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Tribal Sovereign Immunity in the Ninth Circuit: Moving Towards a More Reasonable Test

Julia Johnson*

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I. INTRODUCTION

Imagine one late evening in Anchorage, Alaska, when the snow is falling heavily—leaving nothing but slick, ice-glazed roads—you are riding your motorcycle slowly back home after an exhausting day at work. Your helmet is fastened and you are proceeding cautiously. As you turn the corner, out of nowhere, a drunk driver in a black sedan swerves and slams into you from the right. You are alive, fortunately, but you will need significant medical attention and your motorcycle has been reduced to scrap metal. The driver of the automobile is passed out drunk in the sedan, oblivious to the incident. Within minutes, the paramedics escort you to the hospital, where you undergo invasive surgery. You now require two weeks leave from work to recover. As you seek damages from the driver, you realize the drunk driver is a tribal employee who was racing on an errand for a catering banquet at a tribal casino. As a result of the tribe's sovereign immunity from suit, you cannot recover damages even though the driver was solely at fault. Instead, you are forced to purchase a new motorcycle and pay the outrageous medical expenses yourself. Now imagine if all tribal employees decided to engage in similar conduct—mayhem would result.

* J.D. Duke University School of Law, 2014.

In 2008, a very similar scenario occurred in *Cook v. Avi Casino Enterprises, Inc.* and the Ninth Circuit held that the injured plaintiff could not recover damages, despite the tribal employee's obviously drunken state.[1] For this reason, and others that will be explained below, tribal sovereign immunity is a doctrine desperately in need of revision. With numerous courts questioning the prudence of maintaining tribal immunity in its absolute form and the injustices that often occur to unsuspecting individuals, families, and communities as a result of upholding this immunity, it is now time to revisit tribal immunity and its role in the Ninth Circuit.

Tribal sovereign immunity, grounded in Article I of the United States Constitution,[2] provides tribes and their subsidiaries immunity from lawsuits, and in many cases, makes the tribe or tribal entity judgment-proof.[3] This immunity extends to land claims, rendering tribal land free from taxation, and safeguarding tribal possessions. While providing a constitutional safeguard is theoretically beneficial to protect tribal culture and self-governance in an era that no longer caters to their native lifestyle, it is not difficult to appreciate the doctrine's troubling ramifications.

For instance, because tribal corporations are protected under sovereign immunity so long as they are acting on behalf of the tribe, a tribal corporation may engage in gross negligence, injure, or even kill numerous non-Native Americans, without allowing for just compensation for the victims.[4] Or, as has been demonstrated in the Second Circuit, a tribe may utilize its immunity to prevent the local municipality from foreclosing on lands in its possession, even without properly demonstrating that it possessed sovereignty over the parcel in question.[5] For better or worse, it appears that tribal immunity must now be re-evaluated so that it comes into accordance with the realities of contemporary society. While Congress has yet to definitively decide tribal immunity's fate, there are numerous mechanisms that can be incorporated to better serve the needs of tribes and the communities that surround them in an era in which tribes and non-tribes must interact frequently.

1. Cook v. Avi Enters. Inc. 548 F.3d 718, 720–21, 727 (9th Cir. 2008).
2. U.S. CONST. art. I, §§ 2, 8.
3. *See, e.g. Cook*, 548 F.3d at 726 (holding that tribal sovereign immunity protected a defendant drunk driver from the plaintiff's damages claim).
4. *Id.*
5. *See* Oneida Indian Nation of N.Y v. Madison Cty. 605 F.3d 149, 151–52 (2d Cir. 2010) (holding that the remedy of foreclosure was not available to the county because the tribe was protected by tribal sovereign immunity).

This Article proposes that tribal immunity should be limited in disputes where its application would lead to excessively disruptive or manifestly unjust results. Although such a limitation may require case-by-case analysis, establishing baseline principles for impracticability or overly burdensome application of immunity can help to limit judicial arbitrariness and set a strong precedent. Therefore, over time, a long line of judicial decisions will be available to help define what constitutes an unjust application of tribal immunity, though some degree of judicial discretion will always remain.

Specifically, in tort actions, the Ninth Circuit should grant appropriate remedies to plaintiffs, thus limiting tribal immunity in this context and rightfully permitting a just remedy for unsuspecting victims who previously had no choice but to accept the consequences of the tribe's immunity from suit. Allowing for appropriate remedies, and thereby curtailing tribal immunity in these instances, will not harm the Native American tribes as long as they are carrying proper insurance, which is already the case for many tribes.[6] As a cautionary mechanism, an absolute damages cap should be developed to prevent outrageous judgments against a financially-strapped tribe. Curtailing tribal immunity and allowing for appropriate remedies in tort claims will not restrict tribal self-determination if carefully put into place.

Contract and possessory claims differ from tort claims because parties can anticipate the possibility that tribal immunity may be asserted. Generally, in non-commercial contract and possessory claims, tribal sovereign immunity should remain in its current form. The exception to that general rule would be in disproportionately disruptive circumstances, as will be later defined, or in cases that would lead to a blatant injustice. Moreover, contractors are likely aware of the potential entity's tribal status, and therefore, may be unwilling to enter into economic transactions with tribal companies due to their immunity. Restricting tribal immunity application in these limited instances will likely improve relationships between tribes and the communities they inhabit.

In the alternative, in the context of non-commercial, off-reservation claims, another approach would be to quash the presumption that tribal immunity is in place absent clear and effective consent to give up immunity from suit by placing the

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6. *See* 25 U.S.C. § 450f (c) (2012) (requiring the Secretary to obtain liability insurance for tribes in certain cases).

burden of proof on tribes to demonstrate that tribal immunity is still in force and has not been waived.[7] This is a more conservative alternative than restricting tribal sovereign immunity altogether, though its effects may be less pronounced. Additionally, in the commercial context, tribal sovereign immunity should be disallowed except in the limited instances where a tribe's capacity for self-governance is adversely impacted. Tribal sovereign immunity was designed to safeguard a tribe's capacity to assert sovereignty and maintain an independent government; where a tribe's self-sufficiency is not at issue, tribal sovereign immunity should not be permitted. On the contrary, if waiving tribal sovereign immunity would affect a tribe's capacity for self-governance and its ability to maintain a separate existence—for instance by draining the tribe's resources to the extent that the tribe can no longer function independently—then immunity from suit should be allowed. As a result, tribal resources will be safeguarded while courts will be better able to make decisions based upon justice, instead of mere legal formalities.

In light of the foregoing proposal, this Article addresses the future of tribal sovereign immunity in the Ninth Circuit in four parts.[8] First, this Article reviews the scope of tribal sovereign immunity conferred by the U.S. Constitution and its application to the current era, distinguishing tribal sovereign immunity from tribal sovereignty. Second, this Article reviews the *Oneida* cases and their successors, and argues that both the Second Circuit and the Supreme Court have been transitioning to a more functional application of tribal rights that harmonizes contemporary non-native American interests with those of the Indian tribes, though admittedly reasoning by analogy. Third, this Article analyzes the tribal immunity

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7. *See* DAVID E. WILKINS & K. TSIANINI LOMOWAIMI, UNEVEN GROUND: AMERICAN INDIAN SOVEREIGNTY AND FEDERAL LAW 224 (2002) ("[S]tate and federal governments retain the general power of sovereign immunity itself. Suits may be maintained only by express governmental permission; may be brought only in the manner prescribed by the governments; and are subject to the restrictions imposed by the sovereign ").

8. The Ninth Circuit's approach to tribal sovereign immunity is influential because its jurisdiction contains land home to relatively large populations of Native American tribes mostly unencumbered by the effects of mainstream American development up until the past century. Notably, many Native Americans residing in Alaska continue to rely upon tribal economic endeavors to support their livelihoods. *See, e.g. Tribal Nations*, U.S. CLIMATE RESILIENCE TOOLKIT, https://toolkit.climate.gov/topics/tribal-nations (last visited Sept. 18, 2016) (describing effects of U.S. industrial operations on native livelihood in Alaska).

doctrine in the Ninth Circuit, arguing that although the Ninth Circuit continues to uphold the doctrine, recent decisions suggest that moving toward a functionalist interpretation of tribal immunity is more likely to lead to fair outcomes. Finally, this Article proposes the creation of a more functional test for the Ninth Circuit—one that accommodates practical considerations while simultaneously furthering tribal interests—and examines how considerations in the Ninth Circuit may differ from those in the Second Circuit. This Article then concludes by reviewing policy considerations and argues that revising the doctrine will improve national and tribal well-being.

II. JUSTICE MARSHALL, SOVEREIGN IMMUNITY, AND THE PRESENT ERA

Tribal sovereign immunity has its underpinnings in the early development of the United States. Specifically, the United States Constitution provides that "[t]he Congress shall have [p]ower [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."[9] This provision effectively thrusts Native Americans into the constitutional framework and distinguishes Native American tribes as a separate sovereign entity[10] that may not be taxed.[11] The Supreme Court has since substantiated this position, as best evidenced in the "Marshall Trilogy" when Chief Justice John Marshall articulated the fundamental principles that continue to guide federal Native American law: that tribes possess nationhood status and retain intrinsic powers of self-government.[12]

Thus, tribal rights are derived from a tribe's status as a sovereign entity whose existence is grounded in the Constitution, and

9. U.S. CONST. art. I, § 8, cl. 1–3.

10. *See id.* (placing tribes on the same level as foreign nations).

11. U.S. CONST. art. I, § 2, cl. 3.

12. *See* Johnson v. M'Intosh, 21 U.S. 543, 574 (1823) ("The history of America, from its discovery to the present day, proves, we think, the universal recognition of [complete sovereignty]); *see also* Cherokee Nation v. Georgia, 30 U.S. 1, 39 (1831) ("There can be no dependence so antinational, or so utterly subversive of national existence as transferring to a foreign government the regulation of its trade, and the management of all their affairs at their pleasure"); Worcester v. Georgia, 31 U.S. 515, 561–64 (1832) ("The Cherokee nation is a distinct community occupying its own territory, with boundaries accurately described, in which the laws of Georgia can have no force with the assent of the Cherokees themselves ').

are not conferred by Congress.[13] Because tribal sovereign immunity is not a right granted in isolation but is derived from a tribe's status as a sovereign, it follows that tribal sovereignty is separate and distinct from tribal immunity.[14] Instead, tribal sovereignty encompasses all powers that tribes possess which are not expressly limited by a federal statute or treaty and are not inconsistent with the federal government's relationship with tribes.[15] Specifically, tribal sovereignty includes the tribe's right to govern tribal members and territory, and grants tribes the right to adjudicate claims and enforce rights within Native American territory.[16]

As sovereign entities, Native American tribes are granted sovereign immunity, meaning tribes cannot be sued or hailed into court, and this right prevents suit by both non-Native American and Native American parties.[17] Further, tribal immunity is not limited

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13. Andrea M. Seielstad, *The Recognition and Evolution of Tribal Sovereign Immunity Under Federal Law: Legal, Historical, and Normative Reflections on a Fundamental Aspect of American Indian Sovereignty*, 37 TULSA L. REV. 661, 688–89 (2002).

14. *Id.* at 665; *see generally* CHARLES WILKINSON & THE AMERICAN INDIAN RESOURCES INSTITUTE, INDIAN TRIBES AS SOVEREIGN GOVERNMENTS (1991).

15. Paul A. Matteoni, *Alaska Native Indian Villages: The Question of Sovereign Rights*, 24 SANTA CLARA L. REV. 875, 875 n.1 (1988).

16. *Id.* at 878.

17. Ralph W. Johnson & James M. Madden, *Sovereign Immunity in Indian Tribal Law*, 12 AM. INDIAN L. REV. 153, 190–91 (1984). The rights and restrictions under tribal sovereign immunity are the result of a long line of case law, beginning with the Marshall Trilogy, in which the United States affirmed the rights of Indian nations to assert legal standing in court cases. Next, in 1883, tribal courts were empowered to pass binding judgments, and in 1886, *United States v. Kagama*, 118 U.S. 375, 381–82 (1886), clarified the separation between the State and Indian reservation. Thus, early case law appeared to favor an expansive reading of tribal rights. *Id.* at 190–91. However, in 1887, the passage of the Dawes Act came as a preliminary blow to Indian rights and broke up tribal lands, distributing portions to Indian families, while selling the remainder of the lands to white Americans. *Id. See generally*, TRANSCRIPT OF DAWES ACT (1887), *available at* http://www.ourdocuments.gov/doc.php?flash=true&doc=50&page=transcript.

The twentieth century witnessed a similar trend, in which some tribal rights have been substantially encroached upon while other rights have been maintained. In 1978, *Oliphant v. Suquamish Indian Tribe*, 435 U.S. 191, 210–11 (1978), held that tribal courts lack jurisdiction over individuals who are not the members of an Indian tribe, though numerous questions surrounding this issue were left unanswered. In 1980, *Washington v. Confederated Tribes of Colville Indian Reservation*, 447 U.S. 134, 154 (1980), held that the sovereignty of tribes is subordinate to the United States federal government, though not to individual states. Presently, the federally recognized tribes interact with the United States as sovereign-to-sovereign, in a relationship between one government and another.

to the tribes themselves, but extends to tribally-owned corporations so long as the corporation is acting on behalf of the tribe.[18] Tribal immunity also extends to the employees of tribal corporations while they are acting in their official capacities and within their responsibilities as an employee.[19]

Though tribal immunity confers a safeguard against lawsuits, tribes may waive their immunity when it is in their interests to do so.[20] As granted under the Indian Reorganization Act of 1934, federally recognized tribes may assert sovereign immunity and bar suit.[21] If the tribe chooses to waive immunity, the written waiver must be clear and expressly state that the tribe has consented to suit. The court will then interpret the waiver narrowly.[22] If the tribe has voluntarily waived immunity, the court reviews whether this consent is unequivocal and unmistakable; a waiver of tribal sovereign immunity must be in written form and may not be

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Furthermore, states lack authority over tribal governments acting on tribal lands. *See also* Johnson & Madden, *supra* note 17, at 190–93.

Similarly, in 1981, *Montana v. United States*, 450 U.S. 544, 545–46 (1981), held that tribal nations do possess the capacity to control non-Tribe members, if they are acting upon tribal lands, if it is necessary in order to protect the political and economic interests of the tribe, or if it is necessary to protect the health or wellbeing of their members. Finally, in 1990, *Duro v. Reina*, 495 U.S. 676, 696–97 (1990), held that tribal courts may exclude 'persons whom they deem to be undesirable from tribal lands' and that '[t]ribal law enforcement authorities have the power if necessary, to eject them.

18. Mich. v. Bay Mills Ind. Comm. 134 S.Ct. 2024, 2037 (noting the *Kiowa* court upheld tribal sovereign immunity in commercial activities); Kiowa Tribe of Okla. v. Mfg. Techs. Inc. 523 U.S. 751, 760 (1998) ("Tribes enjoy immunity from suits on contracts, whether those contracts involve governmental or commercial activities and whether they were made on or off a reservation"); *see also Cook*, 548 F.3d at 726 ("[T]he settled law of our circuit is that tribal corporations acting as an arm of the tribe enjoy the same sovereign immunity granted to a tribe itself.").

19. *See e.g. Cook*, 548 F.3d at 727 ("The principles that motivate the immunizing of tribal officials from suit–protecting an Indian tribe's treasury and preventing a plaintiff from bypassing tribal immunity merely by naming a tribal official–apply just as much to tribal employees when they are sued in their official capacity.").

20. Miller v. Wright, 699 F.3d 1120, 1124–25 (9th Cir. 2012); *see also* COHEN'S HANDBOOK OF FEDERAL INDIAN LAW § 7.05 (2009) ("[T]ribal sovereign immunity is rooted in federal common law and reflects the federal Constitution's treatment of Indian tribes as governments in the Indian commerce clause ").

21. 25 U.S.C. § 5123 (acknowledging sovereignty of federally recognized Indian tribes).

22. *Id. see also* INDIAN REORGANIZATION ACT, 25 U.S.C. § 490, § 5139 (2016) ("A tribe may waive in writing any immunity from suit or liability which it may possess ").

implied.[23] Moreover, even if the tribe is deemed immune from suit, in contrast to tribal employees, individual tribal members are typically not extended such immunity; tribal officers only receive immunity if they are found to be acting within the scope of their representative authority.[24] Additionally, the United States federal government may waive a tribe's immunity without tribal consent, though it has recently come under scrutiny as to whether a clear and unambiguous statement by Congress is necessary to waive tribal rights,[25] or whether a government agency may independently waive immunity if deemed necessary.[26]

Tribal sovereign immunity differs from federal immunity namely in scope. Presently, tribal sovereign immunity is broader and less restricted than federal sovereign immunity; federal immunity has narrowed because of its unique relationship with the states, which also retain sovereignty.[27] In addition to being less absolute because it balances a special relationship with the states, the federal government has voluntarily curtailed immunity in several areas, such as for government agencies in instances of demonstrable wrongdoing.[28] For instance, federal immunity has been limited in some circumstances under the Federal Tort Claims Act,[29] which enables private plaintiffs to sue the United States for torts that are

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23. *Id.*

24. United States v. James, 980 F.2d 1314, 1319 (9th Cir. 2009) (stating that individual tribal members are not granted sovereign immunity).

25. Okla. Tax Com'n v. Citizen Bank Potawatomi Ind. Tribe of Okla. 498 U.S. 505, 510 (1991) ("Congress has always been at liberty to dispense with such tribal immunity or to limit it"); *see also* United States v. U.S. Fidelity & Guar. Co. 309 U.S. 506, 512 (1940) (holding that congressional authorization was needed to sue Indian tribes, even though many circuits allow tribes to unilaterally waive their immunity).

26. WILKINS & LOMOWAIMI, *supra* note 7, at 224. Some cases have held that tribal immunity may be waived, but the waiver must be clearly expressed. *Id.* However, during the 1996 hearing on sovereign immunity, a Bureau of Indian Affairs lead attorney stated that no conclusive legal evidence demonstrated that the federal government had the right to waive the tribe's immunity forcibly. *Id.* at 218.

27. Harvey Schweitzer, *Sovereign Immunity and the Foreign-State Enterprise in Alaska,* 4 UCLA–ALASKA L. REV. 343, 347–48 (1975). *See generally* Vicki C. Jackson, *Suing the Federal Government: Sovereignty, Immunity, and Judical Independence*, 35 GEO. WASH. INT'L L. REV. 521 (2003) (discussing limitations of immunity as applied to the federal government).

28. *See* C. Stanley Dees, *The Executive Branch as Penelope: Preserving the Tapestry of Sovereign-Immunity Waivers for Suits Against the United States*, 71 GEO. WASH. L. REV. 708, 708 (2003) ("Over the last 150 years, Congress has piecemeal enacted statutory waivers of federal sovereign immunity. ').

29. 28 U.S.C. §§ 1346(b), 2671–2680 (2012).

caused by federal officials or employees acting in their official capacities. Additionally, in patent claims, the Administrative Procedure Act waives sovereign immunity if the plaintiff requests a review of agency action.[30]

Though this Article will later demonstrate that there are numerous advantages to limiting immunity in some instances, critics may nonetheless suggest that tribal immunity should remain absolute because tribal sovereignty has traditionally conferred a complete right to immunity.[31] Along these lines, critics may argue that absolute immunity is consistent with the drafting history of the Constitution, when the states agreed to limit sovereignty.[32] Therefore, the Native Americans' absence during the negotiations that developed the constitutional framework is notable because states—unlike tribes—explicitly gave up portions of their immunity during this time.[33] Limitations on state sovereignty are sometimes justified on the grounds that states were active participants in the ratification process and had the opportunity to voice their concerns at that time.[34] On the contrary, tribes never relinquished their sovereign rights, neither during ratification nor later, suggesting tribal sovereign immunity should remain absolute.[35] Nonetheless, in response, one may argue that this view towards tribal sovereign immunity is not uniform and that tribes' lack of representation two hundred years ago should not confer a liberal application of tribal sovereign immunity to the extent that domestic interests are

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30. 5 U.S.C. § 702 (2012).

31. Amelia A. Fogleman, *Sovereign Immunity of Indian Tribes: A Proposal for Statutory Waiver for Tribal Businesses*, 79 VA. L. REV. 1345, 1347 (1993) (stating that Indian tribes are the only United States sovereign whose immunity has not been reduced); *see also Johnson v. M'Intosh*, 21 U.S. (8 Wheat.) 543, 574 (1823)("[Indians'] right of possession has never been questioned. The claim of government extends to the complete ultimate title, charged with this right of possession, and to the exclusive power of acquiring that right. ').

32. Merritt Schnipper, *Federal Indian Law—Ambiguous Abrogation: The First Circuit Strips the Narragansett Indian Tribe of Its Sovereign Immunity*, 31 W. NEW ENG. L. REV. 243, 254 (2009).

33. *Id.*

34. *See id.* ("Although not mentioned in the Constitution, the sovereign immunity of the states was recognized in the negotiations and compromises that led to ratification, and is thus fairly said to have a Constitutional basis. '). *See also* Alden v. Maine, 527 U.S. 706, 713 (1999) ("Various textual provisions of the Constitution assume the States' continued existence and active participation in the fundamental processes of governance ').

35. *Id.*

harmed.[36] Instead, balancing both Native American and non-Native American interests will lead to the most optimal application of tribal immunity because tribal rights will remain protected while gross injustices are avoided.

The rights conferred by tribal sovereign immunity are intended to safeguard tribal independence and self-government, though, as will be discussed below, the extent of this right has been debated. Some courts have not viewed the right as absolute, instead abrogating immunity in certain instances where acting otherwise would lead to unjust or overly burdensome results upon the non-Native American party. Other courts have questioned the proper application of tribal sovereign immunity, yet have upheld the law.

III. MODERN REFORMS OF TRIBAL SOVEREIGNTY IMMUNITY

Though tribal sovereign immunity was initially intended to confer substantial rights allowing for tribal sustainability, many courts, including the Supreme Court, have increasingly criticized its application in recent decades and have questioned the prudence of continuing to uphold immunity.[37] Whereas some courts have questioned tribal sovereign immunity while applying it nonetheless, other courts have clearly sought ways to circumvent tribal sovereign immunity by rendering the doctrine inapplicable or by invoking equitable remedies.[38]

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36. *See, e.g.* Santa Clara Pueblo v. Martinez, 436 U.S. 49, 71–72 (1978) (holding that tribal sovereign immunity bars lawsuit regarding a dispute over a tribal ordinance that bans tribal membership for the children of female tribal members' children who choose to marry a non-tribe member); *see also* Haile v. Saunooke, 246 F.2d 293, 298 (4th Cir. 1957) (holding that non-Indians could not bring action against the U.S. for individual injuries occurring on tribal land).

37. *See, e.g.* Kiowa Tribe of Okla. v. Mfg. Techs. Inc. 523 U.S. 751, 758 (1998) ("There are reasons to doubt the wisdom of perpetuating the doctrine [of tribal immunity]."). *See also Bay Mills Ind. Comm.* 134 S.Ct. at 2037 (citing *Kiowa* elucidated sovereign immunity may be inequitable when it applies to off-reservation commercial conduct).

38. *Compare id.* at 758 (applying tribal sovereign immunity despite expressing criticism for the doctrine), *with* Bittle v. Bahe, 192 P.3d 810, 827 (Okla. 2008) ("[T]he Tribe has no sovereign tribal immunity from plaintiff's negligence action."), *overruled by* Sheffer v. Buffalo Run Casino, PTE, Inc. 315 P.3d 359 (Okla. 2013).

While deferring to Congress, the Supreme Court has doubted the prudence of applying tribal immunity in certain circumstances.[39] These criticisms demonstrate that now is the time to revisit the present structure of tribal sovereign immunity. For instance, in 1998, in *Kiowa Tribe of Oklahoma v. Manufacturing Technologies, Inc.*, where an Oklahoma Indian tribe defaulted on a promissory note involving an off-reservation transaction valued at $285,000 plus interest, the Supreme Court begrudgingly held that because tribes possess immunity from suit, the lender could not bring suit to collect the money owed to him.[40] Thus, in a 6-3 decision, the *Kiowa* Court upheld tribal sovereign immunity and extended its application to non-reservation lands.[41] In so doing, Justice Kennedy, writing for the majority, was doubtful of tribal immunity, stating it developed "almost by accident" and mentioning that "[t]here are reasons to doubt the wisdom of perpetuating the doctrine."[42] Justice Kennedy continued by stating that in the present, interdependent era where tribes must interact with non-tribal entities to obtain many goods and services, tribal sovereign immunity may no longer be wise, especially because many unsuspecting victims are unaware of an entity's tribal status.[43] However, the Court was concerned

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39. *Kiowa*, 523 U.S. at 758. *See Bay Mills Ind. Comm.* 134 S.Ct. at 2039 (2014) ("Having held in *Kiowa* that this issue is up to Congress, we cannot reverse ourselves because some may think its conclusion wrong. Congress of course may always change its mind–and we would readily defer to that new decision. ').

40. *Kiowa*, 523 U.S. at 764–65 (Stevens, J. dissenting). There, Justice Stevens doubted the wisdom of unbridled application of tribal sovereign immunity, opining that:

> 'Despite the broad language used in prior cases, it is quite wrong for the Court to suggest that it is merely following precedent, for we have simply never considered whether a tribe is immune from a suit that has no meaningful nexus to the tribe's land or its sovereign functions. Moreover, none of our opinions has attempted to set forth any reasoned explanation for a distinction between the States' power to regulate the off-reservation conduct of Indian tribes and the States' power to adjudicate disputes arising out of such off-reservation conduct.

41. *Id.* at 760.

42. *Id.* at 756–58 (stating that tribal sovereign immunity has been perceived necessary to protect weak tribal governments from the states). *See, e.g.* Mescalero Apache Tribe v. Jones, 411 U.S. 145, 146 (1973) (where the Mescalero Apache Tribe operated a ski resort, the Court expressed doubts that the doctrine should be extended to immunity from local regulations).

43. *Kiowa*, 523 U.S. at 758. ("[I]n our interdependent and mobile society, however, tribal immunity extends beyond what is needed to safeguard tribal self-governance. This is evident when tribes take part in the Nation's commerce.

about creating policy through its judicial decisions and noted the Court's role was to uphold the law and not develop it, and therefore upheld tribal sovereign immunity.[44]

Nonetheless, the Court's defense indicates that upon further review, the court may find tribal sovereign immunity to be outdated and unjust. Justice Kennedy's doubtful support for tribal sovereign immunity in *Kiowa* demonstrates that attitudes toward Indian rights have shifted substantially since many of the early founders, such as Alexander Hamilton who suggested that sovereignty confers an absolute right to immunity from suit, which would likewise extend to Indian nations.[45] Similarly, Justice Kennedy's concerns have been echoed in other courts over the past decade, and several circuits have witnessed a flurry of litigation questioning the proper application of tribal sovereign immunity.[46] The various opinions in *Kiowa* indicate that the U.S. Supreme Court may gradually deviate from the original, absolute interpretation of tribal sovereign immunity, where there is no room for flexibility on behalf of the courts or the parties.[47]

A number of recent cases originating in the Second Circuit have taken a more functional approach towards tribal rights in other contexts, particularly in tribal land possession claims. Many of these opinions are broad enough to suggest that application of original tribal rights should move away from a formalist, bright-line approach. In particular, the *Oneida* cases have involved an ongoing series of disputes between the Oneida Indian Nation ("OIN") and New York municipalities pertaining to territorial sovereignty over land in upstate New York.[48] Moreover, the Supreme Court has

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Tribal enterprises now include ski resorts, gambling, and sales of cigarettes to non-Indians.').

44. *Id.* at 760.

45. *See, e.g.* THE FEDERALIST NO. 81, at 2 (Alexander Hamilton) (J. & A. M'Lean, eds. 1788), https://www.congress.gov/resources/display/content/The+Federalist+Papers#TheFederalistPapers-81 ("It is inherent in the nature of sovereignty not to be amenable to the suit of an individual without its consent. This is the general sense, and the general practice of mankind; and the exemption, as one of the attributes of sovereignty, is now enjoyed by the government of every State in the Union. Unless, therefore, there is a surrender of this immunity in the plan of the convention, it will remain with the States, and the danger intimated must be merely ideal. (emphasis omitted)).

46. *See, e.g.* Memphis Biofuels, LLC v. Chickasaw Nation Indus. Inc. 585 F.3d 917, 922 (6th Cir. 2009) ("This result may seem unfair, but that is the reality of sovereign immunity.').

47. Schnipper, *supra* note 32, at 254.

48. *See generally* Oneida Indian Nation of N.Y v. Oneida Cty. 414 U.S. 661 (1974); Oneida Cty. v. Oneida Indian Nation of N.Y 470 U.S. 226 (1985).

opined on several of the Second Circuit's *Oneida* disputes, and has sent a strong statement that formal adherence to bright-line rules may be impractical when interpreting tribal rights.

Particularly, in 2005, the Supreme Court's opinion in *City of Sherrill, New York v. Oneida Indian Nation of New York*,[49] one of the latest cases in the *Oneida* series, suggests that pragmatic considerations, including the disruption wrought on the non-Indian community and the expectations of the local residents, must be reviewed in disputes involving tribal rights. Though reasoning by analogy, *Sherrill* demonstrates that the Supreme Court continues to disdain a formal application of tribal rights and these sentiments may extend broadly to sustain an inference that a rigid approach should be avoided in tribal sovereign immunity disputes as well. In *Sherrill*, where the OIN sought to reclaim former Indian lands they had long ago lost title to via the open market, the Supreme Court held that the OIN could not unilaterally revive its "ancient sovereignty" over the land, either in whole or in part.[50] The majority opinion, penned by Justice Ruth Ginsburg, reviewed several factors, including the distinctly "New York" character of the area and the settled expectations of its residents, and suggested it would be impracticable and unjust to the non-Indian municipality to hold otherwise.[51] Furthermore, the Court also proposed looking to the effects on the local municipal government and surrounding landowners to determine whether an equitable remedy may be invoked, therefore curtailing tribal rights. The Court noted that the longstanding observances and the settled expectations of those in the community may be used as guideposts.[52]

Because Oneida County and the City of Sherrill were almost entirely populated by non-Indians, by returning the land to the OIN, the expectations and lives of nearly all landowners in the area would

49. City of Sherrill v. Oneida Indian Nation of N.Y 544 U.S. 197, 199 (2005).

50. *Sherrill*, 544 U.S. at 202–03.

51. *Id.* The *Sherrill* court reviewed several other factors in reaching its decision. First, the Court noted that the Oneidas had not held possession of this parcel of land since 1805. *Id.* Second, most of the OIN members had resided outside of New York since the middle of the nineteenth century. *Id.* at 206–07. Third, the area possessed a distinctly non-Indian character and most of the land's current residents were non-Indian. *Id.* at 202. Fourth, the Oneida's exceedingly long delay in seeking judicial relief suggested acquiescence. *Id.* at 221. Finally, the court noted that the wrongs committed against the OIN occurred in the early years after the formation of the United States, and New York had continuously controlled the parcel in question for at least two centuries. *Id.* at 210–11.

52. *Id.* at 218–19.

be disrupted and equitable considerations precluded the application of tribal rights.[53] In ruling against the OIN, the Court also pointed to evidence that New York had possessed regulatory jurisdiction over the land for at least two centuries, during which time the OIN did not contest New York's control.[54] Finally, the court asserted that "long acquiescence" by the tribe may be a controlling factor when it comes to assertions of claims to territory and may be used to indicate the tribe's intent that it no longer wishes to possess the parcels.[55] As a result, the OIN's long absence from the land demonstrated that it would be inappropriate to restore the OIN's sovereignty.[56] The Court argued that the OIN could have asserted the same claims while the land was predominately still wilderness, instead of waiting until after the area had been fully developed.[57] In *Sherrill*, the United States Supreme Court weighed the unfairness to the non-Indian population of upholding tribal rights and returning sovereignty over the land to the OIN after commercial development. In so doing, the *Sherrill* court demonstrated that tribal rights must be balanced with those of the non-Indian community, and that a pragmatic approach must often be taken to achieve this end.

A. The Second Circuit

Later cases in the Second Circuit have attempted to clarify the *Sherrill* court's intentions and have indicated that a functional approach should extend to claims involving other tribal rights and not be limited to land disputes. The Second Circuit's recent decisions suggest that limiting tribal sovereign immunity rights may

53. *Sherrill*, 544 U.S. at 219–20. At the present time, Oneida County and the City of Sherrill are predominately inhabited by non-Indian residents. *Id.*

54. *Id.* at 218; *see also* Ohio v. Kentucky, 410 U.S. 641, 651 (1973) ("The rule, long settled and never doubted by this court, is that long acquiescence by one State in the possession of territory by another and in the exercise of sovereignty and dominion over it is conclusive of the latter's title and rightful authority.") (citation omitted).

55. *Sherrill*, 544 U.S. at 218 ("When a party belatedly asserts a right to present and future sovereign control over territory, longstanding observances and settled expectations are prime considerations."). Therefore, it follows that belated assertions of sovereignty over a territory may be rendered invalid because such claims disrupt the settled expectations of the land, as well as longstanding observances and uses, which may have occurred for centuries. *See id.* (discussing the acquiescence doctrine).

56. *Id.* at 219.

57. *Id.* at 214–15 ("[S]tandards of federal Indian law and federal equity practice preclude the Tribe from rekindling embers of sovereignty that long ago grew cold.").

be supported by *Sherrill*'s reasoning. In particular, *Cayuga Indian Nation of New York v. Pataki* applies *Sherrill*'s holding to a similar tribal land dispute and proposes a test by which *Sherrill* can be applied more effectively.[58]

In *Cayuga*, where the Cayuga Indian Nation sought the return of 64,015 acres of upstate New York land, which the tribe claimed it had been unlawfully dispossessed during the 18th century,[59] the Second Circuit utilized *Sherrill* and clarified its application by proposing the development of an "impact" test, in which "'disruptive,' forward-looking claims are subject to equitable defenses."[60] Under this test, the key criterion is whether the claim is inherently disruptive and its application is not limited to claims involving potentially burdensome remedies. The *Cayuga* court, acknowledging that the Supreme Court had failed to develop a formal standard for determining when *Sherrill*'s equitable defenses may apply, stated that "the broadness of the Supreme Court's statements indicates to us that *Sherrill*'s holding is not narrowly limited to claims identical to that brought by the Oneidas, seeking a revival of sovereignty, but rather, that *these equitable defenses apply to 'disruptive' Indian land claims more generally*."[61] The Court thereby suggested that *any* disruptive application of tribal rights—including, perhaps, tribal sovereign immunity—could be subject to equitable defenses.

Moreover, the court further supported the creation of an "impact" test that would be applicable, even though different claims were at issue, because the claims in *Cayuga* were "comparably disruptive," and the remedies were likewise comparable.[62] As such, the *Cayuga* court demonstrates that *Sherrill*'s holding was left intentionally broad and can be analogized to extend to other tribal rights.[63] Also, as suggested in the Supreme Court's earlier opinion in *Kiowa*, moving towards a functionalist approach of tribal

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58. 413 F.3d 266, 276–77 (2d Cir. 2005).

59. *Id.* at 268.

60. *Cayuga*, 413 F.3d at 277: *see Sherrill,* 544 U.S. at 220 ("Recognizing these practical concerns, Congress has provided a mechanism for the acquisition of lands for tribal communities that takes account of the interests of others with stakes in the area's governance and well-being.").

61. *Id.* at 274 (emphasis added).

62. *Cayuga*, 413 F.3d at 274; *see also* Yankton Sioux Tribe v. United States, 272 U.S. 351, 358 (1926) (discussing the fairness of rescinding land from innocent purchasers).

63. *Cayuga*, 413 F.3d at 274.

immunity is in line with the Court's sentiments towards the doctrine.[64]

Proponents of tribal sovereign immunity reform may argue that *Cayuga* suggests that in the case of a disruption to the settled expectations of those in the local area or an inherent disruption and burden to the non-Indian party, then the application of tribal sovereign immunity should be barred. This requires more than mere inconvenience placed upon the non-Indian party; the disturbance must instead interfere with the longstanding observances or reasonable expectations of individuals who enter into a commercial transaction with an Indian party.[65] Moreover, this application should not be limited to the possessory context, but should extend to disruptive claims more generally. The *Cayuga* court also emphasized the broadness of *Sherrill*'s holding and focused more upon the impact of the resulting remedy than adhering to a proper application of tribal rights.[66] Under *Cayuga*, achieving a just result is more important than following the legal text verbatim.

Accordingly, the Supreme Court and the Second Circuit appear to be moving towards a functionalist interpretation for certain tribal rights. Both *Sherrill* and *Cayuga* suggest that this approach was intended to apply broadly and, in the future, will likely expressly encompass tribal sovereign immunity as well. Nevertheless, the *Sherrill* decision—holding that tribal sovereignty may not be applied when doing so would disrupt the settled expectations of the surrounding landowners and impact the local area—has been criticized because the Court's opinion seems to ignore whether the defendant intentionally harmed the tribe or other reasons the tribal claim may be valid despite being disruptive. *Sherrill* likewise appears to elevate the interests of the mainstream community to a degree greater than ever before, with some criticizing the remedy as "new laches" because they believe that the *Sherrill* Court's decision did not fully comport with a traditional laches remedy.[67] Critics

64. *Id.* *see also Kiowa,* 523 U.S. at 758 (1998) ("[T]ribal immunity extends beyond what is needed to safeguard tribunal self-governance. ').

65. *Id.* at 285.

66. *Id.* at 274.

67. Kathryn E. Fort, *Disruption and Impossibility: The Unfortunate Resolution of the Iroquois Land Claims*, 11 WYO. L. REV. 375, 395 (2011). There, the author argued that only the lowest level of disruption is needed to bring a claim, and therefore states and counties could argue that nearly any claim is disruptive, and may even seek money damages as a remedy. Moreover, an argument may be made that the Second Circuit was applying 'new laches' to a sovereign in order to avoid conflicting with precedent. *Id.*

suggest that lacking any equitable doctrine upon which to grant relief, the *Sherrill* Court instead created an equitable remedy to provide an avenue of relief for the counties where none previously existed.[68] Correspondingly, *Sherrill* may open a floodgate of new equitable defenses in Indian disputes.[69]

B. *The Ninth Circuit*

Though the Supreme Court and the Second Circuit seem supportive of utilizing a functionalist interpretation for some tribal rights, the Ninth Circuit generally follows a bright-line, formalist application of tribal sovereign immunity. While the Ninth Circuit continues to uphold tribal sovereign immunity in its absolute form, there are numerous arguments that demonstrate why a functionalist approach is more appropriate and fair.

In suggesting that the Ninth Circuit should transition to a more functional approach, one need only revisit the case that inspired the introductory narrative, where glaring injustices were wrought upon an unsuspecting victim after tribal sovereign immunity was upheld despite evidence of gross negligence by a tribal employee. In 2008, the Ninth Circuit upheld tribal sovereign immunity in *Cook v. Avi Casino Enterprises, Inc.* for the casino enterprise and its employee because the casino was operated and maintained by a tribal corporation acting on behalf of the tribe despite the employee's obvious intoxication when she hit and injured a motorcyclist with her car.[70] In so doing, *Cook* set forth a strong precedent that tribal sovereign immunity may apply to tribes' profit-generating businesses, and the Court extended this immunity to tribal employees, holding that "tribal immunity protects tribal employees acting in their official capacity and within the scope of their authority."[71] While the *Cook* Court followed a formalist interpretation of tribal sovereign immunity, the Court admitted that "[t]he Supreme Court has somewhat grudgingly accepted tribal sovereign immunity in the commercial context," thereby acknowledging that, as in *Kiowa*, a pragmatic approach to tribal immunity might instead be more effective to prevent glaring injustices, but nonetheless the Ninth Circuit adhered to precedent.[72]

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68. *Id.* at 394–95.
69. *Id.*
70. *Cook*, 548 F.3d at 721–24.
71. *Id.* at 727; *Kiowa*, 523 U.S. at 754–55.
72. *Cook*, 548 F.3d at 725.

Additionally, in *Cook*, the Ninth Circuit utilized the "arm" test developed in *Allen v. Gold Country Casino* for tribal sovereign immunity disputes.[73] The *Cook* court stated, "the settled law of our Circuit is that tribal corporations acting as an arm of the tribe enjoy the same sovereign immunity granted to a tribe itself."[74] However, the "arm" test is problematic because the test extends well beyond safeguarding tribal sustainability and often results in conferring immunity where a tribe's self-governance is not at issue. Although the "arm" test is settled precedent in the Ninth Circuit, the courts should only apply it in limited circumstances. Instead, a corporation's relationship to the tribe's capacity for self-governance should be carefully considered, as opposed to merely reviewing the link to the tribe itself. In particular, the "arm" test sustains an overbroad application of tribal sovereign immunity because not every tribal corporation is always acting to the direct benefit of the tribe, especially in instances of employee negligence. Therefore, immunity should not extend down the chain by default unless these protections are warranted. Nonetheless, despite these criticisms, the "arm" test is frequently applied in tribal sovereign immunity disputes and has been used in the Ninth Circuit to extend tribal sovereign immunity's reach beyond the tribe itself.[75]

Consequently, the Ninth Circuit appears content to maintain a broad interpretation of tribal sovereign immunity, especially in the context of tribal corporations.[76] However, it is not practicable or wise to perpetuate such an expansive application of the doctrine, especially when a tribal corporation has not fully disclosed to the other party that it intends to retain immunity, or in the context of an unsuspecting victim who has no choice but to accept immunity. As will be explained in the following section, the Ninth Circuit should refrain from permitting tribal sovereign immunity in many instances in which a tribe's capacities for self-governance, self-sufficiency, and self-determination will not be harmed. Though more tedious than applying a bright-line rule, doing so

73. 464 F.3d 1044, 1045 (9th Cir. 2006). The actions that the tribal corporations have taken, often on 'behalf' of a tribe, remain a major source of dispute in the Ninth Circuit.

74. *Cook*, 548 F.3d at 725.

75. *Id.*

76. *See id.* (' the settled law of our circuit is that tribal corporations acting as an arm of the tribe enjoy the same sovereign immunity granted to a tribe itself.").

will move the Ninth Circuit towards the national trend of limiting the scope of tribal immunity.

IV RESTRICTIONS ON TRIBAL SOVEREIGN IMMUNITY WHEN FORESEEABILITY IS LACKING

As demonstrated above, an absolute bar to lawsuits against Indian tribes often leads to injustice and continuing tensions. Indian tribes are unique sovereign entities because larger communities, whose cultures and lifestyles are dissimilar to their own, surround them, resulting in constant interaction. As a result, tribal sovereign immunity, in its present form, drives a wedge between Indian tribes and the communities that border them. With contemporary society becoming increasingly interdependent, there is a pressing need to consider how the doctrine will affect the tribe's relationship with non-Indians, especially as they interact in the workplace and with the larger community. Consequently, revising the parameters of tribal sovereign immunity and curtailing its application in circumstances where justice warrants so doing will result in a more equitable use of tribal rights, while safeguarding essential tribal interests, such as self-governance and cultural autonomy.

A. Tort Liability and Commercial Claims

As a result of the potentially gross inequities wrought by unjustly invoking the doctrine, tribal sovereign immunity should be curtailed in instances in which the victims are unsuspecting and helpless, specifically in tort liability cases.[77] Moreover, immunity should be limited—though not curtailed completely—in the commercial context. Tribal corporations, by agreeing to compete on the open market, should not receive an unfair advantage over mainstream corporations.

First, in light of the injustices discussed previously, tort claims are a prime example of "disruptive" Indian disputes that can have a significant, negative impact upon a victim.[78]

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77. *See Cook*, 548 F.3d at 720–21 (dismissing claim for damages on the grounds of tribal sovereign immunity after the tribal corporation allowed an intoxicated employee to drive drunk injuring the plaintiff).

78. *See Cayuga*, 413 F.3d at 268 (discussing damages excess of thirty million dollars following disruptive suits). This argument suggests that the disturbance need not be related to a land claim, but may include disruption more generally. *Sherrill*'s holding may thus be extended, by analogous reasoning, to encompass 'disruptive' Indian claims more generally, therefore including 'disruptive'

Consequently, the injured non-Indian party should be entitled to appropriate damages in tort actions, whether the injury occurred on-reservation or off-reservation. Allowing for non-Indian victims to recover appropriate damages would thereby limit tribal sovereign immunity in this circumstance and will help to prevent glaring injustices such as those depicted in *Cook*, in which the unsuspecting plaintiff was the victim of gross negligence by a tribal employee but recovery was barred.[79]

Furthermore, creating an absolute damages cap or a similar mechanism by which to curtail excessive damages awards will ensure that tribal sustainability is not impacted as a result of this change. Since many damages claims result from the actions of tribal corporations, these awards will continue to be compensated by the tribal corporations or their insurance companies, and the tribe's treasury itself will often not be the source of funding. In addition, tribes and their corporations are unlikely to be excessively burdened by allowing for appropriate damages in tort actions; this is portrayed by the fact that tribes have already assented to application of many non-discriminatory state and federal laws involving penalty fines for off-reservation activities,[80] thereby demonstrating that curtailing tribal sovereign immunity in tort claims is merely another mechanism by which to improve public welfare without significantly infringing on tribal rights.[81] Instead, if instituted properly and within reasonable limits, a tribe's fiscal resources will not be drained and the tribe's sustainability will not be placed at risk.

Secondly, while the rationale behind the need to curtail tribal sovereign immunity in the tort context has been previously

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assertions of tribal immunity that significantly and adversely affect a non-Indian party. *See also Sherrill*, 544 U.S. at 220 (2005) (addressing how disruption of a claim extends to issues of local tax rolls and interests of others).

79. *Cook*, 548 F.3d at 727.

80. *Id.* Tribal sovereign immunity has already been abrogated in several instances when it was in the public interest to do so, though namely via acts of Congress or state governance. For instance, the Tenth Circuit has held that the Safe Drinking Water Act applies to tribes because tribes constitute a municipality under the terms of the Act. Osage Tribal Council v. U.S. Dep't of Labor, 187 F.3d 1174, 1181 (10th Cir. 1999). Similarly, the Eighth Circuit has stated that application of the Resource Conservation and Recovery Act of 1976 curtails tribal sovereign immunity where it conflicts with the Act. Blue Legs v. U.S. Bureau of Indian Affairs, 867 F.2d 1094, 1097 (8th Cir. 1989). Nonetheless, each of these instances of curtailing immunity has come from a clear manifestation by Congress.

81. *See* David Blurton, *Tribal Sovereignty: Alaskan Native Exercise of Sovereign Power*. 12 AM. INDIAN L. REV. 245, 245–46 (1984) (noting that Indian actions outside the reservation are subject to state laws).

portrayed, immunity should also be limited in many commercial claims for similar reasons as elucidated in tort claims. In demonstrating that a more restrictive test is warranted in commercial disputes, one need only look to tribal corporations to see that these entities often invoke immunity to save litigation costs and to obtain advantages over mainstream corporations. However, by agreeing to operate outside of a tribal reservation, tribal corporations should be subjected to the same rules as other businesses under the basic tenants of a capitalist market. In addition, informational imbalances may also arise, such that the tribal corporation knows it may assert sovereign immunity at any time, while the non-Indian party lacks such knowledge. Furthermore, many tribal businesses may be indistinguishable from non-Indian corporations, and the average individual may not be on alert to investigate.[82] Finally, tribal corporations often waive immunity in order to obtain a higher credit rating and in other instances where the tribe itself is not impacted. By allowing tribal corporations the option to maintain immunity, and thereby avoid the risks of lawsuit, these corporations are conferred a significant advantage, even though tribal resources may not be proportionately benefitted nor may the tribe's capacities for self-determination or self-governance be similarly privileged.

Therefore, in the commercial context, courts should carefully review whether tribal self-governance and culture will be impacted and apply tribal sovereign immunity only when the tribe itself will be directly harmed without immunity.[83] Because tribal sovereign immunity exists solely to protect limited and irreplaceable tribal resources from large judgments and safeguard tribal self-governance, immunity should only be available in the commercial context when the tribe's capacities for self-determination, including self-governance and cultural autonomy, or other federal rights, will

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82. Brian C. Lake, *The Unlimited Sovereign Immunity of Indian Tribal Businesses Operating Outside the Reservation: An Idea Whose Time Has Gone*, 1996 COLUM. BUS. L. REV. 87, 101 (1996).

