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Forum

Unfair-Competition Law Reform May Encourage Class Actions

By Jim Burgess

Whenever nonlawyers or lawyers from outside of California hear an explanation of state Business and Professions Code Section 17200, known as the unfair-competition law, the usual reaction is disbelief.

The idea that a person who has not been injured can sue any business to obtain monetary relief on behalf of "the general public" without satisfying basic class-action requirements runs counter to ordinary notions of fairness.

When these same people also hear that the uninjured plaintiffs' lawyers may qualify for huge attorney fees as private attorneys general, the near-universal response is that the unfair-competition law must have been cooked up by lawyers for lawyers.

All of this could change if Proposition 64 passes in November.

Proposition 64 will require that only people who suffer "injury in fact" will be allowed to sue under the unfair-competition law. Proposition 64 also will prohibit representative actions on behalf of the general public. The new law will require plaintiffs to satisfy the class-action requirements to sue on behalf of others.

Proposition 64 represents much-needed reform in response to abusive lawsuits. In some instances, lawyers have used spouses, secretaries and friends as "representative" plaintiffs in questionable lawsuits in the hopes of obtaining large fees.

There is no question that Proposition 64 will end many of these abusive practices without affecting the ability of public prosecutors or injured parties to stop unfair business practices.

But while the proposed new law may eliminate one problem, it also may encourage a different one. By eliminating representative actions, Proposition 64 may encourage plaintiffs to file more class actions, which are more difficult to resolve.

A representative action may be settled by paying the named plaintiff without paying money to the "general public" and without requiring court approval. Class actions, on the other hand, require court approval.

Also, a case brought as a class action generally cannot be settled by paying just the named plaintiff and providing no benefit to class members. In order to gain court approval for the settlement of a class action, the settlement has to be "fair and reasonable" to the class members.

Class actions also can be more expensive to litigate. For one thing, they have an extra layer of discovery. Discovery and motion practice often occur on class certification issues before any discovery or motions are allowed on the merits of the case. Also, experts usually must be retained sooner to respond to class certification motions. The scope of merits discovery and discovery from unnamed class members also adds a significant element of cost to most class actions.

In a class action, if the class is not certified, the plaintiff will appeal because an order denying certification is appealable immediately. But, if the class is certified, the defendant has no right to appeal and must defend the action on the merits before obtaining appellate review.

With a certified class action, the defendant will face a much bigger case to defend against. One reason is that a fluid recovery is allowed in a class action, but not in a representative action.

A fluid recovery under Code of Civil Procedure Section 384 requires that the "unpaid residual" of a class-action settlement or judgment must be distributed to "further the purposes of the underlying causes of action" or to "promote justice for all Californians."

In a representative action brought on behalf of the general public, however, the defendant keeps the unpaid residual.

To be sure, class actions offer the defendant certain advantages over a representative action. Perhaps the key advantage is that the resolution of a class action, whether through settlement or judgment, will be final and given preclusive effect of *res judicata*.

Class members who were given notice of the resolution are barred from suing for the same claim even if they received no benefit from the resolution.

A representative action does not offer the defendant the benefit of *res judicata*. A defendant that settles a representative action may be sued for the same conduct by a different plaintiff that did not receive any benefit from the settlement. The settlement of a representative action may not offer the defendant much "peace of mind."

Class actions offer defendants other benefits, as well. The well-defined standards for class certification, which limit and control the representation of absent parties, impose an obstacle for plaintiffs who want to sue on behalf of others.

Moreover, the plaintiff who brings a class action faces a more expensive and more difficult case to prosecute. The plaintiff faces the same burden of expert costs. The plaintiff must pay for the cost of class notice. Class trials can be more complex because the plaintiff must not only meet its burden of proof but also continue to satisfy the class-action requirements.

Despite the burdens involved with class actions, their number has increased recently. In a recent panel on Section 17200, a panelist noted a 100 percent increase in the number of Section 17200 class actions filed in the last year.

This increase may be attributable to footnote 6 in the Supreme Court's opinion in *Korea Supply Co. v. Lockheed Martin Corp.*, 29 Cal.4th 1134 (2003). In *Korea Supply*, the Supreme Court held that nonrestitutionary disgorgement is not an available remedy in an unfair-competition law action.

Before *Korea Supply*, plaintiffs sought nonrestitutionary "disgorgement of profit" in unfair-competition law actions. Such relief plainly is not available in any action brought by an individual or representative plaintiff under the unfair-competition law.

However, in footnote 6, the *Korea Supply* court stated that the issue of disgorgement in a class-action context was not before the court.

Since *Korea Supply*, there has been a marked increase in the number of unfair-competition law class actions filed by plaintiffs' lawyers looking for the elusive "disgorgement" remedy.

Many of these cases have been filed without regard to whether class actions are appropriate. Further, these cases are predicated on a fundamental misunderstanding of the meaning of footnote 6.

Nonrestitutionary disgorgement is not allowed under the unfair-competition law, period. A class action is merely a method for joining parties in one action. It does not add a remedy to the underlying substantive law.

In a class action, the only "disgorgement" allowed is the distribution of the "unpaid residual" of a restitution award. Nonrestitutionary "disgorgement" remains unavailable under the law even in the class-action context.

Nevertheless, plaintiffs have filed Section 17200 class actions at an increasing rate, based in part on the slim hope provided by footnote 6 that they could recover more than just restitution.

The lesson we learned in the last year is that plaintiffs will resort to class actions with increasing frequency if they have an incentive. The new law proposed in Proposition 64 may encourage more plaintiffs to bring class actions in the short term without regard to whether the class-action procedure is appropriate in those cases.

This trend probably will persist until plaintiffs begin to understand the difficulties presented by the class-action device.

Companies defending against class actions should avoid the temptation of settling questionable class actions by paying large amounts to the attorneys but little to class members. Such a tactic may resolve the short-term problem presented by the lawsuit but will only encourage more class actions of the questionable variety.

Instead, defendants should vigorously defend against class actions - through trial, if necessary. By pursuing an aggressive defense, defendants may discourage plaintiffs from using the class-action vehicle when doing so is not appropriate.

Ultimately, the benefits of Proposition 64 far outweigh any problem that might result. But, let businesses beware. While the new law may reduce the number of lawsuits in the near term, the lawsuits that are filed after the new law goes into effect may be more costly to defend. Be careful what you ask for. You just may get it.

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