SV) | View Bio | jevechius.bernardoni@weil.com | +1 650 802 3265 |
| Audrey Stano (SV) | View Bio | audrey.stano@weil.com | +1 650 802 3275 |