83. *See Sherrill*, 544 U.S. at 219–21 (noting that the reestablishment of Indian sovereign control on the land at issue would burden state and local government and adversely affect neighboring landowners). *Sherrill*'s holding should be extended to tribal sovereign immunity claims, and as such, tribal sovereign immunity's application should be barred in situations where to do otherwise would disproportionately disrupt the local community or harm the public's welfare. *Id.* In evaluating whether tribal immunity should be applied, under *Sherrill*, the court should review whether the basis of the claim brought is intrinsically disruptive in itself, not limiting its analysis to the remedy at issue. *Id.*

be adversely impacted.[84] As a result, tribal sovereign immunity will likely be curbed significantly because a corporation is often only tenuously and indirectly linked to tribal self-governance and tribal practices. Tribal sovereign immunity was not created to confer advantages in the workplace and in commercial endeavors, but was created more narrowly to protect the rights of a sovereign. Consequently, under this interpretation, a court should apply tribal sovereign immunity only if the tribe's cultural and religious practices, tribal government, or economic sustainability would be otherwise at risk, and this will result in a more acceptable and even-handed application of tribal sovereign immunity.[85]

In a more conservative alternative, implementing a policy mandating full disclosure, without waiving tribal sovereignty rights, is another mechanism for courts to consider in resolving commercial disputes. As such, the key criterion that a court must review is whether the tribe had adequately disclosed to the non-Indian party whether or not tribal sovereign immunity had been waived before the dispute.[86] The full disclosure test therefore shifts the burden of proof and places it upon the tribal corporations—the corporation effectively waives its rights to tribal sovereign immunity unless it explicitly informs the other party ahead of time that it will retain immunity.[87] There are numerous reasons why a full disclosure policy should be created, including the need to eliminate

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84. Lake, *supra* note 82, at 97.

85. *See id.* at 92 (noting that courts have looked to the general purposes and long-term goals underlying federal Indian policies and programs, particularly the goals of self-determination and protection of the tribe's economic assets).

86. *Id.* at 91. Tribes should be allowed to maintain immunity for all activities of their choosing, but must openly disclose their intentions and must arrange to compensate those who are voluntarily affected. *Id.*

87. *Id.* at 110–11. The author proposes that

> '[a] tribal entity may retain any part or all of its sovereign immunity in connection with a contract, loan, or any other business transaction, if and only if it does so explicitly in a written instrument signed by all the parties involved in the transaction. The tribal entity may not retain any of its sovereign immunity against tort victims, involuntary creditors, or any other individual or entity which is not a party to the signed agreement.

Id. at 111. In addition, the 'amount of damages awarded as compensation in a tort action against a tribal entity for its off-reservation conduct shall be limited to the total amount of liability insurance coverage carried by the entity, provided that the amount of coverage carried is consistent with industry practice.' *Id.*

the possibility that non-Indian individuals and companies are unaware that the tribe has the right to bar suit. Also, mainstream contractors will be more amenable to, and more likely to engage in business with tribal corporations, if tribal sovereign immunity is openly disclosed before all commercial transactions.[88] Likewise, the full disclosure test also comports with good policy sense because it strikes a balance between abrogating tribal sovereign immunity and retaining it in its absolute form.[89] In purely contractual transactions, the protections necessary shall be the same because the parties will need advance knowledge of the special rights granted to Indian tribes.[90] Finally, limiting tribal sovereign immunity in commercial endeavors is in line with Congress's opinion on tribal rights more generally, which seeks to help tribes reach self-determination, but goes no further.[91]

Although limiting tribal sovereign immunity in tort and commercial disputes will restore balance to the application of tribal rights, there are several criticisms of this position. First, one may counter that tribes, some of which are struggling financially, possess a relationship with the United States as akin to "wards of the state" and consequently would be rendered helpless without special immunities from suit.[92] In addition, one may argue that large judgments against the tribe could drain the tribe's fiscal resources and threaten the tribe's existence.[93] However, under the proposed test, tribal sovereign immunity would still be available if the

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88. *Id.* at 111.

89. *Id.*

90. *See* Katherine J. Florey, *Indian Country's Borders: Territoriality, Immunity, and the Construction of Tribal Sovereignty*, 51 B.C. L. REV. 595, 631–32 (2010) (discussing the complexities of waiving immunity in business deals).

91. DAVID H. GETCHES & CHARLES F. WILKINSON, CASES AND MATERIALS ON FEDERAL INDIAN LAW 151 (2d ed. 1986). Since 1961, Congress has promoted tribal self-governance, self-sufficiency, and self-determination, and has even described it as the 'overriding goal' of Indian congressional policy. *See also* California v. Cabazon Band of Mission Indians, 480 U.S. 202, 216 (1987) ("[t]he inquiry is to proceed in light of traditional notions of Indian sovereignty and the congressional goal of Indian self-sufficiency and economic development.").

92. *Id.*

93. *See* Cherokee Nation v. Georgia, 30 U.S. 1, *17 (1831) (describing the relationship between the U.S. and Indian tribes). There, the Supreme Court opined that '[Tribes] may be denominated domestic dependent nations. They occupy a territory to which we assert a title independent of their will, which must take effect in point of possession when their right of possession ceases. Meanwhile they are in a state of pupilage. Their relation to the United States resembles that of a ward to his guardian." *Id.*

tribe's intrinsic capacities for self-determination were at stake.[94] As noted above, tribal sovereign immunity will only be barred when its application is superfluous and does not directly impact the tribe.

Secondly, critics may argue that a bright-line rule would be more consistent and easier to follow and that invalidating tribal immunity in some contexts but not others will lead to unbridled judicial discretion and result in arbitrary decisions.[95] Nonetheless, in commercial disputes, the distinction for commercial entities under the proposed test is much simpler than it appears. Under the Indian Reorganization Act, tribal entities must file as Section 16 governmental entities or Section 17 corporate entities.[96] While a tribal entity may wrongfully file under Section 16 to confer immunity, the real test for the courts will be to determine which of the two categories the entity in a tribal dispute falls within, and these categories are already well-defined.[97] After enough disputes are decided over time, judicial discretion will be limited between these two categories.

Additionally, judicial arbitrariness may be restrained by intertwining the Ninth Circuit's "arm" test with tribal sovereign immunity.[98] The "arm" test engages in a multi-factor analysis to discern whether or not a corporation is functioning as an "arm" of the tribe.[99] Likewise, the Arizona Supreme Court has proposed

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94. *See* Lake, *supra* note 82, at 112–13 (the solution only requires that the tribal businesses openly acknowledge they are retaining sovereign immunity).

95. *See* Thomas P. McLish, *Tribal Sovereign Immunity: Searching for Sensible Limits*, 88 COLUM. L. REV. 173, 189 (1988) (Acknowledging the risks of judicial capriciousness, the author proposes '[t]he most important factors a court should consider in determining the extent to which tribal immunity furthers the federal policy interests on which it is based are (a) whether the suit arises out of bona fide cultural or religious practices by a tribe; (b) whether the activity was governmental or commercial in nature; (c) whether the activity took place on or off the reservation; and (d) whether recognition of immunity would amount to an unjustifiable windfall to the tribe.').

96. *Id.* at 189–90.

97. *See id.* at 190 (describing the purpose and treatment of Section 16 governmental entities and Section 17 corporate entities); *see also* Fogleman, *supra* note 31, at 1375 (arguing that if a waiver of immunity is applied, the waiver statute should be clear should clearly distinguish between the tribe itself and the tribal corporation, with the latter waiving immunity under section 17 of the Indian Reorganization Act of 1934).

98. *See Cook*, 548 F.3d at 725–26 (applying the 'arm' test and stating 'the settled law of our circuit is that tribal corporations acting as an arm of the tribe enjoy the same sovereign immunity granted to the tribe itself.").

99. *Id.*

a similar provision called the "subordinate entity" test.[100] Under this altered version of the "arm" test, the court reviews whether the corporation is sufficiently related to the tribe's capacities for self-governance or its ability to continue functioning as an independent entity, utilizing a series of pre-defined factors. The court must use these factors as a basis for its decision as to whether self-governance will be impacted. In doing so, it will be difficult for the court to reach wholly dissimilar positions using similar facts. As such, the court need only to expand upon the legal tests it has already created to incorporate a restricted version of tribal sovereign immunity.[101] Moreover, support for curtailing this right already exists with regard to other sovereigns, such as the corporations of foreign nations who seek to engage in commercial activity with the United States.[102] As a result, eliminating tribal sovereign immunity in the commercial context will not thwart tribes' abilities to engage in economic activity or exist independently, and will not threaten the tribes' separate fiscal viability.[103] Where none of these capacities are at issue, but the development merely builds upon the tribe's economic endeavors, the doctrine is inappropriate.

Finally, there are better mechanisms to promote the self-determination of the tribe than by allowing for broad-based tribal immunity.[104] Instead of providing a distinctly negative right to tribal entities, the government could develop a number of endeavors that would aid tribes and foster their self-governance; tribal sovereign immunity is not the most effective mechanism to promote tribal governments, and tribes will only be able to reach parity with mainstream America by competing on the open market.[105]

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100. Dixon v. Picopa Constr. Co. 772 P.2d 1104, 1108–09 (1989). The *Dixon* court stated that most tribal corporations do not meet the criteria regarding protection of tribal self-determination and protection of its assets in order to warrant an application of tribal immunity. *Id.*

101. Blurton, *supra* note 81, at 246.

102. McLish, *supra* note 95, at 191 (stating that commercial activity for foreign countries under the Foreign Sovereign Immunities Act has substantiality curtailed immunity protections); *see also* 28 U.S.C. 97 § 1605 (2012) (stating exceptions to foreign state immunity).

103. McLish, *supra* note 95, at 190.

104. *See* Lake, *supra* note 82, at 94 ("The supreme courts of Arizona, New Mexico, and Oklahoma, however, have reacted by breaking from the majority rule and refusing to extend immunity to the commercial activities of tribal businesses outside the reservation.").

105. *See* McLish, *supra* note 95, at 190 (arguing that Congress should do more to protect tribal economic activity in the non-Indian world).

In sum, limiting tribal sovereign immunity in the tort and commercial context makes good policy sense and will not disproportionately burden tribes; doing so will also restore justice for unsuspecting victims and those who did not have a chance to accept tribal sovereign immunity voluntarily.

B. Noncommercial and Possessory Claims

While commercial and tort claims often portray the most egregious and unsettling outcomes of applying tribal sovereign immunity, invoking immunity in the non-commercial context may also result in an unjust application of tribal rights. The non-commercial context includes purely contractual claims and possessory disputes, with the latter including land and other personal property issues. As in the above instances, tribal sovereign immunity should be limited where conferring immunity would disproportionately disadvantage the non-Indian party, though this shift may necessitate a case-by-case review of each dispute. Consequently, in non-commercial disputes, tribal sovereign immunity should be maintained in most instances, limiting the doctrine only where necessary to protect the interests of the larger community.

First, in the non-commercial context where tribal sovereign immunity is to be applied to a tribe's off-reservation activities, immunity should be curtailed—and other equitable remedies permitted—where its application would be excessively burdensome or unfair to the non-Indian party. The court would look to a pre-determined standard for resolving the issue. In so doing, the court's analysis should loosely follow the reasoning utilized in *Sherrill* and *Cayuga*. Therefore, in non-commercial disputes, the court should consider factors such as excessive delay in bringing the claim and the settled, reasonable expectations of the non-Indian party. Outside of these circumstances, tribal sovereign immunity should be maintained so long as there is no showing of wrongdoing by the tribes, though abandoning a bright-line rule will likely increase judicial discretion. Ideally, the instances in which the doctrine is applied would be quite limited.[106] Finally, when a dispute occurs on

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106. *See* Transcript of Oral Argument at 31, City of Sherrill v. Oneida Indian Nation of N.Y 544 U.S. 197 (2005) (No. 03–855) (Scalia, J. stating that 'really what you're asking the Court to do is to sanction a very odd checkerboard system of jurisdiction in the middle of New York State. Some parcels, the ones the Indians choose to buy and are able to buy, become Indian territory and everything else is governed by New York State. This is just a terrible situation ').

a tribal reservation, tribal sovereign immunity should remain absolute and the court should uphold the tribe's right to act as a sovereign over its own territory.[107]

Secondly, in possessory claims, when tribal sovereign immunity is to be applied to a tribe's off-reservation activities, including land possession disputes, equitable factors should be utilized when considering whether to invoke immunity.[108] Though *Sherrill* explicitly concerns tribal sovereignty, not tribal sovereign immunity, its analysis is particularly pertinent in developing considerations for possessory claims.[109]

In addition, a policy mandating full disclosure, as explained above, should also be implemented in the non-commercial context and, therefore, the tribe should have a duty to disclose whether or not it intends to waive immunity prior to engaging in a transaction with a non-Indian party. As a result, the burden would be placed upon the tribes to demonstrate that tribal sovereign immunity has not been waived, thereby promoting full disclosure of immunity rights well in advance of any potential disputes.[110] Additionally, the jurisdiction permitted by this waiver of immunity should extend, if possible, to federal and state courts, in addition to tribal courts.[111]

In closing, curtailing tribal sovereign immunity in some form is likely still necessary in non-commercial claims to ensure justice for non-Indians who enter into contractual obligations with an Indian party and lack knowledge of tribal sovereign immunity. In instances where the non-Indian party had no reason to suspect that immunity could be invoked, affording equitable remedies will help to reach a fair outcome. The proposed test, modeled after cases originating in the Second Circuit, is quite narrow and will continue to allow for tribal sovereign immunity in the vast majority of cases and only abrogates the doctrine when it is necessary to achieve justice.[112]

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107. *See Sherrill*, 544 U.S. at 226 (Stevens, J. dissenting) (emphasizing that tax immunity for Indian owned land is "the most fundamental of tribal rights and the least disruptive to other sovereigns"). Under the proposed application of tribal sovereign immunity, all non-commercial activities on tribal reservation lands would be granted immunity, as the tribe retains the right to territorial control over its parcels as it deems most appropriate. *Id.* Note also that the foregoing does not apply to tort claims, where, as previously mentioned, tribal immunity should be limited. *Id.*

108. *Id.*

109. McLish, *supra* note 95, at 187.

110. WILKINS & LOMOWAIMI, *supra* note 7, at 224.

111. Fogleman, *supra* note 31, at 1376.

112. *See* NELL JESSOP NEWTON & ROBERT ANDERSON, COHEN'S HANDBOOK OF FEDERAL INDIAN LAW 639–41 (2005) (noting that Congress has restricted tribal

V CONCLUSION

As tribal sovereign immunity moves into a century where tribal entities interact with non-tribes like never before, leaving intact a broad, formalist application of the doctrine simply does not comport with good policy sense. As signaled by the Supreme Court and the Second Circuit, courts are ready to limit tribal immunity so that it re-aligns with the realities of contemporary society; doing so will help to restore justice for non-Native American victims who were previously barred recovery for damages, even when the non-Native American party had been faultless. Though courts must wait for Congress to declare the final word on the future of tribal sovereign immunity, the Supreme Court's hesitations in applying tribal rights in their absolute form, as portrayed in *Kiowa* and *Sherrill*, demonstrate that it is finally time to resolve the issue. Adoption of a more practical test for tribal sovereign immunity will fit with these aims, while leaving much of the doctrine intact. Moreover, under a functional approach, sovereignty rights will continue to level the playing field for Native American tribes, while limiting application where tribal immunity is utilized to create an unfair advantage and simply acts to boost Native American revenues or sanction injustice. In sum, while some protections are necessary to safeguard tribal self-determination in the 21st century, a blanket authorization to invoke tribal sovereign immunity hinders equality and justice for the larger community, and therefore immunity should be limited where it is superfluous and excessively burdensome.

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immunities only in limited circumstances and has rejected broad restrictions on tribal sovereign immunity).

The Role of State Law in Determining the Construction and Validity of Federal Rules of Civil Procedure

Patrick Woolley*

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I. INTRODUCTION

By authorizing the Supreme Court to prescribe "general rules of practice and procedure"[1] in civil actions, the Rules Enabling Act of 1934 sought to encourage development of a uniform federal law of procedure.[2] But although the Rules Enabling Act ("REA") has been the law for more than seventy-five years, the proper relationship between the Federal Rules of Civil Procedure ("Federal Rules") and arguably conflicting state law remains remarkably unsettled and highly controversial. I argue in this paper that courts and commentators have given excessive deference to state law both in *construing* the Federal Rules and in determining their *validity*.

Much of the blame for this state of affairs can be ascribed to the fact that the Federal Rules went into effect the same year that the Court decided *Erie Railroad Co. v. Tompkins*.[3] *Erie* at its most sweeping can be read to require application of state rather than federal law whenever the choice between the two would be outcome determinative.[4] Because virtually "every procedural variation is outcome determinative"[5] in some sense, *Erie* and its progeny arguably called into question the validity of Federal Rules in conflict with state law, a problem the Court addressed primarily by

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1. 28 U.S.C. § 2072(a) (2015).

2. *See* Burlington Northern R.R. Co. v. Woods, 480 U.S. 1, 5 (1987) (noting that '[t]he cardinal purpose of Congress' in enacting the Rules Enabling Act was to 'authoriz[e] the development of a *uniform and consistent* system of rules governing federal practice and procedure' (emphasis added)); Hanna v. Plumer, 380 U.S. 460, 472 (1965) ("One of the shaping purposes of the Federal Rules is to bring about uniformity in the federal courts by getting away from local rules.') (quoting Lumbermen's Mutual Casualty Co. v. Wright, 322 F.2d 759, 764 (5th Cir. 1963)). Before enactment of the Rules Enabling Act, federal courts (in actions at common law) had generally applied the procedural law of the state in which they sat. RICHARD H. FALLON, JR. ET AL. HART AND WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM 538–39 (6th ed. 2009) (discussing the Conformity Act of 1872). And they continued to do so until the Federal Rules of Civil Procedure went into effect in 1938. Sibbach v. Wilson & Co. 312 U.S. 1, 10 (1941) (stating that the Federal Rules, 'if they are within the authority granted by Congress, repeal' the Conformity Act of 1872.).

3. Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938).

4. Guar. Trust Co. v. York, 326 U.S. 99, 110 (1945).

5. *Hanna*, 380 U.S. at 468 (emphasis and internal quotation marks omitted).

construing Federal Rules to avoid conflict with the *Erie* doctrine.[6] The existential threat posed by *Erie* and its progeny to the Federal Rules endured until 1965, when the Court decided *Hanna v. Plumer*.[7]

But even after *Hanna* held that the *validity* of Federal Rules was not governed by *Erie*,[8] the Court continued to *construe* Federal Rules narrowly so as to avoid conflicts with state law.[9] In its most recent cases, the Court has identified the *Erie* policy as a rule of construction relevant to the interpretation of the Federal Rules.[10] The "*Erie* policy" refers to the policy which has its origin in *Erie*'s discussion of the social and political defects of *Swift v. Tyson*,[11] and which the modified outcome-determination test of *Hanna*[12] is

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6. Bernadette Bollas Genetin, *Reassessing the Avoidance Canon in Erie Cases*, 44 AKRON L. REV. 1067, 1082–92 (2013).

7. 380 U.S. 460 (1965).

8. *See id.* at 471–72 ("When a situation is covered by one of the Federal Rules, the question facing the court is a far cry from the typical, relatively unguided *Erie* choice: the court has been instructed to apply the Federal Rule, and can refuse to do so only if the Advisory Committee, this Court, and Congress erred in their prima facie judgment that the Rule in question transgresses neither the terms of the Enabling Act nor constitutional restrictions.").

9. Genetin, *supra* note 6, at 1098–103. "The Supreme Court's post-*Hanna*, *Erie* cases have generally premised avoidance, *when it is used*, on the federalism goals of avoiding interference with important state interests or important state regulatory policies." *Id.* at 1098 (emphasis added). *But see infra* notes 10–13 and accompanying text (noting that the Court has more recently suggested that the scope of a Federal Rule may be narrowed on the basis of *Hanna*'s modified outcome determination test).

10. *See* Shady Grove Orthopedic Assocs. v. Allstate Ins. Co. 559 U.S. 393, 405 n.7 (2010) ("[W]e should read an ambiguous Federal Rule to avoid substantial variations [in outcomes] between state and federal litigation." (internal quotation marks omitted)); Semtek Int'l Inc. v. Lockheed Martin Co. 531 U.S. 497, 504 (2001) (reading Rule 41(b) narrowly in part because the Rule would in many cases violate the federalism principle of *Erie* by "engendering substantial variations [in outcomes] between state and federal litigation which would [l]ikely . . . influence forum choice").

11. 41 U.S. 1 (1842).

12. *Hanna*, 380 U.S. at 468 ("The 'outcome-determination' test therefore cannot be read without reference to the twin aims of the Erie rule: discouragement of forum-shopping and avoidance of inequitable administration of the laws."); *cf.* Guar. Trust Co. v. York, 326 U.S. 99, 109 (1945) (indicating that *Erie* requires application of state law if it would "significantly affect the result of a litigation for a federal court to disregard a law of a State that would be controlling in an action upon the same claim by the same parties in a State court").

designed to implement.[13] Used as a rule of construction, the *Erie* policy counsels a narrow reading of a Federal Rule (or statute) in order to avoid potential conflict with outcome-determinative state law.

State law has also continued to play a role in determining the validity of Federal Rules. In a remarkably influential article, John Hart Ely argued shortly after *Hanna* that a Federal Rule should be deemed invalid as applied when it conflicts with state law enacted for one or more nonprocedural reasons.[14] And some have interpreted the Court's post-*Hanna* decisions as sympathetic to Professor Ely's general approach.[15] Six years ago, a plurality of the Court in *Shady Grove Orthopedic Associates v. Allstate Insurance Co.* flatly rejected Professor Ely's approach.[16] Yet, with the notable exception of the D.C. Circuit, the lower courts that have addressed the issue since then have mostly held—in defiance of the plurality—that a conflict with state law may, in limited circumstances, invalidate a Federal Rule as applied to a given case.[17]

In short, state law continues to cast a long shadow over the Federal Rules. The deference state law has enjoyed is inconsistent with the fundamental purpose of the REA, which is to provide federal rule makers with the authority to prescribe "uniform and consistent"[18] Federal Rules. The validity of a Federal Rule should depend on what the Rule regulates, not on whether it interferes with state law enacted for a substantive purpose. State law should also play a far more limited role in construing a Federal Rule than is often understood. None of this is to suggest that state law does not play a vital role in the analysis. The proper interpretation of state law is crucial to determining whether a valid Federal Rule, properly construed, displaces state law or whether, under the *Erie* policy, state law applies because it addresses an outcome-determinative matter outside the scope of a Federal Rule.

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13. For detailed discussion of the *Erie* policy, see Patrick Woolley, *The Sources of Federal Preclusion Law After* Semtek, 72 U. CIN. L. REV. 527, 542–49 (2003).

14. John Hart Ely, *The Irrepressible Myth of* Erie, 87 HARV. L. REV. 693 (1974).

15. *See infra* note 139.

16. 559 U.S. 393, 409 (2010).

17. *See infra* Part II.B. (discussing the lower courts after *Shady Grove*).

18. *Burlington Northern*, 480 U.S. at 5.

I use the Court's fascinating decision in *Shady Grove* as a principal vehicle to explore these issues. In Part II, I defend the plurality's insistence in *Shady Grove* that the validity of a Federal Rule depends on what the Rule regulates, not on the purposes of state law affected by the Rule.[19] I criticize Justice Stevens's contrary approach, which posits that a Federal Rule is invalid as applied to the extent it conflicts with state law bound up with the definition of a state-created right. I then explain that the lower courts that have concluded that Justice Stevens's *Shady Grove* concurrence is binding are mistaken.

I close Part II by detailing a framework for determining whether a Federal Rule regulates "substance" or "procedure." Federal Rules regulate procedure to the extent they govern the process by which claims and defenses are asserted and adjudicated within a lawsuit. Federal Rules outside this core also regulate procedure to the extent they enforce or implement policy choices that the Court has the authority to make under the REA. Applying this framework to *Shady Grove,* I conclude that the plurality correctly determined that the federal class action rule—Rule 23—regulates procedure and that the Court has power to bar the application of state law that would make it easier or harder to bring a class suit than an individual suit.

In Part III, I advance a measured approach to construing Federal Rules and state law when assessing whether a Federal Rule displaces state law in federal court. I contend that even if courts should generally give statutes their plain meaning, a federal court respectful of federalism should ordinarily read a state statute purposively when the statute relies on a procedural mechanism that is inapplicable in federal court. I also reject the view that unless the express text of a Federal Rule conflicts with state law, the *Erie* policy requires a federal court to apply outcome-determinative state law.[20] The *Erie* policy has its place in construing Federal Rules. But

19. For an especially early defense of the plurality on this point, *see* Stephen B. Burbank & Tobias Barrington Wolff, *Redeeming the Missed Opportunities of* Shady Grove, 159 U. PA. L. REV. 17, 46 (2010) ("In Justice Scalia's plurality opinion in *Shady Grove*, he correctly declined to make the validity of a Federal Rule turn on a particularistic and after-the-fact analysis of the policies underlying state law prescriptions on the very matter that the Federal Rule covered.").

20. *See infra* Part III.B.1.

the *Erie* policy is just *one* of the rules of construction which a court may use when construing an arguably ambiguous Federal Rule. Use of the *Erie* policy to construe a Federal Rule must be harmonized with a principle rooted in the fundamental purpose of the REA. If a Federal Rule, "fairly construed,"[21] can be read to cover a point, the Rule should be so read in order to promote a "uniform and consistent system"[22] of federal procedure. Applying this approach to *Shady Grove*, I determine that the Court erred in finding that New York law simply prohibits the certification of a class suit seeking penalties, not the award of penalties in class litigation. But I also conclude that Rule 23, properly construed, permits a state bar on the award of penalties through the class device to be given effect in federal court only as a factor—*among other factors*—in the Rule 23(b)(3) superiority determination.

II. DETERMINING THE VALIDITY OF A FEDERAL RULE

The REA authorizes the Supreme Court to prescribe "general rules of practice and procedure"[23] in federal civil actions and provides that such rules "shall not abridge, enlarge or modify any substantive right."[24] In this part, I seek to provide a standard for determining the validity of Federal Rules that is both faithful to the purpose of the REA and workable. Like the plurality in *Shady Grove*, I conclude that state law has no role to play in an assessment of a Federal Rule's validity. Federal Rules are valid to the extent they regulate the process within a lawsuit by which claims and defenses are asserted and adjudicated. Federal Rules outside this core are also valid to the extent they implement or enforce policy choices that the Court has authority to make under the REA. I begin my discussion in subpart A with a critique of the plurality and concurring opinions in *Shady Grove*. These opinions engage in the first serious debate between Justices on the proper framework under the REA for determining the validity of a Federal Rule since the

21. *Burlington Northern*, 480 U.S. at 4.
22. *Id.* at 5.
23. 28 U.S.C. § 2072(a) (2015).
24. 28 U.S.C. § 2072(b) (2015).

Court's early decision in *Sibbach v. Wilson & Co.*[25] I defend the plurality's conclusion that the validity of a Federal Rule does not depend on state law while noting its failure to fully flesh out a test for distinguishing between substance and procedure within the meaning of the REA. In subpart B, I explain why the many lower courts that have concluded that the concurring opinion is binding precedent are mistaken. In subpart C, I provide a framework for analyzing the validity of a Federal Rule and apply that framework to Federal Rule 23, the rule at issue in *Shady Grove*.

A. The Debate in Shady Grove

In *Shady Grove*, Sonia Galvez filed suit on behalf of a class against the Allstate Insurance Company in New York federal court, alleging that Allstate routinely refused to pay interest on overdue benefits as required by New York law.[26] The district court dismissed the suit for lack of subject matter jurisdiction, presumably on the ground that less than $5 million was in controversy, and therefore jurisdiction was unavailable under the Class Action Fairness Act. Specifically, the district court reasoned that New York law prohibited bringing a class action to recover a penalty and that statutory interest was a penalty under New York law.[27] The Second Circuit affirmed. The Supreme Court reversed on the ground that the maintenance of the class suit was governed by Federal Rule 23(a) and (b), not New York law.

Justice Scalia wrote for a 5–4 majority of the Court in concluding that there was a direct collision between Rule 23 and state law, but he could put together only a plurality for his analysis of Rule 23's validity under the REA.[28] Justice Stevens, in a

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25. 312 U.S. 1 (1941). *Cf.* Hanna v. Plumer, 380 U.S. 460, 475 (1965) (Harlan, J. concurring) (arguing that federal procedural law—including Federal Rules—may be validly applied only if it does not 'substantially affect those primary decisions respecting human conduct which our constitutional system leaves to state regulation").

26. *See* N.Y Ins. Law § 5106(a) (McKinney 2005) ("All overdue payments shall bear interest at the rate of two percent per month. ').

27. For discussion of the district court's jurisdictional analysis, *see infra* note 252 and 253.

28. The plurality opinion was joined by Chief Justice Roberts and Justices Thomas and Sotomayor (although Justice Sotomayor declined to join Part II.C.).

concurrence, agreed with Justice Scalia that Rule 23 was valid as applied to the case, but disagreed with Justice Scalia's approach to the REA. Justice Ginsburg—with whom Justices Kennedy, Breyer, and Alito joined—dissented. The dissent rejected the view that there was a direct collision between Rule 23 and New York law, and instead—using the analysis the Court has adopted when the Federal Constitution, a federal statute, or a federal rule does not cover the point[29]—concluded that New York law should apply because it was outcome-determinative in the *Hanna* sense.

1. The Plurality Opinion

In the plurality opinion, four Justices—Justices Scalia, Thomas, and Sotomayor and Chief Justice Roberts—came down decisively in favor of the view that the validity of a Federal Rule is not affected by the purpose of state law: "A Federal Rule of Procedure is not valid in some jurisdictions and invalid in others—or valid in some cases and invalid in others—depending upon whether its effect is to frustrate a state substantive law (or a state procedural law enacted for substantive purposes)."[30]

a. *The Plurality's Appropriate Reliance on* Sibbach

In defending its position, the plurality argues that the Court's seminal decision in *Sibbach* controls and that the Court's post-*Sibbach* cases are consistent with its analysis in *Shady Grove*.[31]

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29. *See Shady Grove*, 559 U.S. at 452 (Ginsburg, J. dissenting) ("Because I perceive no unavoidable conflict between Rule 23 and § 901(b), I would decide this case by inquiring 'whether application of the [state] rule would have so important an effect upon the fortunes of one or both of the litigants that failure to [apply] it would be likely to cause a plaintiff to choose the federal court. (quoting *Hanna*, 380 U.S. at 468 n. 9)).

30. *Shady Grove*, 559 U.S. at 409.

31. The plurality wrote:

> We have held since *Sibbach*, and reaffirmed repeatedly, that the validity of a Federal Rule depends entirely upon whether it regulates procedure. *See Burlington Northern*, 480 U.S. at 8 If it does, it is authorized by § 2072 and is valid in all jurisdictions, with

Sibbach focuses on whether the Federal Rule at issue is a rule of "practice and procedure" within the meaning of what is now § 2072(a),[32] and treats the requirement that a Federal Rule "shall not abridge, enlarge or modify any substantive right" in what is now § 2072(b)[33] as simply intended to "*emphasize*"[34] the restriction on the Court's "power to prescribe" set forth in § 2072(a).[35]

In subtle contrast to *Sibbach*, the *Shady Grove* plurality—hewing closely to the Court's post-*Hanna* cases—focuses on the prohibition against modifying, abridging, or enlarging substantive rights set forth in § 2072(b).[36] The difference in emphasis is perhaps explained by the Court's awareness of John Hart Ely's enormously

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> respect to all claims, regardless of its incidental effect upon state-created rights.

Shady Grove, 559 U.S. at 410.

32. 28 U.S.C. § 2072(a) now reads in relevant part as follows: 'The Supreme Court shall have the power to prescribe general rules of practice and procedure for cases in the United States district courts (including proceedings before magistrate judges thereof) and courts of appeals. Until 1988, what is now part of § 2072(a) was part of the same undivided statute. For the sake of simplicity, I hereafter anachronistically refer to Sections 2072(a) and (b) even with respect to cases that were decided before Section 2072 was amended and subdivided.

33. 28 U.S.C. § 2072(b) now reads in relevant part as follows: 'Such rules shall not abridge, enlarge or modify any substantive right.

34. Sibbach v. Wilson & Co. 312 U.S. 1, 10 (1941) (emphasis added).

35. *Id. See also* Kevin M. Clermont, *The Repressible Myth of* Shady Grove, 86 NOTRE DAME L. REV. 987, 1005 (2011) (noting that *Sibbach* 'said that it read the Act's first sentence to limit the Rules to procedural matters, while reading the second sentence as an emphatic definition of procedural matters to mean non-substantive law").

36. Justice Scalia explained the plurality's analysis as follows:

> In the Rules Enabling Act, Congress authorized this Court to promulgate rules of procedure subject to its review, 28 U.S.C. § 2072(a), but with the limitation that those rules 'shall not abridge, enlarge or modify any substantive right, § 2072(b).
>
> We have long held that this limitation means that the Rule must 'really regulat[e] procedure,—the judicial process for enforcing rights and duties recognized by substantive law and for justly administering remedy and redress for disregard or infraction of them, *Sibbach*, 312 U.S. at 14, 61 S. Ct. 422.

Shady Grove, 559 U.S. at 406–07.

influential article, *The Irrepressible Myth of* Erie.[37] Professor Ely took the position that § 2072(a) delegated to the Court the full measure of Congressional authority over procedure articulated in *Hanna v. Plumer*, limited only by § 2072(b).[38] If Professor Ely was correct, the only substantial limit on the Court's procedural rule-making power is found in § 2072(b). The Court deftly avoided addressing (let alone resolving) the question in its post-*Hanna* cases. The Court, in other words, chose not to construe the term "practice and procedure," but focused instead on applying the limits on rule-making power set forth in § 2072(b).[39] The *Shady Grove* plurality

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37. Ely, *supra* note 14.

38. *See infra* note 53 and accompanying text.

39. In *Burlington Northern Railroad v. Woods*, for example, the Court wrote:

> The Rule must be applied if it represents a valid exercise of Congress' rulemaking authority, which originates in the Constitution and has been bestowed on this Court by the Rules Enabling Act.
>
> The constitutional constraints on the exercise of this rulemaking authority define a test of reasonableness. Rules regulating matters indisputably procedural are *a priori* constitutional. Rules regulating matters 'which, though falling within the uncertain area between substance and procedure, are rationally capable of classification as either,' also satisfy this constitutional standard. The Rules Enabling Act, however, contains an additional requirement. The Federal Rule must not 'abridge, enlarge or modify any substantive right 28 U.S.C. § 2072.
>
> Federal Rule 38 regulates matters which can reasonably be classified as procedural, thereby satisfying the constitutional standard for validity. Its displacement of the Alabama statute also satisfies the statutory constraints of the Rules Enabling Act.

Burlington Northern, 480 U.S. at 5, 8 (citations omitted). Notably absent from the Court's analysis is any discussion of the meaning of "general rules of practice and procedure. The Court's analysis could be read as indicating that the authority to prescribe 'general rules of practice and procedure' is coterminous with the power of Congress to enact arguably procedural statutes. *See, e.g.* Martin Redish & Dennis Murashko, *The Rules Enabling Act and the Procedural-Substantive Tension: A Lesson in Statutory Interpretation,* 93 MINN. L. REV. 26, 86 (2008) ("The Court thus saw the limiting provision as carving out a portion of what the enabling provision authorized, but only to the extent that the rule's effect on substantive rights was not 'incidental. '). But given that *Sibbach* had treated the 'substantive rights' language as simply emphasizing the limits inherent in the 'practice and procedure,' language, there was no need in *Burlington Northern* to

followed suit. But the difference in emphasis between the plurality and *Sibbach* does not change the fact that both stated and applied the same test: does the Federal Rule "really regulate[] procedure,—the judicial process for enforcing rights and duties recognized by substantive law and for justly administering remedy and redress for disregard or infraction of them"?[40]

Despite its adherence to *Sibbach*, the plurality expressed unease about whether the "really regulates procedure" test squares with the text of the REA.[41] In fact, *Sibbach*'s focus on § 2072(a)—and its conflation of §§ 2072(a) and (b)—is consistent with the intent of those who drafted the REA. As a historical matter, the limitations placed on the prospective rule-making authority of the Supreme Court were intended to avoid an improper delegation of congressional authority. The understanding of the drafters was that Congress could constitutionally grant the Supreme Court prospective rule-making authority with respect to matters of "practice and procedure," but that the grant of prospective rule-making power with

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discuss both provisions, especially because the latter provision could more easily be read consistently with the standard the Court chose to apply.

40. *Sibbach*, 312 U.S. at 14; *see Shady Grove*, 559 U.S. at 407 (containing similar language).

41. *Shady Grove*, 559 U.S. at 412–13 ("*Sibbach*'s exclusive focus on the challenged Federal Rule—driven by the very real concern that Federal Rules which vary from State to State would be chaos, —is hard to square with § 2072(b)'s terms. '). Martin Redish and Dennis Murashko have argued persuasively that the canon against reading any part of a statute as surplusage should not be applied to the REA:

> [T]he canon, when critically examined, might lose its bite for several reasons. First, descriptive canons draw their strength from the assumption that they accurately generalize how legislators communicate through text. When that assumption breaks down, so too does the canon's claim to validity. In particular, the canon presuming the absence of surplusage has long been criticized for assuming something quite unrealistic about Congress—namely, that legislators are aware of how the various parts of the statute intertwine. One can reasonably ignore the surplusage canon on this ground alone, but ignoring the canon becomes even easier in light of the fact that the redundant provision in the Rules Enabling Act actually served an important strategic purpose in helping to placate those opposed to the Act.

Redish & Murashko, *supra* note 39, at 37–38.

respect to other matters would represent an improper delegation of legislative authority. To the extent courts are empowered to make substantive law, they must do so through elaboration of the common law rather than through prospective rule making. In other words, the limitations of the REA were premised on protecting the separation of powers.[42]

Professors Burbank and Wolff nonetheless have criticized *Sibbach*'s fidelity to the intent of the framers on the ground that the Court in that case deemed the restrictions of the REA to be premised on federalism rather than separation of powers.[43] But whether or not

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42. As Professors Burbank and Wolff have explained:

> [T]he historical record underlying both the 1934 Act and the 1988 amendments establishes: the primary purpose of the Enabling Act's procedure/substance dichotomy is to allocate prospective federal lawmaking between the Supreme Court and Congress, not to protect lawmaking choices already made, and certainly not to protect state lawmaking choices exclusively. To be sure, allocation standards may have the salutary effect of protecting existing lawmaking choices. But that is a secondary consequence of the Enabling Act's primary concern, which is preventing the Supreme Court, exercising delegated legislative power to promulgate court rules, from encroaching upon Congress's lawmaking prerogatives.

Burbank & Wolff, *supra* note 19, at 43. *See also* Donald L. Doernberg, *Horton the Elephant Interprets the Federal Rules of Civil Procedure: How the Federal Courts Sometimes Do and Always Should Understand Them*, 42 HOFSTRA L. REV. 799, 830 (2014) ("[T]o regard the REA's limiting language as a federalism instrument, rather than as a separation-of-powers instrument, is to indulge in a serious misreading of the REA's history and timing."); *id.* at 830–31 (quoting Sain v. City of Bend, 309 F.3d 1134, 1137 (9th Cir. 2002), for the proposition that "the Rules Enabling Act['s] proviso restricting the permissible scope of the rules was designed to serve the purposes of the anti-delegation doctrine by limiting the scope of rules that were adopted with minimal congressional involvement."); Paul D. Carrington, *'Substance' and 'Procedure' in the Rules Enabling Act*, 1989 DUKE L.J. 281, 289 (recognizing that the limits imposed on rulemaking in the REA are founded in the separation of powers). For an exhaustive discussion of the legislative history see Stephen B. Burbank, *The Rules Enabling Act of 1934*, 130 U. PA. L. REV. 1015 (1982).

43. Burbank & Wolff, *supra* note 19, at 17, 27 ("It is even easier to forget—or even to overlook—that although the Court attributed the procedure/substance dichotomy in the first two sentences of the Act to concerns about the allocation of lawmaking power between the federal government and the States, Justice

the majority in *Sibbach* understood the limitations on the rule-making power to be premised on the separation of powers, *Sibbach* concludes in essence that the validity of a Federal Rule does not depend "on a particularistic and after-the-fact analysis of the policies underlying state law."[44] Such an approach appropriately safeguards the separation of powers concerns that animated the legislation.[45] A focus on what a Federal Rule actually regulates, rather than on how Federal Rules may affect state law, fully protects congressional authority to legislate on matters not delegated to the Court. State law governs under this approach only if the matter in question is not governed by a Federal Rule, a federal common law rule, an act of Congress, or the Constitution; state law must govern in these circumstances because there "can be no other law."[46]

Martin Redish and Dennis Murashko, for their part, have criticized *Sibbach* on the ground that its interpretation of the REA is inconsistent with current understandings of the relationship between substance and procedure. They contend that *Sibbach*'s conclusion that 2072(b) simply "emphasize[s]" the restriction on the Court's "authority to prescribe"[47] set forth in § 2072(a) reflects an

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Frankfurter's opinion for the four Justices in the minority discerned correctly that the animating concern of the Act was separation of powers. ').

44. *Id.* at 46.

45. As Professors Burbank and Wolff have argued:

> Justice Scalia's plurality opinion in Shady Grove correctly declined to make the validity of a Federal Rule turn on a particularistic and after-the-fact analysis of the policies underlying state law prescriptions on the very matter that the Federal Rule covered. Apart from its erroneous attention exclusively to state law, such an interpretation is hardly consistent with the vision of uniform and simple Federal Rules that animated the movement that brought us the Enabling Act.

Id. *See also id.* at 51 (Justice Scalia's 'insistence on a test for validity that does not depend on idiosyncratic aspects of state law rings true for a statute that was designed primarily to allocate federal lawmaking power *ex ante*, rather than to protect policy choices (let alone only state law policies) *ex post.*' (emphasis added)).

46. *Hanna*, 380 U.S. at 471–72.

47. *Sibbach*, 312 U.S. at 10.

understanding that substance and procedure are mutually exclusive.[48] It is uncontroversial today that procedure and substance are closely intertwined.[49]

Professor Redish and Mr. Murashko argue that our understanding of the relationship between substance and procedure has changed so significantly since the enactment of the REA that it makes no sense to construe the statute on the basis of the understanding that was prevalent in 1934. They urge a dynamic rather than static interpretation of the limits on rule making attributed to the REA and contend that the Court's decision in *Burlington Northern* provides a sound basis for determining when a rule that has substantive effects is nonetheless authorized under the REA.[50]

48. Redish & Murashko, *supra* note 39, at 37 ("When the original Rules Enabling Act was promulgated into law in 1934, many of its supporters believed that procedure and substance were mutually exclusive."). *See also* Robert Bone, *The Process of Making Process: Court Rulemaking, Democratic Legitimacy, and Procedural Efficacy*, 87 GEO. L.J. 887. 894–97 (1999) (describing attitudes toward the relationship between substance and procedure around the time of the REA's enactment).

49. *See* Bone, *supra* note 48, at 897 (noting that today's proceduralists are 'accustomed to focusing on the substantive effects of procedural rules"); Redish & Murashko, *supra* note 39, at 39 (recognizing that rejection of the view that regulating procedure and impacting substance are mutually exclusive 'better comports with modern understanding of the procedural-substantive intersection"). The inevitable synergy between substance and procedure has led the Court to recognize wisely and without apology that its 'rulemaking under the enabling Acts has been substantive and political in the sense that the rules of procedure have important effects on the substantive rights of litigants. Mistretta v. United States, 488 U.S. 361, 392 (1989);

50. Redish & Murashko, *supra* note 39, at 33 ("We argue the incidental-effects—or, relaxed separation—interpretation fashioned by the Court in Burlington Northern Railroad Co. v. Woods most effectively promotes the two background purposes of the Enabling Act."). In later work, Professor Redish suggests two other ways of "construing the Act's substance-procedure distinction in order to take into account the democratic accountability critique. MARTIN REDISH, WHOLESALE JUSTICE 82 (2009), that is, the critique that accountable officials should make many decisions about Rules now made by the Supreme Court because of the difficulty of separating substance from procedure. *Id.* at 85–86. Neither alternative is supported by legislative history or precedent. And to the extent that democratic accountability is of concern, Congress retains the power to reject federal rules prescribed by the Court and has done so in the past. Professor Redish objects that '[w]ith the Rules in place, congressional inaction effectively amounts to legislative action, in contravention of the Constitution's bicameralism and presentment requirements. *Id.* at 77. This objection erroneously assumes

Burlington Northern authorizes rule makers to prescribe Federal Rules that have an incidental effect on substantive rights and that are reasonably necessary to maintain the integrity of that system of rules.[51] Professor Redish and Mr. Murashko accordingly would discard *Sibbach* as a relic of a bygone era.

The fatal flaw in their argument is the acceptance of Professor Ely's extraordinarily broad construction of § 2072(a). They write: "As Professor Ely observed, this section mandates that rulemaking under the Act concern procedural goals, which he further defined as goals 'designed to make the process of litigation a fair and efficient mechanism for the resolution of disputes.'"[52] Although Professor Ely understood this provision to be coextensive with congressional power over procedure,[53] there is substantial evidence, as I explain in subpart II.A.2., that § 2072(a) was intended to provide much narrower authority to prescribe Federal Rules. Once this evidence is understood, the conclusion that § 2072(b) was intended simply to emphasize the limits that § 2072(a) places on rule-making is fully consistent with the recognition that substance and procedure are intertwined as a practical matter.[54] The definition of "practice

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that a Congressional grant to the Court of power to prescribe Rules of 'practice and procedure' would violate the Constitution. *See* Linda S. Mullenix, *Unconstitutional Rulemaking: The Civil Justice Reform Act and Separation of Powers*, 77 MINN. L. REV. 1283, 1330 (1993) ("Perhaps the best view of rulemaking authority is that it is a constitutionally-and statutorily-shared power, to be exercised in coordination by the legislative and judicial branches.").

51. *See* Burlington N. R.R. Co. v. Woods, 480 U.S. 1, 5 (1987) ("The cardinal purpose of Congress in authorizing the development of a uniform and consistent system of rules governing federal practice and procedure suggests that Rules which incidentally affect litigants' substantive rights do not violate this provision if reasonably necessary to maintain the integrity of that system of rules.").

52. Redish & Murashko, *supra* note 39, at 27.

53. Ely, *supra* note 14, at 718 (stating that Section 2072(a) imposes no limitation "that was not imposed by the Constitution"). Professor Redish and Mr. Murashko conclude that *Burlington Northern* adopts Professor Ely's construction of Section 2072(a). Redish and Murashko, *supra* note 39, at 86. Although this conclusion is plausible, it is not the only plausible reading of the Court's opinion in *Burlington Northern*. *See supra* note 39 (and accompanying text (arguing that the Court in *Burlington Northern* did not address the meaning of Section 2072(a)).

54. *Cf.* Redish & Murashko, *supra* note 39, at 28 ("[R]elying on the notion of mutual exclusivity of procedure and substance, one could construe the second section as nothing more than restatement of the first. . . .").

and procedure" can be tailored appropriately to authorize the creation of "uniform and consistent"[55] Federal Rules without disregarding appropriate limits on judicial rule-making. In short, while the Court's understanding of the substance-procedure distinction has changed since *Sibbach*, there is no need to reject its conclusion that § 2072(b) was intended simply to emphasize the restrictions placed on the Court's rule-making power. As the *Shady Grove* plurality recognized, *Sibbach* and *Burlington Northern* are riffs on the same theme.[56]

b. *The Plurality's Underdeveloped Analysis*

By insisting that what matters is whether a Federal Rule really regulates procedure rather than whether a Federal Rule interferes with a state procedural purpose, the *Shady Grove* plurality weighed in on an issue critical to the proper interpretation of the REA. But the tautological standard *Sibbach* articulates—that a Federal Rule is valid if it really regulates procedure[57]—is of limited

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55. *Burlington*, 480 U.S. at 5. *See* S. REP. NO. 69-1174, at 1 (1926) (identifying as the '*first*' purpose of the Act 'to make uniform throughout the United States the forms of process, writs, pleadings, and motions and the practice and procedure in the district courts in actions at law' (emphasis added)); Joseph A. Wickes, *The New Rulemaking Power of the United States Supreme Court*, 13 TEX. L. REV. 1, 21 (1934) ("The present policy of Congress seems to call for a uniformity of federal practice and procedure generally, as distinguished from conformity to state practice, in the trial of all types of cases in the federal courts. ').

56. Ralph Whitten contends that the *Burlington* Court's insistence that federal rules may not have more than an 'incidental[] [e]ffect' on substantive rights can and should be read to protect state procedural rules that are 'substantively based' from being displaced by an otherwise valid federal rule. Ralph U. Whitten, *Justice Whitten, Nagging in Part and Declaring a Pox on All Houses*, 44 CREIGHTON L. REV. 115, 128–30 (2010). But while *Burlington Northern* states that '[r]ules which incidentally affect litigants' substantive rights do not violate [Section 2072(b)] if reasonably necessary to maintain the integrity of that system of rules, the case is silent about whether the standard it articulates departs from *Sibbach*. *Burlington Northern*, 480 U.S. at 5. Indeed, the Court's cursory analysis of the validity of the Federal Rule in question appears to support the *Shady Grove* plurality's reading of the case: 'The choice made by the drafters of the Federal Rules in favor of a discretionary procedure affects only the process of enforcing litigants' rights and not the rights themselves. *Id.* at 8.

57. *Sibbach*, 312 U.S. at 14.

assistance in resolving what counts as procedural for purposes of the REA. The plurality in *Shady Grove* similarly falls short.

The really-regulates-procedure standard presumably is narrower than Congress's power to enact procedural legislation. *Hanna* makes clear that Congress may legislate with respect to any matter that is even "*arguably* procedural."[58] But *Sibbach* more narrowly confines the Court's prospective rule-making authority to Rules that "*really* regulate[] procedure."[59] The *Shady Grove* plurality appears to recognize this distinction, as its discussion of limitations periods suggests. The plurality states that proper characterization of a Federal Rule similar to a statute of limitations would present a difficult issue of validity under the REA.[60] But there can be little doubt that statutes of limitation are arguably procedural within the meaning of *Hanna*. Such statutes traditionally have been treated as procedural in the conflict of laws,[61] and the Court has held that the Due Process Clause permits a forum state to apply its own law to matters that traditionally were deemed

58. *Hanna*, 380 U.S. at 476 (Harlan, J. concurring) (emphasis added). *See id.* at 472 (majority opinion) ("For the constitutional provision for a federal court system (augmented by the Necessary and Proper Clause) carries with it congressional power to make rules governing the practice and pleading in those courts, which in turn includes a power to regulate matters which, though falling within the uncertain area between substance and procedure, are rationally capable of classification as either."). *Cf. id.* at 476 (Harlan, J. concurring) ("I submit that the Court's 'arguably procedural, ergo constitutional' test moves too fast and far in the other direction.").

59. *Sibbach*, 312 U.S. at 14 (emphasis added). *See* Clermont, *supra* note 35, at 1004 (recognizing that the 'arguably procedural' standard is different from the 'really regulates procedure' standard). *Cf.* John B. Oakley, *Illuminating* Shady Grove*: A General Approach to Resolving* Erie *Problems*, 44 CREIGHTON L. REV. 79, 83 n.18 (2010) ("[I]n my view 'really regulates procedure' is just another way of say[ing] 'arguably procedural.'").

60. *Shady Grove*, 559 U.S. at 414 n. 13 (plurality opinion) (arguing that the 'examples the concurrence offers, including 'statutes of limitations' do not make its broad definition of substantive rights more persuasive, but 'merely illustrate that in rare cases it may be difficult to determine whether a rule 'really regulates' procedure or substance").

61. RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 603 ("If action is barred by the statute of limitations of the forum, no action can be maintained though action is not barred in the state where the cause of action arose.").

procedural in conflict of laws, including statutes of limitation.[62] For that reason, it seems clear that such a statute is arguably procedural and that Congress could enact a statute of limitations for state-law claims brought in federal court. If the really-regulates-procedure standard were coextensive with the *Hanna*'s arguably-procedural standard, the plurality could not have concluded that a Federal Rule in the nature of a statute of limitations would present a difficult issue.

But beyond the implicit recognition that the really-regulates-procedure and the arguably-procedural standards are different and the explicit insistence that state law has no bearing on the REA's substance-procedure distinction, the plurality does not advance an analytical framework for distinguishing between substance and procedure. The plurality simply notes that "in rare cases it may be difficult to determine whether a rule 'really regulates' procedure or substance,"[63] and insists that the Court has "managed to muddle through well enough in the 69 years since *Sibbach* was decided."[64]

2. Justice Stevens's Concurrence

In contrast to the plurality, Justice Stevens rejects the view that the REA analysis may be boiled down to whether a Federal Rule "really regulates procedure."[65] He concludes instead that a Federal Rule must give way even to state rules procedural in form if they are a part of the definition of a state substantive right.[66] In so arguing, Justice Stevens follows in the tradition of John Hart Ely, who argued that § 2072(b) was designed to protect state substantive law from conflicting Federal Rules properly promulgated under § 2072(a).[67] Thus, even while accepting that the certification requirements of Rule 23 involve a matter of "practice and procedure" within the meaning of § 2072(a), Justice Stevens nonetheless insists on

62. Sun Oil Co. v. Wortman, 486 U.S. 717, 726 (1988) (noting that a forum may apply its own statute of limitations to a case even if its only connection with the case is its role as the forum because statutes of limitation traditionally were viewed as procedural in the conflict of laws).

63. *See Shady Grove*, 559 U.S. at 414 n.13.

64. *Id.* at 415.

65. *Id.* at 416–17.

66. *Id.* at 420.

67. *See* Ely, *supra* note 14, at 718–38.

determining whether Rule 23 would "abridge, enlarge, or modify" a substantive right granted by the New York statute at issue in *Shady Grove*.[68]

a. The Mistaken Focus on Federalism

Like Professor Ely, Justice Stevens insists that the REA be construed in the light of federalism concerns and wholly ignores the separation-of-powers concerns that undergird the Act.[69] This tunnel vision manifests itself most tellingly in Justice Stevens's construction of § 2072(a). Although Justice Stevens accepts that the really-regulates-procedure test is "consonant with the Act's first limitation to 'general rules of practice and procedure,'" he makes no effort to explicate the standard.[70] He simply states that according to the plurality it "*apparently*" refers to whether a rule "regulates 'the manner and the means by which the litigants' rights are enforced.'"[71] Professor Ely, for his part, argued that § 2072(a) authorized the Court to prescribe any rule of procedure that Congress would be authorized to enact under its procedural power.[72] For Professor Ely

68. *Shady Grove*, 559 U.S. at 436.

69. Justice Stevens does make brief reference in his opinion to the separation of powers. *See id.* at 425 (arguing that the plurality's construction of the REA 'ignores the separation-of-powers presumption, see Wright et al. § 4509, at 265 '). *Federal Practice and Procedure* states in relevant part:

> Under our notion of the proper distribution of power among the branches of the federal government, primary responsibility for the exercise of federal rulemaking authority is lodged with Congress and not the federal judiciary; thus, the rulemaking authority of the federal courts generally is understood to extend only so far as Congress expressly permits or as is necessary to effectuate important federal policies as defined by Congress.

19 WRIGHT ET AL. FEDERAL PRACTICE AND PROCEDURE § 4509 (2d ed. 1987). Rather than address the separation-of-powers concerns that animated the debate over the REA, Justice Stevens relies on this discussion to buttress his argument that otherwise valid rules of 'practice and procedure' must give way in certain circumstances to state law.

70. *Shady Grove*, 559 U.S. at 424 (Stevens, J. concurring).

71. *Id.* (emphasis added).

72. Ely, *supra* note 14, at 718 (stating that Section 2072(a) imposes no limitation "that was not imposed by the Constitution"). *Federal Practice and Procedure* appears to follow suit:

and those who follow in his footsteps, the real limits on the Court's procedural rule-making authority are found in the requirement that Federal Rules not "modify, abridge or enlarge substantive rights"—a provision Professor Ely and his adherents understand as primarily focused on federalism.[73]

The error of this approach can be illustrated by considering statutes of limitation. Thomas Rowe—who similarly treats § 2072(b) primarily as a federalism limit on the Federal Rules—has argued as follows:

> A notable hypothetical example of a rule that would be valid under REA subsection (a) but run afoul of subsection (b)'s substantive-rights limit would be one establishing a limitations period for state-law claims in federal court. Such a rule would be within the subsection (a) power because of the procedural concerns for docket control and adjudication of stale claims that are among the reasons for statutes of limitations.[74]

> Does the Act delegate rulemaking authority coextensive with Congress' constitutional rulemaking authority under Article III and the Necessary and Proper Clause—that is, authority to regulate any matter that might rationally be treated as procedural? Or does the 'substantive rights' proviso confine the Supreme Court's rulemaking authority within narrower bounds than Congress' constitutional authority, prohibiting regulation by Court-promulgated rule of some or perhaps even all matters within that uncertain area between substance and procedure?

19 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 4509 (2d ed. 1987). As argued *supra*, the Court's post-*Hanna* cases have focused their attention on Section 2072(b) without construing Section 2072(a). *See supra* notes 36-40 and accompanying text.

73. 28 U.S.C. § 2072(b). Because Federal Rules may affect federal as well as state substantive rights, Professor Ely's contention that Federal Rules may be invalid as applied arguably safeguards both federalism and the separation-of-powers.

74. Thomas Rowe, *Sonia, What's a Nice Person like You Doing in Company like That?*, 44 CREIGHTON L. REV. 107. 110 (2010). *See also* Ely, *supra* note 14, at 726–27 (stating that a Federal Rule prescribing a limitations period would satisfy Section 2072(a) because 'Congress could constitutionally enact a statute

Justice Stevens similarly argues that statutes of limitations are "*in some sense* procedural rules"[75] before concluding that if the Court "were to promulgate a federal limitations period, federal courts would still, *in some instances*, be required to apply state limitations periods."[76] Justice Stevens and Professor Rowe—like Professor Ely—erroneously assume that § 2072(a) grants the Court rule-making power that is coextensive with Congress's power to legislate with respect to matters that are arguably procedural. But their conclusion rips the REA from its historical moorings.

A sophisticated lawyer at the time the REA was enacted would have understood that a statute of limitations was ordinarily procedural for conflict-of-laws purposes,[77] but was not a matter of "practice" within the meaning of the Conformity Act, the statute that generally governed federal procedure in actions at law before the promulgation of the Federal Rules.[78] Nor was the conclusion that

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prescribing a limitation period for diversity cases, but would fall afoul of Section 2072(b) because limitations periods are established in part for the 'substantive purpose of relieving people's minds after the passage of the designated period ").

75. *See Shady Grove*, 559 U.S. at 425 n.9 (Stevens, J. concurring) ("[S]tatutes of limitations, although *in some sense* procedural rules, can also be understood as a temporal limitation on legally created rights; if this Court were to promulgate a federal limitations period, federal courts would still, *in some instances*, be required to apply state limitations periods. (emphasis added)).

76. *Id.* (emphasis added). For another example of Justice Stevens's inattention to the separation-of-powers constraints of the REA in this context, see his opinion for the Court in *West v. Conrail*, 481 U.S. 35 (1987), discussed *infra* in note 222.

77. *See, e.g.* RESTATEMENT (FIRST) OF THE CONFLICT OF LAWS (1934) (discussing statutes of limitation in a chapter entitled 'Procedure"). *Cf. id.* § 605 ("If by the law of the state which has created a right of action, it is made a condition of the right that it shall expire after a certain period of limitation has elapsed, no action begun after the period has elapsed can be maintained in any state. ').

78. *See* 17 Stat. 196 § 5 (1872) ("That the practice, pleadings, and forms and modes of proceeding in other than equity and admiralty causes in the circuit and district courts of the United States shall conform, as near as may be, to the practice, pleadings, and forms and modes of proceeding existing at the time in like causes in the courts of record of the State within which such circuit or district courts are held, any rule of court to the contrary notwithstanding.). It was the Rules of Decision Act ("RDA"), now codified at 28 U.S.C. § 1652, rather than the Conformity Act that was understood to require application of state statutes of limitations. As the Court explained in 1895: "[T]o no class of state legislation has

state statutes of limitations ordinarily applied in federal court motivated by federalism concerns—that is, a desire to avoid modification of state substantive rights. Rather, state statutes of limitation applied even to federal claims in the absence of an applicable federal statute of limitations because courts were not understood to have the power to elaborate limitations periods as a matter of common law.[79]

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the [Rules of Decision Act] been more steadfastly and consistently applied than to statutes prescribing the time within which actions shall be brought within its jurisdiction. Campbell v. Haverhill, 155 U.S. 610, 614 (1895). *See* M'Cluny v. Silliman, 28 U.S. 270, 277 (1830) (holding that under the RDA, '[t]he acts of limitations of the several states, where no special provision has been made by congress, form a rule of decision in the courts of the United States, and the same effect is given to them as is given in the state courts"). The Court more recently has taken the position that state statutes of limitation do not apply of their own force in such cases but may be borrowed as a matter federal common law in an appropriate case. *See, e.g.* DelCostello v. International Brotherhood of Teamsters, 462 U.S. 151, 158–61 (1983).

79. *See* Movie Color Ltd. v. Eastman Kodak Co. 288 F.2d. 80, 83 (2d Cir. 1961) (Friendly, J.) (noting that the reason for applying state statutes of limitation to federal claims in the absence of a federal statute of limitation was because 'selection of a period of years [is] not the kind of thing judges do '). As Professor Burbank has explained:

> Since the beginning of the Republic, the federal courts have struggled with the problem of limitations periods for federal statutes that do not specify the time within which a suit must be brought. Unable to fill the gaps with judge-made rules, but unwilling to indulge the notion that a federal statutory claim is timeless, the federal courts found in the Rules of Decision Act's reference to the 'laws of the several states' the path of least resistance.

Stephen B. Burbank, *Of Rules and Discretion: The Supreme Court, Federal Rules and Common Law*, 63 NOTRE DAME L. REV. 693, 693–94 (1988); *see also* Stephen B. Burbank, *Interjurisdictional Preclusion, Full Faith and Credit and Federal Common Law: A General Approach*, 71 CORNELL L. REV. 733, 769 n.167 (1986) ("Even so simple a matter as placing limitation periods on private actions requires a statute; no common law principle explains why a cause of action valid on one day should be barred the next.') (quoting Richard Epstein, *The Social Consequences of Common Law Rules*, 95 HARV. L. REV. 1717, 1721 (1982)). State courts have also renounced authority to create limitations periods. *See, e.g.* Acxiom Corp. v. Leathers, 961 S.W.2d 735, 737 (Ark. 1998) ("[T]ime limitations during which a claim may be asserted exist only to the extent that they are created by statute.') (quoting Estate of Escher, 407 N.Y.S.2d 106, 109 (N.Y Surr. 1978));

It could be argued that an unrestricted delegation of power over procedure, if constitutional, would have given the Court power to prescribe a limitations period by rule. But the REA carefully limited its grant of authority to "the forms of process, writs, pleadings, and motions, and the practice and procedure in civil actions."[80] The term "practice and procedure" as used in this context is susceptible to a much narrower interpretation than the term procedural in the conflict of laws,[81] especially when coupled with the admonition that the Federal Rules "shall neither abridge, enlarge, nor modify the substantive rights of any litigant." As a 1926 Senate Report stated:

> Neither in England nor in any State of the United States where the courts are vested with the rule-making power, has it been assumed that the delegation of that power to them authorizes them to deal with such substantial rights and remedies as those just referred to. In Delaware, Virginia, New Jersey, and Colorado, where the courts have for years had power to make rules of practice and procedure, they have never assumed to make rules relating to limitations of actions, attachment or arrest, juries or

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Shewbrooks v. A.C. & S. Inc. 529 So.2d 557, 564 (Miss. 1988) ("Limitations on the time within which an action must be brought are created by statute only.").

80. Act of June 19, 1934, Pub. L. No. 73-415, 48 Stat. 1064.

81. *See, e.g.* Winberry v. Salisbury, 68 A.2d 332, 334 (N.J. App. Div. 1949) ("The grant of power to make rules governing the practi[c]e and procedure in all our courts does not include in its scope all adjective law. Most lawyers would probably agree that the Supreme Court is not empowered to make rules that would supersede the Statute of Frauds or the Statute of Limitations, for instance."); Gustavus Ohlinger, *Questions Raised by the Civil Advisory Committee on Rules of Civil Procedure for the District Courts of the United States*, 11 U. CIN. L. REV. 445, 451 (1937) ("On familiar canons of statutory construction it can well be argued that it was the intent of Congress to limit the general term 'practice and procedure' to particulars of the kind set out in the preceding enumeration, that is, to matters *ejusdem generis* as 'forms of process, writs, pleadings and motions' and that the general term cannot be extended to include matters of jurisdiction, power, modes of proof, rules of evidence and substantive law."). *See also* Wickes, *supra* note 55, 23 ("[R]ules of evidence have not customarily been treated as matters of 'practice and procedure' by the Supreme Court and the lower federal courts.").

> jurors or evidence; and in each of those States such matters are reserved for statutory regulation.[82]

In view of the foregoing, it seems likely that those who enacted the REA would have been bemused by Justice Stevens's suggestion in *Shady Grove* that the Court could prescribe a limitations period by Federal Rule that would apply in the absence of a conflicting state statute of limitations characterized as substantive. Put another way, construing the REA's limits on rule making as focused on federalism would have the effect of granting the Court power to prescribe Federal Rules that Congress did not intend to authorize the Court to prescribe.[83]

Conversely, a federalism reading of the REA would also have the effect of interfering with a fundamental purpose of the act—that is, to give the Court authority to prescribe a "uniform and consistent" set of Federal Rules. Justice Stevens argues that

> Congress has not mandated that federal courts dictate to state legislatures the form that their substantive law

82. S. REP. NO. 69-1174 at 9–10 (1926). The report, of course, substantially pre-dates enactment of the REA, but it provides useful guidance on the meaning of the act. For discussion of the proper uses of the 1926 Senate Report, *see infra* note 158.

83. Although Professor Burbank would deny the Court the power to prescribe rules touching on limitations periods, *see* Stephen B. Burbank, *Hold the Corks: A Comment on Paul Carrington's* 'Substance' and 'Procedure' in the Rules Enabling Act, 1989 DUKE L.J. 1012, 1020–22, my approach is less absolute. I would ask whether the Court was prescribing a Rule affecting limitations periods to further a federal policy within its rule-making power. *See infra* Part II.C. Relation-back rules in connection with the amendment of pleadings, for example, *might* be justifiable on the ground that federal pleading policy—a matter clearly within the Court's rule making power—otherwise would be frustrated. *See* Carrington, *supra* note 42, at 311 ("Without the relation-back provision, the purpose of Rule 8 would have been frustrated by courts holding that minor and cosmetic pleading amendments were precluded by an applicable statute of limitations.'). *Cf.* Burbank, *supra* note 42, at 1021 (declining to 'claim overreaching' with respect to the relation back provision of the 1938 version of Rule 15(c) in part because 'decisions discovering a new cause of action in an amended pleading were hardly predictable.'). Professor Carrington concludes that '[r]ulemakers do have authority under the first sentence of the Act to make *general* limitations law that is integral to the federal procedural system of which it is a part. Carrington, *supra* note 42, at 321.

> must take. And were federal courts to ignore those portions of substantive state law that operate as procedural devices, it could in many instances limit the ways that sovereign States may define their rights and remedies. When a State chooses to use a traditionally procedural vehicle as a means of defining the scope of substantive rights or remedies, federal courts must recognize and respect that choice.[84]

It is true, of course, that the REA does not purport to dictate the form that state substantive law must take. But it was clear in 1934—and remains clear today—that if a state chooses to accomplish a substantive purpose through procedural means, other sovereigns are not required by the Constitution to rewrite their law of procedure for the purpose of adjudicating the case.[85] The question is whether the REA should nonetheless be construed to require Federal Rules to give way in such circumstances. On this point, the legislative history seems clear. Proponents of the REA sought the promulgation of uniform Federal Rules in part because of the complications of a procedural regime that required application of both federal and state procedural law in federal actions.[86] The *York* case soon put the vision

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84. *Shady Grove*, 559 U.S. at 420 (Stevens, J. concurring).

85. *See* Sun Oil Co. v. Wortman, 486 U.S. 717, 722 (1988) ("Since the procedural rules of its courts are surely matters on which a State is competent to legislate, it follows that a State may apply its own procedural rules to actions litigated in its courts.'); *Hanna*, 380 U.S. at 472 ("[T]he constitutional provision for a federal court system (augmented by the Necessary and Proper Clause) carries with it congressional power to make rules governing the practice and pleading in those courts, which in turn includes a power to regulate matters which, though falling within the uncertain area between substance and procedure, are rationally capable of classification as either.').

86. The 1926 Senate Report stated:

> [T]he practice of the law in the district courts of the United States [is] the most difficult and uncertain of the whole civilized world. This is not solely because the district courts are called upon to apply the constantly changing statutes of 48 States—a task that, in itself, is appalling—but because [the Conformity Act of 1872] gives the district courts a discretion in the use of the words 'as near as may be, which, being liberally exercised, has introduced so many exceptions

of a uniform procedure in federal courts out of reach when a matter is not covered by a Federal Rule, a federal statute, or the constitution,[87] but the legislative history nonetheless strongly suggests that when a Federal Rule of "practice and procedure" is on point, deference to state law is not appropriate. A reading of § 2072(b) that gives federalism priority is plausible only if the legislative history is ignored.[88]

Justice Stevens's approach to the REA also misconstrues relevant precedent, including the Court's decision in *Sibbach*.[89] Although some of the pre-*Hanna* cases on which Justice Stevens relies turned on whether a purportedly procedural state rule is part of the definition of a state substantive right—the question Justice Stevens would pose under § 2072(b)—none of these cases involved consideration of the validity of a Federal Rule.[90] Rather, these cases turned on an *Erie* analysis, an analysis that is especially protective of state law. These *Erie* cases provide dubious authority for Justice Stevens's suggested analysis. As for *Sibbach*, Justice Stevens can do no more than state that "[*i*]*f* the Federal Rule" in *Sibbach* "had in fact displaced a state rule that was sufficiently intertwined with a state right or remedy, then *perhaps* the Enabling Act analysis would have

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> to the general rule of the statute that it is impossible to exaggerate the confused condition into which we have fallen.

S. REP. NO. 69-1174 at 2 (1926).

87. Guar. Trust Co. v. York, 326 U.S. 99, 109 (1945) ("[T]he intent of [*Erie*] was to insure that, in all cases where a federal court is exercising jurisdiction solely because of the diversity of citizenship of the parties, the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of a litigation, as it would be if tried in a State court.").

88. Justice Stevens does not cite to any of the legislative history in his concurrence. The only section of *Federal Practice and Procedure* on which Justice Stevens relies in his concurrence states that "the legislative history of the Enabling Act is surprisingly sketchy, and with respect to the 'substantive rights' proviso is virtually nonexistent, 19 WRIGHT ET AL. FEDERAL PRACTICE AND PROCEDURE § 4509 (2d ed. 1987), and does not cite to Professor Burbank's essential work on the legislative history of the Act. *See Shady Grove*, 559 U.S. at 422 (Stevens, J. concurring).

89. The precedent Justice Stevens misconstrues includes Byrd v. Blue Ridge Rural Elec. Coop. Inc. 356 U.S. 525 (1958); Cohen v. Beneficial Indus. Loan Corp. 337 U.S. 541, (1949); Ragan v. Merch. Transfer & Warehouse Co. 337 U.S. 530 (1949).

90. For discussion of these cases, *see* Genetin, *supra* note 6, at 1087–94.

been different."[91] But even Justice Stevens's speculation about how *Sibbach* might have come out is not well grounded.

His speculation rests on the conclusion that the Court in *Sibbach* addressed only whether the Court had authority to promulgate the Federal Rules in question and not whether those Rules—even if validly promulgated—should in appropriate circumstances give way to conflicting state law under § 2072(b).[92] To support this reading, Justice Stevens highlights the Court's statement that "argument touching the broader questions of Congressional power and of the obligation of federal courts to apply the substantive law of a state [was] foreclosed."[93] But *Sibbach* unmistakably addressed the meaning of § 2072(b), concluding that the section was intended to "*emphasize*" the restriction on the "authority to prescribe" granted in § 2072(a) to "matters of pleading and court practice and procedure,"[94] a construction of the statute that both accords with the legislative history[95] and is not contradicted by any of the Court's later cases construing the REA. While not specifically addressing the argument that Justice Stevens makes in *Shady Grove*, *Sibbach* rejects the view that § 2072(b) imposes limits

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91. *Shady Grove*, 559 U.S. at 428 (emphasis added).

92. For a defense and elaboration of Justice Stevens's view, see Allan Ides, *The Standard for Measuring the Validity of a Federal Rule of Civil Procedure: The* Shady Grove *Debate Between Justices Scalia and Stevens*, 86 NOTRE DAME L. REV. 1041 (2011). *See also* Katherine T. Struve, *Institutional Practice, Procedural Uniformity, and As-Applied Challenges Under the Rules Enabling Act*, 86 NOTRE DAME L. REV. 1181 (2011) (arguing that Justice Stevens's reading of *Sibbach* is correct). Rowe, *supra* note 74, at 109 '[W]hatever else *Sibbach* and later cases may have done, they have never squarely addressed the possibility that subsection (b)'s substantive-rights limit has independent force. '). *Cf.* Clermont, *supra* note 35, at 1014–15 n.135 (rejecting Justice Stevens's reading of *Sibbach*).

93. Sibbach v. Wilson & Co. 312 U.S. 1, 9 (1941). As Justice Scalia notes '[i]t is clear from the context that this passage referred to the *Erie* prohibition of court-created [common-law] rules that displace state law. *Shady Grove*, 559 U.S at 411 n.9 (plurality opinion).

94. *Sibbach*, 312 U.S. at 10 (emphasis added).

95. *See* Burbank, *supra* note 42, at 1107 ("It appears that the Supreme Court was correct in *Sibbach* and subsequent cases to the extent that it failed to attribute independent meaning to the Act's second sentence, and thus to impute to the second sentence limitations not imposed by the first. ').

on the validity of Federal Rules over and above the limits imposed by § 2072(a).[96]

Finally, Justice Stevens cites a preemption case, *Wyeth v. Levine*, to support the argument that a federal statute does not displace a state's law "unless that was the clear and manifest purpose of Congress."[97] *Wyeth* rests on the proposition that

> [i]n all pre-emption cases, and particularly in those in which Congress has 'legislated in a field which the States have traditionally occupied,' we 'start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'[98]

But even if one assumes that preemption cases govern the displacement of state law in diversity cases,[99] and ignores the congressional purpose evidenced in the REA's legislative history, *Wyeth* is inapposite. The "practice and procedure"[100] of the federal courts is not an area within "the historic police powers of the States."[101]

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96. *Sibbach*, 312 U.S. at 10 ("Hence we conclude that [the REA], was purposely restricted in its operation to matters of pleading and court practice and procedure. Its two provisos or caveats [including the substantive rights proviso] emphasize this restriction. ').

97. Wyeth v. Levine, 555 U.S. 555, 565 (2009) (quoting Medtronic, Inc. v. Lohr, 518 U.S. 470, 485 (1996)).

98. *Id.*

99. Margaret Thomas has argued that '[t]he Court's opinions treat diversity preemption as a form of preemption operating analogously to 'hard' preemption, thereby justifying the use of preemption's analytic tools in diversity cases." *See* Margaret S. Thomas, *Constraining the Federal Rules of Civil Procedure through Federalism Canons of Statutory Interpretation*, 16 N.Y.U. J. LEGIS. & PUB. POL'Y 187, 194–95 (2013); *see also id.* at 195 n.16 (citing Justice Stevens's opinion in *Shady Grove*). In fact, the only opinion Professor Thomas cites which clearly supports that conclusion is Justice Stevens's concurring opinion in *Shady Grove*.

100. 28 U.S.C. § 2072(a) (2015).

101. *Wyeth*, 555 U.S. at 565. Professor Thomas argues that what matters is whether the application of a Federal Rule would 'undermine' state policymaking in areas left by Congress to the states that fall within the states' historic police powers. Thomas, *supra* note 99, at 258. She contends that Section 901(b), the New York provision at issue in *Shady Grove*, 'falls squarely within its police

In short, Justice Stevens's arguments in support of reading § 2072(b) to promote federalism—while not implausible as a textual matter—ignore legislative history and misconstrue the Court's precedents. Section 2072(b) should be understood as simply reinforcing the separation-of-powers limits imposed by § 2072(a) on Court rule making. But even if one assumes that federalism is the animating principle of § 2072(b), Justice Stevens's approach is misguided for the reasons discussed in the next subpart.

b. *Justice Stevens's Flawed Approach to Promoting Federalism*

While following in the tradition of Professor Ely, Justice Stevens suggests an interpretation of § 2072(b) that is more protective of the Federal Rules than Professor Ely's interpretation. Professor Ely argued that a substantive right for purposes of § 2072(b) is "a right granted for one or more nonprocedural reasons, for some purpose or purposes not having to do with the fairness or efficiency of the litigation process."[102] By contrast, Justice Stevens argues that § 2072(b) means that "federal rules cannot displace a State's definition of its own rights or remedies."[103]

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power to regulate the general welfare, and thus should have prevailed over Rule 23 in a diversity case heard in federal court, even though New York's mode of regulation might conflict with Rule 23. *Id.* But such an understanding would in effect privilege the procedural choices of a state over a Congressional policy in favor of uniformity in an area of law peculiarly within the prerogative of the federal government, that is, the rules governing the practice and procedure of federal courts. Thus, the federalism canon should not be understood to require displacement of Rule 23 by Section 901(b).

102. Ely, *supra* note 14, at 725. *See id.* at 724 ("We have, I think, some moderately clear notion of what a procedural rule is—one designed to make the process of litigation a fair and efficient mechanism for the resolution of disputes.").

103. Shady Grove Orthopedic Assocs. v. Allstate Ins. Co. 559 U.S. 393, 418 (2010). It is unclear whether, by this formulation, Justice Stevens means to indicate that the protection afforded to substantive rights by section 2072(b) is confined to the following: (1) the elements relevant to a claim for relief, (2) remedies available in connection with such a claim, and (3) rules procedural in form that are bound up with these elements and remedies. I see no basis in the legislative history or the Court's cases for so limiting the meaning of "substantive right. I do not pursue this point further here because most substantive rights fit

If a state rule takes the form of a procedural rule, Justice Stevens argues, § 2072(b) does not protect the rule unless it is "part of [the] State's framework of substantive rights or remedies."[104] As he explains, '[a] 'state procedural rule, though undeniably 'procedural' in the ordinary sense of the term,' may exist 'to influence substantive outcomes,' and may in some instances become so bound up with the state-created right or remedy that it defines the scope of that substantive right or remedy."[105] When procedure and substance are bound up in such a way, a Federal Rule should be deemed invalid to the extent it otherwise would displace the state rule. Justice Stevens further imposes a high burden of proof before a court may conclude that a rule procedural in form should be deemed part of the definition of a substantive right:

> [T]he bar for finding an Enabling Act problem is a high one. The mere fact that a state law is designed as a procedural rule suggests it reflects a judgment about how state courts ought to operate and not a judgment about the scope of state-created rights and remedies.
>
> The mere possibility that a federal rule would alter a state-created right is not sufficient. There must be little doubt.[106]

Justice Stevens elaborates on the standard he proposes by analyzing whether Rule 23 should be applied notwithstanding its conflict with § 901(b),[107] the provision at issue in *Shady Grove*. First, he determines that § 901(b) is a procedural rule, at least in form.[108]

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within this narrow definition and because Justice Stevens's approach is subject to criticism on more important grounds.

104. *Id.* at 419.

105. *Id.* at 419–20 (quoting Judge Posner's decision in S.A. Healy Co. v. Milwaukee Metro. Sewerage Dist. 60 F.3d 305, 310 (7th Cir. 1995)).

106. *Id.* at 432.

107. *See* N.Y C.P.L.R. 901(b) (MCKINNEY DATE) ("Unless a statute creating or imposing a penalty, or a minimum measure of recovery specifically authorizes the recovery thereof in a class action, an action to recover a penalty, or minimum measure of recovery created or imposed by statute may not be maintained as a class action.")

108. *See Shady Grove*, 559 U.S. at 436 (Stevens, J. concurring) (according significance to the fact that Section 901(b) is 'a rule in New York's procedural code about when to certify class actions brought under any source of law").

Second, he concludes that it is doubtful that § 901(b) defines New York's substantive rights and remedies because "[t]he text of CPLR § 901(b) expressly and unambiguously applies not only to claims based on New York law but also to claims based on federal law or the law of any other State."[109] Having so characterized the statute, Justice Stevens considers the legislative history. He concedes that based on the legislative history "one can argue that class certification would enlarge New York's 'limited' damages remedy," but decides that in the light of the "plausible competing narratives," the import of the statute's "plain" text should be respected.[110] He insists that if the legislative history is susceptible to an interpretation that would treat a state rule as procedural, the rule may be deemed part of the definition of a state substantive right only if the plain meaning of the state provision so requires or the state's highest court has resolved the question. Thus, he concludes that § 901(b) should not be deemed a part of the definition of a state substantive right.[111]

Even if Justice Stevens correctly concluded that § 901(b) is not part of New York's definition of substantive rights, his analysis is problematic. That is because he failed to recognize the limited utility of statutory text and legislative history in addressing the interpretive problem he sought to resolve. The text of § 901(b)—like most statutes in the United States—is wholly silent on the question of its scope for conflict-of-laws purposes. Because legislatures typically legislate with wholly domestic cases in mind, statutes and legislative history rarely address the question of a statute's scope for conflict-of-laws purposes.[112] Consider, for example, the following California statute: "Every person who, intentionally and without the

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109. *Id.* at 432.

110. *Id.* at 436.

111. *Cf.* Burbank & Wolff, *supra* note 19, at 71–72 (discussing Weber v. U.S. Sterling Secs. 924 A.2d 816 (Conn. 2007), a Connecticut Supreme Court case applying Section 901(b) under Connecticut choice-of-law rules).

112. For a statement of this fundamental choice-of-law principle, see Larry Kramer, *Vestiges of Beale: Extraterritorial Application of American Law*, 1991 S. CT. REV. 179, 204 ("[M]ost laws are silent when it comes to multistate cases, because lawmakers typically work with wholly domestic situations in mind.'). Justice Stevens mistakenly suggests that this principle is inapplicable when, as with Section 901(b), a statute is directed to a court. *See Shady Grove*, 559 U.S. at 433 n.16 (Stevens, J. concurring) (arguing that 'a presumption against extraterritoriality makes little sense' when a statute is directed to a court).

consent of all parties to a confidential communication records the confidential communication "[113] is subject to a civil lawsuit.[114] We can presume the statute will be applied in a California court to a telephone conversation between two Californians in California. But the circumstances in which a state statute (or common law rule) should be applied outside of a wholly domestic case cannot be determined without applying relevant choice-of-law rules.

Justice Stevens's approach to the construction of § 901(b) in fact is generally consistent with the traditional approach to choice of law. Rules defined as procedural apply to claims asserted in the forum but not to those asserted outside it.[115] That said, in limited circumstances, a rule procedural in form may be treated as substantive. Statutes of limitation illustrate this distinction. Although statutes of limitation traditionally were treated as procedural, and therefore (in the absence of a borrowing statute) were applicable to all claims brought in the forum,[116] so-called "built-in" statutes of limitation were an important exception: when the statute creating the substantive right included a built-in limitations period, the limitations period was deemed substantive.[117] Justice Stevens similarly seems to believe that a procedural provision built into an otherwise clearly substantive statute is bound up with the definition of a state substantive right.[118]

113. Cal. Penal Code § 632(a) (West 2010).

114. Cal. Penal Code § 637.2 (West 2010).

115. *See* RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 585 (1934) ("All matters of procedure are governed by the law of the forum.").

116. *See supra* notes 61-62 and accompanying text.

117. *See* Bournias v. Atl. Mar. Co. 220 F.2d 152, 154 (2d Cir. 1955) ("The common case [where limitations are treated as 'substantive'] is where a statute creates a new liability, and in the same section or in the same act limits the time within which it can be enforced, whether using words of condition or not.") (quoting Davis v. Mills, 194 U.S. 451, 454 (1904)) (brackets in original).

118. *See Shady Grove*, 559 U.S. at 420–21 (Stevens, J. concurring) (A state procedural rule "may in some instances become so bound up with the state-created right or remedy that it defines the scope of that substantive right or remedy."). After *Shady Grove*, a number of lower courts have focused on where a rule that is procedural in form is located in state law without considering the purpose of the rule. *See* Harris v. Reliable Reports, Inc. No. 1:13-CV-210 JVB, 2014 WL 931070, at *8 (N.D. Ind. March 10, 2014) (finding state law controlling because "[t]he New York law that the Supreme Court in *Shady Grove* held must yield to Rule 23 was a generally applicable procedural rule, whereas the opt-in provisions apply only to actions under the state wage and hour laws and are

But there is reason to question Justice Stevens's commitment to protecting a state's definition of substantive rights when a state does not use a traditional approach to define substance and procedure. In jurisdictions that use modern approaches to choice of law, the fact that a rule is procedural in form may provide little guidance. California's statutes of limitations, for example, are found in the Civil Procedure Code, but the California Supreme Court has indicated that a "governmental interest analysis" determines whether the California statute of limitations should be applied in a given case, and the purposes attributed to a statute of limitations under this approach are not necessarily procedural.[119] Although New York continues to apply the traditional substance-procedure distinction to statute-of-limitations issues,[120] it is unclear whether it would do so with respect to the issue raised by § 901(b). But Justice Stevens fails even to ask how New York would resolve the choice-of-law issue. If Justice Stevens is serious about protecting a "state's definition of its

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part of the statutes that created the underlying substantive rights"); Stalvey v. Am. Bank Holdings, Inc. No. 4:13-cv-714, 2013 WL 6019320, at *4 (D.S.C. Nov. 13, 2013) ("The case at bar is different from the state procedural law at issue in *Shady Grove* [h]ere, the prohibitions against class actions ingrained in the very text of the SCUTPA and Consumer Protection code are substantive portions of South Carolina law[.]"); Lisk v. Lumber One Wood Preserving, LLC, No. 3:13-cv-01402-AKK, 2014 WL 66512, at *7 (N.D. Ala. Jan. 8, 2012), *rev'd*, 792 F.3d 1331 (11th Cir. 2015) (holding that a bar on class actions defines the scope of state-created rights and remedies because '[i]t is contained in the same section of the Alabama Code that creates a private right of action and its text limits its application to private rights of action brought under the ADPTA'").

119. *See, e.g.* McCann v. Foster Wheeler, LLC, 225 P. 3d 516, 527 (Cal. 2010) (determining that governmental interest analysis governs choice-of-law issues). Governmental interest analysis, the leading theoretical approach in the United States, explicitly looks to the policy of a statute to determine whether it should be construed as having extraterritorial effect in a particular case. *See* Eugene F. Scoles, Peter Hay, Patrick Borchers & Symeon C. Symeonides, CONFLICT OF LAWS § 2.9 at 26–27 (West 4th ed.) (explaining that Brainerd Currie, the father of governmental interest analysis, 'focused directly on the content of the substantive laws of the states implicated in [a] conflict,' and 'argued that the 'ordinary processes of construction and interpretation' would reveal the policies underlying those laws and would, in turn, determine their intended sphere of operation *in terms of space*"); *id.* at 26 ("Currie resorted to the method of statutory construction and interpretation that courts employ in fully domestic cases.'").

120. *See* Tanges v. Heidelberg N. Am. Inc. 710 N.E. 2d 250 (N.Y 1999) (discussing statutes of limitations and statutes of repose).

own rights or remedies,"[121] he cannot ignore a state's choice-of-law rules, even if those rules require a focus on the purpose rather than the text or placement of state law.

Justice Stevens's approach appears rooted in his concern about the "costs involved in attempting to discover the true nature of a state procedural rule."[122] But focusing on where a rule procedural in form is located in a state's statutes represents at best a second-best approach to drawing the boundary between substance and procedure.[123] While concern about cost is legitimate, Justice Stevens's approach sacrifices the accurate definition of state substantive rights on the altar of federal judicial efficiency.[124] This is a remarkable position for a Justice who insists that federalism is the underlying purpose of § 2072(b).[125] It is, after all, the responsibility of federal courts—not state legislatures—to safeguard the integrity of state law in federal court. Indeed, a proponent of an approach friendlier than Justice Stevens's to state law could lob virtually the same criticism at him that he lobbed at Justice Scalia:

121. *Shady Grove*, 559 U.S. at 418 (Stevens, J. concurring).

122. *Id.* at 432 (Stevens, J. concurring).

123. Thus, it is not surprising that courts applying modern choice-of-law approaches that permit the consideration of statutory purposes increasingly have treated statutes of limitation as 'substantive, even when the statutes are found within a state's procedural code. The notion that a limitations period is substantive only if found within the statute creating the state substantive right is an understanding no longer adhered to by many states. *See* Symeon C. Symeonides, *Choice of Law in the American Courts in 2012*, 61 AM. J. COMP. L. 217, 278 (2013) ("[T]he number of states that continue to characterize statutes of limitation as procedural and apply the *lex fori* is now down to twenty-seven, a bare majority.").

124. Justice Stevens's approach may also have a negative effect on state efficiency. *See, e.g.* Jack Friedenthal, *Defining the Word 'Maintain' Context Counts*, 44 AKRON L. REV. 1139, 1143 n.30 (2011) ("As Justice Ginsburg indicates in the dissent, it would make no sense to have 'embedded the limitation in every provision creating a cause of action for which a penalty is authorized.'"); *Shady Grove*, 559 U.S. at 447 (Ginsburg, J. dissenting) ("The New York Legislature could have embedded the limitation in every provision creating a cause of action for which a penalty is authorized; § 901(b) operates as shorthand to the same effect.")

125. *See Shady Grove*, 559 U.S. at 420–21 (Stevens, J. concurring) ("Congress has not mandated that federal courts dictate to state legislatures the form that their substantive law must take.").

> The question, therefore, is not what rule *we* think would be easiest on federal courts. The question is what rule Congress established. Although Justice SCALIA may generally prefer easily administrable, bright-line rules, his preference does not give us license to adopt a second-best interpretation of the Rules Enabling Act.[126]

In short, those intent on using the REA to protect conflicting state law from otherwise valid Federal Rules are unlikely to find Justice Stevens's approach attractive.[127] If the aim is to protect state substantive rights even from otherwise valid Federal Rules, the most effective approach is to focus exclusively on the purpose of state law. That is why John Hart Ely in his classic article argued that the proper test is whether the state rule was promulgated for one or more non-procedural reasons. For that reason, it is likely the Court in a future case will choose between the plurality's approach and an approach that interprets § 2072(b) as protecting state rules promulgated with a substantive purpose from otherwise valid Federal Rules. Justice Stevens's approach is unlikely to survive.

B. The Lower Courts After Shady Grove

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126. *Id.* at 426. The irony is that Justice Scalia's approach to the REA is more easily administrable and almost certainly closer to the rule that Congress meant to establish.

127. *See, e.g.* Whitten, *supra* note 56, at 132 (2010) (stating that Justice Stevens's 'interpretive approach essentially amounts to a 'clear statement' policy' and arguing that 'this is far too stingy an approach to interpreting state law.'); Joseph P. Bauer, *Shedding Light on* Shady Grove: *Further Reflections on the* Erie *Doctrine from a Conflicts Perspective*, 86 NOTRE DAME L. REV. 939, 973 n.185 (2011) (remarking that Justice Stevens's approach 'is decidedly inhospitable to the federalism values of *Erie*' and insisting that '[i]t is misguided to impose some sort of 'burden of proof' on the state to show that its laws have substantive goals before the federal courts will decline to preempt them by Federal Rules.'). Helen Hershkoff, Shady Grove: *Duck-Rabbits, Clear Statements, and Federalism*, 74 ALB. L. REV. 1703, 1718 (2011) (noting that Justice Stevens's construction of New York law 'effectively allows a non-elected federal judge to prescribe law-making processes for elected state representatives and to penalize explanations that are considered to be insufficient under a federal standard.').

With the notable exception of the D.C. Circuit,[128] lower courts mostly have concluded that Justice Stevens's analysis of the REA governs,[129] despite its clear rejection by the plurality. The

128. *See* Abbas v. Foreign Policy Grp. LLC, 783 F.3d 1328, 1337 (D.C. Cir. 2015) (rejecting reliance on Justice Stevens's concurrence because '[u]nless and until the Supreme Court overrules or narrows its decision in *Sibbach,* that case remains good law and is binding on lower courts. '). *See also* Passmore v. Baylor Health Care System, 823 F.3d 292, 298-99 (5th Cir. 2016) (relying on the standard set forth in *Sibbach* to conclude that the state statute in question could not be applied in federal court).

129. *In re* Packaged Ice Antitrust Litig. 779 F. Supp. 2d 642, 660 (E.D. Mich. 2011) ("Courts interpreting the *Shady Grove* decision, and searching for guidance on this issue, have concluded that Justice Stevens' concurrence is the controlling opinion by which interpreting courts are bound. '). *See, e.g.* Garman v. Campbell Cty. Sch. Dist. No. 1, 630 F.3d 977, 983 & n.6 (10th Cir. 2010) (concluding that Justice Stevens's concurrence is controlling.); McKinney v. Bayer Corp. 744 F. Supp. 2d 733, 747 (N.D. Ohio 2010) (finding Justice Stevens's opinion to be the "narrowest and, thus, controlling opinion"); *In re* Whirlpool Corp. Front-Loading Washer Prods. Liab. Litig. No. 1:08–WP–65000, 2010 WL 2756947, at *2 (N.D. Ohio July 12, 2010) (finding Justice Stevens's approach controlling because he was 'the crucial fifth vote' in the *Shady Grove* decision), *vacated on other grounds sub nom,* Whirlpool Corp. v. Glazer, 133 S. Ct. 1722 (2013); Bearden v. Honeywell Int'l. Inc. No. 3:09–1035, 2010 WL 3239285, at *10 (M.D. Tenn. Aug. 16, 2010) ("Here, that means that Justice Stevens's concurrence is the controlling opinion. '); Driscoll v. Geo. Wash. Univ. 42 F. Supp. 3d 52, 61 n.5 (D.D.C. 2012) (finding that Justice Scalia's opinion controls whether Rule 23 answers the question in dispute, but Justice Stevens's opinion controls the determination of whether applying Rule 23 would violate the Rules Enabling Act); Leonard v. Abbott Labs. Inc. No. 10–CV–4676(ADS)(WDW), 2012 WL 764199, at *12 (E.D.N.Y Mar. 5, 2012) ("[T]he court agrees with the majority of district and circuit courts that have found Justice Stevens'concurring opinion was on the 'narrowest grounds'[] and therefore is the controlling opinion. '); Williams v. Chesapeake La. Inc. Civ. A. No. 10–1906, 2013 WL 951251, at *4 (W.D. La. Mar. 11, 2013) (concluding that Justice Stevens's opinion is controlling because he agreed with the plurality, but on narrower grounds); *In re* Nexium (Esomeprazole) Antitrust Litig. 968 F. Supp. 2d 367, 409 (D. Mass. 2013) (finding Justice Stevens's opinion in *Shady Grove* to be controlling because it is narrower than the plurality opinion); Lisk v. Lumber One Wood Preserving, LLC, 993 F. Supp. 2d 1376, 1383 (N.D. Ala. 2014) (stating that Justice Stevens's opinion is controlling). *See also* Tait v. BSH Home Appliances Corp. No. SACV 10–711 DOC (ANx), 2011 WL 1832941, at *8–9 (C.D. Cal. May 12, 2011) (applying Justice Stevens's opinion because it 'can be viewed as both 'narrower' than the other holdings and as 'represent[ing] a common denominator. '); Digital Music Antitrust Litig. 812 F. Supp. 2d 390, 415–16 (S.D.N.Y 2011) (applying Justice Stevens's approach because his concurrence formed the 'narrowest

conclusion that Justice Stevens's concurrence controls is often premised on *Marks v. United States*.[130] In that case, the Court held that "[w]hen a fragmented Court decides a case and no single rationale explaining the result enjoys the assent of five Justices, 'the holding of the Court may be viewed as that position taken by those Members who concurred in the judgments on the narrowest grounds. '"[131] I am skeptical, however, that *Marks* provides assistance to courts seeking *terra firma* in this difficult area.[132]

Commentators have explained that the best justification for the *Marks* doctrine "assumes that a common thread runs through the reasoning of the various opinions in a plurality decision."[133] But

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grounds' in *Shady Grove*) (quoting *In re* Wellbutrin XL Antitrust Litig. 756 F. Supp. 2d 670, 675 (E.D. Pa. 2010)); Phillips v. Philip Morris Cos. 290 F.R.D. 476, 479–80 (N.D. Ohio 2013) (applying Justice Stevens's test because 'a clear majority of courts have applied Stevens's narrower holding as the controlling opinion for use in determining whether a federal rule may displace a conflicting state law. '); Harris v. Reliable Reports Inc. No. 1:13-CV-210 JVB, 2014 WL 931070, at *7–8 (N.D. Ind. Mar. 10, 2014) (relying on Justice Stevens's concurrence to hold that state wage and hour laws were not preempted by Rule 23).

130. Marks v. United States, 430 U.S. 188 (1977). *See supra* note 129.

131. *Marks*, 430 U.S. at 193 193 (1977).

132. For an excellent critique of the notion that Justice Stevens's opinion in *Shady Grove* is controlling, see Andrew J. Kazakes, Comment, *Relatively Unguided: Examining the Precedential Value of the Plurality Decision in* Shady Grove Orthopedic Associates v. Allstate Insurance Co. *and its Effects on Class Action Litigation*, 44 LOY. L.A. L. REV. 1049 (2011). For a rare district court opinion that recognizes how problematic it is to treat Justice Stevens's opinion as controlling under *Marks*, see Chief Judge Moskowitz's opinion in *In re Hydroxycut Mktg. & Sales Practices Litig.* 299 F.R.D. 648 (S.D. Cal. 2014).

133. Berkolow, *Much Ado About Pluralities: Pride and Precedent Amidst the Cacophony of Concurrences, and Re-Percolation after* Rapanos, 15 VA. J. SOC. POL'Y & L. 299, 327 (2008). Berkolow writes:

> The rationale underlying this justification is that 'it constitutes a least common denominator upon which all of the Justices in the majority agree, even though some would support the decision on broader grounds. This 'least common denominator' approach ascribes agreement to the Justices on the reasoning for the result. By imputing consensus in this way, it lends the imprimatur of a holding, as though from a majority opinion, to the narrowest grounds of a fractured opinion. Lower courts seek such imprimatur when determining the controlling rule from a case. But this justification has a major flaw: in some cases, no consensus, implicit or otherwise,

"[w]hen genuine agreement on the reasoning is lacking," and an implicit consensus can be cobbled together only by associating "Justices with propositions they expressly rejected,"[134] the "implicit consensus" rationale does not provide a sound basis for invoking *Marks*.[135] In *Shady Grove*, the plurality and the concurrence disagree on the nature of the REA analysis.[136]

Nor is it clear that Justice Stevens decided *Shady Grove* on the narrowest grounds.[137] To begin with, in the absence of an

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> exists. Implicit consensus can only be realized when the least common denominator—the 'narrowest grounds'—is logically enveloped by broader positions.

Id. at 327–28.

134. *Id.* at 328. Berkolow identifies a second rationale for the *Marks* doctrine:

> A second justification for the *Marks* doctrine, predictive value, is based on the idea that '[t]he principle objective of this *Marks* rule is to promote predictability in the law by ensuring lower court adherence to Supreme Court precedent. Essentially, this justification is based on the idea that 'the controlling opinion in a splintered decision is that of the Justice or Justices who concur on the 'narrowest grounds' because this narrowest ground represents a legal standard that may accurately predict what the Supreme Court would do when faced with a similar factual situation.

Id. This rationale has been properly 'criticized as failing to accurately predict the outcome of future Supreme Court decisions' as Justices, for example, 'may retire or reconsider their position when confronted with a new set of facts. *Id.* at 328–29.

135. *Id.* at 328.

136. Kazakes, *supra* note 132, at 1064 (noting that because Justice Scalia's and Justice Stevens's opinions 'represent parallel lines of analysis, each extending from the facts to the result without meeting or touching each other, neither opinion may be viewed as dispositive under *Marks*).

137. Clermont, *supra* note 35, at 1015 n.137 ("[I]n *Shady Grove* the word 'narrowest' has no clear meaning. '). For a creative argument that the parts of the opinion that Justice Sotomayor joined are controlling under *Marks*, see Craig Cagney, *O Sonia, Where Art Thou? Why Justice Sotomayor's Silent 'Opinion' Should Serve as* Shady Grove's *Holding*, 80 FORDHAM L. REV. 189 (2011). Mr. Cagney, in my view, over-reads what can be gleaned from Justice Sotomayor's decision not to join Part II.C. of the majority opinion. *Cf.* Jeffrey W. Stempel, Shady Grove *and the Potential Democracy-Enhancing Benefits of* Erie *Formalism*, 44 AKRON L. REV. 907, 928 (2011) (suggesting that Justice Sotomayor did not join Part II.C. of Justice Scalia's opinion "perhaps because [] she viewed it as

implicit consensus, there is no obvious way of determining which opinion was decided on the narrowest grounds. As one commentator has noted:

> [T]he narrowest opinion may be the one most clearly tailored to the specific fact situation before the Court and thus applicable to the fewest cases, in contrast to an opinion that takes a more absolutist position or suggests more general rules. [Another] possibility would regard the narrowest opinion as the one that departs the least from the status quo. This approach would interpret narrowness as an aspect of judicial conservatism, in the sense not only of conformity to precedent and tradition in the law, but also to established social, moral, or political values.[138]

At best, these two methods of determining which opinion was decided on the narrowest grounds point in different directions. Both the plurality's and Justice Stevens's opinions were intended to provide a general framework for determining the validity of Federal Rules and were not limited in this regard to the facts before the Court. It is nonetheless true that the plurality's opinion is more sweeping or absolutist than Justice Stevens's. On the other hand, the plurality's opinion can reasonably be viewed as narrower than Justice Stevens's because it hews closely to the Court's existing precedent. Justice Stevens's concurrence, by contrast, proposes a significant extension of existing law. That his approach has never been adopted by the Court is evident in his insistence that *Sibbach*

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surplusage, perhaps because it seemed an almost *ad hominem* attack on the reasoning of a colleague providing a crucial vote, or perhaps because her own *Erie* approach is not as formalistically supportive of the Federal Rules of Civil Procedure when in conflict with state law").

138. Linda Novak, *The Precedential Value of Supreme Court Plurality Decisions*, 80 COLUM. L. REV. 756, 763–64 (1980). *See also* United States v. Cundiff, 555 F.3d 200, 209 (6th Cir. 2009) (stating that the 'narrowest' opinion refers to the one which relies on the 'least' doctrinally 'far-reaching-common ground' among the Justices in the majority: it is the concurring opinion that offers the least change to the law"). Professor Novak also recognized that 'decisions based on statutory grounds have traditionally been regarded as 'narrower' than ones based on constitutional grounds. Novak, *supra* note 138, at 763. Neither Justice Scalia's nor Justice Stevens's opinion is premised on the Constitution.

does not foreclose his more state-law friendly approach and his commendable refusal to cite the Court's conclusory post-*Hanna* cases to support his innovative reading of the REA.[139]

Some lower courts nonetheless have implicitly argued that Justice Stevens's opinion is more judicially conservative because it would lead to federal courts disregarding fewer state laws.[140] This line of reasoning, however, ignores the fact that Justice Stevens's approach is arguably the more radical because it would permit the invalidation of a Federal Rule as applied because of conflicting state law, something wholly without precedent in the Court's jurisprudence.

Finally, some lower courts have indicated that Justice Stevens's opinion in *Shady Grove* controls because the concurrence "agreed with Justice Ginsburg's four-member dissent that 'there are some state procedural rules that federal courts must apply in diversity cases because they function as a part of the State's definition of substantive rights and remedies.'"[141] The problem with

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139. Relying at least loosely on the work of John Hart Ely, a few lower courts have found a Federal Rule invalid as applied when the rule conflicted with a state law enacted for one or more nonprocedural reasons. For a collection of authorities, see Clermont, *supra* note 35, at 1009 n.101, Struve, *supra* note 92, at 1202–03.

140. *See, e.g.* Williams v. Chesapeake La. Inc. No. Civ. A. 10-1906, 2013 WL 951251, at *4 (W.D. La. Mar. 11, 2013) ("This Court agrees that Justice Stevens reached the same result as the plurality through a narrower ground—'narrower' because Justice Stevens's opinion requires federal preclusion of fewer state laws.'); McKinney, 744 F. Supp. 2d at 747 ("Because Justice Stevens's concurring opinion would permit some state law provisions addressing class actions—whereas Justice Scalia's opinion in Part II–B (which only had the support of four Justices) would broadly prohibit any state law that conflicted with Rule 23—Justice Stevens's opinion is the narrowest and, thus, controlling opinion.').

141. *In re* Wellbutrin XL Antitrust Litig. 756 F. Supp. 2d at 674. *See also* Leonard v. Abbott Labs, Inc. No. 10-CV-4676(ADS)(WDW), 2012 WL 764199 (E.D.N.Y March 5, 2012) ("Justice Stevens's concurring opinion was on the 'narrowest grounds.'"); *In re* Trilegiant Corp. Inc. 11 F. Supp. 3d 82, 92 (D. Conn. 2014) (determining that Justice Stevens's concurring opinion was on the narrowest grounds).

Justice Stevens writes in the first paragraph of his concurrence that he 'agree[s] with Justice GINSBURG that there are some state procedural rules that federal courts must apply in diversity cases because they function as a part of the State's definition of substantive rights and remedies. Shady Grove Orthopedic Assocs. v. Allstate Ins. Co. 559 U.S. 393, 416–17 (2010) (Stevens, J. concurring). But Justice Ginsburg simply notes Justice Stevens's reference to this concept in a

this analysis, of course, is that the dissent pointedly refused to address the proper construction of the REA.[142] To the extent that an implicit consensus can be found between the concurrence and the dissent, it is about the appropriateness of sensitivity to important state regulatory interests in the construction of a Federal Rule,[143] not

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footnote making the case that five Justices agree that Federal Rules should be *interpreted* with 'sensitivity to important state interests' and a will to 'avoid conflict with important state regulatory policies. *Id.* at 442 n.2.

142. *See* Abbas, 783 F.3d at 1337 (concluding that neither the plurality nor the concurrence 'can be considered the *Marks* middle ground or narrowest opinion, as the four Justices in dissent simply did not address the issue"). Kevin Clermont has argued that the dissent implicitly agreed with the *plurality's* interpretation of the REA by failing to reject it:

> The dissent, by Justice Ginsburg for Justices Kennedy, Breyer, and Alito, signified assent to the plurality's understanding of *Sibbach* mainly by silence As a matter of logic, one could argue that the dissent never had to reach the REA's meaning—but with Justice Stevens vocally raising the point upon a 4-1-4 split vote, it would be more than strange for Justice Ginsburg to abdicate a majority position by failing to reach a point on which she shared to any degree Justice Stevens's view.

Clermont, *supra* note 35, at 1015–16. *Cf.* Alexandra D. Lahav, *Two Views of the Class Action*, 79 FORDHAM L. REV. 1939, 1943 (2011) (arguing that '[t]he implication of the dissent's position is that in this case the class action rule violated the Rules Enabling Act, which prohibits the alteration or enlargement of a substantive right"). I disagree with Professor Clermont on this point. The dissent may have refused to address the appropriate REA analysis to make the point that the plurality and concurrence had attempted to resolve a wholly unnecessary issue. That said, given the dissent's solicitude for state law, it seems likely that some or all of the dissenters would reject the plurality's approach to the REA as insufficiently deferential to state law. Indeed, to the extent one or more of the dissenters believed that even Justice Stevens's approach to the REA was insufficiently deferential, *see supra* notes 122–27 and accompanying text, they might well have concluded that the way to avoid writing Justice Stevens's approach into law, see *Marks*, 430 U.S. at 197, was to avoid taking any position at all on the REA in this case.

143. *See Shady Grove*, 559 U.S. at 421 (Stevens, J. concurring) ("In some instances, the 'plain meaning' of a federal rule will not come into 'direct collision' with the state law, and both can operate. *Walker*, 446 U.S. at 750, n.9. In other instances, the rule 'when fairly construed, *Burlington Northern R. Co.* 480 U.S. at 4, with 'sensitivity to important state interests and regulatory policies, *Gasperini*, 518 U.S. at 427, n.7, will not collide with the state law. (some internal citations omitted)). The significance of this agreement is open to question because

the appropriate analysis under the REA. For that reason, it is incorrect to say that "[t]he five justices in the concurrence and the dissent concluded that the validity of Federal Rules of Civil Procedure turns, in part, on the rights afforded by the state rule that the Federal Rule displaces."[144]

In short, *Marks*—understood properly—provides no assistance to lower courts seeking guidance about what an REA analysis requires. Under these circumstances, the most that can be drawn from *Shady Grove* is that when a Federal Rule is not in conflict with a state-law rule that is bound up with a state substantive right, the Federal Rule must be applied[145]—a result that can be reached by applying either Justice Scalia's or Justice Stevens's analysis of the requirements of the REA.[146] *Shady Grove* provides no binding authority, however, for cases in which a Federal Rule conflicts with a state rule that is bound up with a state substantive right. That said, lower courts faced with an REA analysis should carefully consider whether the plurality opinion—while not itself precedential—constitutes an accurate appraisal of the Court's precedents on the meaning of the REA. The Court's statement in *Sibbach* that § 2072(b) was simply intended to emphasize the restrictions set forth in § 2072(a) is powerful evidence that the plurality opinion states the law.

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the concurrence and the dissent disagree so strongly on the degree of appropriate sensitivity. Moreover, to the extent the *Erie* policy is used as a rule of construction—the plurality's alternative—state law is at least as well protected as under Justice Ginsburg's standard. In any event, the key question is not whether 'sensitivity to important state interests and regulatory policies' is ever appropriate as a rule of construction, but *when*. As I argue in the next section, a rule of construction appropriate in one context may not be appropriate in another.

144. *In re* Digital Music Antitrust Litigation, 812 F. Supp. 2d 390, 415 (S.D.N.Y 2011). For a case arguing that Justice Stevens's opinion controls because he 'rejects the *per se* approach offered by the plurality and the dissenters and, in so doing, finds common ground with both groups, see *Tait v. BSH Home Appliances Corp.* No. SACV 10-711 DOC (ANx), 2011 WL 1832941, at *10 (C.D. Cal. May 12, 2011).

145. Had Justice Stevens so limited his opinion, the concurrence would properly be viewed as stating the holding under the 'narrowest grounds' view with respect to the REA question.

146. For an application of *Shady Grove* in this context, see *Knepper v. Rite Aid Corp.* 675 F.3d 249, 265 (3d Cir. 2013).

C. A Framework for Analysis

The plurality in *Shady Grove* was correct to conclude that state law plays no role in determining the validity of a Federal Rule. But the plurality provides little guidance on how to classify a Federal Rule as substantive or procedural. In this subpart, I seek to fill this critical gap in the plurality's analysis in a way that is both faithful to the purposes of the REA and workable. In subpart 1, I provide a general approach to the classification of a Federal Rule as procedural or substantive. In subpart 2, I apply this general approach to Rule 23—the Federal Rule at issue in *Shady Grove*—and conclude that Rule 23 is a rule of "practice and procedure" within the meaning of the REA.

1. Classifying a Federal Rule under the Rules Enabling Act—General Considerations

Because a Federal Rule that straddles the constitutional line between substance and procedure will (if inconsistent with state law) typically interfere with one or more nonprocedural state purposes, an approach like Professor Ely's that is based on the purpose of state law need not focus on classifying a Federal Rule as procedural or substantive. By contrast, a rigorous application of the plurality's approach—which rejects consideration of the purpose of state law—necessarily requires careful classification of a Federal Rule as one of "practice and procedure" or of substance.

The soundest approach to classification begins by identifying types of rules that regulate the process by which claims and defenses are asserted and adjudicated within a lawsuit. Such rules should be deemed rules of "practice and procedure," within the meaning of § 2072(a).[147] Rules outside this core should be deemed matters of

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147. This definition is consistent with that provided in the Senate Report. *See* S. REP. NO. 69-1174 at 9–12 (1926) (clarifying that the rule does not attempt to affect substantive rights or remedies). Professor Burbank provides an alternative classification scheme for which he also finds support in the legislative history. *See infra* notes 156–59 and accompanying text. Donald Doernberg, for his part, has suggested that another way of distinguishing between substance and procedure would be to ask whether

"practice and procedure" to the extent that they enforce or implement policy choices permitted under the Court's rule-making authority. Classification of this sort does not deny that rules of "practice and procedure" may have important substantive effects. It simply recognizes that the intertwined nature of substance and procedure does not change the need to find a way to allocate decision-making authority between the Court on the one hand and Congress and state legislatures on the other that will not undermine the fundamental purpose of the REA—that is, to give the Court power to prescribe a uniform system of Federal Rules to govern "practice and procedure" in the federal courts.

For the most part, there is consensus about what *kind* of rules are the appropriate subject of rule making. No one would disagree, for example, that pleading and discovery rules are properly classified as procedural, even if particular rules of pleading or discovery—Rule 9(b), requiring heightened pleading for allegations of fraud, and Rule 26(b)(3), addressing the work-product doctrine, for example—may have a substantive purpose or effect.

The classification of other kinds of rules—rules of preclusion, for example—is more controversial. It is worth

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> the state law and Federal Rule at issue tend to establish or negate an element of the claimant's cause of action or a defense on the merits. If the state law does not, then it is procedural, but that is not the end of the inquiry. One must still ask whether the Federal Rule does tend to establish or negate an element. If so, it trenches upon REA-forbidden territory; otherwise it is 'procedural' for REA purposes and can apply. Courts seem to have had far less trouble agreeing on what goes to the merits than on what constitutes substance versus procedure. I shall refer to this as the elements approach.

Donald L. Doernberg, *'The Tempest'* Shady Grove Orthopedic Associates, P.A. v. Allstate Insurance Co. *The Rules Enabling Act Decision That Added to the Confusion—But Should Not Have*, 44 AKRON L. REV. 1147. 1185 (2011). Professor Doernberg ultimately argues for a broader 'behavioral' approach: 'It may be better to ask whether, before the litigation began and assuming the parties were fully aware of the competing rules, they would rationally have ordered their conduct in accord with one of the rules. *Id.* at 1186. *See id.* at 1185–99 (explicating and applying the behavioral and elements approaches). Professor Doernberg makes a useful contribution to the debate, but I worry that he too narrowly defines substance, both as a matter of legislative intent and as a matter of sound policy. *See, e.g. infra* notes 148–49 and accompanying text.

discussing the proper classification of preclusion rules in some detail because the exercise illustrates the various considerations that should govern whether a particular rule should be classified as substantive or procedural for purposes of the REA. And as discussed below, some of these considerations strongly support the argument that the certification requirements of Rule 23 displace the independent operation of any state law that purports to bar certain forms of relief in class litigation.

Preclusion law—at least in the abstract—appears to be outside the purview of rule makers,[148] and it makes sense to treat it as occupying a different category than rules of pleading and discovery. It is sometimes said that rules of preclusion are substantive because they cut off rights.[149] But this insight, important as it is, does not adequately distinguish pleading rules from rules of preclusion. A failure to assert an affirmative defense in an answer or an answer amended as a matter of course, for example, will also cut off a substantive right unless the court grants leave to amend. What distinguishes such a waiver from preclusion is that the waiver has no operation beyond the lawsuit in which it was made. In other words, a pleading waiver represents application of a rule that regulates the process by which claims and defenses are asserted and adjudicated within a lawsuit. By contrast, when an application of preclusion is premised solely on the failure to assert a claim or defense, the effect may be felt outside the lawsuit in which the failure occurred. Moreover, the law of preclusion does far more than cut off substantive rights based on a failure to assert a claim or affirmative

148. *See* Woolley, *supra* note 13, at 580–89. *But see* Doernberg, *supra* note 147, at 1196 (arguing that the REA would authorize a federal rule prescribing that dismissals on statute-of-limitations grounds are to be given claim-preclusive effect "because preclusion is not an element of any claim or any defense on the merits' and "because the rules of claim preclusion address intra-litigation conduct only, being designed to encourage consolidation of all claims from a single incident into a single action").

149. *See* Robert N. Clinton, *Rule 9 of the Federal Habeas Corpus Rules: A Case Study on the Need for Reform of the Rule Enabling Acts*, 63 IOWA L. REV. 15, 59 (1977). Professor Clinton argues "that rules which cut off remedies (like statutes of limitation and preclusion rules) should be viewed as substantive in deference to the legal maxim that there is no right without a remedy. Woolley, *supra* note 13, at 585.

defense. A judgment establishes the rights of the parties to the judgment through application of preclusion law.

The harder question is whether Federal Rules that touch on preclusion may ever be classified as rules of "practice and procedure" within the meaning of the REA. I have argued elsewhere that the Court should be understood to have limited power to prescribe rules of preclusion when such rules are used to enforce Federal Rules valid under the REA: "Authority to regulate litigation behavior cannot easily be separated from authority to establish penalties for litigation misconduct."[150] To illustrate, a policy against lack of diligence in the conduct of an action that is "enforced by a preclusion rule that forbids the refiling of claims has greater force than a policy permitting the refiling of claims."[151] In short, the key question in determining whether the Court has authority to prescribe a rule of preclusion under the REA should be whether the function of the preclusion rule is to enforce a policy choice that the Court has the power to make through the Federal Rules.[152] Professor Redish and Mr. Murashko properly ground this principle in the test the Court enunciated in *Burlington Northern* for the validity of a Federal Rule:[153] "Rules which incidentally affect litigants' substantive rights do not violate this provision if reasonably necessary to maintain the integrity of that system of rules."[154] Strikingly, in both cases in which the Court has applied this precise formulation, it upheld the validity of Federal Rules authorizing sanctions for specified conduct in litigation.[155]

150. Woolley, 72 U. CINCINNATI L. REV. at 585.

151. *Id.*

152. *Id.*

153. *See* Redish & Murashko, *supra* note 39, at 89–91 (arguing that the Court's test in *Burlington Northern* provides a basis for distinguishing the circumstances in which rule makers may prescribe rules of preclusion from those in which they cannot).

154. Burlington N. R.R. Co. v. Woods, 480 U.S. 1, 5 (1987).

155. *Id.* Business Guides, Inc. v. Chromatic Commc'ns Enters. Inc. 498 U.S. 533, 552 (1991). *Cf.* Michael Risinger, *'Substance' and 'Procedure' Revisited with Some Afterthoughts on the Constitutional Problems of 'Irrebuttable Presumptions'* 30 U.C.L.A. L. REV. 189, 207–09 (1982) (discussing the proper characterization of sanctions for litigation misconduct and concluding that they can be characterized as procedural, at least when a separate lawsuit is not required to obtain an order of sanctions).

Denying rule makers authority to prescribe appropriate sanctions for violation of a Federal Rule that they have validly prescribed would artificially separate two complementary aspects of rulemaking: prescribing the obligation and prescribing the sanction for violation of the obligation. For that reason, it makes sense to conclude that Congress granted the Court authority to prescribe sanctions to enforce otherwise valid Federal Rules. In short, even a rule of preclusion may be classified as a rule of "practice and procedure" in limited circumstances.

Professor Burbank takes a different position, insisting that because preclusion rules may cut off substantive rights, they are outside the authority granted to the Court to prescribe Federal Rules pursuant to the REA.[156] While recognizing that enforcement mechanisms are crucial to the Federal Rules, Professor Burbank nonetheless asserts that preclusion rules must either be enacted by Congress or developed through the common law process because the REA was not intended to give the Court authority to prescribe rules of preclusion of any sort.[157]

The legislative history does not specifically address "whether the Court should have authority to promulgate preclusion rules for the limited purpose[] of enforcing procedural obligations validly

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156. Burbank, *Interjurisdictional Preclusion*, *supra* note 79, at 772 ("Read in the light of its history, the Enabling Act does not authorize Federal Rules that predictably and directly affect rights claimed under the substantive law.'); Burbank, *supra* note 42, at 1128 ("Clearly preclusive doctrines like a statute of limitations, laches, or res judicata dramatically affect the ability of litigants to enforce their substantive rights and, therefore, determine in a practical sense whether those rights exist at all, at least when viewed from the point in time at which they are asserted.').

157. Burbank, *Interjurisdictional Preclusion*, *supra* note 79, at 773 ("In authorizing the Court to promulgate Federal Rules, Congress must have contemplated that the federal courts would interpret them, fill their interstices, and, when necessary, ensure that their provisions were not frustrated by other legal rules.'). As I have noted elsewhere, '[i]f the Court has authority to promulgate Federal Rules governing limited aspects of preclusion law, there can be no question that courts have common-law authority to protect the integrity of the Federal Rules through uniform common-law rules of preclusion. Woolley, *supra* note 13, at 592. But if the Court is denied the power to prescribe such rules, it is far from clear that the Court will be able to turn to uniform federal common-law rules to enforce procedural obligations validly imposed under the REA. *Id.* at 592–94.

imposed under the REA."[158] Professor Burbank ultimately rests his argument on a broader claim: "Read in the light of its history, the Enabling Act does not authorize Federal Rules that predictably and directly affect rights claimed under the substantive law."[159] Preclusion rules written to enforce procedural obligations validly imposed under the REA run afoul of this standard. But the standard Professor Burbank suggests is overbroad and unworkable. As I have argued elsewhere: "Any procedural system will have identifiable and predictable effects on substantive rights, even with respect to matters that everyone would agree are matters of practice and procedure."[160]

I have so far focused exclusively on the use of preclusion as a sanction for the violation of a procedural obligation validly imposed by the REA. But the principle that a Federal Rule which might

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158. Woolley, *supra* note 13, at 583–84. *See also* Redish & Murashko, *supra* note 39, at 72–74 (arguing that Professor Burbank 'fails to recognize that the predictable-and-identifiable test was at most peripheral to the report on which he relies and does not flow from it with any reasonable degree of certainty"). Professor Redish and Mr. Murashko more broadly criticize Professor Burbank's reliance on a 1926 Senate Report in understanding the intent of the legislators who enacted the Rules Enabling Act of 1934. Redish & Murashko, *supra* note 39, at 67–72. While many of their arguments have force, my reading of the Report and law review articles published at about the time the REA was enacted leaves me with no doubt that the Senate Report accurately describes basic and widely shared understandings about the nature of court rulemaking at the time the REA was enacted, and it is for these basic and widely-shared understandings that the Report should be read and cited. I do not believe Professor Burbank's 'identifiable and predictable effect on substantive rights' test represents a basic and widely shared understanding of the limits on rule making at the time the REA was enacted.

Professor Burbank's reliance on a 1985 House Report that preceded the 1988 reenactment of the REA to support his 'identifiable and predictable' test is also unpersuasive. *See* Woolley, *supra* note 13, at 588–89 (noting that there is support in a 1985 Report of the House Judiciary Committee for the distinction drawn by Professor Burbank but concluding 'there is no evidence that the Senate that enacted the Rules Enabling Act of 1988 wished to adopt the conclusions of the 1985 House Judiciary Committee"); *see also* Redish and Murashko, *supra* note 39, at 74–76 (criticizing Professor Burbank's reliance on the legislative history of the 1988 reenactment).

159. Burbank, *Interjurisdictional Preclusion*, *supra* note 79, at 772. *See also* Burbank, *supra* note 42, at 1114 ("The pre-1934 history suggests an intent to exclude rulemaking by the Supreme Court, and to require that any prospective federal lawmaking be done by Congress, where the choice among legal prescriptions would have a predictable and identifiable effect on such rights.'").

160. Woolley, *supra* note 13, at 589–90.

otherwise be categorized as substantive may be deemed a rule of "practice and procedure" when it is "reasonably necessary to maintain the integrity" of valid Federal Rules should not be limited to Federal Rules imposing sanctions. Consider, for example, a Federal Rule governing the preclusive effect of a judgment rendered on the basis of a Rule 12(b)(6) motion to dismiss for failure to state a claim. Whether judgments based on such motions are entitled to the same preclusive effect as judgments based on motions for summary judgment or judgments after trial "bears significantly on the effective management of litigation under the Federal Rules."[161] Because a Federal Rule designed to affect a litigant's choice of motion implements a policy choice at the core of procedural rulemaking, the Court as rule maker should have the authority to require that motions be deemed interchangeable for the purpose of preclusion law.[162] That state preclusion law may discriminate against judgments based on one kind of motion or another should be irrelevant.

The principle that federal rule makers may prescribe rules to prevent application of state law from skewing federal practice by favoring one federal procedural device over another has significance beyond the law of preclusion. Of particular relevance here, federal rule makers should be deemed to have the power to prohibit application in federal court of state law that would make it easier or harder to bring a class suit than an individual suit. The conclusion that federal rule makers should have such authority rests on the premise that a Federal Rule authorizing the aggregation of claims through the class device is itself a rule of "practice and procedure," a proposition defended in the next subpart.[163]

The power of federal rule makers to displace state law that discriminates in favor of the class device or against it is least controversial when the discriminatory state law purports to regulate a matter that is obviously procedural. Few would question, for

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161. *Id.* at 585.

162. There is good reason to believe that the rule makers exercised this. authority in prescribing Rule 41(b). But the Supreme Court appears to have rendered irrelevant this exercise of authority while trying to avoid a construction of Rule 41(b) in a different context that would have raised serious questions of validity under the REA. *See* Woolley, *supra* note 13, at 594–601 (explaining that the Court read Rule 41(b) more narrowly than was required to avoid running afoul of the Rules Enabling Act).

163. *See infra* Part II.C.2.

example, that federal law may displace a state class action rule that bars certification of class suits predominately for money damages. But discriminatory state law does not always take an obviously procedural form. Consider, for instance, the enactment of a state statute that bars the award of money damages in class litigation. Because remedies are substantive for purposes of the REA, it could be argued that a Federal Rule that purports to displace a state law bar on class action remedies is outside the scope of the federal rule making power.

The form of a state statute, however, should not affect the power of federal rule makers to displace a statute that discriminates against the class device. It is the *individual* cause of action that is protected as property under the Due Process Clause[164] and that properly serves as a baseline for determining whether a Federal Rule "abridges, enlarges, or modifies" a substantive right.[165] In other words, a Federal Rule that regulates whether claims that could be asserted individually may be aggregated when doing so would be fair and efficient is properly deemed a matter of "practice and procedure." Thus, a Federal Rule that displaces state law that discriminates in favor of the class device or against it should be deemed valid. Conversely, the Federal Rules cannot encroach on substantive rights articulated in connection with an individual cause of action, even if the purpose of the encroachment is to make it easier or harder to bring a class action in federal court.

In short, the REA should be construed to authorize displacement of state law that regulates the class device. But this power need not be exercised. Indeed, it sometimes may be

164. *See* Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 807–08 (1985) (stating that a cause of action "is a constitutionally recognized property interest possessed by each of the plaintiffs."); Logan v. Zimmerman Brush Co. 455 U.S. 422, 428 (1982) (emphasizing that Mullane v. Cent. Hanover Bank & Trust Co. 339 U.S. 306, (1950), "held that a cause of action is a species of property protected by the Fourteenth Amendment's Due Process Clause.").

165. The *Shady Grove* plurality takes a similar tack. *See* Shady Grove Orthopedic Assocs. v. Allstate Ins. Co. 559 U.S. 393, 408 (2010) (stating that joinder rules "neither change plaintiffs' separate entitlements to relief nor abridge defendants' rights; they alter only how the claims are processed. A class action, no less than traditional joinder (of which it is a species), merely enables a federal court to adjudicate claims of multiple parties at once, instead of in separate suits. And like traditional joinder, it leaves the parties' legal rights and duties intact and the rules of decision unchanged.").

appropriate to permit state law to discriminate in favor of the class device or against it. Federal rule-makers can permit such discrimination by failing to regulate the matter. When a Federal Rule does not cover the point in question, *Erie* requires application of outcome-determinative state law unless the need for a uniform federal common-law rule outweighs the *Erie* policy.[166]

2. Rule 23 and the REA

The plurality in *Shady Grove* identified rules of joinder as rules of "practice and procedure,"[167] and there is support in the scholarly literature for the view that such rules are at the core of procedure.[168] I accept that rules of joinder are rules of "practice and procedure" within the meaning of the REA, at least insofar as such rules purport to impose obligations only on those who have been properly served with process or have otherwise joined the litigation as parties. In this subpart, I focus on whether Rule 23 is properly considered a "joinder rule" for purposes of the REA, as the plurality in *Shady Grove* claimed. I conclude that the plurality's characterization of Rule 23 as a joinder rule represents a correct understanding of the limited function of Rule 23 in class litigation. I recognize that Rule 23 does not actually require the joinder of absent parties, but the aggregative effect of Rule 23 is close enough to traditional joinder to justify characterizing the Rule as a joinder rule for the purpose of assessing its validity.

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166. For discussion of whether a federal interest may override the *Erie* policy and justify a uniform federal common law rule of procedure, and if so when, see Woolley, *supra* note 13, at 559–72 (relying in part on *Byrd v. Blue Ridge Electric Cooperative* for the proposition that the *Erie* policy is not absolute). There is evidence from the oral argument in *Shady Grove* that Justice Ginsburg at least views *Byrd* as quite limited. In questioning an effort to give *Byrd* a broader reading, she remarked: 'I thought *Byrd* turned on the characteristics of a Federal court and that is the judge/jury relationship. Transcript of Oral Argument at 17, *Shady Grove*, 559 U.S. 393 (2010) (No. 08–1008).

167. *Shady Grove*, 559 U.S. at 408.

168. *See, e.g.* Larry B. Solum, *Procedural Justice*, 78 S. CAL. L. REV. 181, 195 (2004) ("A theory of substance and procedure must either count pleading and joinder as procedural and classify the duty of care in negligence as substantive, or offer a compelling explanation as to why our considered conviction about these paradigm cases is in error.").

The plurality contends that the class device—like other "rules allowing multiple claims (and claims by or against multiple parties) to be litigated together"—is "valid" because it "merely enables a federal court to adjudicate claims of multiple parties at once, instead of in separate suits. And like traditional joinder, it leaves the parties' legal rights and duties intact and the rules of decision unchanged."[169] In *Shady Grove*, for example, Rule 23 enabled the aggregation of penalty claims that the class members held as a matter of right under New York law.[170] While the aggregative power of class device might have had a practical effect on the amount that the class defendant would pay in damages, the legal rights of the parties to the class suit were not affected.[171] In other words, certification of a federal class action did not entitle class members to anything to which they would not have been entitled in individual litigation.

Rejecting this analysis, Professors Burbank and Wolff emphasize that the prospect of class certification is the single most important factor in the dynamics of litigation or settlement in any proceeding in which class treatment is on the table: "Certification can transform unenforceable negative-value claims into an industry-changing event and dramatically alter the litigation or settlement

169. *Shady Grove*, 559 U.S. at 408. The plurality carefully qualifies this conclusion: 'Rule 23—at least insofar as it allows willing plaintiffs to join their separate claims against the same defendants in a class action—falls within § 2072(b)'s authorization. *Id.*

170. *Id.*

171. To the extent that a class representative in a class suit seeking money damages is imposed on a class member without her consent, the class device arguably does modify the cause of action for damages, at least if the absent class member does not wish to sue or if a settlement may be imposed on the absentee without her consent. Because the right to sue and control the vindication of one's legal rights is so closely linked to a person's property interest in his or her cause of action, *see* Patrick Woolley, *Rethinking the Adequacy of Adequate Representation*, 75 TEX. L. REV. 571 (1997), nonconsensual representation through an adequate representative could also be understood—at least in some circumstances—to 'modify, abridge, or enlarge' a property right. Indeed, Sergio Campos has gone so far as to suggest that "title"—albeit legal as opposed to beneficial title—is transferred in a class suit from the class members to the class attorney. Sergio J. Campos, *Proof of Classwide Injury*, 37 BROOK. J. INT'L L. 751, 775 (2012). But the key question for purposes of the REA is whether the Federal Rules are responsible for this modification. As I explain *infra*, any modification of this sort flows not from Rule 23 but from the role of adequate representation in the law of preclusion. *See infra* notes 176-182 and accompanying text.

value of high-stakes individual claims."[172] From this perspective, the plurality's conclusion in *Shady Grove* that Rule 23 is akin to a joinder device embodies a remarkably naïve understanding of the class device. Indeed, Professors Burbank and Wolff insist that the plurality's equation of Rule 23 with joinder "exhibits a lack of sophistication that is difficult to fathom."[173]

But while Professors Burbank and Wolff do a masterful job of exploring the transformative effect of class certification on the liability of a defendant, their critique of the plurality opinion is ultimately unpersuasive. The transformative effect of class certification that Professors Burbank and Wolff note is the result not of Rule 23 itself but of a network of common law and statutory rules addressing the availability of attorneys' fees for class counsel and the preclusive effect of class judgments on absent class members. Although Rule 23 sets out a procedure for requesting attorneys' fees, for example, it does not purport to determine whether class counsel is entitled to attorneys' fees.[174] That question is governed by common law and statute.[175] There similarly seems to be little basis

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172. Burbank & Wolff, *supra* note 19. Professor Redish similarly highlights the effect of class litigation on substantive rights:

> Because the very threat of class action liability is often overwhelming, defendants who are averse to 'betting the company' will generally seek to settle the moment a class action is certified. More fundamentally, by so dramatically altering the manner in which individually held substantive claims are adjudicated, the modern class action inevitably impacts—if only indirectly—foundational substantive values concerning wealth distribution and the policing of corporate behavior.

REDISH, *supra* note 51, at 62-63.

173. Burbank & Wolff, *supra* note 19, at 63 ("Read against th[e] history [of the class action], the Court's treatment of the interplay between the Enabling Act and the proper interpretation of Rule 23 in *Shady Grove* exhibits a lack of sophistication that is difficult to fathom.").

174. *See* FED. R. CIV. P. 23(h) ("In a certified class action, the court may award reasonable attorney's fees and nontaxable costs that are authorized by law or by the parties' agreement. The following procedures apply . . . .").

175. Whether federal courts may elaborate uniform federal common-law rules governing attorneys' fees in class suits addressing state-law claims is beyond the scope of this paper. The answer depends on whether the *Erie* policy is outweighed by a federal interest in uniform federal common law rules on the

for concluding that Rule 23—as opposed to the common law of res judicata—grants class representatives the power to bind absent members of the class. Indeed, the notion that a representative in appropriate circumstances may bind an absentee in class litigation long predates Rule 23 and the REA.[176]

Rule 23 authorizes a class representative in specified circumstances to maintain a class suit on behalf of members of the class and sets out procedures for the protection of class members and the administration of the suit. Like the joinder rules, Rule 23 provides guidance to parties about what claims must be asserted and to absentees about how they may participate. Rule 23 "contemplates"[177] that a properly constituted class will bind absentees. But the Federal Rule does not authorize a court to exercise personal jurisdiction over absent class members, nor does it prescribe the binding effect of a judgment on absentees over whom the Court has personal jurisdiction.

The 1966 Amendments to Rule 23 do provide that class members in a class suit certified under Rule 23(b)(3) who fail to opt out will be included in the class.[178] The Advisory Committee Notes are careful to state, however, that the class court cannot determine the res judicata effect of its class certification decision.[179] Indeed, the

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subject. *See supra* note 166 (citing authority for the proposition that the *Erie* policy may be outweighed by other federal policies).

176. The circumstances in which an absentee may be bound by a class judgment nonetheless have changed over time. *See* Geoffrey C. Hazard, Jr. John L. Gedid & Stephen Sowle, *An Historical Analysis of the Binding Effect of Class Suits*, 146 U. PA. L. REV. 1849 (1998) (discussing the history of *res judicata* in class suits); Robert G. Bone, *Personal and Impersonal Litigative Forms: Reconceiving the History of Adjudicative Representation*, 70 B.U. L. REV. 213 (1990) (book review) (discussing the history of group litigation).

177. Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356, 389 n.128 (1967).

178. *See* FED. R. CIV. P. 23(c)(3) (1966) ("The judgment in an action maintained as a class action under subdivision (b)(3), whether or not favorable to the class shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed, and who have not requested exclusion, and whom the court finds to be members of the class. ').

179. *See* FED. R. CIV. P. 23(c)(3) advisory committee's notes to 1966 amendment ("Although thus declaring that the judgment in a class action includes the class, as defined, subdivision (c)(3) does not disturb the recognized principle

Reporter for the 1966 Revision expressly clarified that the Federal Rule does not purport to determine the binding effect of a class judgment.[180] It would be surprising if the Advisory Committee had sought to do otherwise. It is well accepted that the preclusive effect of a judgment—at least generally—is outside the rule-making authority granted by the REA. For reasons I explain in detail above, federal rule makers should be deemed to have power to prescribe rules of preclusion to implement or enforce joinder rules with respect to persons who have been joined to a suit as parties.[181] But absent class members, by definition, have not been joined. In short, the law of preclusion—rather than Rule 23—determines whether, and in what circumstances, the right of absentees to sue may be extinguished by class representation.[182]

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that the court conducting the action cannot predetermine the *res judicata* effect of the judgment.").

180. Professor Kaplan explained that proposed

> Subdivision (c)(2) makes clear that the judgment in any class action maintained as such extends to the class (excluding opters-out in (b)(3) cases), whether or not favorable to the class. This is a statement of how the judgment shall read, not an attempted prescription of its subsequent res judicata effect, although looking ahead with hope to that effect.

Kaplan, *supra* note 177, at 393. *See also id.* at 392 (stating that notice "joins with other features of the new rule in helping to justify the ultimate extension of the judgment in (b)(3) cases to all members of the class, except those who requested exclusion from the action" and noting that *Hansberry v. Lee*, 311 U.S. 32 (1940), suggests "that the validity of class adjudication is related to the fairness of the procedural forms through which the adjudication is attained."). The Advisory Committee that drafted the 1938 version of Rule 23 similarly deleted draft language that purported to state the preclusive effect of a class judgment. Woolley, *supra* note 13, at 586.

181. *See supra* notes 148–60 and accompanying text.

182. Uniform federal common-law rules of preclusion are likely to govern because whether a federal class judgment binds absent class members depends on the validity of the judgment vis-à-vis the absentees. *See* Woolley, *supra* note 13, at 565 ("When a judgment becomes final, when a judgment is valid, and when, if at all, a final and valid judgment may be disregarded for equitable reasons, are matters that warrant uniform federal rules . . . ."); Stephen B. Burbank, *Forum Shopping and Federal Common Law*, 77 NOTRE DAME L. REV. 1027, 1040 n.60 (2002) (arguing "that uniform federal rules are necessary to determine the preconditions, such as validity and finality, that determine whether there is a [federal] judgment entitled to consideration for preclusive effect").

It is true, however, that the 1966 Advisory Committee revised Rule 23 in light of then-existing constitutional, statutory, and common law principles for the purpose of making the federal class device a more powerful vehicle for the vindication of substantive rights than had been the case before. And the Rule itself has helped shape rules of law that are well beyond the jurisdiction of federal rule makers. In addition to its effect on the development of preclusion law governing the rights of absentees to litigation,[183] the procedural opportunities made available through Rule 23 have shaped federal causes of action.[184] The inevitable synergy between substance and procedure has led the Court to recognize wisely and without apology that its "rulemaking under the Enabling Acts has been substantive and political in the sense that the rules of procedure have important effects on the substantive rights of litigants."[185]

If the REA is not to become a relic, the Act cannot be construed to prohibit Federal Rules that have a practical effect on substantive rights. But that does not mean that the practical effect of Federal Rules on substantive rights should be of no concern. Rule makers should be extraordinarily attentive to the practical effect of Federal Rules on substantive rights and should carefully consider whether Federal Rules should be drafted or amended to mitigate that practical effect.[186] In fact, as discussed in detail below, the drafters of the 1966 Amendment to Rule 23 included language in the Rule that

183. *See, e.g.* Smith v. Bayer Corp. 131 S. Ct. 2368, 2380 (2011) (determining that "[n]either a proposed class action nor a rejected class action may bind nonparties").

184. For a classic article exploring this reality, see Hal S. Scott, *The Impact of Class Actions on Rule 10b-5*, 38 U. CHI. L. REV. 337 (1971).

185. Mistretta v. United States, 488 U.S. 361, 392 (1989); *see also* Woolley, *supra* note 13, at 590 ("[I]t is precisely because procedural rules have an identifiable and predictable effect on substantive rights that interest groups fight about which procedural regimes are appropriate."). *Cf.* Burbank, *supra* note 42, at 1114 ("The pre-1934 history [of the REA] suggests an intent to exclude rulemaking by the Supreme Court, and to require that any prospective federal lawmaking be done by Congress, where the choice among legal prescriptions would have a predictable and identifiable effect on such rights.").

186. *See* Richard A. Nagareda, *The Litigation-Arbitration Dichotomy Meets the Class Action*, 86 NOTRE DAME L. REV. 1069, 1088–89 (2011) ("The inclination of the plurality to foreclose fine-grained consideration of state law effectively places the guardianship of state autonomy not in the courts but, instead, in the rulemaking process prescribed by the Rules Enabling Act.").

requires courts to take into account the practical effect that a class suit might have on substantive rights. Specifically, Rule 23(b)(3) requires that a court find that the class device is the superior means of proceeding before certifying a Rule 23(b)(3) class suit. We should trust the rules committees—as supervised by the Court and Congress—to strike the proper balance between the Federal Rules and their practical effect on state law. Invalidation under the REA should be reserved for circumstances in which a Federal Rule promulgated by the Court has been misclassified as procedural.

III. THE CONSTRUCTION OF FEDERAL RULES AND STATE LAW

A valid Federal Rule displaces state law to the extent both "cover[] the point,"[187] or as *Hanna* put it, to the extent there is a "direct collision"[188] between state and federal law. That determination requires construction of the Federal Rule and state law. This part addresses the principles that should govern the construction of Federal Rules and state law in a direct collision analysis and applies those principles to the issue presented in *Shady Grove*.

The Court's conclusion in *Shady Grove* that New York law did no more than regulate class certification made application of the plurality's approach child's play. Because both Rule 23 and § 901(b) address the certification of a class suit, Rule 23 displaces New York law. Subpart A argues, however, that the Court's interpretation of New York law was indefensibly wooden. The New York statute relied on an obviously procedural mechanism to implement a separate policy that penalties not be recoverable in a class suit. When a procedural mechanism chosen by the state legislature would be inoperative in federal court, a federal court ordinarily should read state law purposively to avoid the unnecessary frustration of any state substantive purposes. Applying that approach, § 901(b)—or state common law premised on § 901(b)—should be read to bar not only certification of a class suit for penalties, but also an award of penalties in class litigation.

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187. Walker v. Armco Steel Corp. 446 U.S. 740, 750 (1980).
188. *Hanna*, 380 U.S. at 472.

Subpart B nonetheless contends that Rule 23 should be construed to displace New York law. Giving effect to a New York ban on penalty awards in class litigation independently of the Federal Rules would circumvent the certification criteria of Rule 23. It would do so by making pointless the certification of class suits seeking penalties under state law. Because both Rule 23 and New York law regulate the appropriateness of class treatment in this context, Rule 23 must govern.

This construction of Rule 23 would be problematic if Federal Rules must be read narrowly in order to vindicate the *Erie* policy. But reliance on the *Erie* policy as a rule of construction must be harmonized with other rules of construction, including the rule that if a Federal Rule, "fairly construed,"[189] can be read to cover a point, the Federal Rule should be so read in order to promote uniformity and consistency.[190] Placed in the proper context, the *Erie* policy provides no warrant to circumvent the certification criteria of Rule 23, but simply a basis for considering New York law as a factor—among other factors—in deciding whether the class device would be superior to other means of resolving a dispute for which certification under Rule 23(b)(3) is sought.

A. The Construction of State Statutes

Because the text of § 901(b) prohibits the certification of a class suit seeking damages, and because Allstate simply sought enforcement of this textual bar, there was no need to ascertain whether § 901(b)—or state common law premised on the purposes of § 901(b)[191]—might impose additional proscriptions.[192] The Court

189. *Burlington Northern*, 480 U.S. at 4.

190. *Id.* at 5.

191. *Cf.* FALLON, *supra* note 2, at 607 (defining federal common law as "federal rules of decision whose content cannot be traced directly by traditional methods of interpretation to federal statutory or constitutional commands"); *id.* ("As specific evidence of legislative purpose with respect to the issue at hand attenuates, all interpretation shades into judicial lawmaking."). State common law, of course, need not be tied—even loosely—to a specific state statute or constitutional provision. But for purposes of this paper, I assume that any bar in New York law on the award of penalties in class litigation would be tied in some way to Section 901(b).

192. The dissent is sometimes misunderstood as construing Section 901(b) to bar a particular *remedy* in a class suit rather than (or in addition to) barring class

nonetheless concluded that "§ 901(b) says nothing about what remedies a court may award; it prevents the class actions it covers from coming into existence at all."[193] The Court's conclusion is based on a wholly textual approach to § 901(b).[194] But read purposively, "section 901(b) reflects a policy judgment by the New York legislature that statutory damages are not appropriate remedies in class actions."[195]

Even if federal courts should ordinarily construe state statutes textually, the Court's reliance on the plain meaning of § 901(b) is problematic. A strict focus on the text—rather than the purpose—of

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certification itself. But the analysis is more subtle. While the dissent focuses on what it views as the pertinent purpose of Section 901(b), it accepts—at least for the purposes of the decision—that this purpose is to be effected through a bar on class certification. *See* Shady Grove Orthopedic Assocs. v. Allstate Ins. Co. 559 U.S. 393, 437 (2010) (Ginsburg, J. dissenting) ("The New York Legislature has barred this remedy, instructing that, unless specifically permitted, 'an action to recover a penalty, or minimum measure of recovery created or imposed by statute may not be maintained as a class action. N.Y Civ. Prac. Law Ann. (CPLR) § 901(b) (West 2006). The dissent relies on the purpose of Section 901(b)—which it understands as designed to bar the award of penalties in class litigation—simply to analyze the respective pertinence of Section 901(b) and Rule 23 to the dispute before the Court. Specifically, the dissent argues that the bar on certification in Section 901(b) was designed to bar a particular remedy and that remedies are not within the ambit of Rule 23. See id. at 447 (Ginsburg, J. dissenting) ("Rule 23 authorizes class treatment for suits satisfying its prerequisites because the class mechanism generally affords a fair and efficient way to aggregate claims for adjudication. Section 901(b) responds to an entirely different concern. '). Thus, Justice Ginsburg had no difficulty concluding that there was no direct collision between Section 901(b) and Rule 23, and that Section 901(b) barred certification of the class. But while the majority disagreed with the dissent's direct-collision analysis, there does not appear to be any disagreement among the Justices that Section 901(b), if properly applied in *Shady Grove*, would expressly bar certification of a suit seeking penalties through the class device.

193. *Id.* at 401.

194. Justice Scalia writes: 'The manner in which the law 'could have been written, *post* at 1472, has no bearing; what matters is the law the Legislature *did* enact. We cannot rewrite that to reflect our perception of legislative purpose[.]' *Id.* at 403 (citing Oncale v. Sundowner Offshore Servs. Inc. 523 U.S. 75, 79–80. (1998)).

195. Adam N. Steinman, *Our Class Action Federalism:* Erie *and the Rules Enabling Act after* Shady Grove, 86 NOTRE DAME L. REV. 1131, 1156–57 (2011). For a fascinating discussion of the legislative history of Section 901(b), see Jeffrey W. Stempel, Shady Grove *and the Potential Democracy-Enhancing Benefits of* Erie *Formalism*, 44 AKRON L. REV. 907 (2011).

a state statute can lead to remarkably arbitrary distinctions in cases of this sort.[196] It makes no sense, for example, to treat a statute providing that "a suit to recover more than $1,000,000 may not be maintained as a class action"[197] as having a different meaning from a statute which states that "no more than $1,000,000 may be recovered in a class action"[198] when, as Justice Ginsburg notes, "[t]here is no real difference in the purpose and intended effect of these two hypothetical statutes."[199] One would expect these hypothetical statutes to lead to precisely the same result in the courts of an enacting state, notwithstanding the differences in wording. Thus, even the possibility that differences in wording would lead a federal court to give these statutes radically different effects is troubling.

As Thomas Main has perceptively noted, legislatures tend to legislate against the background of their own procedural law.[200] And because § 901(b) bars the New York courts from certifying class suits seeking penalties, it likely never occurred to the legislature to address how its policy judgment on appropriate remedies in class litigation should be implemented in jurisdictions that would treat the express directive of the section as governing only procedure in the courts of New York. Nor would it be respectful of federalism to fault the New York legislature for focusing on the courts of its state when drafting legislation.[201]

As Craig Green aptly put it:

> [I]t seems a deep irreality to imagine that states would draft their laws with an eye to how those laws might be applied by federal courts in diversity cases as they relate to Federal Rules. The vast majority of cases governed by section 901(b) are state-court cases, and the statute was drafted accordingly.[202]

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196. *See infra* notes 197-200 and accompanying text.

197. *Shady Grove*, 559 U.S. at 448.

198. *Id.*

199. *Id.*

200. Thomas O. Main, *The Procedural Foundation of Substantive Law*, 87 WASH. U. L. REV. 801 (2010).

201. *See supra* notes 202–05 and accompanying text.

202. Craig Green, *Black-and-White Judging in a World of Grays*, 46 TULSA L. REV. 391, 402 (2011); *see also id.* ("To split Scalia's chosen textualist hair, in

Under these circumstances, a federal court respectful of federalism should construe purposively a state statute that seeks to vindicate a policy objective through a procedural mechanism inapplicable in federal court,[203] at least if the highest court of the state in which the federal court sits would not insist on a purely textual construction of the statute.[204] New York's highest court uses a "generally purposive approach"[205] to statutory construction, strongly suggesting the court would read § 901(b)—or state common law premised on § 901(b)—as barring an award of penalties in class litigation.[206] And even a state court ordinarily committed to textualism would—if presented with a certified question by a federal court—likely construe a statute of its own state purposively when the procedural mechanism chosen by the legislature would be inoperative in federal court.[207] For a state court to do otherwise

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this particular context, seems distant from any system for enforcing any codified 'legislative intent, much less any 'democratic will. '). Mechanically focusing on the silence of Section 901(b) is even more problematic because the Class Action Fairness Act was not enacted until 2005, 30 years after enactment of Section 901(b). *Id.*

203. *See supra* notes 193-200 and accompanying text.

204. Abbe Gluck has argued that '*Erie* requires federal courts, in most cases, to apply state interpretive methodology to state statutory questions. Abbe Gluck, *Intersystemic Statutory Interpretation: Methodology as 'Law' and the* Erie *Doctrine,* 120 YALE L.J. 1898, 1997 (2011). *Cf.* Eric Lane, *How to Read a Statute in New York: A Response to Judge Kaye and Some More*, 28 HOFSTRA L. REV. 85, 87 (1999) ("[A]pproaches to statutory interpretation are not divisible into 'state' and 'federal.' Differences in interpretive approaches are the product of individual judicial sensibilities and not, for the most part, particular jurisdictions. '). Although I am sympathetic to Professor Gluck's approach, I do not seek to defend it here.

205. Gluck, *supra* note 204, at 1933.

206. *See* Steinman, *supra* note 195, at 1156–57 ("It would be no stretch at all to 'guess' that New York's highest court, if confronted with the question, would indeed hold that statutory-penalty remedies are unavailable in a class action under New York law. ').

207. The specific problem of statutory interpretation addressed in this paper is unlikely to arise in a suit filed in state court, but 'nearly all states have adopted procedures that permit federal courts, while retaining jurisdiction of a case, to certify uncertain state law issues to the state's supreme court for authoritative resolution. FALLON, *supra* note 2, at 1072. *See, e.g.* N.Y COMP. CODES R. & REGS. tit. 22, § 500.27(a) (2008) ("Whenever it appears to the Supreme Court of the United States, any United States Court of Appeals, or a court of last resort of any other state that determinative questions of New York law are involved in a

would frustrate the vindication of any state substantive purposes embedded in the state rule.

Although the Court took a different approach in *Shady Grove*, its decision does not prevent federal courts from using a purposive approach to state law going forward. As Abbe Gluck has noted, "[t]he U.S. Supreme Court generally [has] not treat[ed] its statements about statutory interpretation methodology as law."[208] That said, the choice between a purposive and textual reading of statutes like § 901(b) is likely to make a difference only if Federal Rules are read narrowly so as to avoid conflict with state law. I turn in the next subpart to the principles that govern the construction of Federal Rules.

B. The Construction of Federal Rules

The Court concluded that "§ 901(b) says nothing about what remedies a court may award; it prevents the class actions it covers from coming into existence at all."[209] Thus, the Court reasoned, it "need not decide" whether a state statute with that effect "would conflict with Rule 23."[210] The Court did not elaborate on why a state

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case pending before that court for which no controlling precedent of the Court of Appeals exists, the court may certify the dispositive questions of law to the Court of Appeals.").

208. Gluck, *supra* note 204, at 1902 ("Five votes in agreement with respect to the interpretive principles used to decide one case do not create a methodological precedent that carries over to the next case, even where the same statute is being construed."); *id.* at 1910 (noting that '[e]ven when a majority of Justices agrees on an interpretive principle in a particular case (e.g. 'committee statements are not reliable legislative history'), that principle is not viewed as 'law' for the next case' and that '[t]he Justices either believe that they cannot bind other Justices' (or future Justices') methodological choices or have implicitly concluded that it would not be wise to do so.'). *But see id.* at 1911 (stating that the Court has implicitly reached agreement on some interpretive canons and 'a few exceptional areas of law for which the Court has effectively settled on a single interpretive approach').

209. *Shady Grove*, 559 U.S. at 401.

210. *Id.* ("We need not decide whether a state law that limits the remedies available in an existing class action would conflict with Rule 23; that is not what § 901(b) does."). The Court continued in a footnote:

> Contrary to the dissent's implication we express no view as to whether state laws that set a ceiling on damages recoverable in a single suit are pre-empted As Allstate and the dissent note,

law limiting remedies in class litigation might be displaced by Rule 23 in a class suit brought in federal court. Kevin Clermont nonetheless takes *Shady Grove* to mean that "any state law that directly impedes or facilitates joinder must fall to Rule 23" because "what claims or parties may or must proceed together in a federal action, or must proceed separately, is for the Rules to decide."[211] By contrast, Adam Steinman argues that Rule 23 may be deemed to conflict with state law only when the text of the Federal Rule explicitly mandates a result contrary to state law.[212] When Rule 23 is silent, he contends, the *Erie* policy requires application of state class action law.[213] These distinct approaches would lead to radically different results. Professor Clermont's approach would leave no doubt that § 901(b) could not properly be applied in federal court. Professor Steinman's approach, on the other hand, would require the federal courts to apply § 901(b) and any common law derived therefrom. I reject both Professor Steinman's and Professor Clermont's approaches, although I ultimately come down much closer to Professor Clermont than Professor Steinman.

> several federal statutes also limit the recovery available in class actions But Congress has plenary power to override the Federal Rules, so its enactments, unlike those of the States, prevail even in case of a conflict.

Id. at 401 n.4.

211. Clermont, *supra* note 35, at 1030.

212. Professor Steinman explains:

> Put simply, there is a difference between state law conflicting with a Federal Rule of Civil Procedure (which triggers the REA's 'substantive rights' standard) and state law conflicting with the federal judiciary's gloss on a Federal Rule whose text provides only a vague or ambiguous standard (which triggers the more state-friendly 'twin-aims' standard). If the vague standard set forth in the Federal Rule can be applied in a way that is consistent with state law, then the Federal Rule does not truly collide with state law.

Steinman, *supra* note 195, at 1145–46.

213. *Id.*

1. The Proper Role of the *Erie* Policy as a Rule of Construction

In arguing that Rule 23 should be construed narrowly to avoid interference with the *Erie* policy, Professor Steinman relies on a line of Supreme Court authority that culminates in *Shady Grove.* As Justice Scalia articulated the relevant principle, "we should read an ambiguous Federal Rule to avoid 'substantial variations [in outcomes] between state and federal litigation' because it is reasonable to assume that 'Congress is just as concerned as we have been to avoid significant differences between state and federal courts in adjudicating claims.'"[214]

Professor Steinman takes this principle to mean that the *Erie* policy governs unless the express text of a Federal Rule explicitly resolves the question.[215] There is reason to doubt, however, that the principle is as far reaching as he suggests. To begin with, his understanding does not actually use the *Erie* policy as a rule of construction. Rather, the rule of construction that Professor Steinman appears to suggest is that a Federal Rule should be given only the meaning that its explicit text expressly requires;[216] the *Erie*

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214. 559 U.S. at 405 n.7. Justice Scalia writes in full:

> If all the dissent means is that we should read an ambiguous Federal Rule to avoid 'substantial variations [in outcomes] between state and federal litigation, *Semtek Int'l Inc. v. Lockheed Martin Corp.* 531 U.S. 497, 504 (2001) (internal quotation marks omitted), we entirely agree. We should do so not to avoid doubt as to the Rule's validity—since a Federal Rule that fails *Erie*'s forum-shopping test is not *ipso facto* invalid, see *Hanna v. Plumer,* 380 U.S. 460, 469–472 (1965)—but because it is reasonable to assume that 'Congress is just as concerned as we have been to avoid significant differences between state and federal courts in adjudicating claims, *Stewart Organization, Inc. v. Ricoh Corp.* 487 U.S. 22, 37–38 (1988) (Scalia, J. dissenting). The assumption is irrelevant here, however, because there is only one reasonable reading of Rule 23.

Id. (some internal citations omitted).

215. Steinman, *supra* note 191, 1145–46.

216. In this regard, Professors Steinman and Doernberg share a remarkably similar approach to the construction of Federal Rules, although they describe their approaches differently. Professor Doernberg argues that 'the Court has taken a read-my-lips approach to questions about the scope of Federal Rules. Donald Doernberg, *supra* note 42, at 832. In other words, '[t]o determine the scope of a

policy would then apply as it ordinarily would in the absence of a federal statute or Federal Rule on point. In short, Professor Steinman would radically shift the boundary between statutory interpretation and the elaboration of federal common law by narrowly confining the authority of statutes and Federal Rules, and dramatically expanding the matters addressed by common law. While the *Erie* policy ensures that an expansion of the federal common law of procedure will not come at the expense of federalism concerns, the minimalist scope Professor Steinman would give Federal Rules fails to give sufficient respect to the fundamental legislative policy choice that undergirds the REA.[217]

Congress enacted the REA to promote uniformity across the federal courts and to improve the quality of procedural justice afforded in those courts.[218] Uniformity of procedure across the federal courts is not a policy that Congress wrote into the law lightly. Before the REA was enacted, the Conformity Act of 1872 had

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Rule—whether it speaks to the issue *sub judice*—the Court looks only at its language, almost defiantly refusing to make inferences. *Id.* at 831. For a collection of other authorities on the construction of Federal Rules, see Clermont, *supra* note 34, at 1021 n.161.

217. Professors Dudley and Rutherglen have persuasively argued that this fundamental policy is even more important today:

> [I]t compromises the entire federal court system when the Court overreacts and distorts the Federal Rules to accommodate state law. The efficient, fair, and uniform operation of the federal courts is a matter of ever-greater concern in a time of the increasing nationalization of law practice. The federal courts now handle over seven times as many diversity cases, and are staffed by over four times as many Article III judges, as when *Erie* was decided. This growth in the volume of federal litigation and the size of the federal judicial system requires uniform rules applied without distortion to give clear guidance to the parties and to the judges who decide their cases.

Earl C. Dudley, Jr. & George Rutherglen, *Deforming the Federal Rules: An Essay on What's Wrong with the Recent* Erie *Decisions*, 92 VA. L. REV. 707, 748 (2006).

218. *See* Burbank, *supra* note 42, at 1023-24 ("It was common knowledge at the time the Rules Enabling Act was passed that it represented the conclusion of a campaign, conducted for more than twenty years by the American Bar Association, for a uniform federal procedure bill authorizing the Supreme Court to promulgate rules of procedure in civil actions at law. '); *supra* note 2 (citing case authority).

generally required federal trial courts to apply state procedural law to actions filed on the law side.[219] Thus, the notion that federal courts should be governed by uniform federal rules had to overcome the heavy weight of historical practice. Indeed, some version of the REA was under consideration for twenty-two years before it was enacted into law.[220] Given this history, there is no reason to think that Congress that enacted the REA would have wished to undermine the uniformity of otherwise valid rules of civil procedure by having them construed narrowly so as to require application of outcome-determinative state law.[221] Put simply, the *Erie* policy—which focuses on vertical uniformity between state and federal courts—is in tension with the fundamental policy that animates the REA—that federal rule makers should have power to ensure uniformity of procedure across the federal courts.[222]

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219. *See* Geoffrey C. Hazard, Jr. *Has the* Erie *Doctrine Been Repealed by Congress?*, 156 U. PA. L. REV. 1629, 1640 (2008) ("The Conformity Act of 1872 conveniently provided that a federal district court should, for cases at law, generally follow the procedure of the state in which the court sat ").

220. I have calculated the number of years between the introduction in 1912 of a bill in Congress by Henry Clayton and Charles Culberson to the enactment of the REA in 1934. *See* Wickes, *supra* note 55, at 9 ("The bill was introduced in 1912 in the House of Representatives by Chairman Henry D. Clayton of the House Judiciary Committee and in the Senate by Chairman Charles A. Culberson of the Senate Judiciary Committee. "). For detailed discussion of the various bills and the debate over them, see Burbank, *supra* note 42, at 1050-98.

221. *Cf.* Wickes, *supra* note 55, at 12 (noting with dissatisfaction that federal practice under the Conformity Act of 1872 was a 'hybrid practice' in which 'the practice now obtaining in the federal trial courts sitting in any one state is different from the practice obtaining in the federal trial courts in any other state, and is also different from the practice of the courts of the state in which these federal courts are sitting. ').

222. Federal Rules—even when construed in light of the *Erie* policy—cannot properly be given one meaning for state claims and a different meaning for federal claims. To conclude otherwise ignores the fundamental policy of the REA, that is, the promotion of a uniform and consistent set of procedural rules. The Court unfortunately lost sight of this principle in *West v. Conrail*, 481 U.S. 35, 38 (1987) (construing Rule 3 to toll the statute of limitations with respect to a federal claim). *West* anomolously suggests that Rule 3 should be read narrowly to avoid *Erie* problems when a court is faced with a state-law claim, but not when a court is faced with a federal claim. *Id.* at 39 n.4. The result in *West* can be justified because the Court has power to elaborate federal common-law rules addressing tolling with respect to federal claims. Burbank, *Of Rules and Discretion*, *supra* note 77, at 693. But the Court's reasoning should be treated as a 'sport.

Unless the tension between the *Erie* policy and the fundamental policy of the REA is recognized, it is easy to overstate the significance of the Court's conclusion in *Shady Grove* that ambiguous Federal Rules should be read narrowly to avoid interference with the *Erie* policy. The *Erie* policy has its place in the construction of Federal Rules, but it should not be given pride of place. To the extent the *Erie* policy is treated as it should be—as just *one* of the rules of construction that a court may use in construing ambiguous Federal Rules[223]—it can and should be harmonized with other rules of construction, including the principle that if a Federal Rule, "fairly construed,"[224] can be read to cover a point, the Federal Rule should be so read in order to promote "uniform and consistent systems"[225] of federal practice.[226] This principle is so central to

223. *See, e.g. Shady Grove*, 559 U.S. at 421 (Stevens, J. concurring) (stating that a Federal Rule, like any federal law, must be interpreted in light of many different considerations).

224. *Burlington Northern*, 480 U.S. at 4.

225. *Id.* at 5.

226. To the extent an ambiguous Federal Rule is construed in light of this principle, the content of this uniform and consistent system of rules should be elaborated in the shadow of Rule 1. FED. R. CIV. P. 1 (requiring that the federal rules "be construed, administered, and employed by the court and the parties to secure the just, speedy, and inexpensive determination of every action and proceeding."); *see* Robert G. Bone, *Improving Rule 1: A Master Rule for the Federal Rules,* 87 DENV. U. L. REV. 287, 287–88 (2010) (noting that Rule 1 "sets forth the basic philosophical principle for the construction of the rules," and "is critical to the operation of the Federal Rules as a whole"); *id.* at 288 ("The Federal Rules are purposefully designed to delegate broad discretion to trial judges, and Rule 1 is meant to guide that discretion in socially-productive ways."); *see generally,* Patrick Johnston, *Problems in Raising Prayers to the Level of Rules: The Example of Federal Rule of Civil Procedure 1,* 75 B.U. L. REV. 1325 (1995). Professor Bone has recommended that Rule 1 be modified because "it is misleading and counterproductive today." Bone, *supra*, at 288.

Proponents of treating the *Erie* policy as the key to construing the federal rules may be tempted to read the reference to the 'construct[ion]' of the rules "to secure the *just* ... determination of every action" to include the *Erie* policy; the *Erie* policy, after all, was premised in significant part on the conviction that application of different law in state and federal courts will lead to inequitable administration of the laws. But such a reading of Rule 1 would be both ahistorical and inconsistent with the fundamental policy of the REA. Put simply, had the Congress that enacted the REA believed that applying different rules of procedure in state and federal court was somehow unjust, the REA would not have been enacted. From this perspective, it makes sense to understand the reference to the "just

understanding of the appropriate scope of the Federal Rules that the Court in *Burlington Northern* emphasized the importance of a uniform and consistent system of Federal Rules while addressing the *validity* of a Federal Rule.[227] In light of this central principle, the *Erie* policy should be invoked only when there is good reason to be skeptical that a Federal Rule is intended to cover an issue as opposed to uncertainty about how a Federal Rule should be understood to cover the issue.[228] The Court's discussion in *Burlington Northern* and its decision in *Gasperini v. Center for the Humanities* illustrate this distinction.

The question in *Burlington Northern* was whether there was a direct collision between a federal rule of appellate procedure and an Alabama statute.[229] Rule 38 provided, "[i]f the court of appeals shall determine that an appeal is frivolous, it may award just damages and single or double costs to the appellee."[230] The Alabama statute, on the other hand, provided that the plaintiff was entitled to recover ten percent of the damages as a penalty for the defendant's unsuccessful appeal if a stay of the judgment had been granted pending appeal.[231]

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determination of every action' to refer the fairness of the procedural rules used to conduct the litigation in federal court without regard to whether the rules applied in federal court track those of the state in which the federal court sits.

227. *Burlington Northern*, 480 U.S. at 5 ("The cardinal purpose of Congress in authorizing the development of a *uniform and consistent* system of rules governing federal practice and procedure suggests that Rules which incidentally affect litigants' substantive rights do not violate [Section 2072] if reasonably necessary to maintain the integrity of that system of rules. '(emphasis added)).

228. The Court's sole opinion explicitly relying on the *Erie* policy as a rule of construction did so while simultaneously stating another rule of construction that led to the same result. Specifically, in *Semtek* a unanimous Court refused to read Federal Rule of Civil Procedure 41(b) as stating a rule of preclusion, in part because doing so would arguably violate the jurisdictional limitation of the Rules Enabling Act. *See Semtek*, 531 U.S. at 503–04. Use of the *Erie* policy as a rule of construction in such a case is unnecessary, but harmless. For an earlier post-*Hanna* case in which the Court's construction of the Rule appears to have been designed to avoid running afoul of the jurisdictional limits of the REA, see Walker v. Armco Steel Corp. 446 U.S. 740 (1980).

229. *Burlington Northern*, 480 U.S. at 4.

230. *Id.* at 5.

231. The Court in *Burlington Northern* quoted the relevant Alabama statute as follows:

> 'When a judgment or decree is entered or rendered for money, whether debt or damages, and the same has been stayed on appeal by

Although the federal rule and the state statute arguably covered different subjects, the Court found that there was in fact a direct collision between Rule 38 and the state statute.

The Court concluded that Rule 38 provides in effect that no damages can be awarded for an unsuccessful appeal, unless the appeal is frivolous. That the Court's interpretation of Rule 38 was not mandated by the rule's express language is demonstrated by the fact that Alabama had a virtually identical version of Rule 38 that operated hand-in-hand with the state statute.[232] The Court found that Rule 38 covered the point not because the express text of the rule required that result, but because the Court concluded that a narrow reading of Rule 38 to accommodate state law would interfere with the discretion that appellate courts would otherwise be entitled to exercise under Rule 38.[233] Thus, the Court gave the ambiguous appellate rule a broad construction to promote uniformity with respect to a matter within the concern of the prescribed rule, fairly construed.

The rule of construction stated in *Burlington Northern*, among other things, may properly be used to fill in gaps in Rule 56—the summary judgment rule—on matters like the nature and the extent of the triggering burden faced by a moving party without the burden of production at trial. At least until the Court made the text of Rule 56 more explicit in 2010, the text of Rule 56 provided little guidance on these matters. Noting that "the language of Rule 56 [did] not dictate a particular approach to determining how a party

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> the execution of bond, with surety, if the appellate court affirms the judgment of the court below, it must also enter judgment against all or any of the obligors on the bond for the amount of the affirmed judgment, 10 percent damages thereon and the costs of the appellate court Ala. Code § 12–22–72 (1986).

Burlington Northern, 480 U.S. at 3.

232. *See* Alabama Rule of Appellate Procedure 38 ("In civil cases, if the appellate court shall determine on motion or *ex mero motu* that an appeal is frivolous, it may award just damages and single or double costs to the appellee."); *Burlington Northern*, 480 U.S. at 7 ("Respondents argue that, because Alabama has a similar Appellate Rule which may be applied in state court alongside the affirmance penalty statute, a federal court sitting in diversity could impose the mandatory penalty and likewise remain free to exercise its discretionary authority under Federal Rule 38.").

233. *Burlington Northern*, 480 U.S. at 8.

'show[s]' that no genuine issue of material fact exists,"[234] or "specify any particular approach to gauging whether evidence is sufficient to create a 'genuine issue' as to any given fact,"[235] Professor Steinman argued that *Erie* considerations called for the application of state law to fill in the gaps.[236] But it seems implausible that the drafters of Rule 56 intended to leave matters so central to the operation of summary judgment to the vagaries of state law. For that reason, it would be inappropriate to invoke the *Erie* policy as a rule of construction in this context.

By contrast, use of the *Erie* policy as a rule of construction would have been appropriate in *Gasperini*. One of the questions before the Court in that case was the proper interpretation of Rule 59. At the time, Rule 59 provided that "[a] new trial may be granted for any of the reasons for which new trials have heretofore been granted in actions at law in the courts of the United States."[237] William Gasperini claimed that the proper standard for determining whether a verdict was excessive was found not in New York law, but in the "shock the conscience" standard typically applied in federal court.[238] In a decision addressing a number of other questions, Justice Ginsburg, writing for the majority, concluded that Rule 59 gave district courts the power to review jury verdicts for excessiveness, but that state law provided the standard for determining whether a judgment based on state law was excessive.[239]

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234. Adam N. Steinman, *What is the* Erie *Doctrine? (And What Does It Mean for the Contemporary Politics of Judicial Federalism)*, 84 NOTRE DAME L. REV. 245, 284 (2008).

235. *Id.*

236. *Id.* (arguing that '*Gasperini* indicates that the standards a federal court should use to evaluate whether a moving defendant has made the requisite 'show[ing]' and whether a plaintiff's evidence is sufficient to create a 'genuine issue' are not dictated by the Rules themselves, and concluding as a result that 'whether state or federal law governs these matters should be viewed as an unguided *Erie* choice"). Professor Steinman makes a similar argument with respect to pleading standards under Rule 8. *See id.* at 285 (discussing Rule 8).

237. Gasperini v. Ctr. for Humanities, Inc. 518 U.S. 415, 467–68 (1996).

238. *Id.* at 420–21.

239. *Id.* at 437 n.22. The majority explained:

> Rule 59(a) is as encompassing as it is uncontroversial. It is indeed 'Hornbook' law that a most usual ground for a Rule 59 motion is that 'the damages are excessive. See C. Wright, Law of Federal Courts 676–677 (5th ed.1994). Whether damages are excessive for the

Justice Scalia in dissent argued that it was the federal standard for excessiveness that provided, in the words of Rule 59, a "reason" for the grant of a new trial in federal courts.[240] Neither the majority opinion nor Justice Scalia's dissent explicitly invoked the *Erie* policy as a rule of construction. But because the language in Rule 59 is indefinite and provides no basis for thinking that it contemplates, let alone prescribes, a federal standard for excessiveness, the Court should have narrowly construed Rule 59 to avoid interference with the *Erie* policy.[241]

The relationship between choice of law and the predominance requirement of Rule 23(b)(3) provides an even clearer illustration of the proper use of the *Erie* policy in the construction of Federal Rules. I have argued elsewhere that Rule 23 cannot properly be understood to authorize courts to invoke the predominance requirement of Rule 23(b)(3) to modify—even in a limited fashion—the general rule that a federal court must apply the choice-of-law

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> claim-in-suit must be governed by *some law*. And there is no candidate for that governance other than the law that gives rise to the claim for relief—here, the law of New York. See 28 U.S.C. §§ 2072(a) and (b) ("Supreme Court shall have the power to prescribe general rules of procedure' '[s]uch rules shall not abridge, enlarge or modify any substantive right")

Id. *Cf. id.* at 440 n.1 (Stevens, J. dissenting) ("Because there is no conceivable conflict between Federal Rule of Civil Procedure 59 and the application of the New York damages limit, this case is controlled by *Erie.* ').

240. *Id.* at 467–68.

241. Justice Ginsburg instead invoked the principle that Federal Rules should be construed 'with sensitivity to important state interests. *Id.* at 427 n.7 ("Federal courts have interpreted the Federal Rules, however, with sensitivity to important state interests and regulatory policies. '). There seems to be little difference between this principle and the *Erie* policy. A choice between state and federal law that is outcome determinative in the *Hanna* sense will almost certainly bear on important state interests and regulatory policies. Indeed, Justice Scalia quoted language similar to Justice Ginsburg's to support his view that the *Erie* policy may be used as a rule of construction. *See* Stewart Org. Inc. v. Ricoh Corp. 487 U.S. 22, 38 (1988) (Scalia, J. dissenting) (quoting P. Bator, D. Meltzer, P. Mishkin, & D. Shapiro, HART AND WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM 828 (3d ed. 1988) for the proposition that '[t]he Supreme Court has continued since *Hanna* to interpret the federal rules to avoid conflict with important state regulatory policies' to support use of the *Erie* policy as a rule of construction).

rules of the State in which it sits.[242] The predominance requirement, for example, does not authorize federal courts to displace a state-law presumption in favor of forum law, a presumption that requires application of the law of the forum unless the proponent of applying foreign law is able to demonstrate the applicability and content of that law.[243] As I explained, the state choice of law burden and the federal certification burden are analytically distinct:

> Determining whether common issues of law or fact predominate does not require displacing state choice-of-law rules. It requires only an evaluation of the impact of choice-of-law decisions on the viability of a class suit. Put another way, if the laws of multiple jurisdictions must be applied under applicable state choice-of-law rules, the party seeking certification bears the burden of demonstrating that certification of a class would nonetheless be appropriate despite the relevance of multiple bodies of law. But that obligation does not kick in until after the court has concluded that the law of more than one state will apply.[244]

Because the text of the Rule does not expressly allocate the choice of law burden to the party seeking certification of a class, proper construction of Rule 23 depends on whether conflating the choice of law and certification burdens would further the purpose of the predominance requirement. Broadly speaking, the "predominance requirement largely focuses on whether use of the class device in a particular case would be an efficient use of judicial resources."[245] And the ability of a court to make that determination does not depend on whether a federal court applies or declines to

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242. *See, e.g.* Patrick Woolley, Erie *and Choice of Law After the Class Action Fairness Act*, 80 TUL. L. REV. 1723, 1739–43 (discussing Rule 23 and the predominance requirement).

243. For discussion of the presumption in favor of forum law, *see id.* at 1728–29; Patrick Woolley, *Choice of Law and the Protection of Class Members in Class Suits Certified Under Rule 23(b)(3)*, 2004 MICH. ST. L. REV. 799, 802 & n.13. The term 'foreign' law refers to any law that is not the law of the forum.

244. Woolley, *supra* note 242, at 1741.

245. *Id.*

apply a state-law presumption in favor of forum law. In other words, there is good reason to be skeptical that the Rule was intended to address the issue at all. For that reason, the predominance requirement of Rule 23 should be read narrowly in light of the *Erie* policy so as to exclude choice of law from its ambit.

In short, while it is sometimes appropriate to invoke the *Erie* policy in construing the Federal Rules narrowly, federal courts at other times should construe Federal Rules broadly to promote a "uniform and consistent system"[246] of federal procedure.

Justice Ginsburg's conception of the Court's *Erie* cases may pose an obstacle, however, to a context-sensitive application of rules of construction. Specifically, Justice Ginsburg arguably reads the Court's *Erie* jurisprudence to always require that Federal Rules be construed "with sensitivity to important state interests and to avoid conflict with important state regulatory policies."[247] As she writes in *Shady Grove*, "both before and after *Hanna*, federal courts have been cautioned by this Court to 'interpre[t] the Federal Rules with sensitivity to important state interests,'" and a will "to avoid conflict with important state regulatory policies."[248]

The doctrinal history in fact is far more complicated than the passage quoted above suggests. To begin with, the cases that predate *Hanna* were decided during a period in which, at a minimum, there was confusion about whether federal rule makers had authority to prescribe Federal Rules that were inconsistent with the *Erie* policy. Thus, courts construing Federal Rules during this period had every incentive to read Federal Rules as narrowly as possible to avoid the invalidation of a Federal Rule, an incentive that no longer exists now that *Hanna* has clarified that the federal rule makers are not bound by the *Erie* policy. It is true, of course, that the Court since *Hanna* has sometimes read Federal Rules with sensitivity to important state interests and to avoid conflicts with state regulatory policy. But there has been more diversity in interpretive approaches than Justice Ginsburg notes in her dissent. Although she cites *Walker v. Armco Steel Corp.*, *Gasperini*, and *Semtek* to support the

246. *Burlington Northern*, 480 U.S. at 5.

247. *See Shady Grove*, 559 U.S. at 442 (Ginsburg, J. dissenting) (discussing the Court's jurisprudence before and after *Hanna* as requiring sensitivity to state interest when interpreting Federal Rules).

248. *Id.*

rule of construction she advocates, she ignores *Burlington Northern* and *Business Guides, Inc. v. Chromatic*, neither of which gave the Federal Rule at issue a narrow reading.[249]

Despite Justice Ginsburg's apparent insistence on reading Federal Rules narrowly, it is possible to read her opinion in *Shady Grove* as less absolutist than might appear at first glance. Specifically, she writes at the start of her discussion about rules interpretation: "[W]e have avoided immoderate interpretations of the Federal Rules that would trench on state prerogatives *without serving any countervailing federal interest*."[250] The italicized language suggests that there are circumstances in which a Federal Rule need not be read narrowly to avoid a clash with state law. Justice Ginsburg's dissent suggests that *Shady Grove* is not such a case. In the next subparts, I discuss, among other things, why Justice Ginsburg was incorrect to conclude that there is no federal interest in displacing § 901(b) as a limit on federal class actions independent of Rule 23.

2. Construing the Certification Requirements of Rule 23

The Court in *Shady Grove* concluded that there was a direct collision between the certification requirements of Rule 23 and a state law bar on the certification of a class seeking penalties.[251] The direct collision question is more difficult if state law bars the award of penalties or if (as Justice Ginsburg suggested) a state-law ban on certification of a class seeking penalties is deemed the functional equivalent of a ban on the award of penalties. The Federal Rules should effectuate state remedial law rather than select which

249. *Id.* at 439–42 (citing *Walker*. *Gasperini*, and *Semtek* to support a narrow construction of Federal Rules). *Cf.* Business Guides, Inc. v. Chromatic Commc'ns Enters. Inc. 498 U.S. 533, 568 (Kennedy, J. dissenting) (stating that the Court's interpretation of Rule 11 has the potential to encroach on 'matters reserved to the States' and arguing that '[w]hether or not Rule 11 as construed by the majority exceeds our rulemaking authority, there is a 'reasonable, alternative interpretation which is more consistent with the text of the Rule.'); *Burlington Northern*, 480 U.S. 1 (concluding that federal rule of appellate procedure 38 was inconsistent with Alabama state law despite a strong textual argument to the contrary).

250. *Id.* at 439 (emphasis added).

251. *Id.* at 430.

remedies should be provided for violations of state law. Thus, if § 901(b)—or common law premised on § 901(b)—is characterized as part of New York's remedial law, the *Erie* policy should be invoked to avoid a construction of Rule 23 that would interfere with New York law. But New York law barring the award of penalties in class litigation is better characterized as regulating aggregation.

A state, of course, may choose to modify the substantive rights of individuals who have claims against a defendant by imposing a limit on the total liability of the defendant. But although Justice Ginsburg appears to analogize New York law to a damages cap,[252] the analogy is fatally flawed because New York law does not impose a hard cap or even a judicially-administered excessiveness limit on the total liability of a defendant for penalties. As Justice Scalia explained: "Allstate's aggregate liability does not depend on whether the suit proceeds as a class action. Each of the 1,000-plus members of the putative class could (as Allstate acknowledges) bring a freestanding suit asserting his individual claim."[253]

Because the class suit in *Shady Grove* sought only penalties, application of a New York ban on penalties would have the same effect on class members in *Shady Grove* as a hypothetical statute barring an award of money damages in class litigation. If applied in federal court, a state law that categorically *requires* dismissal of a suit *because it is a class suit* would undermine the carefully crafted certification criteria set forth in Rule 23. This sort of interference with the integrity of the certification requirements of Rule 23 should not be permitted. The same analysis should apply even if other forms of relief would be available in the class suit. Although the effect of state law in such a case would be less far-reaching and thus less obviously objectionable than a complete lack of relief, state law

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252. *Shady Grove*, 559 U.S. at 446–47 (Ginsburg, J. dissenting) ("Sensibly read, Rule 23 governs procedural aspects of class litigation, but allows state law to control the size of a monetary award a class plaintiff may pursue."); *see* Green, *supra* note 202, at 397 ("For Ginsburg, section 901(b) was legally equivalent to a statutory damages cap, which has nothing to do with Federal Rule 23.").

253. *Shady Grove*, 559 U.S. at 408. Professor Tidmarsh agrees that the Court reached the right result in *Shady Grove*, Jay Tidmarsh, *Procedure, Substance, and* Erie, 64 VAND. L. REV. 877, 913–17 (2011), but argues that the federal courts should respect 'a statute that caps the damages available in a class action at some level (whether a flat amount or a percentage of either the harm caused or the defendant's assets.). *Id.* at 917.

would still bar certification of certain issues, and thus would impermissibly interfere with the certification requirements of Rule 23.

It is nonetheless true that the certification provisions of Rule 23 do not explicitly prohibit giving independent effect to state statutes that would forbid an award of penalties in class litigation. It could be argued that the *Erie* policy requires the federal courts to avoid interference with a New York policy that bears on remedies in class litigation. Indeed, the Court's unanimous decision in *Semtek* at least superficially seems to support this result. In *Semtek*, the Court read Rule 41(b) narrowly to avoid any effect on state preclusion law. A federal court arguably should do the same in reading Rule 23 to avoid any effect on state remedial law.

It is important to keep in mind, however, that a sound construction of the REA would have prohibited the Court from prescribing a Federal Rule that resolved the question posed in *Semtek*—whether a judgment dismissing a suit on statute of limitations grounds should be given claim- or issue-preclusive effect.[254] In essence, the Court stripped Rule 41(b) of any preclusive effect to save the Federal Rule from invalidation. The Court did so without recognizing that there was an alternative construction of Rule 41(b) that would have appropriately addressed the limitations issue without affecting the use of preclusion to enforce procedural policies within the scope of the REA.[255] As noted earlier, whether judgments based on motions to dismiss are entitled to the same preclusive effect as judgments based on motions for summary judgment or judgments after trial "bears significantly on the effective management of litigation under the Federal Rules of Civil Procedure"[256] and should be deemed within the scope of the Court's rule-making power.

A rule that channels litigation in or out of the class device—as does New York's ban on penalties in class actions—similarly

254. *See supra* notes 147-162 and accompanying text (describing the limited authority of federal rule makers to prescribe rules of preclusion.

255. *See* Woolley, *supra* note 13, at 598–601 (arguing that a limitations dismissal by a federal court sitting in a state that would give such a dismissal only issue-preclusive effect should be treated under Rule 41(b) as a 'jurisdictional' dismissal rather than a dismissal on the merits).

256. *Id.* at 585.

bears on the effective management of litigation. The *Erie* policy has no place as a rule of construction in such a case. As discussed above, a Federal Rule should not be read narrowly to avoid conflict with state regulatory policy when doing so would interfere with a legitimate federal procedural policy established under the authority of the REA.[257] Thus, Rule 23 should be read to displace the independent operation of state law that—like § 901(b)—undermines the certification criteria of Rule 23.

None of this is to say that a ban on penalties should not be given appropriate weight *under* the certification criteria set forth in Rule 23, specifically, as I explore below, the requirement that class litigation be "superior to other available methods for fairly and efficiently adjudicating" a controversy.[258] But to the extent that a New York ban on penalties in class litigation is relevant to the superiority requirement, state law would be invoked to give effect to Rule 23, *not* as an independent limitation on the use of the class device in federal court.

Professor Clermont suggests that *Shady Grove* may require even broader displacement of state law—that "any state law that directly impedes or facilitates joinder must fall to Rule 23."[259] He writes, for example, that a state can

> facilitate federal certification by changing its conflict-of-laws rules to make a single state's law govern in mass tort cases. But if the state ma[kes] the new law apply only in class actions, I think, with some trepidation, that *Shady Grove* would cause Rule 23 to trump the provision in federal court.[260]

For the reasons explained above, I believe the Court has power to prescribe a Federal Rule requiring a federal court to apply the *same* choice of law rules that a State would apply to an individual action.[261] Although choice-of-law rules are often properly

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257. *See supra* notes 218-28 and accompanying text (arguing that Federal Rules should be interpreted consistently with the fundamental policy of the REA).

258. FED. R. CIV. P. 23(b)(3).

259. Clermont, *supra* note 35, at 1030.

260. *Id.* at 1031.

261. *See supra* notes 163-66 and accompanying text (arguing that the principle that federal rule makers may prescribe rules to prevent application of

characterized as substantive and thus outside the rulemaking power,[262] the effect of a rule requiring equal application of state substantive law across federal joinder devices would implement a policy choice that rule-makers are entitled to make, notwithstanding its "incidental effect"[263] on substantive rights. But the preemptive scope that Professor Clermont would afford Rule 23 is insufficiently tethered to the Rule. A Federal Rule displaces state law only if the Federal Rule covers the point addressed by state law.[264] It is not the case that Rule 23 covers anything that would "directly impede[] or facilitate[]"[265] aggregation through the class device. As I have argued at length elsewhere, Rule 23, for example, does not address choice of law.[266] Nor does Rule 23 provide authority for granting attorneys' fees to class counsel,[267] even though the availability of attorneys' fees may be crucial to whether a class suit proceeds.

Thus, a New York ban on the award of penalties in class litigation should be displaced, not because it impedes federal class litigation, but because it is in conflict with the certification requirements of Rule 23. In the absence of displacement, a federal court would be required to dismiss a class action—and only a class action—in which only penalties are available, thus rendering pointless the elaborate certification criteria in Rule 23 that are designed to determine whether a class suit is appropriate. Although state-law rules governing choice of law and attorney compensation in class litigation may impede or facilitate aggregation by affecting

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state law from skewing federal practice by favoring one federal procedural device over another also applies to the choice between a class suit and individual litigation). In the absence of a Rule requiring a federal court to apply the same choice of law rules that a state would apply to an individual action, federal courts are required by *Klaxon Co. v. Stentor Electric Mfg. Co. Inc.* 313 U.S. 487, 496–97 (1941) to apply the same choice-of-law rules to a class action as would the courts of the state in which they sit, whether state law would favor or disfavor a class suit. *See* Woolley, *supra* note 243, at 816–18 (discussing the proper application of *Klaxon* in cases brought under current law).

262. *See* Woolley, *supra* note 242, at 1766 ("[M]ost choice-of-law rules cannot be characterized independently from the rules they select. '); *id.* at 1758–69 (explaining that conclusion).

263. *Burlington Northern*, 480 U.S. at 5.

264. Walker v. Armco Steel Corp. 446 U.S. 740, 750 (1980).

265. Clermont, *supra* note 35, at 1030.

266. Woolley, *supra* note 242, at 1739–46.

267. *See supra* notes 174-75 and accompanying text.

whether the predominance and superiority requirements of Rule 23 will be satisfied, these state-law rules cannot be said to be in conflict with the certification requirements of Rule 23. Nor is there any other basis on which to conclude that Rule 23 displaces state-law rules governing choice of law or attorney compensation.

3. State Law and the Superiority Requirement

In order to certify a 23(b)(3) class suit, a court must find that a class action is "superior to other available methods for fairly and efficiently adjudicating the controversy."[268] Yet none of the briefs in *Shady Grove* considered the impact of the superiority requirement on certification of the class at issue,[269] and the Justices followed the lead of the parties in this regard. The Justices focused instead on whether § 901(b) presented an obstacle to class certification independently of Rule 23.[270] As Richard Nagareda perceptively noted, the Court's failure to discuss an integral aspect of the certification requirements under Rule 23(b)(3) may mislead those who fail to recognize that *Shady Grove* addressed an artificially narrow question.[271] Ironically, the *Shady Grove* dissenters may have been among the first to fall victim to the misleading way in which *Shady Grove* was framed. As discussed below, a proper interpretation of the superiority

268. FED. R. CIV. P. 23(b)(3) (stating that a class action may be maintained if 'the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for fairly and efficiently adjudicating the controversy").

269. Nagareda, *supra* note 186, at 1084 ("[N]one of the briefs submitted to the Supreme Court in *Shady Grove* appears to have flagged the potential superiority obstacle under Rule 23.').

270. *Shady Grove*, 559 U.S. at 399–401.

271. Nagareda, *supra* note 186, at 1084 ("The peculiar posture of *Shady Grove* influences the way that one should understand the Court's holding that New York section 901(b) is not binding in a federal diversity case—that is, as a ruling that section 901(b) does not comprise a determinative, open-and-shut reason for the federal court to withhold class treatment, not as a decision that endangers the distinct, discretionary inquiry into superiority under Rule 23(b)(3) in cases involving statutory damages."); *id.* ("[*S*]*hady Grove* has a tendency to convey the mistaken impression that section 901(b) stood as the only meaningful obstacle to class certification, with satisfaction of Rule 23 being a foregone conclusion, once section 901(b) is deemed nonbinding.').

requirement goes far to address the concerns that Justice Ginsburg articulated in her dissent.

Rule 23 does not expressly address the role that state law should play in determining whether the class action is "superior to other available methods for fairly and efficiently adjudicating a controversy."[272] Relying on the open-ended nature of the superiority analysis, however, Professor Steinman argues that the superiority requirement should be read consistently with the *Erie* policy, meaning that certification of a federal class suit that could not be certified under state law would not satisfy the superiority requirement:

> New York's law barring statutory-damages class actions does not unavoidably clash with Rule 23, because Rule 23's superiority requirement can be interpreted consistently with New York law. Federal courts need only adopt New York's conclusion that the danger of remedial overkill makes statutory-damages class actions a bad idea and, therefore, not "superior to other available methods for fairly and efficiently adjudicating the controversy." Where the class asserts claims arising under such a state's law, the state's view that a class action is superior to individual adjudication could legitimately displace the federal judiciary's often more hostile approach. Either way, a federal court would be prohibited from deviating from state class action law if doing so would run afoul of *Erie*'s twin aims, such as by encouraging forum shopping.[273]

272. *Shady Grove*, 559 U.S. at 396 n.1.

273. Steinman, *supra* note 195, at 1147. *See also id.* at 1145–46 (noting that '[n]o precise formula is provided for how a court should measure whether common issues 'predominate, or how a court should balance the costs and benefits of class treatment to decide whether a class action would be 'superior, and arguing that the Court's use of the *Erie* policy as a rule of construction means that 'if the vague standard set forth in the Federal Rule can be applied in a way that is consistent with state law the Federal Rule does not truly collide with state law"); *id.* at 1148 ("Rule 23(b)(3)'s vague 'superiority' requirement is not

As argued above, Professor Steinman's penchant to read any ambiguous Federal Rule as narrowly as possible to avoid interference with the *Erie* policy is unsound. Read fairly, the superiority requirement requires federal courts to consider *both* fairness *and* efficiency. Thus, even assuming that the *Erie* policy—rooted in the view that fairness requires equal treatment among those who can take advantage of diversity jurisdiction and those who cannot—should be dispositive with respect to fairness, the superiority requirement cannot be reduced to the *Erie* policy. Moreover, there is no reason to limit even the meaning of fairness to compliance with the *Erie* policy in a provision that addresses a matter at the core of federal procedural policy—the wisdom of aggregating claims.

That is not to say that state law is irrelevant to the superiority inquiry. The open-ended nature of the superiority requirement suggests that state law may be considered when it bears on whether class litigation in federal court is the superior means of proceeding. And the *Erie* policy is one way to bring state law to bear in evaluating whether certification of a class suit for money damages is fair. In fact, it may be the only way to do so for judges resistant to a purposive analysis of state law. But for judges who accept a purposive approach, considering the purposes of state law will provide a more precise way of evaluating the fairness of certifying a class suit in federal court that could not proceed in state court.

Take § 901(b), for example. As Professor Nagareda noted, § 901(b) appears to have been enacted to address the distortive effect of class litigation on state remedial law.[274] Designing procedural

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deep enough to displace state law on the permissibility of a class action in a particular set of circumstances.').

274. Nagareda, *supra* note 186, at 1081 (arguing that 'the whopping difference in liability exposure occasioned by class treatment' in statutory damages cases 'would distort, rather than effectuate, underlying law not calibrated with the notion of market-wide private enforcement in mind"). *See also Shady Grove*, 559 U.S. at 445 n.3 (Ginsburg, J. dissenting) (discussing the distortive effect of class litigations). Justice Stevens suggested in his concurrence that New York may simply have concluded that certification of a class for penalties was unnecessary. *See id.* at 434 (Stevens, J. concurring) ("[S]ome opponents of a broad class-action device 'argued that that there was no *need* to permit class actions in order to encourage litigation when statutory penalties provided an aggrieved party with a sufficient economic incentive to pursue a claim.'). As Justice Ginsburg noted in her dissent, it seems implausible to read the legislative

rules to avoid undue distortion of the substantive law is at the heart of procedural decision-making. Indeed, it fits within the definition of procedure the Court in *Sibbach* enunciated: "the judicial process for enforcing rights and duties recognized by substantive law and for *justly administering remedy and redress* for disregard or infraction of them."[275] Because some distortion of substantive law is inevitable no matter what the procedural regime, a well-designed procedural system will seek to minimize—at an acceptable cost—the distortion. From this perspective, it is up to the drafters of the Federal Rules—not the State of New York—to determine whether the possibility that a class action will distort the remedial scheme created by the substantive law of New York should be addressed by the federal courts and, if so, how. The superiority requirement of Rule 23 in fact provides a mechanism within the four corners of the Rule to address the distortive effect that certification of a class may have on state remedial law,[276] albeit a more limited mechanism than that provided by New York law.

Whether the use of the class device in a particular case would have a distortive effect on substantive rights naturally depends on what a state seeks to accomplish by authorizing particular remedies for a violation of substantive law. Thus, state law has a critical role to play in determining whether certification of a class suit would be unfair.[277] Where, as in *Shady Grove*, the legislature has expressed

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history in that way. *See id.* at 444–45 (Ginsburg, J, dissenting) (discussing the reason behind New York's decision to block class-action proceedings). The class device can sensibly be viewed as unnecessary in this context only if it would be burdensome and expensive when weighed against alternative means of proceeding.

275. Sibbach v. Wilson & Co. 312 U.S. 1, 14 (1941) (emphasis added). As argued above, see notes 251-253 and accompanying text, Section 901(b) cannot properly be understood to 'modify, abridge or enlarge' the remedies available for violations of substantive law. The question Section 901(b) seeks to address is whether the class device is an appropriate way of giving effect to penalty awards authorized by the substantive law.

276. Nagareda, *supra* note 186, at 1085 ("Even if New York section 901(b) is not strictly binding in a federal diversity case in the Erie sense that state provision properly informs the discretionary judicial inquiry into superiority under Rule 23(b)(3).").

277. Professor Green, in discussing *Shady Grove*, suggests that the concern expressed in the legislative history about awarding penalties in class litigation is not limited to concern about distortion of state remedial law:

concern about the distortive effect of awarding penalties in a class suit, federal courts should respect that judgment. A federal court may also deny class certification to avoid the distortion of state remedial law even when the state legislature has been silent.[278] But federal courts should avoid concluding that a class suit would distort state remedial law if use of the class device would be permitted in state court.[279]

The superiority requirement also requires consideration of whether use of the class device would be efficient in a particular case, but this factor should have little influence in a case like *Shady Grove*. As Justice Ginsburg noted, the plaintiffs could file the class suit in *Shady Grove* in federal court only because of the jurisdiction-friendly standards of the Class Action Fairness Act.[280] Thus, failure

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> New York's cited risks of 'overkill' and 'annihilation' with respect to class-action defendants are not just about fears of "too much justice' as a matter of substantive liability. There may also be procedural coercion in the fact of aggregation itself, such that defendants who face massive settlement pressure in cases where 'individual proof of damages is unnecessary' will not get a sufficiently fair hearing of their defense.

Green, *supra* note 202, at 403. To the extent this procedural concern is present, a federal court may properly reach an independent judgment on the superiority question without considering state law.

278. Nagareda, *supra* note 186, at 1081 ("Even in the face of silence in underlying law concerning the interaction of statutory damages with the class action mechanism, it is far from clear that certification should be forthcoming under Rule 23.').

279. Professor Nagareda apparently would have disagreed with this conclusion because he seems to have viewed the superiority requirement as providing authority—quite apart from the substantive law—for denying certification of suits involving certain kinds of statutory damages on the ground that class litigation would be distortive. *Id.* at 1082 n.64 ("The superiority problem arises most acutely when the underlying statute affords no latitude for avoidance of remedial overkill in the aggregate"). Whether the Due Process Clause imposes independent limits on the availability of statutory damages and whether such limits may justify denial of class certification (as opposed to a remittitur) is beyond the scope of this paper. For one view, see Sheila B. Scheuerman, *Due Process Forgotten: The Problem of Statutory Damages and Class Actions*, 74 MO. L. REV. 103 (2009).

280. The jurisdictional provisions of CAFA are so jurisdiction friendly that the Court could have avoided ruling on the relationship between Rule 23 and Section 901(b) by recognizing that the district court had improperly concluded that CAFA jurisdiction depends on certification of a class. Subject matter jurisdiction

to proceed with the class suit would not have burdened the federal courts with individual litigation.[281] For all these reasons, the superiority requirement should lead a federal court in a case like *Shady Grove* to conclude that the class device is not the superior means of proceeding and deny certification, unless it would be appropriate to certify an issue class on the question of liability alone.[282]

Had Justice Ginsburg focused on the superiority requirement in *Shady Grove*, it is at least open to question whether she would have found cause to dissent. Although it was clear in *Shady Grove* that federal courts did not have an efficiency interest in hearing the class action,[283] attention to the efficiency prong of the superiority

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under CAFA does *not* depend on the eventual certification of a class suit. *See* Nagareda, *supra* note 186, at 1083 n.65 (noting that the 'inclination of the district court to dismiss the lawsuit outright appears to stem from a misunderstanding as to subject matter jurisdiction.'). CAFA (with exceptions not relevant here) grants original jurisdiction to federal district courts over a *class action* involving minimal diversity if the aggregate amount in controversy is in excess of $5 million. *See* 28 U.S.C. § 1332(d)(2) (2014). The term 'class action' is defined as 'any civil action *filed* under rule 23 of the Federal Rules of Civil Procedure or similar State statute or rule of judicial procedure authorizing an action to be brought by 1 or more representative persons as a class. 28 U.S.C. § 1332(d)(1)(B) (2014) (emphasis added). And Section 1332(d)(8) expressly provides that '[t]his subsection [i.e. 1332(d)] shall apply to any class action before or after the entry of a class certification order by the court with respect to that action. 28 U.S.C. § 1332(d)(8) (2014). Thus, 'CAFA jurisdiction attaches when a case is *filed* as a class action,' *In re* Burlington N. Santa Fe Ry. Co. 606 F.3d 379, 381 (7th Cir. 2010), and 'denial of class certification does not divest federal courts of jurisdiction,' Metz v. Unizan Bank, 649 F.3d 492, 500 (6th Cir. 2011) (collecting cases).

281. The statement in the text assumes that federal courts would not permit plaintiffs to file class actions in federal court that lack merit for the purpose of obtaining diversity jurisdiction over their individual claim under the Class Action Fairness Act. *See* 28 U.S.C. § 1359 (2014). ("A district court shall not have jurisdiction of a civil action in which any party, by assignment or otherwise, has been improperly or collusively made or joined to invoke the jurisdiction of such court.').

282. An issue class on liability arguably would not run afoul of state-law limits on class action remedies. If the issue class were successful, absent class members would then be required to file individual suits to take advantage of the preclusive effect of the decree and obtain damages.

283. *Shady Grove*, 559 U.S. at 448 n. 14 (Ginsburg, J. dissenting) ("There is no risk that individual plaintiffs seeking statutory penalties will flood federal courts with state-law claims that could be managed more efficiently on a class basis; the diversity statute's amount-in-controversy requirement ensures that small

requirement might have led Justice Ginsburg away from the conclusion that there was *no* federal interest in preventing state statutes like § 901(b) from barring class certification independently of the requirements of Rule 23. Instead, she might have recognized that the superiority requirement is open-ended enough to authorize consideration of state law in cases like *Shady Grove* as part of an accommodation between state and federal interests, an approach she favored in *Gasperini*.

IV CONCLUSION

Federal Rules should not be emasculated by excessive deference to state law. If state law conflicts with a Federal Rule that regulates "practice and procedure," state law must give way in federal court. To require instead that Federal Rules that regulate "practice and procedure" give way—even in limited circumstances—to a state law with a substantive purpose would undermine the fundamental purpose of the REA—i.e., to grant the Court authority to create a uniform and consistent set of Federal Rules governing "practice and procedure" unfettered by the vagaries of state law. The fundamental purpose of the REA similarly suggests that if a Federal Rule, fairly construed, can be read to cover a point, the Federal Rule should be so read in order to promote the uniformity and consistency of federal practice. The Court, of course, need not exercise the power delegated in the REA when deference to state law would be the better course. We should trust the rules committees—as supervised by the Court and Congress—to strike the proper balance between uniform federal rules and state law.

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state-law disputes remain in state court.'). I assume that a federal court in a case like *Shady Grove* should consider efficiency only *within* the federal system. Given that New York policy is hostile to use of the class device, a federal court need not weigh whether New York state courts would be burdened with individual litigation in the absence of a federal class suit. I do not address the extent to which, if at all, the superiority requirement would require taking into account burdens on state courts in other contexts.

Controversy and Oversight: Recent Developments in 702 Surveillance and Article III Jurisprudence

Adam Dec*

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I. INTRODUCTION

Of the articles establishing the three main branches of government, Article III is the shortest. In just 369 words, it outlines the role of the judiciary, establishes the Supreme Court, allows for inferior courts, grants life tenure to federal judges, and provides the only criminal definition found in the Constitution.[1] Importantly,

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1. U.S. CONST. art. III. Though Article I references piracy and counterfeiting, *id.* art. I, and Article II allows for impeachment for "treason,

Article III also limits federal judicial power "to all [c]ases arising under this [c]onstitution, the [l]aws of the United States, and [t]reaties made under their [a]uthority; to all [c]ases of admiralty and maritime [j]urisdiction; [and] to [c]ontroversies to which the United States shall be a [p]arty [or] between two or more [s]tates [or] between a [st]ate and [c]itizens of another [s]tate [or] between [c]itizens of different [s]tates."[2]

Judicial power is "the power of a court to decide and pronounce a judgment and carry it into effect between persons and parties who bring a case before it for decision."[3] Cases and controversies are "claims or contentions of litigants brought before the courts for adjudication by regular proceedings established for the protection or enforcement of rights, or the prevention, redress, or punishment of wrongs."[4] Essentially, cases or controversies are claims that a court is able to act upon through litigation. Article III jurisprudence has developed these basic ideas into the modern doctrines of justiciability: standing, ripeness, mootness,[5] and a prohibition on federal advisory opinions.[6]

At the surface, these requirements seem to strictly prohibit federal exercise of judicial power in non-contentious or advisory hearings.[7] But conceptual problems arise when considering other generally accepted but less obvious exercises of judicial power, such as applications for naturalization, federal benefits claims, applications for criminal warrants, bankruptcy, and declaratory judgments.[8] Such proceedings are often *ex parte* or otherwise lack distinct adverse parties.[9] The source and scope of the federal judiciary's ability to exercise power over *ex parte* and other

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bribery, or other high crimes and misdemeanors, *id.* art. II § 4, the Constitution treats no criminal offense as thoroughly as treason. Article III strictly defines the specific acts of treason, provides a standard for conviction, and limits the punishments available. *Id.* art. III, § 3.

2. *Id.* art. III, § 2.

3. Muskrat v. United States, 219 U.S. 346, 356 (1911).

4. Smith v. Adams, 130 U.S. 167, 173–74 (1889).

5. Lea Brilmayer, *The Jurisprudence of Article III: Perspectives on the 'Case or Controversy' Requirement*, 93 HARV. L. REV. 297, 299 (1979).

6. *See* Letter from John Jay, James Wilson, John Blair, James Iredell, and William Paterson, Justices of the U.S. Supreme Court, to George Washington, President of the U.S..(August 8, 1793), http://founders.archives.gov/documents/Washington/05-13-02-0263; *Muskrat*, 219 U.S. at 362.

7. *See supra* notes 5–6.

8. James E. Pfander & Michael J.T. Downey, *In Search of the Probate Exception*, 67 VAND. L. REV. 1533, 1539 (2014).

9. *Id.*

noncontentious matters is the subject of some debate.[10] Neither academic treatises nor the Supreme Court have resolved these conceptual problems.

This Note focuses on a modern conflict between Article III and the application of judicial power: the Foreign Intelligence Surveillance Act of 1978 (FISA),[11] and its modern incarnation, the Foreign Intelligence Surveillance Act of 1978 Amendments Act of 2008 (FISAAA).[12] More specifically, this Note overviews the evolving role of the modern surveillance program known as Section 702[13] and analyzes the vague legal framework surrounding the surveillance program by comparing Section 702 to more familiar and generally accepted exercises of Article III power. Finally, this Note argues that previously relied upon understandings of Section 702's compliance with Article III are obsolete. Regardless of the particular understanding adopted, modern courts must clearly articulate the specific legal framework that comports with the use of Article III powers in conducting Section 702 surveillance. Recent developments have allowed litigation of individual Section 702 challenges, offering a timely and unique opportunity for the United States judiciary to both conclusively address the justifications for its role in Section 702 surveillance and to better clarify judicial powers under Article III in general.

II. BRIEF HISTORY OF FISA & SECTION 702

As the scope of government surveillance grew with the emergence of modern communications technology, the need for

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10. *Id. see also* James E. Pfander & Daniel D. Birk, *Article III Judicial Power, the Adverse Party Requirement, and Non-Contentious Jurisdiction*, 124 YALE L.J. 1346 (2015) (arguing that Article III embraces judicial power over both contested and uncontested matters).

11. 50 U.S.C. §§ 1801–1885c (2012).

12. FISA Amendments Act of 2008, Pub. L. No. 110-261, 122 Stat. 2463 (codified at 50 U.S.C. §§1812, 1881, 1881a-1881g, 1885, 1885a-1885c (2012)).

13. For a comprehensive history and analysis of both Section 702 surveillance and U.S. foreign intelligence operations in general, *see generally* Laura K. Donahue, *Bulk Metadata Collection: Statutory and Constitutional Considerations*, 37 HARV. J.L. & PUB. POL'Y 757 (2014) (outlining the history of domestic surveillance, the original enactment of FISA, and the evolution of past NSA programs in the context of bulk collection and Section 215 surveillance); *see also* Laura K. Donahue, *Section 702 and the Collection of International Telephone and Internet Content*, 38 HARV. J.L. & PUB. POL'Y 117 (2015) (discussing in great depth the evolution of Section 702 from September 2001 to 2015).

procedural and judicial safeguards also grew.[14] In the 1960s, Congress established procedural requirements for government wiretapping by passing Title III of the Omnibus Crime Control and Safe Streets Act.[15] Title III partially codified the Supreme Court's holding in *Katz v. United States,* which held that the government was required to obtain judicial authorization prior to conducting domestic surveillance.[16] But Title III did not extend to "the constitutional power of the President to obtain foreign intelligence information deemed essential to the security of the United States, or to protect national security information against foreign intelligence activities."[17] Further, in *United States v. U.S. District Court of the Eastern District of Michigan*—known as *Keith*—the Supreme Court held that the warrant requirement of the Fourth Amendment extended to domestic surveillance programs, but not necessarily to foreign intelligence programs.[18] In effect, the interception of foreign intelligence had been unregulated up until the late 1970s. But following a string of scandals—most notably the Watergate Scandal—the Senate Select Committee to Study Government Operations with Respect to Intelligence Activities (known as the

14. *See* S. REP. NO. 94-755, Book II, at 6–7 (1976) (summarizing the scope of domestic and international communications surveillance including over 250,000 letters opened by either the CIA or FBI between 1940–1970, over 300,000 persons indexed by a CIA computer system, and millions of intercepted telegrams) [hereinafter CHURCH COMMITTEE REPORT].

15. Omnibus Crime Control and Safe Streets Act of 1968, Pub. L. No. 90-351, 82 Stat. 197, 211–25 (codified as amended in scattered sections of 18 U.S.C.); *see also* Philip M. Bridwell & Jamil N. Jaffer, *Updating the Counterterrorism Toolkit: A Brief Sampling of Post-9/11 Surveillance Laws and Authorities*, *in* THE LAW OF COUNTERTERRORISM 235 (Lynne K. Zusman ed. 2011) (discussing government surveillance prior to 1978).

16. Katz v. United States, 389 U.S. 347, 356 (1967) (holding that, with few exceptions, the Fourth Amendment requires prior authorization for a wiretap under 18 U.S.C. § 2516); *see also* Omnibus Crime Control and Safe Streets Act of 1968, Pub. L. No. 90-351, 82 Stat. 197, 211–25 (establishing the procedural requirements and justification for wiretapping and electronic surveillance); CHURCH COMMITTEE REPORT, *supra* note 15, at 188 (noting that Congress enacted Title III in response to *Katz*).

17. Omnibus Crime Control and Safe Streets Act of 1968, Pub. L. No. 90-351, 82 Stat. 197, 214.

18. *See* United States v. U.S. Dist. Court [hereinafter *Keith*], 407 U.S. 297, 321–22 (1972) ("We emphasize, before concluding this opinion, the scope of our decision. As stated at the outset, this case involves only the domestic aspects of national security. We have not addressed and express no opinion as to, the issues which may be involved with respect to activities of foreign powers or their agents.'). This holding has been interpreted as suggestive of a 'Foreign Intelligence Exception' to the warrant requirement.

Church Committee) exposed a number of abusive domestic *and* foreign intelligence programs.[19] By the late 1970s, U.S. foreign intelligence programs would come under congressional regulation for the first time.

In 1978, Congress enacted the Foreign Intelligence Surveillance Act ("FISA") to alleviate (1) judicial confusion over a foreign intelligence exception to the Fourth Amendment,[20] (2) civilian concerns over intelligence abuses, and (3) the need to provide legitimate legal standards for foreign intelligence operations.[21] FISA did this in two ways: first, it established the Foreign Intelligence Surveillance Court ("FISC"), a special court consisting of eleven district court judges selected by the Chief Justice of the U.S. Supreme Court, to review applications for national security investigations; second, it established the specific process that executive agencies must follow in order to apply for and conduct such investigations without violating the rights of Americans.[22]

A. Statutory Structure

Under the traditional FISA procedure, an executive agency wanting to conduct a national security investigation must first submit

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19. *See* CHURCH COMMITTEE REPORT, *supra* note 14, at 56–83 (1976) (discussing the use of foreign intelligence agencies to investigate various domestic organizations for their political beliefs or international connections).

20. *See Keith*, 407 U.S. at 308 (requiring, when applying the Fourth Amendment in internal security matters, that there must be a balancing duty of the government to protect the domestic security while protecting individual privacy and freedom). Since *Keith* and the enactment of FISA, the Court has not had occasion to formally articulate a foreign intelligence exception. Yet, commentators and lower courts have recognized its existence. *See, e.g.* United States v. Truong Dinh Hung, 629 F.2d 908, 913 (4th Cir. 1980); United States v. Buck, 548 F.2d 871, 875 (9th Cir. 1977); United States v. Butenko, 494 F.2d 593, 605 (3d Cir. 1974); United States v. Brown, 484 F.2d 418, 426 (5th Cir. 1973).

21. *See* S. REP. NO. 95–701, at 91 (1978) ("[I]t seems that those who normally should be surveilling are afraid to act without firm legal mandate This bill provides such standards in limited circumstances More important, it represents a genuine attempt—perhaps the first attempt by Congress—to think through and to balance the citizen's competing claims to security from foreign powers, their agents and international terrorists, and to security from electronic surveillance by his own government."); *see also* United States v. Rosen, 447 F. Supp. 2d 538 (E.D. Va. 2006) (holding that when the Foreign Intelligence Surveillance Court (FISC) has probable cause to believe that the potential target of requested authorized surveillance is engaged in unlawful activities, the FISC may authorize surveillance of a U.S. person).

22. *Id.*

a FISA application for approval of both the Attorney General and FISC. Traditional FISA applications must include certain information, such as the identity of the target, the nature of the places under surveillance, the type of information sought, the means of surveillance, and the period of time surveillance is required.[23] If the Attorney General approves the application, then FISC reviews the application during *in-camera* and *ex parte* proceedings.[24] The applications usually remain classified and, if approved, remain sealed throughout most of the subsequent national security investigation. Because the classified nature of these proceedings causes a the lack of public transparency, to alleviate the appearance as a "rubber stamp" court, the judges must be drawn from seven distinct circuits, and may only serve for staggered, non-renewable terms of seven years.[25]

FISC must approve applications if there is probable cause that the target is a "foreign power" or "agent of a foreign power."[26] FISA limits such applications in several ways. No "United States person" may be targeted based on activities "protected by the [F]irst [A]mendment"[27] and all applications must follow "minimization procedures" to limit the retention or dissemination of sensitive information (except for law enforcement or foreign intelligence purposes).[28]

The procedures required by FISA applied specifically to "electronic surveillance."[29] Further, FISA required FISC approval of

23. 50 U.S.C. § 1805(c) (2012).

24. U.S. FOREIGN INTELLIGENCE SURVEILLANCE COURT R. P. 17(b).

25. 50 U.S.C. § 1830 (2012); *Foreign Intelligence Surveillance Court*, FED. JUDICIAL CTR. http://www.fjc.gov/history/home.nsf/page/courts_special_fisc.html (last visited October 1, 2016).

26. 50 U.S.C. § 1805(a) (2012).

27. *Id. see also* 50 U.S.C. § 1801(i) (' 'United States person' means a citizen of the United States, an alien lawfully admitted for permanent residence an unincorporated association a substantial number of members of which are citizens of the United States or aliens lawfully admitted for permanent residence, or a corporation which is incorporated in the United States, but does not include a corporation or an association which is a foreign power ').

28. 50 U.S.C. § 1801(h).

29. 50 U.S.C. § 1802. Electronic surveillance was specifically defined as:

> (1) the acquisition by an *electronic, mechanical, or other surveillance device of the contents of any wire or radio communication* sent by or intended to be received *by a particular, known United States person who is in the United States*, if the contents are acquired by intentionally targeting that United States person, under circumstances in which a person has

applications concerning surveillance of communications in the United States for foreign intelligence purposes, but not surveillance of communications overseas.[30]

Prior to 2001, upon approval of an application for electronic surveillance, FISC could issue orders granting or denying permission to conduct electronic surveillance, obtain business or pen register records, conduct wiretaps, and perform physical searches of buildings or persons.[31] Following the September 11th attacks, Congress provided the government—and FISC in particular—with additional surveillance powers through the USA PATRIOT Act[32]

> a reasonable expectation of privacy and a warrant would be required for law enforcement purposes;
>
> (2) the acquisition by an *electronic, mechanical, or other surveillance device of the contents of any wire communication* to or from a person in the United States, without the consent of any party thereto, *if such acquisition occurs in the United States*;
>
> (3) the intentional acquisition by an *electronic, mechanical, or other surveillance device of the contents of any radio communication*, under circumstances in which a person has a reasonable expectation of privacy and a warrant would be required for law enforcement purposes, and *if both the sender and all intended recipients are located within the United States*; or
>
> (4) the installation or use of an *electronic, mechanical, or other surveillance device in the United States for monitoring to acquire information, other than from a wire or radio communication*, under circumstances in which a person has a reasonable expectation of privacy and a warrant would be required for law enforcement purposes.

50 U.S.C. § 1801(f) (emphasis added).

30. By carefully defining electronic surveillance, Congress intentionally avoided placing limitations on overseas operations. H.R. Rep. No. 95-1283, pt. 1, at 22, 27 (1978) ("The Committee has explored the feasibility of broadening this legislation to apply overseas, but has concluded that certain problems and unique characteristics involved in overseas surveillance preclude the simple extension of this bill to overseas surveillances. ').

31. 50 U.S.C. §§ 1805(a), 1841–45, 1861–62. Originally only permitting electronic surveillance, FISA was amended between 1978–2001 to include a wider range of foreign intelligence operations.

32. Uniting and Strengthening America By Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT Act) Act of 2001, Pub. L. 107-56, 115 Stat. 272, 278–96 (2001) (codified as amended in scattered sections of 18 U.S.C and 50 U.S.C.).

and the Intelligence Reform and Terrorism Prevention Act of 2004.[33] These powers included the ability to conduct roving wiretaps, to authorize the surveillance of individuals lacking any connection to foreign powers (known as "lone wolf" terrorists), and to obtain a wider range of third party business records.[34] But the original 1978 language defining electronic surveillance increasingly limited FISA and the programs operating under its authority.[35]

Though Congress had not intended to limit the collection of overseas intelligence, the original statutory language became more restrictive due to dramatic shifts in the nature of electronic communications between 1978 and 2006.[36] In 1978 almost all transoceanic communications were satellite communications, which were considered "radio communications" under the 1978 statute.[37] Such radio communications were only subject to the FISA requirements if the surveillance targeted a U.S. person or all the targeted participants were located in the U.S.[38] But modern transoceanic telecommunications are conducted through fiber optic cables and are considered "wire communications" under the 1978 statute.[39] Such wire communications were subject to the FISA requirements if the surveillance was merely acquired in the U.S.[40] Thus, as communications technology shifted, the scope and impact of FISA expanded by requiring court orders before conducting intelligence operations on foreign targets that would have been unregulated in 1978.[41]

Drafting and submitting individualized applications for overseas intelligence gathering "slowed and in some cases prevented

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33. Intelligence Reform and Terrorism Prevention Act of 2004, Pub. L. 108-458, 118 Stat. 3638, 3742–43 (codified as amended at 50 U.S.C. § 1801 (2012)).

34. *See* Bridwell & Jaffer, *supra* note 15, at 238.

35. *See infra* notes 36-43.

36. *FISA Hearing: Hearing Before the Permanent Select Comm. on Intelligence*, 110th Cong. 37, 41 (2007) (statement of Kenneth L. Wainstein, Assistant Att'y Gen. for Nat'l Sec.) [hereinafter *FISA Hearing*].

37. *Id.* at 40.

38. *Id.*

39. *Id.* at 41.

40. Foreign Intelligence Surveillance Act of 1978, Pub. L. No. 95-511, 92 Stat. 1783 (emphasis added).

41. *FISA Hearing*, *supra* note 43, at 41 (statement of Kenneth L. Wainstein) ("This unintended expansion of FISA's scope hampered our intelligence capabilities and caused us to expend resources on obtaining court approval to conduct intelligence activities directed at foreign persons overseas Thus, considerable resources of the Executive Branch and the FISA Court were being expended on obtaining court orders to monitor the communications of terrorist suspects and other national security threats abroad. ').

the acquisition of foreign intelligence information."[42] Following the September 11th attacks, intelligence officials were desperate to amend FISA to eliminate these unintended limitations.[43]

B. FISA Amendments

In response to the unintended modern limitations on FISA, Congress enacted a series of intelligence reforms to shift the statutory focus from *how or where* communications were sent, to *whose* communications were being intercepted.[44] Congress enacted the Protect America Act of 2007,[45] amending FISA by explicitly excluding surveillance directed at individuals "reasonably believed to be located outside the United States." It also required the Attorney General and the Director of National Intelligence (DNI) to certify that certain criteria were met before requiring service providers to distribute communications to U.S. officials.[46] The Protect America Act was short lived, expiring only 180 days after its enactment.

After the Protect America Act expired,[47] Congress passed FISAAA, which provided

> [n]otwithstanding any other provision of law the Attorney General and the Director of National Intelligence may authorize jointly, for a period of up to 1 year from the effective date of authorization, the

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42. PRIVACY AND CIVIL LIBERTIES OVERSIGHT BOARD, REPORT ON THE SURVEILLANCE PROGRAM OPERATED PURSUANT TO SECTION 702 OF THE FOREIGN INTELLIGENCE SURVEILLANCE ACT 18 (2014) [hereinafter PCLOB REPORT].

43. FISA for the 21st Century: Hearing Before the S. Comm. on the Judiciary, 109th Cong. 8-9 (2006) (statement of Michael Hayden, Director, Central Intelligence Agency) ("[T]he revolution in telecommunications technology has extended the actual impact of the FISA regime far beyond what Congress could ever have anticipated in 1978 For reasons that seemed sound at the time, current statute makes a distinction between collection 'on a wire' and collection out of the air. When the law was passed, almost all local calls were on a wire and almost all long haul communications were in the air. In an age of cell phones and fiber optic cables, that has been reversed. .with powerful and unintended consequences for how NSA can lawful acquire a signal."), available at https://www.gpo.gov/fdsys/pkg/CHRG-109shrg43453/pdf/CHRG-109shrg43453.pdf.

44. Wainstein, supra note 42 ("[I]f a surveillance is directed at a person in the United States, FISA generally should apply: if a surveillance is directed at persons overseas, it should not.").

45. Protect America Act of 2007, Pub. L. No. 110-55, 121 Stat 552 (2007) (codified as amended at 50 U.S.C. 36 § 1801 et. Seq.) [hereinafter PAA].

46. *Id.*

47. *Id.*

> targeting of persons reasonably believed to be located outside the United States to acquire foreign intelligence information.[48]

Known as Section 702, this provision of FISAA permits the surveillance of overseas communications as intended by the original 1978 Act.

III. FISAA SECTION 702: STRUCTURE & SAFEGUARDS

FISAAA contains several safeguards to alleviate concerns over a perceived expansion of surveillance authority under Section 702 by providing for judicial review.[49] Most notably, FISAAA requires the Attorney General and DNI to adopt targeting and minimization procedures, and to certify to FISC, along with "any supporting affidavit, under oath and under seal," that such procedures are in place and have been either approved, submitted, or will be submitted to FISC within 30 days of any acquisition under Section 702.[50] Further, the certification must attest that the procedures are "consistent with the requirements of the [F]ourth [A]mendment."[51] FISC then reviews the certifications, along with the targeting and minimization procedures, to assess whether it satisfies the required elements and to ensure that "the targeting and minimization procedures are consistent with the requirements of [the statute] and with the [F]ourth [A]mendment."[52] If FISC finds the targeting or minimization procedures lacking, then the court must issue an order, along with a written statement of reasons, for the government to either (1) correct the identified deficiencies, or (2) cease the surveillance.[53] Thus, under FISAAA, overseas foreign

48. Foreign Intelligence Surveillance Act of 1978 Amendments Act of 2008, Pub. L. No. 110-261, 122 Stat. 2440 (2008) (codified at 50 U.S.C. § 1881a (2012)). Notably, the original definition of 'electronic surveillance' remains largely unchanged, except for a computer hacker exception to the collection of 'wire communication. 50 U.S.C. § 1801(f)(2). FISAAA simply provides for surveillance 'notwithstanding' that definition.

49. *See* 50 U.S.C. § 1881a(b) (prohibiting the targeting of any U.S. person inside or outside the U.S. including situations in which a person has a reasonable expectation of privacy and a warrant would be required under the Fourth Amendment, or where a U.S. person is 'reverse targeted' by targeting a person outside the U.S. for the actual purpose of surveilling a U.S. person).

50. 50 U.S.C. § 1881a(g)(2).

51. 50 U.S.C. § 1881a(g)(2)(A)(iv).

52. 50 U.S.C. § 1881a(i)(3)(A).

53. 50 U.S.C. § 1881a(i)(3)(B)–(C).

intelligence surveillance, which was previously unsupervised and unregulated by the 1978 statute, is now subject to judicial review.

In general, Section 702 allows the Attorney General and DNI to authorize the targeting of non-U.S. persons who are reasonably believed to be located outside the United States by compelling communications service providers to deliver foreign intelligence information.[54] Applications under Section 702 are substantially different than traditional FISA surveillance applications. While traditional applications are individualized and include specific information concerning a target,[55] Section 702 applications are *annual certifications* identifying the categories of foreign intelligence information sought, and the targeting and minimization procedures to be used,[56] leading some critics of Section 702 to compare the FISC certifications to general warrants or Writs of Assistance prohibited by the Fourth Amendment.[57]

A. Targeting Procedures

Persons targeted under Section 702 may not intentionally include U.S. persons or persons known to be in the United States.[58] A U.S. person is either a citizen of the United States, an alien lawfully admitted for permanent residence, an unincorporated association of U.S. persons, or a corporation incorporated in the United States.[59] These two rules—that a target be a non-U.S. person and reasonably believed to be located outside the U.S.— are referred to as the "foreignness requirement" for Section 702 targeting.[60] The Attorney General and DNI must submit for approval to FISC

54. PCLOB REPORT, *supra* note 49, at 20.

55. The individual application must include the identity of the specific target, facts justifying probable cause that the target is a foreign power or agent, the minimization procedures for any foreign intelligence information gathered, and a certification of the type of foreign intelligence information sought. U.S.C. §§ 1804(a), 1805(a), (c).

56. *See* PCLOB REPORT, *supra* note 49, at 26 ("Through court filings or the testimony of witnesses at hearings before the FISC, the government also submits additional information explaining how the targeting and minimization procedures will be applied and describing the operation of the program in a way that defines its scope.").

57. Megan Carpentier, *Sen. Wyden: FISA's 'General Warrants' Are Like the 'Writs of Assistance' the Founding Fathers Despised*, RAWSTORY (December 27, 2012), http://www.rawstory.com/2012/12/sen-wyden-fisas-general-warrants-are-like-the-writs-of-assistance-the-founding-fathers-despised.

targeting procedures that are "reasonably designed" to ensure that Section 702 surveillance is limited to such foreign targets, and to prevent the "intentional acquisition" of wholly domestic communications.[61]

B. *Minimization Procedures*

Section 702 minimization procedures parallel those for domestic wiretaps under Title III of the Omnibus Crime Control and Safe Streets Act[62], and are a safeguard against the acquisition, retention, and dissemination of sensitive or otherwise non-publically available electronic surveillance information.[63] With the exception of criminal evidence, such information may not be acquired, retained, or disseminated in ways that are inconsistent with foreign intelligence needs.

> [F]or example, minimization at the acquisition stage is designed to [e]nsure that the communications of non-target U.S. persons who happen to be using a FISA target's telephone, or who happen to converse with the target about non-foreign intelligence information, are not improperly disseminated. Similarly, minimization at the retention stage is intended to ensure that 'information acquired, which is not necessarily necessary for obtaining, producing, or disseminating foreign intelligence information, be destroyed where feasible.'[64]

Thus, in assessing minimization efforts, a court must determine whether intelligence officials have shown a "high regard for the right of privacy and have done all they reasonably could do to avoid unnecessary intrusion."[65]

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62. As discussed *supra* Part II, Title III was enacted in response to *Katz* and established warrant procedures for conducting domestic surveillance such as wiretaps. It requires that every order approving domestic intercepts must be conducted in such a way 'as to minimize the interception of communications not otherwise subject to interception, and limits the disclosure of such information. 18 U.S.C. § 2518. Similarly, Section 702 minimization procedures limit the acquisition and dissemination of information of US persons acquired through Section 702 surveillance.

63. 50 U.S.C. § 1881a(e).

64. United States v. Rosen, 447 F. Supp. 2d 538, 551 (2006) (quoting In re Sealed Case, 310 F. 3d 717, 731 (2002).

65. *Id.*

C. *FISC Review under Section 702 & Constitutional Concerns*

FISC's review of a Section 702 application's targeting procedures—which ensure that the surveillance will not intentionally target U.S. persons or persons within the U.S.—is limited: FISC does not hear evidence presented by the government, does not apply a probable cause standard to targeted individuals, and does not determine whether the individuals are located outside the United States.[66] Rather, FISC only determines whether the targeting procedures are reasonably designed to ensure compliance with the statute and the Fourth Amendment.[67]

FISC's review of Section 702 minimization procedures—which safeguards against the acquisition, retention, and dissemination of sensitive or otherwise non-publically available electronic surveillance information—is not as limited as that of the targeting procedures; FISC reviews the proposed minimization procedures under the same standard as those of traditional FISA applications.[68] The court must determine whether the "specific procedures" are "reasonably designed" to control the acquisition, retention, and dissemination of non-publically available U.S. person information.[69] Importantly, FISC also determines whether the proposed minimization procedures also comply with the Fourth Amendment.[70]

In evaluating Section 702 certifications, FISC considers the procedures themselves, the related affidavits of national security officials, and additional filings, responses, and sworn testimony provided by the government.[71] Just like FISC proceedings for traditional FISA applications, FISC reviews of Section 702 applications are almost exclusively ex parte.[72] Representations made

66. 50 U.S.C. §§ 1881a(i)(3)(A)–(B).

67. 50 U.S.C. §§ 1881a(i)(3)(A)–(B).

68. *See* 50 U.S.C. § 1881a(i)(2)(C) (incorporating the standards under 50 U.S.C. § 1801(h) or § 1821(4) requirement to evaluate Section 702 minimization procedures).

69. *See* 50 U.S.C. § 1881a(i)(2)(C) ("The minimization procedures adopted in accordance with subsection (e) to assess whether such procedures meet the definition of minimization procedures under section 1801(h) ").

70. 50 U.S.C. §§ 1881a(i)(3)(A)–(B).

71. 50 U.S.C. § 1881a(c).

72. As a reminder, this Note is concerned with implications of Article III. This Note does not address critics' claims of FISA as a violation of the Fourth Amendment nor the constitutionality of ex parte hearings. Interestingly, Congress recently amended FISA to allow the designation of "Amicus Curiae" to assist the court in considering issues of privacy, civil liberties, and communication

to the court are binding on the government, and incidents of noncompliance with procedures previously approved by the court must be timely reported.[73] Prior opinions of the court and the consequences of noncompliance are often treated as precedent and have informed the court's interpretation and assessment of proposed procedures.[74] In at least one instance, foreign intelligence information collected in violation of the proposed procedures was purged entirely.[75]

Overall, FISC's assessment and certification of a Section 702 application is an assessment of whether the government's procedures for the upcoming year are constitutional under the Fourth Amendment.[76] In this way, FISA Court orders are "prospective, not retrospective. That is to say, they authorize government action going forward (often for a specific period of time) that is subject to compliance with various procedural rules imposed (and administered) by the FISA Court."[77] Commentators like Professors Marty Lederman and Steve Vladeck have noted FISC's role under Section 702 as a potential violation of Article III of the United States Constitution.[78] But while previous incarnations of FISC review have

technology in the context of intelligence collection. *See* USA Freedom Act of 2015, Pub. L. No. 114-23, 129 Stat. 268, 279 (2015) (codified as amended at 50 U.S.C. § 1803). However, these 'friends of the court' are appointed by and answer to the court; they do not represent individual clients. Thus, while FISC hearings may now include non-government lawyers, Section 702 certifications are still largely non-adversarial.

73. FISC R. P. 13.

74. PCLOB REPORT, *supra* note 49, at 30.

75. Redacted, 2011 WL 10945618, at *27 (FISA Ct. Oct 3, 2011).

76. *See* PCLOB REPORT, *supra* note 49, at 81 ("FISC's mandate to ensure compliance with the Fourth Amendment is expressly enumerated in the statute "); *see also* Redacted, 2011 WL 10945618, at *5 (FISA Ct. Oct 3, 2011) (finding that in reviewing the amendments to certification under 702, "the court must determine whether the targeting and minimization procedures are consistent with the requirements of the Fourth Amendment").

77. Steve Vladeck, *Article III, Appellate Review, and the Leahy Bill: A Response to Orin Kerr*, LAW FARE (July 31, 2014), http://www.lawfareblog.com/article-iii-appellate-review-and-leahy-bill-response-orin-kerr.

78. Marty Lederman & Steve Vladeck, *The Constitutionality of a FISA 'Special Advocate,* JUST SECURITY (November 4, 2013), http://justsecurity.org/2873/fisa-special-advocate-constitution (noting that past Article III challenges to FISA have been based on the ex parte, non-adversarial nature of FISA hearings); *see also* Steve Vladeck, *The FISA Court and Article III*, 72 WASH. & LEE L. REV. 1161 (2015); *Foreign Intelligence Electronic Surveillance: Hearing on H.R. 5794, 9745, 7308, and 5632 Before the Subcomm. on Legis. of the Permanent Select Comm. on Intelligence*, 95th Cong. 224 (1978), (statement of Laurence Silberman) http://www.cnss.org/data/files/Surveillance/FISA/1970s_Cong_Hearings/C_fisa011078_part_1c.pdf (arguing the secret nature of FISA violated Article III); *but*

been *universally* upheld as constitutional, those determinations were always based on an analogy to traditional search warrants. Since federal courts routinely issue individualized search warrants without violating Article III, FISC review of targeting is similarly in compliance with Article III.[79] In contrast, Section 702 certifications are non-individualized, year-long approvals of a broad surveillance program.[80] Further still, FISC appears to preemptively determine whether or not the program comports with the Fourth Amendment before those procedures are even implemented. Finally, recent revelations concerning the scope of Section 702 surveillance and the unique role of FISC have attracted additional attention and scrutiny. Indeed, "it's not at all clear how there is *ever* an Article III case or controversy when the government files an application" under Section 702.[81] This is a question that courts must resolve independently, without reliance on the warrant analogy.

IV ARTICLE III OVERVIEW

Judicial power is limited to resolving cases and controversies. Article III of the United States Constitution states:

> The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority; to all Cases affecting Ambassadors, other public Ministers and Consuls; to all Cases of admiralty and maritime Jurisdiction; to Controversies to which the United States shall be a Party; to Controversies between two or more States; between a State and Citizens of another State; between Citizens of different States;

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see id. at 214 (statement of Philip Lacovara) (arguing that ex parte proceedings 'are familiar to our jurisprudence from the earliest days of the republic, and that federal judges entertain ex parte hearings without violating Article III because the judges actions can be challenges at some later proceeding, such as an evidentiary challenge in a criminal trial).

79. *See* United States v. Megahey, 553 F. Supp. 1180 (E.D.N.Y 1982) (finding that FISC's power to approve electronic surveillance in ex parte proceedings does not violate Article III); *see also* Vladeck, *supra* note 83 (discussing how search warrants in criminal cases do not violate Article III because they are ancillary to subsequent judicial proceedings).

80. 50 U.S.C. § 1881a (2012).

81. Vladeck, *supra* note 77.

> between Citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.[82]

The implications of this requirement are far reaching, giving rise to familiar justiciability doctrines of "ripeness," "mootness," and "standing."[83] Importantly, the case and controversy requirement restricts the power of the federal judiciary to act, prohibiting courts from considering constitutional issues outside the context of a concrete "case" or "controversy."[84]

A. *Case or Controversy Requirement*

In general, the case or controversy requirement "confine[s] the business of federal courts to questions presented in an adversary context and in a form historically viewed as capable of resolution through the judicial process."[85] An Article III case arises "when any question respecting the Constitution, treatise or laws of the United States has assumed such a form that the judicial power is capable of acting on it."[86] And under "standing" and "ripeness" doctrines, the judiciary may only determine issues "when the facts of a particular case require their resolution for a just adjudication on the merits."[87] This suggests that a conflict between adverse parties is an absolute prerequisite to the exercise of Article III power.

B. *An Uncertain Adversarial Requirement*

But courts and scholars have been unable to consistently define the extent of this adverse-party requirement or why federal courts are "allowed" to exercise judicial power in non-adverse proceedings.[88] For example, the federal judiciary routinely

82. U.S. CONST. art. III, § 2.

83. *See* Brilmayer, *supra* note 5, at 297 (discussing the theoretical underpinnings and appropriateness of justiciability rules).

84. *Id.*

85. EPA v. Massachusetts, 127 S.Ct. 1438, 1452 (2007) (quoting Flast v. Cohen, 392 U.S. 83 (1968)).

86. *In re* Summers, 325 U.S. 561, 566–67 (1945) (internal quotation omitted).

87. Colon v. Howard, 215 F.3d 227, 235 (2d Cir. 2000) (Walker, J. concurring).

88. *See* Pfander & Birk, *supra* note 10, at 1351 (citing Martin H. Redish & Andrianna D. Kastanek, *Settlement Class Actions, the Case-or-Controversy Requirement, and the Nature of the Adjudicatory Process*, 73 U. CHI. L. REV. 545,

participates in naturalization proceedings, government pension and benefits claims, criminal warrant applications, class-action certifications or settlements, and various administrative bankruptcy hearings.[89] Some scholars have argued that despite the language used in Article III jurisprudence, the case or controversy requirement allows for non-adversarial proceedings.[90] Alternatively, these powers may simply be "anomalies that have become too entrenched to question."[91] Finally, these justiciability limitations may simply be prudential, self-imposed guidelines by the judiciary designed to maximize the limited resources of the courts.[92] If this is the case, the judiciary has the discretion to ignore a lack of adverseness if doing so wouldn't threaten judicial efficiency.

In any case, whether Article III requires adversity between parties is unclear, particularly with regard to issues of national security. With the increased role of the law and courts in national security, courts have a responsibility to better articulate the source of non-adversarial judicial powers in a predominantly adversarial legal system.

The judiciary's strong language in favor of an adversarial system, and its neglect in articulating the legal foundation of non-adversarial powers, has cast doubt on these non-adverse proceedings and Article III in general. For example, Article III has drawn criticism as an "unnecessary and unnatural"[93] or

548, 552 (2006) (noting that neither courts nor scholars have devoted sustained attention to the theoretical underpinnings of the adverse-party requirement and arguing that an analysis of the foundations of the requirement had not been previously "undertaken by jurist or scholar.")).

89. *Id.*

90. *See* Pfander & Birk, *supra* note 10, at 1355 ("We suggest that the answer lies in recognizing that federal courts may constitutionally exercise not one but two kinds of judicial power: power to resolve disputes between adverse parties and power to entertain applications from parties seeking to assert, register, or claim a legal interest under federal law. The second, less familiar power, was known in Roman and civil law as 'voluntary' or 'non-contentious' jurisdiction and extended to the registration of contracts, the application for legal benefits, and the recordation of a legal status or interest.").

91. RICHARD H. FALLON, JR. ET AL. HART AND WECHSLER'S THE FEDERAL COURTS AND THE FEDERAL SYSTEM 84–85 (6th ed. 2009).

92. United States v. Windsor, 133 S. Ct. 2675 (2013) (noting that concrete adverseness is merely a prudential "matter[] of self-governance" rather than a limitation contained in Article III).

93. FALLON, ET AL. *supra* note 92, at 838-39 (citing Louis L. Jaffe, *The Citizen as Litigant in Public Actions: The Non-Hohfeldian or Ideological Plaintiff*, 116 U. PA. L. REV. 1033 (1968); Henry P. Monaghan, *Constitutional Adjudication: The Who and When*, 82 YALE L. J. 1363 (1973); Kenneth E. Scott, *Standing in the Supreme Court—A Functional Analysis*, 86 HARV. L. REV. 645 (1973); Mark V.

"countermajoritarian"[94] restriction on access to the courts. Indeed, when a court dismisses a case – either because the party has no standing, or because the dispute is not ripe, or because any remedies are now moot – laypersons and lawyers cynically view the court as using overly legalistic technicalities to avoid politically divisive issues.[95] This, critics argue, allows judges to abdicate a crucial but politically dangerous role: reviewing and resolving constitutional violations against the politically disenfranchised.[96]

But many have argued that Article III is widely misunderstood, and offers a valuable and principled limitation on federal judges' ability to opine on abstract legal issues.[97] For example, the Article III doctrines give courts the tool to avoid adjudicating a difficult matter better left for more competent or qualified decision makers, namely legislatures.[98] By requiring things like standing, they argue, Article III ensures that the party adjudicating an issue has an individual interest in the outcome and an incentive to ensure that the court hears all relevant information concerning the argument. The case or controversy requirement may also bolster the legitimacy of the judiciary by limiting a judge's

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Tushnet, *The New Law of Standing: A Plea for Abandonment*, 62 CORNELL L. REV. 663 (1977)).

94. Alexander M. Bickel, *The Least Dangerous Branch* (1962).

95. *See* Raoul Berger, *Standing to Sue in Public Actions: Is It a Constitutional Requirement?* 78 YALE L.J. 816, 839 (1969) (discussing the appropriateness of certain claims being brought in federal court).

96. *See* Brilmayer, *supra* note 5, at 301 ("[T]he courts are seen as having primary responsibility to take action when necessary to curb majoritarian excesses. ').

97. *See Rescue Army v. Municipal Court*, 331 U.S. 549, 570 n. 34 (1947) ("It has long been the Court's 'considered practice not to decide abstract, hypothetical or contingent questions or to decide any constitutional question in advance of the necessity for its decision or to formulate a rule of constitutional law broader than is required by the precise facts to which it is to be applied or to decide any constitutional question except with reference to the particular facts to which it is to be applied.'" (quoting *Federation of Labor v. McAdory*, 325 U.S. 450, 461 (1945); *Tennessee Pub. Co. v. American Nat'l Bank*, 299 U.S. 18 (1936). *But see Flast v. Cohen*, 392 U.S. 83, 95-96 (1968) (noting inconsistencies between 19th century English courts' ability to resolve abstract disputes or issue declaratory judgments and the American constitutional approach to limiting judicial resolution of cases to specific).

98. Such decision makers could be other political bodies, professional organizations, or the parties themselves. *See* Brilmayer, *supra* note 5, at 311.

ability to adjudicate any matter – or overturn any precedent – she wishes on a whim.[99]

While Article III remains largely underexplored, for better or worse, it has been interpreted as requiring, or at least favoring, an adversarial proceeding as a prerequisite to judicial action.

C. *Standard Challenge to FISA Under Article III*

Congress noticed some of the potential conflict between Article III and FISA at the outset.[100] Early critics argued that the *ex parte* nature of the proceedings violated the adversarial requirements of Article III.[101] In response, the Office of Legal Counsel ("OLC") issued an opinion coinciding with the adoption of the original 1978 statute.[102] In it, John Harmon, an attorney in the OLC for the Carter Administration, argued that the traditional FISA application process was analogous to the traditional function of approving criminal search warrants, which do not violate Article III because they are "ancillary" to future criminal proceedings.[103] According to this approach, traditional FISA applications do not violate the case or controversy requirement because – like criminal warrants – they are prerequisites for the future adjudication of an individualized case. Courts were responsive to this analogy, and FISA withstood subsequent challenges. Harmon's assessment was often articulated with approval in cases such as *United States v. Megahey,*[104] *United*

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99. *See* Brilmayer, *supra* note 5, at 304–05 (arguing that the Article III requirements, along with stare decisis, allows for consistency and stability across the judiciary).

100. *See supra* note 78.

101. *Id.*

102. *See* Foreign Intelligence Electronic Surveillance: Hearings on H.R. 5794, 9745, 7308, and 5632, Before the Subcomm. on Legis. of the Permanent Select Comm. on Intelligence, 95th Cong. 26–31 (1978) (statement of John M. Harmon, Assistant to Hon. Edward P. Boland) (opining that '[w]hile the judge's role in assessing the application is limited, we still believe he is able to exercise judgment on matters requiring a legal conclusion, thus satisfying Article III).

103. *Id.*

104. 553 F.Supp. 1180, 1197 (1982) ("Applications for electronic surveillance submitted to FISC pursuant to FISA involve concrete questions respecting the application of the Act and are in a form such that a judge is capable of acting on them, much as he might otherwise act on an ex parte application for a warrant. [t]he FISC judge is not faced with an abstract issue of law or called upon to issue an advisory opinion, but is, instead, called upon to ensure that the individuals who are targeted do not have their privacy interests invaded, except in compliance with the detailed requirements of the statute. ').

States v. Johnson,[105] *United States v. Cavanaugh*,[106] In re *Kevork*,[107] *United States v. Belfield*,[108] and In re *Sealed Case*.[109] Thus, while the Supreme Court has not taken the opportunity to consider FISA's place in Article III jurisprudence, traditional FISA surveillance based on individualized applications are fairly well established.

Section 702, however, is critically different in a number of ways. First, while traditional FISA applications rarely lead to criminal proceedings, [110] hearings concerning Section 702 evidence are even rarer because there is no statutory requirement to notify a criminal defendant that Section 702 evidence is being used against him.[111] Thus, traditional FISA applications' ancillary connection to criminal warrants is virtually nonexistent in Section 702 requests.

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105. 952 F.2d 565 (1st Cir. 1991), *cert. denied*, 506 U.S. 816 (1992) (holding that the FISA process does not violate the Fourth Amendment).

106. 807 F.2d 787 (9th Cir. 1987) ("The FISA court does not violate article III.").

107. 634 F. Supp. 1002, 1014 (S.D. Cal. 1985) ("The ex parte nature of FISC proceedings is also consistent with Article III. Government applications for warrants are always ex parte. Authorizations under Title III are issued on an ex parte basis. The FISA court retains all the inherent powers that any court has when considering a warrant.").

108. 692 F.2d 141, 148 (D.C. Cir. 1982) (upholding FISA's non-adversarial scheme, and approving of the role of FISC by noting that "the privacy rights of individuals are ensured not through mandatory disclosure, but through its provisions for in-depth oversight of FISA surveillance by all three branches of government").

109. 310 F.3d 717, 732 n.19 (FISA Ct. Rev. 2002) ("In light of *Morrison v. Olson* and *Mistretta v. United States* we do not think there is much left to an argument that the statutory responsibilities of the FISA court are inconsistent with Article III case and controversy responsibilities of federal judges [or] because of the secret, non-adversary process.").

110. *Drones and the War on Terror: When Can the U.S. Target Alleged American Terrorists Overseas? Hearing Before the H. Comm. on the Judiciary*, 113th Cong. 31 (2013) (statement of Robert Chesney), http://www.brookings.edu/~/media/research/files/testimony/2013/02/27-drones-chesney/robert-chesney-testimony_house-committee-on-judiciary_-02272013.pdf ("In theory, the FISC avoids this [Article III] problem for the same reason that ordinary search warrant proceedings do: there may well come a point down the line at which the warrant may be contested in an adversarial setting. This is, however, a razor-thin legal fiction.").

111. *See e.g.* United States v. Isa, 923 F.2d 1300, 1305 (8th Cir. 1991) (information obtained from FISA surveillance used as evidence in state murder prosecution); 50 U.S.C. § 1806(c) (2012); ANDREW NOLAN, RICHARD M. THOMPSON II, & VIVIAN S. CHU, CONG. RESEARCH SERV. R43260, INTRODUCING A PUBLIC ADVOCATE INTO THE FOREIGN INTELLIGENCE SURVEILLANCE ACT'S COURTS: SELECT LEGAL ISSUES,18 (2013) ("Targets of FISA orders, on the other hand, are generally not notified of the surveillance, and have no statutory method of contesting their legality or requesting a return of the things taken.").

Second, Section 702 applications are speculative, non-individualized, and look nothing like a warrant.[112] While warrants investigate a particular individual's past behavior, Section 702 applications are forward looking, and concern annual procedures for an entire surveillance program. Thus Section 702's unique scheme places considerable strain on the warrant analogy, upon which the above opinions affirming pre-2008 FISA applications relied.[113] Third, and perhaps most importantly, while pre-2008 FISA challenges concerned a potential Article III conflict about the non-adversarial, *ex parte* nature of the hearings, Section 702 seems to implicate another Article III doctrine altogether: the prohibition against advisory opinions. Courts have noted that it "is well known [that] the federal courts established pursuant to Article III of the Constitution do not render advisory opinions."[114] This prohibition on advisory opinions is perhaps the most under examined threat to Section 702, and one future courts will undoubtedly have to resolve.

D. *The Advisory Opinion Problem*

"[T]he oldest and most consistent thread in the federal law of justiciability is that the federal courts will not give advisory opinions."[115] Famously, in 1793, President Washington wrote a letter to the Justices of the Supreme Court requesting their opinion on the ongoing neutrality crisis between the United States and the warring nations of England and France.[116] On August 8, 1793, concerned about maintaining "the Lines of Separation drawn by the Constitution" and the Justices' role as "Judges of a court of last Resort," the Justices declined to give an advisory opinion.[117] This has since been interpreted as evidence of a constitutional bar on

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112. *See* Lederman & Vladeck, *supra* note 78 (discussing the 702 warrant process and its non-individualized and general nature).

113. *Id.*

114. United Pub. Workers of Am. v. Mitchell, 330 U.S. 75, 89 (1947).

115. Flast v. Cohen, 392 U.S. 83, 96 (1968) (quoting CHARLES ALAN WRIGHT, FEDERAL COURTS 34 (1963)).

116. William R. Casto, *The Early Supreme Court Justices' Most Significant Opinion*, 29 OHIO N.U. L. REV. 173, 178–80 (2002).

117. *See* Letter, *supra* note 6 (the Justices declined to issue an advisory opinion). *But see* Casto, *supra* note 116, at 192–95 (suggesting that the practice had been to issue advisory opinions in both weighty and mundane matters, in both English and American courts in the late 18th century). Casto convincingly argues that, though modern courts interpret it as such, the 1793 letter was never intended as an absolute bar on advisory opinions. *Id.* Indeed, many Justices, including Chief Justice Jay, wrote several advisory opinions after 1793. *Id.*

advisory opinions.[118] Modern Article III courts cannot give opinions in the nature of advice on legislative or executive action, the argument goes, because Article III *itself* prohibits the consideration of "abstract" or "unfocused" questions removed from the disposition at issue.[119]

> [T]he implicit policies embodied in Article III, and not history alone, impose the rule against advisory opinions on federal courts reflect[ing] the complementary constitutional considerations expressed by the justiciability doctrine: Federal judicial power is limited to those disputes which confine federal courts to a rule consistent with a system of separated powers and which are traditionally thought to be capable of resolution through the judicial process.[120]

Critics of the current scheme argue that "FISC's review of the procedures is nothing more than an abstract assessment" of surveillance in violation of Article III's ban on advisory opinions.[121] Indeed, under Section 702, FISC must determine whether the proposed electronic surveillance as provided for in the targeting and minimization procedures proposed by the intelligence agencies complies with the Fourth Amendment, and must issue a written

118. *See* Muskrat v. United States, 219 U.S. 346, 362 (1911) (holding that the case or controversy requirement does not allow the Court to give opinions 'in the nature of advice concerning legislative action,—a function never conferred upon it by the Constitution, and against the exercise of which this Court has steadily set its face from the beginning"); United States v. Fruehauf, 365 U.S. 146, 157 (1961) ("Such [advisory] opinions, such advance expressions of legal judgment upon issues which remain unfocused because they are not pressed before the Court with that clear concreteness provided when a question emerges precisely framed and necessary for decision from a clash of adversary argument exploring every aspect of a multifaceted situation embracing conflicting and demanding interests, we have consistently refused to give.").

119. *Fruehauf*, 365 U.S. at 157 (holding that the Court could not regard an issue "posed, in its most evidently abstract form as other than a request for an advisory opinion, which are prohibited).

120. *Flast*, 392 U.S. at 96–97.

121. *See* Memorandum in Support of Motion for Summary Judgment at 49, Amnesty Int'l USA v. McConnell, Case No. 08-cv-06259 (JKG) (Sept. 12, 2008) (stating that it is "nothing more than an abstract assessment of the general rules" that would govern assessment of a surveillance program started entirely by the Executive Branch).

opinion explaining the reasons why they do or do not.[122] Since Article III purports to prohibit advice on a legislative or executive action, FISC's preemptive certification of the targeting or minimization procedures adopted by the NSA, FBI or CIA as complying with the requirements of FISAAA and the Fourth Amendment is questionable.

E. Potential Solutions

First, with regard to the case and controversy requirement, the courts should clarify that the government's submission of its application for certification creates a case or controversy under the laws of the United States in a form that judicial power is capable of acting on it.[123] The application *itself* is sufficient to create an Article III case or controversy. That it is decidedly non-adversarial is of little concern to Article III, lest other non-adversarial judicial powers be invalidated. Perhaps, as suggested by *Fruehauf,* Article III only prohibits advance expressions of opinion "which remain unfocused because they are not pressed before the Court with that clear concreteness provided" by the adversarial system.[124] Indeed, while FISC review of Section 702 certifications is non-adversarial and is "limited" to reviewing the targeting and minimization procedures (but not probable cause or individuals targeted), it is focused and robust in other ways.[125] FISC reviews the procedures themselves,[126] the core sets of documents implementing the procedures —including affidavits from foreign intelligence officers, supplemental reports, and notifications of noncompliance[127] —as well as communications *actually acquired.*[128] Thus, FISC is not reviewing Section 702 as an abstract question divorced from real-world facts. Rather, FISC approves Section 702 applications based on sworn affidavits of intelligence officers and *actual* surveillance

122. 50 U.S.C. § 1881a(i)(3)(A)–(C). The requirement to issue an opinion for all orders approving Section 702 certifications is unique to Section 702.

123. *See* U.S. Const. art. III § 2 (Article III prohibits courts from considering constitutional issues outside of a case or controversy).

124. *Fruehauf,* 365 U.S. at 157.

125. PCLOB REPORT, *supra* note 49, at 25.

126. 50 U.S.C. §§ 1881a(d)(2), (e)(2), (i)(1)(A), (i)(2)(C). Notably FISC review of Section 702 minimization procedures is conducted under the same standard as traditional FISA minimization procedures, which has consistently been upheld.

127. PCLOB REPORT, *supra* note 49, at 28–30. These documents further inform FISC regarding how the government is *actually* applying the procedures.

128. Redacted, 2011 WL 10945618, at *9 (FISA Ct. Oct. 3, 2011).

conducted, and it expects to be fully, accurately, and timely informed of the implementation of the proposed procedures.[129]

Further, Article III may only prohibit advisory opinions that would not traditionally be supported by a historical understanding of a separation of powers. Indeed, as noted above, the ban on advisory opinions is traced back to the 1793 letter from Chief Justice Jay, which was famously concerned with maintaining "the Lines of Separation drawn by the Constitution between the three Departments of Government."[130] The jurisprudence on advisory opinions similarly notes that Article III power must be "consistent with a system of separated powers and which are traditionally thought to be capable of resolution through the judicial process."[131] Paradoxically, the very Justices who imposed the prohibition on advisory opinions—as well as representatives in the Executive and Legislative branches—presumed that Article III courts had the power to hear warrant proceedings and to issue certifications on concrete matters of national security. As early as 1791, warrant proceedings to enforce an excise tax on whiskey could be heard by "any court of the United States."[132] This tax eventually resulted in a popular revolt in western Pennsylvania, known as the Whiskey Rebellion. President Washington called upon the Militia Act of 1792 to raise the forces necessary to suppress the rebellion. But under the statute, a federal judge had to first certify that local authorities could not enforce the law.[133] On August 4, 1794, almost exactly a year *after* the letter purporting to ban advisory opinions, Justice Wilson submitted an opinion to the President that the "[l]aws of the United States are opposed, and the Execution thereof obstructed by Combinations too powerful to be suppressed by the ordinary Course of judicial Proceedings, or by the Powers vested in the Marshal of that District."[134]

Because Justice Wilson's review was not that of an abstract assessment question divorced from real-world facts, it was likely a

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129. PCLOB REPORT, *supra* note 49, at 30–31.

130. *See* Letter, *supra* note 6 (stating that the lines of separation between bodies of government 'afford strong arguments against the [p]ropriety' of issuing advisory opinions).

131. Flast v. Cohen, 392 U.S. 83, 97 (1968).

132. An Act Repealing, After the Last Day of June Next, the Duties Heretofore Laid Upon Distilled Spirits Imported from Abroad, and Laying Others in Their Stead; and also upon Spirits Distilled Within the United States, and for Appropriating the Same, ch. 15, §32, 1 Stat. 199–207 (1791).

133. An Act to provide for calling forth the Militia to execute the laws of the Union, suppress insurrections, and repel invasion, 1 Stat. 264–65 (May 2, 1792).

134. Letter from Justice Wilson to President Washington (August 4, 1794).

constitutional exercise of non-adversarial Article III power. So too is FISC's review of Section 702. Indeed, though it is initially unclear why FISC should be able to approve of the constitutionality of an entire surveillance program in light of a categorical ban on advisory opinions, the jurisprudence and historic use of non-adversarial Article III power seems to allow for Section 702's certification process.

V RECENT DEVELOPMENTS

Coupled with increased declassification of documents and media scrutiny following the Snowden leaks,[135] the recent PCLOB public report on the role of FISC and 702 reveal a more extensive program than previously understood. With increased attention, courts have seen challenges to Section 702 in and out of court.

A. Section 702 Litigation

Ironically, due to the classified nature of the foreign intelligence information collected and retained, plaintiffs lacked standing to challenge Section 702 surveillance until recently.[136] However, following *Clapper*, the DOJ began notifying defendants when evidence against them was acquired or derived from Section 702 surveillance. Recent criminal cases have asserted Fourth Amendment challenges to Section 702.[137] Thus, parties with standing are now challenging Section 702 under many of the grounds noted above.[138] Unfortunately, the government is

135. This article, though it discusses similar subject matter, takes no position on the leak of classified documents or the consequences of the leak.

136. Clapper v. Amnesty Int'l USA, 133 S.Ct. 1138, 1148 (2013) (holding that plaintiffs, a coalition of attorneys, human rights organizations, and media organizations lacked standing because they could not prove their communications were collected, and it was "highly speculative that the Government will decide to target the communications of non-U.S. persons with whom [the organizations] communicate").

137. United States v. Muhtorov, No. 12-cv-00033-JLK-1 (D. Colo. Jan. 1, 2014), Ecf No. 520; *see also* United States v. Hasbajrami, No. 11-cv-00623 (E.D.N.Y Feb. 24, 2014) Ecf No. 65; United States v. Mihalik No. 11-cv-00833 (S.D.Cal. Aug. 29, 2011); United States v. Mohamud, 941 F. Supp.2d 1363 (D.Or. 2013). These defendants received belated notices of surveillance and are challenging both the evidence collected and the FISA program as a whole.

138. Defendant's Motion to Suppress Evidence Obtained or Derived from Surveillance Under the FISA Amendments Act and Motion for Discovery, United States v. Muhtorov, No. 12-cr-00033-JLK-1 (D. Colo. Jan. 29, 2014) ("The FAA violates Article III because it authorizes the FISC to issue mass acquisition orders

responding to these suits with the same analogies to criminal warrants it successfully used in the Harmon OLC Opinion and *In re Sealed Case*. But as noted, these successful defenses concerned traditional FISA applications. However, Section 702 is materially distinct from traditional FISA applications. Since DOJ only just started notifying 702 defendants, these cases are unlikely to go away. Over the next several years, district courts and courts of appeals will hear Section 702 challenges. It is unlikely that the warrant analogy will hold up.

B. Judicial Opportunities

Perhaps in an effort to protect the government's undefeated record, or to shelter Section 702 surveillance from further scrutiny, courts have been hesitant to honestly address the obvious differences in Section 702, and instead relied upon pre-2008 case law. Reliance on such case law is insufficient and unwise. Because Section 702 surveillance is easily distinguishable from traditional FISA orders, most recent case law is fundamentally flawed and vulnerable to reversal. Not only is Section 702 a complex and controversial program deserving of its own treatment, but it allows judicial oversight in a surveillance program that was unregulated by the 1978 law. By relying on flawed analogies, courts are allowing clear defects in the legal architecture that threaten to undermine the entire scheme. Though electronic collection of foreign intelligence information is at an all-time high, so too is judicial oversight of such surveillance. District Courts should not shy away from the differences of 702 surveillance, instead they should embrace them and give an honest assessment of Section 702's Article III challenges. In doing so, the judiciary has an opportunity to better articulate the role that Article III plays in defining the power of the judiciary, and specifically the source and nature of non-adversarial exercises of power.

VI. CONCLUSION

Since September 11th, the United States has adopted both new techniques and multiple surveillance programs that are a source of controversy in contemporary politics. Because specific details of

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in the absence of any case or controversy and requires the court to review the legality and constitutionality of the government's programmatic procedures in the abstract.").

these programs can be shrouded in secrecy, the legal framework for the programs is often mysterious as well. Recent congressional debates surrounding renewal of the USA PATRIOT Act have dominated news cycles, however, relatively little attention has been paid to a broader and more fundamental underlying issue: the role of the judiciary in certifying and approving surveillance under Section 702.[139] Section 702 of the FISAAA implicates important Article III doctrines of justiciability, standing, and adversity.

Ultimately, FISA surveillance will be challenged on whether it truly comports with the Fourth Amendment. But the more overlooked, and perhaps more interesting, question, is whether it comports with the case or controversy requirement of Article III. This note has argued that it likely does, but that due to the classified and politically volatile nature of the program, insufficient attention has been given to FISC's role in approving surveillance under Section 702. Given the new details concerning FISC's role in Section 702 surveillance, the judiciary should take the opportunity to provide clarity and stability to the legal and constitutional justifications for FISC's role under Section 702, and to Article III in general.

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139. While the USA PATRIOT Act expired on June 1, 2015, many of the programs were reformed and restored by the passage of the USA Freedom Act, Pub. L. No. 114-23, 129 Stat. 268 (2015). Importantly, the USA Freedom Act had little substantive effect on FISC's role in certifying targeting and minimization procedures under Section 702.

Disproportionate Sentencing Guideline Recommendations in Fraud-on-the-Market

Rachel Mathisen*

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I. INTRODUCTION

One of the goals in enacting the original Federal Sentencing Guidelines was to correct the apparent discrepancy in sentence severity between white-collar and other nonviolent criminals.[1] The U.S. Sentencing Commission believed that the Guidelines' objectives would be best served by imposing "short but certain terms

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1. S. REP. NO. 98-225, at 77 (1984), *as reprinted in* 1984 U.S.C.C.A.N. 3182; Stephen Breyer, *The Federal Sentencing Guidelines and the Key Compromises Upon Which They Rest*, 17 HOFSTRA L. REV. 1, 20 (1988); U.S. SENTENCING COMM'N, SUPPLEMENTARY REPORT ON THE INITIAL SENTENCING GUIDELINES AND POLICY STATEMENTS 21–26 (1987).

of confinement for many white-collar offenders "[2]

Presently, however, the Guidelines recommend sentences for high-loss securities frauds that are "patently absurd on their face."[3] A first time offender charged with a high loss securities fraud could face life in prison without the possibility of parole. For perspective, the average murder sentence is nineteen years. It is no wonder that judges routinely use their discretion to depart downward from the Guidelines' minimum recommendation.[4]

To understand why the Guidelines recommend such excessive sentences for high-loss securities frauds, it is first important to have a general understanding of how the Guidelines work. Because the goal of the Guidelines is to provide the most objective sentence possible, the Guidelines calculate a Specific Offense Level by adding a Base Offense Level, specific to each type of offense, with Specific Offense Characteristics (SOCs), which either mitigate or increase the sentence length depending on the individual's specific conduct or characteristics. Once the court has calculated the Specific Offense Level, the court then looks up the corresponding sentencing range on the Sentencing Table. As one would expect, a higher Specific Offense Level corresponds to a longer sentencing range. Therefore, the sentencing range is almost entirely determined by how many and which SOCs apply.

Economic crimes are calculated under § 2B1.1, which currently provides nineteen SOCs, including a loss table with up to thirty offense level increases and level enhancements for harming a certain numbers of victims, violations of securities or commodities law, jeopardizing the solvency of a financial institution, and using

2. Breyer, *supra* note 1, at 20.

3. United States v. Adelson, 441 F. Supp. 2d 506, 515 (S.D.N.Y 2006).

4. Judges have always been allowed to depart from the Guidelines' recommendation where the recommendation is unreasonable. *See* Frank O. Bowman III, *The 2001 Federal Economic Crime Sentencing Reforms: An Analysis and Legislative History*, 35 IND. L. REV. 5, 39 (2001) (need parenthetical). In 2005, the Supreme Court ruled that mandatory guidelines were unconstitutional and made the Guidelines discretionary. United States v. Booker, 543 U.S. 220, 227 (2005). Judges can depart if they determine that the Guidelines do not accurately assess the sentence in the particular case. Peugh v. United States, 133 S. Ct. 2072, 2089 (2013). Judges might also be able to depart from the Guidelines because they disagree with the policy behind the recommendation in the guideline. *See* Kimbrough v. United States, 552 U.S. 85, 109–10 (2007) (finding that a federal district court does not abuse its discretion by concluding that Sentencing Guidelines' crack cocaine/powder cocaine disparity yields sentence 'greater than necessary' to achieve sentencing statute's objectives in a particular case).

sophisticated means.[5] For defendants charged with high loss fraud, offense levels increase logarithmically not only because the significant increase in levels provided by the loss table, but also because many of the SOCs, especially loss, correlate strongly with one another.[6]

This exponential effect is especially enormous in a branch of securities fraud, commonly referred to as fraud-on-the market, where a defendant fraudulently inflates or deflates the value of a publicly traded security or commodity or submits false information in a public filing with the SEC; the Bernie Ebbers WorldCom disaster is a notorious example of fraud-on-the-market.[7] Because several of the § 2B1.1 SOCs are automatically engaged when the individual commits securities fraud and because these offenses sometimes involve billions of dollars in losses, the Guidelines lead to extremely long prison sentences. For example, an officer of a publicly traded company convicted of securities fraud faces a Guideline sentence of life in prison without parole in virtually every case.[8] Unfortunately, judicial discretion does not resolve the problem because it routinely leads to drastically dissimilar sentences for similarly situated defendants.[9]

Recognizing this enormous problem, the U.S. Sentencing Commission proposed amendments to § 2B1.1 in January 2015.[10] Specifically, the Sentencing Commission initially proposed changing the loss calculation specific to fraud-on-the-market offenses from loss to gain.[11] But when faced with opposition from the Department

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5. U.S. SENTENCING COMM'N, GUIDELINES MANUAL § 2B1.1(b) (2014) [hereinafter USSG 2014].

6. *See infra* Part II.B (discussing the logarithmic effect on sentence length caused by overlapping SOCs).

7. *See infra* Part II.A.1 (discussing United States v. Ebbers, 458 F.3d 110 (2d Cir. 2006)).

8. *See infra* Part II; Frank O. Bowman III, *Sentencing High-Loss Corporate Insider Frauds After* Booker, 20 FED. SENT'G REP. 167, 170 (2008) (explaining that the cumulative effect of the SOCs and loss table is especially egregious for high-loss corporate frauds); United States v. Parris, 573 F. Supp. 2d 744, 745 (E.D.N.Y 2008) ("[W]e now have an advisory [G]uidelines regime where any officer or director of virtually any public corporation who has committed securities fraud will be confronted with a [G]uidelines calculation either calling for or approaching lifetime imprisonment.").

9. *See infra* Part II (citing to cases in which similarly situated defendants were given extremely different sentences and reviewing statistical data evidencing the frequency and extent to which judges depart from the Guidelines).

10. Notice of Proposed Amendments to the Sentencing Guidelines, 80 Fed. Reg. 2570 (Jan. 16, 2015).

11. *Id.* at 84–88.

of Justice, the Commission backpedaled and made only modest changes to the loss calculation in the finalized amendments.[12] These modest changes are not designed to lessen the disproportionate sentences for fraud-on-the-market offenders.[13]

Because the Guidelines recommend draconian sentences for high-loss fraud-on-the-market offenses and judges regularly depart downward, the current Guidelines do not provide meaningful or reasonable sentencing recommendations in these cases. The proposed amendments fail to address the underlying problems that cause disproportionate sentences. If the problems inherent in the loss calculation, loss table, and the cumulative effect of overlapping SOCs for fraud-on-the-market offense are not addressed, the Guidelines will continue to recommend disproportionate sentences and are in danger of irrelevancy.

Part I explains the current problems with the sentencing calculation for fraud-on-the-market offenses. Part II provides evidence of the Guideline's flaws in practice. Part III outlines the initial draft amendments and explains why the Commission ultimately rejected them in favor of a more modest approach. Part IV proposes possible solutions to the problems in the Guidelines and addresses why these solutions have not gone into effect.

II. FRAUD-ON-THE-MARKET UNDER THE CURRENT § 2B1.1 GUIDELINE AND ITS PROBLEMS

Since 1989, several amendments to the Guidelines have led to longer sentences for fraud crimes in general.[14] In the context of fraud-on-the-market in particular, these amendments have been

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12. U.S. SENTENCING COMM'N, AMENDMENTS TO THE SENTENCING GUIDELINES 12–14 (Apr. 30, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/reader-friendly-amendments/20150430_RF_Amendments.pdf [hereinafter AMENDMENTS TO THE SENTENCING GUIDELINES].

13. *See infra* Part III (explaining that the proposed amendment did not address the loss calculation or cumulative SOCs, the two reasons for disproportionate sentences in securities and fraud cases).

14. *See* Frank O. Bowman III, Pour encourager les autres? *The Curious History and Distressing Implications of the Criminal Provisions of the Sarbanes-Oxley Act and the Sentencing Guidelines Amendments That Followed,* 1 OHIO ST. J. CRIM. L. 373, 389 (2004) (noting that the Commission amended the Guidelines several times since the first Guidelines in 1989; these amendments progressively led to longer sentencing recommendations for white-collar offenders); *see also infra* Part II (explaining that data shows that the recommendation has increased for fraud offenses).

disastrous. The disproportionately long sentences for fraud-on-the-market offenses not only stem from the loss table and the interactions between SOCs but also result from the method for calculating loss for fraud-on-the-market offenses.

The following section first explains the loss calculation for fraud-on-the-market offenses and how it increases sentencing length while inadequately addressing causation and culpability. Next, the section explains the role of SOCs in disproportionately long sentences for fraud-on-the-market offenses.

A. The Loss Calculation for Fraud-on-the-Market

What constitutes a "loss" in fraud-on-the-market cases "is a critical determinant of the length of a defendant's sentence"[15] and often "the single most important factor in the application of the Sentencing Guidelines" because it provides the greatest number of offense level increases in § 2B1.1.[16] The rationale for this is that loss is used as a proxy for culpability[17]—it attempts to quantify the harm that the defendant caused and provide for longer sentencing based on economic loss.

Under § 2B1.1, loss is "the reasonably foreseeable pecuniary harm that resulted from the offense."[18] The goal of this definition was "to make loss a better proxy measurement of the defendant's guilty mind than it had been under the former definition" by defining it in terms of causation.[19] The definition reflects the belief that punishment "should be based only on the defendant's conduct and the consequences that causally stem from it."[20] But proving that the crime caused the loss in a fraud-on-the-market case creates a unique difficulty not present in other fraud cases.

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15. United States v. Rutkoske, 506 F.3d 170, 179 (2d Cir. 2007); *see also* Scotland Duncan, *Recalculating 'Loss' in Securities Fraud*, 3 HARV. BUS. L. REV. 257, 258 (2013) (analyzing the impact of loss calculations on the length of sentences in securities and commodities fraud cases).

16. Peter J. Henning, *White Collar Crime Sentences After* Booker: *Was the Sentencing of Bernie Ebbers Too Harsh?*, 37 MCGEORGE L. REV. 757, 767 (2006).

17. *See* Bowman, *supra* note 4, at 39 ("[S]tealing more is worse than stealing less and merits greater punishment, not only because a larger loss inflicts a greater harm, but also because one who desires to inflict a large harm is customarily thought to have a more reprehensible condition of mind than one who desires to inflict a small one. To this extent, actual loss is not a bad proxy for mental state.").

18. U.S. SENTENCING COMM'N, GUIDELINES MANUAL § 2B1.1 note 2(A)(i) (2001) [hereinafter USSG 2001].

19. Bowman, *supra* note 4, at 41.

20. Mark Harris & Anna Kaminska, *Defending the White-Collar Case at Sentencing*, 20 FED. SENT'G REP. 153, 156 (2008).

Typical common law fraud cases involve "face-to-face transactions, [where] the inquiry into an investor's reliance upon information is into the subjective pricing of that information by that investor."[21] In contrast, in securities fraud cases,

> the market is interposed between seller and buyer and, ideally, transmits information to the investor in the processed form of a market price. Thus the market is performing a substantial part of the valuation process performed by the investor in a face-to-face transaction. The market is acting as the unpaid agent of the investor, informing him that given all the information available to it, the value of the stock is worth the market price.[22]

This complicates proving causation both at the individual investor level—did the investor actually rely on the misrepresentation—and at the market level—was the change in market price actually caused by the misrepresentation. Until recently, the Guidelines did not reflect the inherent differences between calculating loss in common law fraud cases and fraud-on-the-market cases.[23] In fact, the Guidelines did not address how to calculate loss in fraud-on-the-market cases at all.[24] Instead the Guidelines gave the general guidance that a "court need only make a reasonable estimate of the loss based on available information" including factors like fair market value.[25]

Without specific guidance from the Guidelines, courts dealing with the inherent problems of calculating loss for fraud-on-the-market offenses developed two very different methods: the Market-Adjusted Method (MAM), which does not consider external

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21. Basic Inc. v. Levinson, 485 U.S. 224, 244 (1988) (quoting *In re* LTV Sec. Lit. 88 F.R.D. 134, 143 (N.D. Tex. 1980)).

22. *Id.*

23. *See* U.S. SENTENCING COMM'N, GUIDELINES MANUAL § 2B1.1 (2011) (failing to explain how to calculate loss for fraud-on-the-market offenses) [hereinafter USSG 2011].

24. *Compare* USSG 2011, *supra* note 22, § 2B1.1, *with* U.S. SENTENCING COMM'N, GUIDELINES MANUAL § 2B1.1 note 3(F)(ix) (2012) [hereinafter USSG 2012]; *see also* Duncan, *supra* note 14, at 258–59 ("Until recently, the Guidelines did not expressly provide for any method of loss calculation that a court must use in securities or commodities cases. ').

25. USSG 2011, *supra* note 22, § 2B1.1 note 3(C).

market forces when calculating changes in the value of a security,[26] and the Modified Rescissory Method (MRM), which multiplies the number of harmed shares by the difference between the average stock price during the fraud and the average stock price after disclosure.[27]

1. The Market-Adjusted Method (MAM)

Before the 2012 amendment specifically provided for a calculation, the Second,[28] Fifth,[29] and Tenth[30] Circuits all adopted the Market-Adjusted Method (MAM). Following the Supreme Court's rationale for civil securities fraud in *Dura Pharmaceuticals*,[31] each of these circuit courts "recognized that 'a loss calculation involving publicly traded stock' that fails 'to distinguish between the effects of the alleged misconduct and the effects of general market conditions is inherently flawed and thus unreasonable.'"[32] The general market conditions that may vary the

26. *See, e.g.* Duncan, *supra* note 14, at 263 (explaining the Market-Adjusted Method calculation).

27. *See, e.g.* Duncan, *supra* note 14, at 261 (explaining the Modified Rescissory Method calculation).

28. *See, e.g.* United States v. Rutkoske, 506 F.3d 170, 179 (2d Cir. 2007) ("In such cases, '[l]osses from causes other than the fraud must be excluded from the loss calculation. (quoting United States v. Ebbers, 458 F.3d 110, 128 (2d Cir. 2006))).

29. *See, e.g.* United States v. Olis, 429 F.3d 540, 546 (5th Cir. 2005) ("District courts must take a 'realistic, economic approach to determine what losses the defendant truly caused or intended to cause.'" (quoting United States v. W. Coast Aluminum Heat Treating Co. 265 F.3d 986, 991 (9th Cir. 2001))).

30. *See, e.g.* United States v. Nacchio, 573 F.3d 1062, 1078–79 (10th Cir. 2009) (explaining the importance of "examin[ing] the movement of a stock's price after the relevant information is made public in order to determine the proper measure of the illicit profit").

31. Dura Pharm. Inc. v. Broudo, 544 U.S. 336, 337 (2005). The Court rejected the Ninth Circuit's holding that civil "plaintiffs need only establish, *i.e.* prove, that the price *on the date of purchase* was inflated because of the misrepresentation." *Id.* at 342 (internal quotations removed). Instead, district courts must consider "the tangle of factors affecting [stock] price' in calculating the economic loss and loss causation in civil securities fraud cases. *Id.* at 343. The Court based its reasoning in tort law's proximate causation requirement and noted, "the statute expressly imposes on plaintiffs the burden of proving that the defendant's misrepresentations caused the loss for which the plaintiff seeks to recover." *Id.* at 345–46.

32. Duncan, *supra* note 14, at 262–63 (quoting Brief for Charles F. Dolan et al. as Amici Curiae in Support of Petitioners at 9, Rigas v. United States, No. 09-1456, 2010 WL 2665558); *see also* Movitz v. First Nat'l Bank of Chicago, 148 F.3d 760, 763 (7th Cir. 1998) (applying MAM in a civil fraud context because

price of shares include "changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events."[33]

Applying the Supreme Court's rationale to criminal sentencing, the Second Circuit in *U.S. v. Ebbers*[34] rejected the District Court's loss calculation, which used the difference between the WorldCom stock price from a random day during the fraud and the stock price from a random day after the disclosure of the fraud.[35] Instead, the Second Circuit insisted "[t]he loss must be the result of the fraud," and instructed that "[l]osses from causes other than the fraud must be excluded from the loss calculation."[36] The loss in WorldCom stock price could have been attributable to "(1) planned sharp reductions in capital expenditures, (2) lay-offs affecting 17,000 employees, (3) the abandonment of non-core businesses, and (4) the deferral or elimination of dividends."[37] These factors may have attributed to up to thirty-six percent of the total calculated loss.[38]

Although MAM rightfully seeks to hold a defendant responsible only for losses caused by the defendant's fraud, it might be difficult, if not impossible, to actually implement.[39] Even though MAM aims to tighten the causal link between the crime and the loss, it is uncertain whether or not an extrinsic factor caused the change in stock value and, if so, how much change it caused. Because of this uncertainty, many circuits rejected this approach and instead followed the Modified Rescissory Method (MRM).[40] This circuit split created inconsistencies in the length of sentences for fraud-on-the-market offenses.

'[t]o hold the defendant liable for [loss wholly beyond the defendant's control] would produce overdeterrence by making him an insurer against conditions outside his control").

33. *Dura Pharm.* 544 U.S. at 343.

34. United States v. Ebbers, 458 F.3d 110, 126–28 (2d Cir. 2006).

35. *Id.* at 126; *see also* Transcript of Sentencing Hearing at 24–26, 113–15, United States v. Ebbers, 2005 WL 6016053 (S.D.N.Y 2005) (No. 02CR1144), (adopting the probation department's recommendation to calculate loss as the difference between the WorldCom stock price from a random day during the fraud and the stock price from a random day after the disclosure of the fraud).

36. *Ebbers*, 458 F.3d at 128.

37. *Id.*

38. *Id.* The Second Circuit would have remanded Ebber's sentencing to reconsider these factors in the loss calculation had the total loss not been well above $1 billion, 'or ten times greater than the $100 million dollar threshold for the 26-level enhancement. *Id.* (citing the loss table in § 2B1.1 (USSG 2001)).

39. There are few, if any, district court cases where MAM is actually used.

40. *See* Duncan, *supra* note 14, at 261 (noting that the Third and Eleventh Circuits adopted MRM).

2. The Modified Rescissory Method (MRM)

The Modified Rescissory Method (MRM) is based in the theory that "the market price reflects all representations concerning the stock."[41] Under MRM, loss is calculated by multiplying the number of harmed shares by the difference between the average stock price during the fraud and the average stock price after disclosure.[42] Thus, MRM does not take into account outside market factors that might have influenced the loss in share price.[43]

Causation between the misrepresentation and the loss is presumed.[44] Specifically, "causation is adequately established by proof of purchase and of the materiality of misrepresentations, without direct proof of reliance."[45] Under MRM, proof of reliance is not necessary because an "investor who buys or sells stock at the price set by the market does so in reliance on the integrity of that price."[46] Further, "[b]ecause most publicly available information is reflected in market price, an investor's reliance on any public material misrepresentations, therefore, may be presumed."[47]

In applying MRM to loss calculations for civil securities fraud, the Supreme Court in *Basic Inc. v. Levinson*[48] noted that, as a practical matter, "[r]equiring a plaintiff to show a speculative state of facts, *i.e.* how he would have acted if omitted material information had been disclosed or if the misrepresentation had not been made, would place an unnecessarily unrealistic evidentiary burden on [a civil] plaintiff who has traded on an impersonal market."[49] Further, reliance on the market is legislatively encouraged because "Congress expressly relied on the premise that securities markets are affected by information, and enacted legislation to facilitate an investor's reliance on the integrity of those markets."[50]

After the Supreme Court's decision in *Dura Pharmaceuticals* in 2005, it was unclear whether courts could apply MRM to civil

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41. Note, *The Fraud-on-the-Market Theory*, 95 HARV. L. REV. 1143, 1154 (1982).
42. Duncan, *supra* note 14, at 261.
43. *Id.*
44. *See* Blackie v. Barrack, 524 F.2d 891, 906 (9th Cir. 1975) ("Proof of reliance is adduced to demonstrate the causal connection between the defendant's wrongdoing and the plaintiff's loss. ').
45. *Id.* (applying MRM).
46. Basic Inc. v. Levinson, 485 U.S. 224, 247 (1988).
47. *Id.*
48. *Id.*
49. *Id.* at 245.
50. *Id.* at 246.

securities fraud cases and even less clear whether they could apply it to sentencing calculations.[51] Several Circuits continued to rely on MRM to calculate loss in criminal fraud-on-the-market cases, reading *Dura Pharm* as limited to the civil context and expressly against the intentions of Congress.[52] To distinguish between the civil and criminal context, the Ninth Circuit in *United States v. Berger*,[53] for example, noted that in the civil context, the plaintiff bears the burden of showing the harm sustained, whereas in the criminal context, the "court gauges the amount of loss *caused*, i.e., the harm that society as a whole suffered from the defendant's fraud."[54] To

51. *See, e.g.* United States v. Berger, 587 F.3d 1038, 1045 (9th Cir. 2009) (considering and rejecting the idea that *Dura Pharmaceuticals* applies to the Guidelines).

52. *See* Duncan, *supra* note 14, at 261 (reviewing the loss calculation methods used by several circuits). Duncan found that MRM has been adopted by the Third Circuit, *see, e.g.* United States v. Brown, 595 F.3d 498, 524 (3d Cir. 2010) (upholding the lower court's loss calculation as the difference between the average stock selling price before and after the fraud was disclosed); the Eleventh Circuit, *see, e.g.* United States v. Snyder, 291 F.3d 1291, 1295 (11th Cir. 2002) ("[I]t is preferable to calculate the victims' loss by determining 'the approximate number of victims and an estimate of the average loss to each victim' ") (quoting U.S. SENTENCING COMM'N, GUIDELINES § 2 F1.1 cmt. n.9 (2000) [hereinafter USSG 2000); and, in at least some form, by the Ninth Circuit, *compare Berger*. 587 F.3d at 1045 (noting the Guidelines condone measuring loss by overvaluation, U.S. SENTENCING COMM'N, GUIDELINES § 2 F1.1 cmt. n.7(a) (1995) [hereinafter USSG 1995], and finding that 'were *Dura Pharmaceuticals*'s loss causation rule applied to criminal sentencing enhancements, that principle's plain rejection of the overvaluation loss measurement method would collide with Congress's clear endorsement of that method"); *with* United States v. Zolp, 479 F.3d 715, 719 (9th Cir. 2007) (explaining that 'the court must disentangle the underlying value of the stock, inflation of that value due to the fraud, and either inflation or deflation of that value due to unrelated causes. ').

53. 587 F.3d 1038 (9th Cir. 2009).

54. *Id.* at 1044. The court further explained:

> Whether and to what extent *a particular individual* suffered actual loss is not usually an important consideration in criminal fraud sentencing. Therefore, where the value of securities have been inflated by a defendant's fraud, the defendant may have caused aggregate loss to society in the amount of the fraud-induced overvaluation, even if various individual victims' respective losses cannot be precisely determined or linked to the fraud. As a result, the principle underlying the *Dura Pharmaceuticals* Court's reluctance to allow mere overvaluation as a basis for establishing loss is generally not present in the criminal sentencing context, and we are not persuaded that it would be appropriate to expand the *Dura Pharmaceuticals* rule to the criminal sentencing context.

further support this distinction, the Ninth Circuit pointed to the Guidelines' comments which endorsed a "flexible approach to loss calculation" and "condone[d] measuring loss by overvaluation."[55]

In circuits applying MRM, the sentencing recommendation was naturally longer than a sentencing recommendation using MAM because outside market forces were not taken into account. The sentencing disparity caused by the circuit split led to confusion among judges on how to properly and fairly calculate loss in a fraud-on-the-market case.

3. The Guidelines Method

In 2010, Dodd–Frank section 1079A(a)(1)(A) directed the Commission to "review and, if appropriate, amend" the Guidelines applicable to "offenses relating to securities fraud in order to reflect the intent of Congress that penalties for the offenses under the [G]uidelines and policy statements appropriately account for the *potential and actual harm to the public and the financial markets from the offenses*."[56] In response, the Commission created a new

Id.

55. *Berger,* 587 F.3d at 1044–45. To support the flexible view of loss, the court cites § 2F1.1, cmt. n.8, USSG 1995, *supra* note 51, which explains, 'The court need only make a reasonable estimate of the loss, given the available information. *Berger*. 537 F.3d at 1045 n.10. To support that the Guidelines condone measuring loss by overvaluation, the court cited to § 2F1.1, cmt. n.7(a), USSG 1995, *supra* note 51, which states:

> A fraud may involve the misrepresentation of the value of an item that does have some value (in contrast to an item that is worthless). Where, for example, a defendant fraudulently represents that stock is worth $40,000 and the stock is worth only $10,000, the loss is the amount by which the stock was overvalued (i.e. $30,000).

Berger. 537 F.3d at 1045. It is important to note that in the 2014 version of § 2B1.1 there is a somewhat analogous provision for the flexible view of loss, but there is no analogous provision condoning overvaluation. *See* USSG 2014, *supra* note 5, § 2B1.1 cmt. n.3(C) (stating that when estimating loss, there are multiple factors to be considered that are based on a flexible view of loss, such as '[t]he approximate number of victims [multiplied by] the average loss to each victim, while no factor mentioned accounts for overvaluation).

56. Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111–203, § 1079A, 124 Stat. 1376 (codified at 28 U.S.C. § 994 (2012)) (emphasis added). Additionally, section 1079A(a)(1)(B) requires that:

provision specifically addressing the loss calculation in fraud-on-the-market cases.[57] The Guidelines partially adopted a MRM calculation, creating a rebuttable presumption that:

> the actual loss attributable to the change in value of the security or commodity is the amount determined by—
>
> (I) calculating the difference between the average price of the security or commodity during the period that the fraud occurred and the average price of the security or commodity during the 90-day period after the fraud was disclosed to the market, and
>
> (II) multiplying the difference in average price by the number of shares outstanding.[58]

This calculation is more cost efficient than MAM because it does not require expert testimony to identify outside market forces and estimate these forces' impact on the stock price. Because the calculation is based on publically recorded securities prices, it is

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> In making any amendments to the Federal Sentencing Guidelines and policy statements the United States Sentencing Commission shall—
>
> (i) ensure that the Guidelines and policy statements reflect—
>
> (I) the serious nature of the offenses described in subparagraph (A);
>
> (II) the need for an effective deterrent and appropriate punishment to prevent the offenses; and
>
> (III) the effectiveness of incarceration in furthering the objectives described in subclauses (I) and (II);
>
> (ii) consider the extent to which the Guidelines appropriately account for the potential and actual harm to the public and the financial markets resulting from the offenses;
>
> (iii) ensure reasonable consistency with other relevant directives and Guidelines and Federal statutes;
>
> (iv) make any necessary conforming changes to Guidelines; and
>
> (v) ensure that the Guidelines adequately meet the purposes of sentencing, as set forth in section 3553(a)(2) of title 18, United States Code.

Id.

57. USSG 2014, *supra* note 5, § 2B1.1 cmt. n.3(F)(ix).

58. *Id.*

relatively easy to calculate the average security price.

This calculation also addresses issues raised by several cases, including *Ebbers*, which did not take the fluctuation of stock prices over a period of time into account.[59] The new Guideline calculation controls for short-term market variability to an extent because it averages the price over a time period that short-term variability may occur.[60]

To further complicate the loss calculation, the Guideline calculation does not strictly follow MRM because the Guidelines allow for judges to control for outside market forces, as they would under MAM, if they see fit. The Guidelines explain that "the court *may* consider, among other factors, the extent to which the amount so determined includes significant changes in value not resulting from the offense (*e.g.*, changes caused by external market forces, such as changed economic circumstances, changed investor expectations, and new industry-specific or firm-specific facts, conditions, or events)."[61] Thus, the Guidelines create an optional MAM calculation: the court can control for outside forces if it wants, or completely ignore outside forces if it finds the MRM calculation reasonable. Not all courts will calculate loss in fraud-on-the-market cases similarly and each judge may not calculate it the same way in all cases.

Courts now must decide whether to rely on the rebuttable presumption or control for market forces. The difficulty is that MRM

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59. United States v. Ebbers, 458 F.3d 110, 126 (2d Cir. 2006); *see supra* notes 33–37 and accompanying text (explaining that the lower court in the *Ebbers* case calculated loss as the difference between the stock price on a random day before the fraud was uncovered and a random day after the fraud was uncovered).

60. However, others have posited, '[t]he longer the span of time, the more likely it is that extraneous factors might affect the loss calculation, because 'stock prices react quickly to the arrival of new information new information is often fully incorporated in a stock price within one trading day. Duncan, *supra* note 14, at 266 (citing Kevin P. McCormick, *Untangling the Capricious Effects of Market Loss in Securities Fraud Sentencing*, 82 TUL. L. REV. 1145, 1166 (2008)); Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549, 560 (1984); Mark L. Mitchell & Jeffry M. Netter, *The Role of Financial Economics in Securities Fraud Cases: Applications at the Securities and Exchange Commission*, 49 BUS. LAW. 545, 557 (1994)). However, the efficacy of the 'efficient market theory, which also serves as the theoretical basis of MRM, was largely called into question after the Enron scandal. *See, e.g.* John Cassidy, *The Greed Cycle*, THE NEW YORKER, Sept. 23, 2002, at 64, 64 (explaining that the Enron scandal demonstrated that securities fraud could easily be hidden from the market price, demonstrating that stock prices sometimes do not react quickly to new information).

61. USSG 2014, *supra* note 5, § 2B1.1 cmt. n.3(F)(ix) (emphasis added).

is objective, unfair, and leads to disproportionate sentencing while MAM is subjective and expensive. For a judge, MRM might be more attractive because the sentence would be economically efficient to calculate and is afforded a rebuttable presumption upon appeal. But, when courts calculate without considering outside market forces, the loss calculation is artificially inflated because the calculation attributes more to the defendant than he actually caused and the defendant receives a higher offense level than someone who committed a similar crime that was unaffected by market forces. All of these effects lead to sentencing recommendations that are neither closely nor causally related to the actual effects of the crime. However, MAM might be more attractive to judges because the inherent fairness of considering only those effects that are causally related.

Because the new calculation has only been in place for four years and there are few fraud-on-the market cases that go to trial each year, it is uncertain whether this calculation has resolved any of the initial ambiguity.

B. Logarithmic Sentencing and the SOCs

In addition to the calculation of loss, the logarithmic structure of the sentencing table and the overlapping SOCs lead to disproportionate sentencing.

1. Loss Table

After five years of inquiry and in response to a series of high profile frauds, in 2001 the Commission concluded that the Guidelines did not provide for severe enough sentences for white-collar criminals.[62] In response, the Commission implemented the Economic Crimes Package to increase the values in the loss table.[63]

The Commission changed the loss table so that lower loss offenders would receive less time while higher loss offenders would be sentenced more harshly—a $100,000,000 loss led to a twenty-six

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62. *See* Bowman, *supra* note 13, at 392–402 (detailing the WorldCom and Enron frauds in 2001 and explaining the reaction of both the public and Congress in response).

63. USSG 2001, *supra* note 17. § 2B1.1; *see also* Bowman, *supra* note 13, at 389 (explaining that the commissioners specifically expressed concern that too many white-collar offenders avoided jail-time by increasing the values in the loss table).

offense level increase.[64] The year before, this same $100,000,000 loss would only have led to an eighteen level increase, or a prison sentence seventy months shorter.[65] Because the sentencing table has logarithmic effect on length of sentence,[66] adding more loss offense levels at the top of the table drastically increased the length of sentence for defendants who caused high-losses.

The current loss table considers larger losses than the tables before it. Compared to the 2001 loss table, put in place by the Economic Crimes Package, the 2014 table has two new levels for losses of $200,000,000 and $400,000,000 with twenty-eight and thirty offense level increases respectively.[67] The rest of the levels have remained constant since 2001, despite inflation.[68] If a court finds that the fraud caused a $400 million loss, without considering other SOCs, the defendant has a total offense level of thirty-seven,[69] calling for a sentencing range of 210 to 262 months, or more than seventeen years in prison; for a $200 million loss, a minimum of fourteen years in prison.[70]

To some, this might seem like a just punishment, especially because these calculations are well under the statutory maximum,[71] but it is important to note that this calculation has not added any one of the eighteen other SOCs in the 2014 version of § 2B1.1.[72] An offense level of thirty-seven is only five level enhancements away from life in prison without parole.[73] Additionally, this initial calculation assumes that the loss calculation accurately reflects not

64. USSG 2001, *supra* note 17, § 2B1.1(b)(1)(N).

65. USSG 2000, *supra* note 51, § 2B1.1. The comparison calculates the loss without considering any other SOCs and uses the minimum range. *Id.*

66. *See* USSG 2001, *supra* note 17, § 5A (providing that the difference in minimum sentence between an offense level of 13 and 15 is 6 months, whereas the difference in minimum sentence between an offense level of 40 and 41 is 68 months); *see also* Bowman, *supra* note 7, at 170 (describing the effect as a '25 percent rule' where 'the same one-offense-level increase [for a high total offense level] increases the defendant's minimum sentence by 3 years and his maximum sentence from 30 years to life imprisonment").

67. USSG 2014, *supra* note 5, § 2B1.1.

68. However, the proposed amendments discussed in the following section now account for changes in inflation. AMENDMENTS TO THE SENTENCING GUIDELINES, *supra* note 11, at 12–14.

69. USSG 2014, *supra* note 5, § 2B1.1. Assuming the offense has a statutory maximum of at least 20 years, the defendant has a base offense level of 7. *Id.*

70. *Id.* at § 5A.

71. The statutory maximum for fraud-on-the-market can be 25 years. 18 U.S.C. § 1348 (2012) (Securities and commodities fraud).

72. USSG 2014, *supra* note 5, § 2B1.1.

73. *Id.* at § 5A.

only the actual monetary loss but also the defendant's culpability in the fraud; this is not a safe assumption. Further, as the following section explains, the SOCs' cumulative effect drastically increases the offense level.

2. Factor Creep: Cumulative Effect of SOCs in Fraud-on-the-Market Offenses

The intention of the Commission in passing the Economic Crimes Package was to increase sentencing through increasing the loss table.[74] It did not intend for the SOCs from the 2000 version of the Guidelines to have a cumulative effect with the new loss table.[75]

Further, a year after the Economic Crimes Package took effect, Congress passed the Sarbanes-Oxley Act in response to public outrage from the Enron and WorldCom securities and accounting fraud scandals.[76] Sarbanes-Oxley created new substantive securities fraud offenses, increased statutory maximums,[77] and gave legislative directives to the Commission.[78] In response to the legislative directives that largely called for enhancements that were already in place or that had been intentionally removed two years before, the Commission passed emergency amendments that enacted a "minimalist view."[79] The amendment:

1. further increased loss table levels and added two new levels for losses of more than $200 million and $400 million;

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74. *See* Bowman, *supra* note 13, at 388–89 (noting that the intention of the 2001 amendment was to increase offense level only through increases in the loss table).

75. *See* Bowman, *supra* note 4, at 32–38 (explaining the procedural history of the 2001 amendments).

76. For discussion of Sarbanes-Oxley and the Guidelines, *see* Bowman, *supra* note 13, at 392–440.

77. Bowman, *supra* note 13, at 394. Most of Sarbanes-Oxley's statutory maximum increases are beyond the reach of this paper. But it is significant for fraud-on-the-market to note that Sarbanes-Oxley raised the maximum sentence for violation of the Securities Exchange Act of 1934 § 32(a), 15 U.S.C. § 78f(a), from 10 years to 20 years. Additionally, the increases in statutory maximums ultimately have an effect on the total sentencing level in the Guideline. *See* USSG 2014, *supra* note 5, § 2B1.1(a)(1) (requiring a base offense level increase if the statutory maximum is 20 years or more); USSG 2012, *supra* note 23, § 5G1.2(d).

78. *See* Bowman, *supra* note 13, at 405–15 (providing an in-depth examination of the legislative directives and the inconsistencies therein).

79. USSG 2012, *supra* note 23, § 2B1.1; *see also*, Bowman, *supra* note 13, at 415 (discussing the minimalist view adopted the Sentencing Commission).

2. added a 2 level enhancement to the victim's table for 250 or more victims;
3. added a 4 level enhancement for "conduct that substantially endangered the solvency or financial security" of large corporations;
4. added a 4 level enhancement for securities law violations by an officer of publicly traded company.[80]

Because of Sarbanes-Oxley, without even adding the loss table to the offense level calculation, an officer of a publicly traded company who committed a typical securities fraud would receive an offense level ten levels higher than the year before.[81]

In the 2014 version of §2B1.1, there are 19 SOCs, including the loss table. This does not include the many subsections within almost all SOCs or the general sentencing enhancements.[82] In theory it might appear prudent to have so many SOCs so that each sentencing is more specific to the actual conduct. In practice, these SOCs correlate to cumulate the effects.

The Commission has recognized the problem commonly referred to as "factor creep."[83] The Commission explained that "[i]t is possible to imagine countless circumstances that would make an offense more serious," but sometimes these circumstances overlap.[84] Addressing the problem, it concluded that "[i]t is difficult to argue that any of these considerations are irrelevant, yet, as more and more adjustments are added to the sentencing rules, it is increasingly difficult to ensure that the interactions among them, and their cumulative effect, properly track offense seriousness."[85]

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80. Bowman, *supra* note 13, at 415–16.

81. Assuming a securities fraud that endangered the financial security of a large corporation with more than 250 shareholders. *Compare* USSG 2012, supra note 23, § 2B1.1 (sentencing guidelines pre-Sarbanes–Oxley), *with* USSG 2011, *supra* note 22, § 2B1.1 (sentencing guidelines post-Sarbanes–Oxley).

82. USSG 2014, *supra* note 5, § § 3B1.1, 3B1.2.

83. U.S. SENTENCING COMM'N, FIFTEEN YEARS OF GUIDELINE SENTENCING: AN ASSESSMENT OF HOW WELL THE FEDERAL CRIMINAL JUSTICE SYSTEM IS ACHIEVING THE GOALS OF SENTENCING REFORM 137–38 (2004), http://www.ussc.gov/sites/default/files/pdf/research-and-publications/research-projects-and-surveys/miscellaneous/15-year-study/15_year_study_full.pdf [hereinafter FIFTEEN YEARS OF GUIDELINE SENTENCING].

84. *Id.* The Commission used the example that in a sale of drugs offense, 'one might wish to enhance punishment for selling drugs 1) near a school yard, 2) near a prison, 3) near a drug treatment facility, 4) in the presence of a minor, 5) by employing a minor, or 6) to a pregnant woman. *Id.*

85. *Id.*

Reflecting back on warnings by Justice Stephen Breyer, a former Sentencing Commissioner and original drafter of the Guidelines, the Commission cautioned, "[c]omplex rules with many adjustments may foster a perception of a precise moral calculus, but on closer inspection this precision proves false. Adjustments that appear necessary to achieve proportionate punishment may in actuality result in arbitrary distinctions among offenders."[86]

Cumulative SOCs have become particularly egregious for fraud-on-the-market sentencing calculations. One court has noted, "we now have an advisory [G]uidelines regime where any officer or director of virtually any public corporation who has committed securities fraud will be confronted with a [G]uidelines calculation either calling for or approaching lifetime imprisonment."[87]

Indeed, if the defendant is an officer or a director of a publicly traded company, the defendant will automatically be subjected to:

- a 4 level enhancement for substantially endangering the solvency or financial security of a publicly traded company[88]
- a 4 level enhancement for violating a securities law where the defendant is an officer or director of a publicly traded company; a broker or dealer; or an investment advisor[89]
- a 3 level enhancement for a leadership role[90]
- a 2 level enhancement for abusing a position of trust.[91]

This thirteen level increase can be the difference between eight years

86. FIFTEEN YEARS OF GUIDELINE SENTENCING, *supra* note 82, at 137–38 (citing Stephen Breyer & Kenneth Feinberg, *The Federal Sentencing Guidelines: A Dialogue*, 26 CRIM. L. BULL. 26(5), 9 (1999)).

87. United States v. Parris, 573 F. Supp. 2d 744, 754 (E.D.N.Y 2008).

88. USSG 2014, *supra* note 5, § 2B1.1(b)(16)(B). *See also* Bowman, *supra* note 7. at 170–71 (arguing that any securities fraud substantially endangers the solvency or financial security of a publicly traded company).

89. *Id.* at § 2B1.1(b)(19).

90. *Id.* at § 3B1.1.

91. *Id.* at § 3B1.3 ("If the defendant abused a position of public or private trust, or used a special skill, in a manner that significantly facilitated the commission or concealment of the offense, increase by 2 levels.').

in prison and life without parole.[92]

Further, it is difficult to conceive a high loss fraud-on-the-market that would not involve numerous victims. If the publicly traded company had more than 250 shareholders, as is typical, each of whom lost money from the fraud, the director would receive a six level enhancement.[93] If this director's fraud caused even the median loss for securities fraud, $3 million,[94] the court would add eighteen levels because of the loss alone.[95] Thus, this director would have an offense level of forty-three and face life in prison under the Guidelines.[96]

The problem with § 2B1.1 is not that these SOCs are irrelevant; the problem is the strong correlation between them. Several of these SOCs are factors that "loss [once] served as a rough

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92. USSG 2014, *supra* note 5, § 5A (providing that offense level 30 corresponds to a 97–121 month sentencing range while offense level 43 provides for life in prison without parole).

93. *Id.* at § 2B1.1(b)(2):

> (Apply the greatest) If the offense–
>
> (A) (i) involved 10 or more victims; or (ii) was committed through mass-marketing, increase by **2** levels;
>
> (B) involved 50 or more victims, increase by **4** levels; or
>
> (C) involved 250 or more victims, increase by **6** levels.

Id.

94. U.S. SENTENCING COMM'N, ECONOMIC CRIME PUBLIC DATA BRIEFING 21 (Jan. 9, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150109/fraud_briefing.pdf [hereinafter ECONOMIC CRIME PUBLIC DATA BRIEFING].

95. This calculation may appear absurd and unsupported by Commission data that has found that the average guideline minimum for securities fraud is 84 months and that most high loss crimes get less than 3 SOCs. *See id.* at 14 (depicting the quantitative breakdown of federal sentencing data, separating out the statistics for securities fraud). But this fails to consider that most cases are plea-bargained. Frank Bowman argues that the data does not reflect the reality of the cumulative effect because prosecutors and defendants bargain away SOC enhancements to facilitate plea-bargaining. Frank Bowman, Comment on Proposed Amendments to Economic Crime Guideline, § 2B1.1, at 9 (Feb. 19, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150312/Bowman.pdf. If this theory is true, the Commission's data does not accurately reflect the severity of factor creep and inflates the threat to settle.

96. USSG 2014, *supra* note 5, §§ 2B1.1, 3B1.1, 2; 5A.

proxy" but now have independent weight themselves.[97] For example, loss and number of victims correlate while also both serving as proxies for culpability. It makes sense for the Guidelines to become more precise, but the Guidelines need to compensate by lowering the loss table that serves as a proxy for these factors so that the calculation doesn't consider the same factor twice.

III. THE GUIDELINES IN PRACTICE

Just as the calculations from the previous section demonstrate that the recommendations for fraud-on-the-market are excessive, case law and data released by the Commission both demonstrate that, in practice, the Guidelines recommend sentences so disproportionate that judges refuse to follow them.

A. *Case Examples*

Bernie Ebbers, the former WorldCom CEO, was sentenced to twenty-five years in spite of a Guidelines recommendation of thirty years to life in prison.[98] On appeal, the Second Circuit found the twenty-five year sentence reasonable, even though it noted that "[u]nder the Guidelines, it may well be that all but the most trivial frauds in publicly traded companies may trigger sentences amounting to life imprisonment," because the "Guidelines reflect Congress' judgment as to the appropriate national policy for such crimes" and the sentence was already a nineteen level downward departure.[99] Ebbers's WorldCom fraud instigated the initial push for longer sentences for white-collar criminals—this story does not inspire sympathy. Other cases, however, demonstrate the Guidelines' failure to suggest reasonable punishments for securities fraud.

The district judge in *United States v. Adelson*[100] lamented, "This is one of those cases in which calculations under the Sentencing Guidelines lead to a result so patently unreasonable as to require the Court to place greater emphasis on other sentencing factors to derive a sentence that comports with federal law."[101] As CEO, Adelson joined an ongoing conspiracy to materially misstate the company's financial results, thereby artificially inflating the

97. Bowman, *supra* note 7, at 170.
98. Transcript of Sentencing Hearing, *supra* note 34, at 59.
99. United States v. Ebbers, 458 F.3d 110, 129 (2d Cir. 2006).
100. 441 F. Supp. 2d 506 (S.D.N.Y 2006).
101. *Id.* at 506.

company's stock price.[102]

> After the fraud was uncovered, the accounting employees who actually designed the fraud entered into cooperation agreements with the Government, in return for which they became eligible for the substantially reduced sentences that they ultimately received. [One co-conspirator] was given a "non-guideline" sentence of 3 months' imprisonment, which the Government did not appeal. However, at Adelson's sentencing the Government argued that the Sentencing Guidelines *called for a sentence of life imprisonment,* cabined only by the maximum of 85 years permitted under the counts of which Adelson was convicted.[103]

Calculating loss attributable to Adelson was particularly problematic because "[d]uring the time of his participation, the price of [the] stock was not further inflated."[104] Faced with a disproportionate sentence, the court relied on 18 U.S.C.A. § 3553(a)[105] to consider other factors and impose a three and a half year sentence.[106]

Other cases have demonstrated how high-losses lead to egregiously disproportionate sentencing ranges.[107] But, because

102. *Adelson*, 441 F. Supp. 2d at 507.

103. *Id.* (emphasis added).

104. *Id.* at 513.

105. 18 U.S.C.A. § 3553(a) (2010) provides for subjective factors for judges to consider in determining the sentence. The court in *Adelson* explained its use of 18 U.S.C.A. § 3553(a):

> Where the Sentencing Guidelines provide reasonable guidance, they are of considerable help to any judge in fashioning a sentence that is fair, just, and reasonable. But where, as here, the calculations under the Guidelines have so run amok that they are patently absurd on their face, a Court is forced to place greater reliance on the more general considerations set forth in section 3553(a), as carefully applied to the particular circumstances of the case and of the human being who will bear the consequences. This the Court has endeavored to do Whether those reasons are reasonable will be for others to judge.

Adelson, 441 F. Supp. 2d at 515.

106. *Adelson*, 441 F. Supp. 2d at 515.

107. *See, e.g.* United States v. Parris, 573 F. Supp. 2d 744, 754 (E.D.N.Y 2008) (sentencing the defendant to five years imprisonment 'in the face of an advisory guideline range of 360 to life' for a 'pump and dump' stock

judges have sentencing discretion, as the next section explains, judges rarely follow the Guidelines, especially for high-loss securities fraud.

B. Commission Data: Judges Frequently Depart Downward in Fraud-on-the-Market Cases

Because judges depart from the Guidelines where they find the Guidelines' recommendations unreasonable, the Sentencing Commission's data is useful for determining whether a sentencing recommendation was reasonable.[108] Although it is commonly believed that judges began departing from the Guidelines after *Booker*[109]—where the Supreme Court found that mandatory sentencing Guidelines were unconstitutional and made the Guidelines discretionary—departures across all crimes are consistent with pre-*Booker* levels.[110]

However, economic crimes sentenced under § 2B1.1 are the only group of crimes, besides pedophilia, in which judges have used their discretion to depart further from the Guidelines each year.[111] This trend largely started in 2003 after the Sarbanes-Oxley mandate caused longer sentencing recommendations under § 2B1.1 by

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manipulation scheme—scored an offense level 42 based on upward adjustments for more than $2.5 million of loss, more than 250 victims, sophisticated means, officer/director status, role in the offense, and obstruction of justice). For discussion and further examples, *see* James E. Felman, Am. Bar Ass'n, Testimony for the Hearing on Proposed Amendments to the Federal Sentencing Guidelines Regarding Economic Crimes 4–8 (Mar. 12, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150312/Felman.pdf (outlining cases in which high-losses led to disproportionately large sentences to argue that the Commission should reduce its reliance on loss as a measure of culpability).

108. This assumption is based on the fact that although District Court judges may not presume that the Guidelines create a reasonable sentence, and must make an individualized assessment of the facts presented, Appellate Courts may, but are not required to, presume that a sentence within the Guidelines is reasonable. Gall v. United States, 128 S. Ct. 586, 596–97 (2007); Rita v. United States, 551 U.S. 338, 351 (2007); Peugh v. United States, 133 S. Ct. 2072, 2080 (2013).

109. *See, e.g.* Ryan W. Scott, *Inter-Judge Sentencing Disparity After Booker: A First Look*, 63 STAN. L. REV. 1 (2010) (using empirical data to assess whether judges departed before *Booker*).

110. U.S. SENTENCING COMM'N, REPORT ON THE CONTINUING IMPACT OF *UNITED STATES V. BOOKER* ON FEDERAL SENTENCING 60 (Dec. 2012), http://www.ussc.gov/sites/default/files/pdf/news/congressional-testimony-and-reports/booker-reports/2012-booker/Part_A.pdf#page=2 [hereinafter REPORT ON THE CONTINUING IMPACT OF *BOOKER*].

111. *Id.* at 67.

imposing a higher loss table while failing to control for added SOCs, particularly SOCs relating to securities fraud.[112]

It is unsurprising that, as average Guidelines minimum sentences for § 2B1.1 offenses increased with each year since 2003, both the frequency and magnitude of departures also increased.[113] In 2003, eighty-three percent of cases were sentenced within the Guidelines' ranges.[114] By 2012, defendants were sentenced within the Guidelines' ranges in only half of § 2B1.1 cases.[115] In 2003, the average Guideline minimum sentence and the average sentence imposed for § 2B1.1 offenses were both 10 months.[116] But, by 2012 the average Guideline minimum under § 2B1.1 had nearly tripled to twenty-nine months while the average sentence imposed increased to twenty-two months.[117]

The imposed sentences have more than doubled while the disparity between the imposed and Guideline minimum sentences have widened. This indicates that judges have adopted the Commission's goal of longer sentences for white-collar offenders but judges think that the Guidelines recommend unreasonable punishments for § 2B1.1 offenders.[118]

Further, the magnitude with which judges depart from § 2B1.1 recommendations is even greater for fraud-on-the-market

112. *See supra* Part IIB (explaining the cumulative effect of the SOCs and the loss table). Although the Commission's data revealed an increase in departures of § 2B1.1 recommendations after *Booker* in 2005, because the average departure across all crimes has remained constant before and after *Booker*. it is likely more telling that the average imposed sentence under § 2B1.1 has almost tripled since 2003 while the average actual sentence imposed has doubled but failed to keep pace with the Guideline recommendation. ECONOMIC CRIME PUBLIC DATA BRIEFING, *supra* note 93, at 5; REPORT ON THE CONTINUING IMPACT OF *BOOKER*, *supra* note 109, at 60.

113. ECONOMIC CRIME PUBLIC DATA BRIEFING, *supra* note 93, at 6.

114. *Id.* at 5, figure 1.

115. *Id.*

116. *Id.* at 6, figure 2.

117. *Id.*

118. Despite the more than double increase in actual sentence length between 2003 and 2012, at least one critic has argued for mandatory minimums in order to decrease departure frequency and severity, implicitly arguing that the current sentencing Guidelines, which provide life-in-prison for fraud offenses, are reasonable, reflect Congress's thorough understanding of public policy, and are necessary for deterrence. John D. Esterhay, *'Street Justice' for Corporate Fraud—Mandatory Minimums for Major White-Collar Crime*, 22 REGENT U. L. REV. 135, 161 (2009) ("Thus, judges are giving breaks to white-collar crime when compared to street crime, and they give the biggest breaks to those defendants that Congress specifically wanted to punish more harshly through the implementation of the WCCPA.").

offenses than other § 2B1.1 offenses because downward departures increase logarithmically as the loss attributed to the crime increases.[119] With a median loss of $3,321,521 in 2012, securities fraud has the highest median loss of § 2B1.1 offenses—mortgage fraud, the offense with the second-highest loss, caused a mere $777,750 loss.[120] Unsurprisingly, sentence recommendations are significantly higher for securities fraud than any other § 2B1.1 offense.[121] Therefore, the data shows that high-loss securities fraud has the most disproportionate sentencing recommendations.

At first glance, disproportionate sentencing recommendations do not appear to be a problem because courts may simply depart downward. However, the current Guidelines fail in their responsibility to both judges and to those who are sentenced. Judges must still begin with the Guidelines' recommendations, which are supposed to provide guidance.[122] But one federal judge has noted that he "would have much preferred a sensible guidelines range to give some semblance of real guidance."[123] For offenders, this failure has higher costs.

IV RESPONDING TO DISPROPORTIONATE SENTENCING: THE PROPOSED AMENDMENTS

In January 2015, the Commission released its proposed draft amendments for the Guidelines with special emphasis on § 2B1.1 and fraud, in particular.[124] The proposed amendments would change the calculation for fraud-on-the-market from loss to gain. After

119 ECONOMIC CRIME PUBLIC DATA BRIEFING, *supra* note 93, at 11, figure 6.

120. *Id.* at 21.

121. *Id.* at 20. The average Guideline minimum for securities and investment fraud was 84 months while the Guideline minimum for identity theft, the next highest minimum, was 48 months. *Id.* The average Guideline minimum for §2B1.1 offenses is just over 32 months and the standard deviation is 18.45 months, making the minimum for securities fraud more than two standard deviations away from the next highest offense minimum, around three standard deviations from the mean, and almost triple the average minimum for §2B1.1 offenses. *Id.*

122. Kimbrough v. United States, 552 U.S. 85, 101 (2007); *see also* Gall v. United States, 552 U.S. 38, 49 (2007) ("As a matter of administration and to secure nationwide consistency, the Guidelines should be the starting point and the initial benchmark.").

123. United States v. Parris, 573 F. Supp. 2d 744, 751 (E.D.N.Y 2008).

124. U.S. SENTENCING COMM'N, PROPOSED AMENDMENTS TO THE SENTENCING GUIDELINES 72 (Jan. 16, 2015) http://www.ussc.gov/sites/default/files/pdf/amendment-process/reader-friendly-amendments/2015014-RFP-Amendments.pdf [hereinafter PROPOSED AMENDMENTS].

public comment, the Commission made only one modest change to the calculation of loss for fraud-on-the-market in its final version of the proposed amendments. Neither the initially proposed draft amendments nor the proposed amendments directly addressed the loss table or the cumulative effect of the SOCs that together lead to excessive sentencing recommendations.

A. Initial Proposed Amendment: From Loss to Gain

When the Commission decided to amend §2B1.1, it expressly acknowledged that sentences for high-loss frauds—or as the data demonstrates, securities frauds specifically—were not working. The Chair of the Commission noted that the Commission believed that "the fraud guideline may not be fundamentally broken for most forms of fraud. [because] sentences on average hew fairly closely to the Guidelines for all but the highest dollar values, over $1 million in loss."[125] Instead of directly addressing the sentence length for securities fraud by lowering the loss table or removing the correlating SOCs, the Commission addressed the way in which loss is calculated for fraud-on-the-market offenses.

The Commission proposed using "gain, rather than loss, for purposes of [the loss table] if the offense involved (i) the fraudulent inflation or deflation in the value of a publicly traded security or commodity and (ii) the submission of false information in a public filing with the Securities and Exchange Commission or similar regulator."[126] This seemed to be an effort to both lower the offense level and address the criticisms that the fraud-on-the-market calculation does not accurately consider causation.

The change from loss to gain might have solved the causation issues inherent under MRM. Critics could no longer lament that MRM infers reliance by shareholders. Although some experts criticized that a measure of gain would still allow for outside market forces to inflate a defendant's offense level,[127] gain would allow the court to use a proxy more closely tied to culpability. Gain is "often a

125. Patti B. Saris, U.S. Sentencing Comm'n, Remarks for Public Meeting 2 (Jan. 9, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150109/Remarks.pdf.

126. PROPOSED AMENDMENTS, *supra* note 123, at 86.

127. Catherine M. Foti, N.Y Council of Def. Lawyers, Testimony Before the United States Sentencing Commission for the Hearing on 2015 Proposed Amendments to the Federal Sentencing Guidelines 10–12 (Mar. 12, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150312/Foti.pdf

better measure of culpability than loss when loss is driven largely by the severity of the stock market reaction to the public disclosure of the fraud multiplied by the number of outstanding shares."[128] In turn, judges may have followed the gain calculation more because of its relationship to culpability.[129]

Proponents for the change from loss to gain cite that gain is already used to calculate enhancements for insider trading.[130] In insider trading cases, the court can look directly at the defendant's funds to calculate the SOC. In the context of fraud-on-the-market, however, it may not be that easy.[131]

The Department of Justice responded to the proposed amendment by arguing that gain is an improper measure for fraud-on-the-market offenses for two reasons.[132] First, measuring gain instead of loss is directly against Dodd–Frank's mandate for the Commission to ensure that penalties for securities fraud "appropriately account for the *potential and actual harm* to the public and financial market from the offenses."[133] Second, "the gain from an offense is itself often hard to ascertain."[134] This is because

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128. Eric A. Tirschwell, Practitioners Advisory Group, Testimony Before the United States Sentencing Commission 9 (Mar. 12, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150312/Tirschwell.pdf.

129. *Id.* He argued that

> gain is often a better measure of culpability than loss when loss is driven largely by the severity of the stock market reaction to the public disclosure of the fraud multiplied by the number of outstanding shares. Neither the market's reaction nor the number of outstanding shares is necessarily or even usually well-correlated to the seriousness of fraud itself or the defendant's culpability.

Id.

130. *See, e.g.* FOTI, *supra* note 126, at 10 (arguing that gain would be a better measurement of culpability in fraud-on-the-market offenses because it is already used for insider trading offenses and because it is a more direct measure of culpability). It makes sense that gain is used instead of loss for insider trading. A court would be incapable of finding out who lost money and how much money they lost because loss to third parties is not evident in insider trading cases.

131. *See* U.S. Dep't of Justice, Views on the Proposed Amendments to the Federal Sentencing Guidelines and Issues for Comment Published by the U.S. Sentencing Commission in the Federal Register on January 16, 2015, at 35 (Mar. 9, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/public-hearings-and-meetings/20150312/DOJ.pdf ("[T]he gain from [a] [fraud-on-the-market] offense is itself often hard to ascertain. ').

132. *Id.* at 33–35.

133. *Id.* at 33–34 (citing section 1079A(a)(1)(A) of Dodd–Frank).

134. *Id.* at 35.

securities fraud does not often result in direct financial gain to the defendant. The defendant fraudulently inflates the securities price for the benefit of the company. However, the defendant does sometimes achieve monetary gains, but those gains are difficult to quantify because they are achieved indirectly. These gains can "include, for example, increased stature within the company, which may lead to bonuses and promotions." [135] Thus, "[c]ourts would have to determine what portion of a defendant's earnings from his company is traceable to his fraud, and what portion of his earnings he would have received anyway, an inherently difficult endeavor."[136] Finally, the DOJ pointed to cases that demonstrated that fraud-on-the-market cases often "cause catastrophic harm to the markets but result in comparatively little gain for the defendant."[137]

B. Finalized Amendment: Any Appropriate Method

The Commission presumably took the DOJ's stance to heart. In its finalized version, which took effect in November 2015,[138] the Commission reverted to a calculation that merely changes the rebuttable presumption of MRM to a suggestion that courts use MRM. The amendment's loss calculation now provides:

> In a case involving the fraudulent inflation or deflation in the value of a publicly traded security or commodity, ~~there shall be a rebuttable presumption that~~ **the court in determining loss may use any method that is appropriate and practicable under the circumstances. One such method the court may consider is a method under which** the actual loss

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135. *Id.*

136. *Id.*

137. *Id.* at 34 (citing United States v. Brincat, No. 1:2005-cr-00093 (N.D.Il. 2006) (shareholders lost $2 billion, but the defendant never sold his stock to profit from the scheme); United States v. Harris, No. 1:09-cr-00406-TCB-JFK (N.D.GA. 2012) (defendants committed a fraud to keep the company running and gained only a few hundred thousand dollars, but shareholders lost $44 million); United States v. Elles, No. 1:11-CR-485-AT-AJB (N.D.GA. 2012) (the loss to shareholders was $150 million, but the defendants did not receive any monetary gain apart from ordinary compensation and bonuses)). *But see generally* Cassidy, *supra* note 59 (arguing that fraud-on-the-market offenders are motivated by monetary gains through stock options).

138. U.S. SENTENCING COMM'N, AMENDMENTS TO THE SENTENCING GUIDELINES 30 (Apr. 30, 2015), http://www.ussc.gov/sites/default/files/pdf/amendment-process/reader-friendly-amendments/20150430_RF_Amendments.pdf [hereinafter AMENDMENTS TO THE SENTENCING GUIDELINES].

> attributable to the change in value of the security or commodity is the amount determined by—
>
> > (I) calculating the difference between the average price of the security or commodity during the period that the fraud occurred and the average price of the security or commodity during the 90-day period after the fraud was disclosed to the market, and
> >
> > (II) multiplying the difference in average price by the number of shares outstanding.[139]

The amendment still includes the suggestion that courts may consider external market forces. The only real change from the 2014 version is that there is no longer a rebuttable presumption that MRM calculates loss accurately. The amendment does, however, seem eerily similar to the pre-2013 ambiguous language that led to the MAM-MRM Circuit split. The amendment fails to address any of the factors that lead to disproportionately long sentences for fraud-on-the-market offenses.

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139. AMENDMENTS TO THE SENTENCING GUIDELINES, supra note 137, at 30. The amendments explain,

> the amendment revises the special rule at Application Note 3(F)(ix) relating to the calculation of loss in cases involving the fraudulent inflation or deflation in the value of a publicly traded security or commodity. When this special rule was added to the guidelines, it established a rebuttable presumption that the specified loss calculation methodology provides a reasonable estimate of the actual loss in such cases. As amended, the method provided in the special rule is no longer the presumed starting point for calculating loss in these cases. Instead, the revised special rule states that the provided method is one method that courts may consider, but that courts, in determining loss, are free to use any method that is appropriate and practicable under the circumstances. This amendment reflects the Commission's view that the most appropriate method to determine a reasonable estimate of loss will often vary in these highly complex and fact-intensive cases.
>
> This amendment, in combination with related revisions to the mitigating role guideline at §3B1.2 (Mitigating Role), reflects the Commission's overall goal of focusing the economic crime guideline more on qualitative harm to victims and individual offender culpability.

Id. at 25–26.

V POSSIBLE SOLUTIONS THAT WOULD LOWER THE DISPROPORTIONATE SENTENCES FOR FRAUD-ON-THE-MARKET OFFENSES

Because the Guidelines have repeatedly failed to address the disproportionate recommendations for fraud-on-the-market offenses, it is important to outline possible solutions and briefly explain why the Commission will most likely not implement them.

First, the Commission could formally adopt MAM and require that courts control for external market forces in the loss calculation. This would make the loss calculation, and therefore the offense level, more closely tied to the loss that the defendant actually caused. However, as explained above, this option would be costly and would increase subjectivity.

Second, the Commission could delete the highest loss levels in the loss table.[140] Very few cases every year have losses in the top three levels.[141] Because of this, it makes little sense to create a wide distribution for so few cases. However, this alone would not solve the problem of the overlapping SOCs and the automatic thirteen-level offense level increase for securities fraud crimes.

Third, in combination with the second suggestion, the Commission could eliminate the overlapping SOCs for fraud-on-the-market. Deleting the securities-law violation SOC alone would lead to a four-level decrease. Because the SOC for "endangering the solvency of a publicly traded company" already covers securities frauds, there is no need for securities law violation SOC.

Finally, the least likely but most effective option: delete the loss table for fraud-on-the-market offenses. This option would reflect the fact that both loss and gain are improper proxies for culpability in fraud-on-the-market offenses, reflect that both loss and gain are impractical to calculate for fraud-on-the-market offenses, and actually make fraud-on-the-market sentencing recommendations proportionate.

Because fraud-on-the-market offenders are motivated by keeping the companies they work for afloat, and in turn keeping their highly lucrative jobs, the actual loss to the market is merely incidental to their culpability.[142] Scholars have criticized the Guidelines for using loss as a proxy where more direct measures of

---

140. BOWMAN, *supra* note 97, at 15–16.

141. *Id.* '[O]nly 56 of the more than 7,000 defendants sentenced under 2B1.1 (or roughly 0.7%) fell into [the top three loss levels.]' *Id.*

142. *But see generally* Cassidy, *supra* note 59 (arguing that fraud-on-the-market offenders are motivated by monetary gains through stock options).

culpability, like motive, are available.[143] This critique is even more salient for fraud-on-the-market offenses where neither loss to the market nor personal gain is the objective.[144] Here, loss is not an appropriate measure of culpability at all. Unlike other economic offenses, like theft or common law fraud, where an offender directly harms victims, in fraud-on-the-market offenses it is impossible to truly determine who was harmed and the extent of harm because of external market forces.

As demonstrated above, loss is not easily calculated because external market forces contribute to the total loss. Similarly, as the DOJ pointed out, gain is mostly non-existent because the motivation of the fraud is often to benefit the company, not the individual actor. The purpose of a proxy is to provide a measurement that comes close to objectively quantifying something subjective and unquantifiable, like culpability. Because proxies are imperfect in that they do not directly measure culpability, even objective proxies are inexact. Thus, it is important for proxies to be objectively based and easily quantifiable so that another layer of inaccuracy is not added to the already inexact calculation. The fact that both gain and loss fail to provide objectively quantifiable measurements means that each fails as a proxy.

Additionally, because the Commission has modified the victim's table, there is already a very reliable and quantifiable measurement for culpability in the new proposed Guidelines. Under the proposed Guidelines, the loss table changes from measuring the number of victims, to measuring the hardship to those victims. The amendments read:

> (2) (Apply the greatest) If the offense—
>
> > (A) (i) involved 10 or more victims; ~~or~~ (ii) was committed through mass-marketing; or (iii) **resulted in substantial financial hardship to one or more victims**, increase by 2 levels;
> >
> > (B) ~~involved 50 or more victims~~ **resulted in substantial financial hardship to five or more victims**, increase by 4 levels; or
> >
> > (C) ~~involved 250 or more victims~~ **resulted in substantial financial hardship to 25 or more**

143. *See* Bowman, *supra* note 7, at 171-72.

144. *See, e.g.* U.S. Dep't of Justice, *supra* note 130, at 33–35.

> **victims**, increase by 6 levels.[145]

Instead of inquiring whether the defendant caused monetary harm to financial markets involving thousands of people, the court would only need to inquire into the harm to at most twenty-five people. Although this does not resolve the causation issues, it measures culpability more directly than either loss or gain.

These proposed changes that actually address the disproportionate sentencing problem will most likely never be imposed because there is not a large incentive for the Commission or Congress to change the status quo. Congress does not have a strong incentive to direct the Commission to change the Guidelines because, as previously explained, public sentiment is against high-loss securities fraud defendants. Congress also doesn't have an incentive to direct the Commission to change 2B1.1 because judicial discretion means that few of these disproportionate sentencing recommendations will be implemented anyway.

VI. CONCLUSION

Although the Commission proposed creative and thoughtful solutions to solve the problem of disproportionate sentences for fraud-on-the-market offenses, without a stronger incentive to implement these solutions, the Guidelines will become irrelevant for securities fraud crimes. Currently, the incentive to change the Guidelines is lacking due to overwhelming public sentiment against white-collar criminals, the strong influence of the DOJ in the amendment process, the relatively few fraud-on-the-market offenses litigated each year, and the judiciary's ability to freely depart from the Guidelines. Without amending the sentencing calculation for fraud-on-the-market, sentences will have few bases in culpability and more in the individual whims of the court.

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145. PROPOSED AMENDMENTS, *supra* note 123, at 77 (emphasis added).

Did the FTC Actually Lose POM Wonderful? Health Claims, Prior Substantiation, and the First Amendment

Ryan McCarthy*

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I. INTRODUCTION

How sure do we want to be that what a company says about its product is actually true? The answer to this question is likely going to differ for each person. Because an advertisement affects more than a single person, however, there must be a policy that suits the needs of the general public.

The FTC is responsible for developing a standard for this, and its answer is the Prior Substantiation Doctrine. The Prior Substantiation Doctrine restricts commercial speech that has no evidentiary basis.[1] The FTC considers a claim, its context, and also requires a reasonable level of evidence.[2] The question becomes even more difficult when the parties have to deal with burdensome efforts

1. *See infra* Part II (discussing the details of the prior substantiation doctrine).
2. *Id.*

to gather the required amount of evidence required or the constraints imposed by the First Amendment's Commercial Speech Doctrine.[3]

As might be expected, acquiring evidence to support a claim that can be difficult to evaluate, like claims related to health, can be problematic for a party.[4] Thus, health related claims frequently show the tension between the Prior Substantiation Doctrine and the First Amendment. Indeed, the most recent collision between these two doctrines played out in the D.C. Circuit between POM Wonderful (POM) and the FTC over claims that its pomegranate juice prevented and mitigated medical issues related to heart health, erectile dysfunction, and prostate cancer.[5] The FTC, working under the Prior Substantiation Doctrine, required POM to support its disease-related claims with two random human clinical trials (RCT).[6] POM argued that this heavy burden was not necessary to advance the FTC's interest, namely protecting consumers by ensuring accurate information in the market, and thus, was prohibited by the Commercial Speech Doctrine under the First Amendment.[7] The circuit court agreed with POM and limited the FTC's power to require RCTs. In reaching this holding, the court presumed that the scientific community could determine a study's accuracy and assess relevant scientific evidence.[8]

Part I will outline the Prior Substantiation Doctrine and the FTC's general enforcement powers. Part II addresses the inevitable question of how much evidence is required to bring a claim against a company. The DC Circuit's decision in *POM Wonderful* is discussed in Part III of this Note. Part IV argues that, because there are many ways a party funding research can manipulate outcomes and hide unfavorable results, the court's presumptions may be false often enough to warrant allowing the FTC to have broader power to require multiple RCTs. Lastly, this Note argues in Part V that the FTC, along with private plaintiff attorneys, should create the

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3. *See infra* Part III (discussing the First Amendment challenge and limits to the prior substantiation doctrine).

4. U.S. FED. TRADE COMM'N, DIETARY SUPPLEMENTS: AN ADVERTISING GUIDE FOR INDUSTRY 8–9 (2001), https://www.ftc.gov/system/files/documents/plain-language/bus09-dietary-supplements-advertising-guide-industry.pdf [hereinafter SUPPLEMENT POLICY STATEMENT].

5. POM Wonderful, LLC v. FTC, 777 F.3d 478, 483 (D.C. Cir. 2015); *infra* Part III.A.

6. *POM Wonderful*, 777 F.3d at 489; *infra* Part IV.A.

7. *POM Wonderful*, 777 F.3d at 501.

8. *See infra* Part IV.C (discussing the court's logical reasoning and presumptions in detail).

opportunity for the D.C. Circuit to cabin the holding of *POM Wonderful* to the facts of that case.

II. FTC'S ENFORCEMENT POWER AND PRIOR SUBSTANTIATION DOCTRINE FRAMEWORK

The FTC possesses power to enforce advertisement claim restrictions pursuant to Section 5 of the FTC Act, which forbids, "[u]nfair methods of competition and unfair or deceptive acts or practices in or affecting commerce."[9] The scope of this power is delineated, in part, by Section 12 of the FTC Act, which defines a false advertisement[10] as "an unfair or deceptive act or practice in or affecting commerce within the meaning of section [5] of [the FTC Act]."[11] The FTC has authority to further set out the meaning of "unfair or deceptive acts or practices in or affecting commerce (within the meaning of section [5] of [the FTC Act])" through the promulgation of "statements of policy" pursuant to Section 18.[12] The guidelines, while not self-executing, are an indication of the FTC's interpretation of Section 5. If an entity or person disseminating information does not adhere to the guidelines, the FTC may seek to impose liability.

The FTC's *Policy Statement Regarding Advertising Substantiation* (*Substantiation Statement*) and its *Deception Policy Statement* form the touchstones of the Prior Substantiation Doctrine. The *Deception Policy* is a more specific inquiry into the *Substantiation Policy*.[13] Under the FTC's *Deception Policy*, determining whether there is deception in violation of Section 5 requires a three-step inquiry into (1) what claims are conveyed in an advertisement, (2) whether those claims are false, misleading, or unsubstantiated, and (3) whether the claims are material to

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9. 15 U.S.C. § 45 (2012).

10. 15 U.S.C. § 52 (2012) ("false advertisement for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase in or having an effect upon commerce, of food, drugs, devices, services, or cosmetics").

11. *Id.*

12. 15 U.S.C. § 57a (2012).

13. *Policy Statement Regarding Advertising Substantiation*, *appended to* Thompson Med. Co. 104 F.T.C. 648, 839 (1984), *aff'd*, 791 F.2d 189 (D.C. Cir. 1986) FTC (Mar. 11, 1983), http://www.ftc.gov/bcp/guides/ad3subst.htm [hereinafter *Substantiation Policy*]; *Policy Statement on Deception*, *appended to* Cliffdale Assocs. Inc. 103 F.T.C. 110, 174 (1984), FTC (Oct. 14, 1983), https://www.ftc.gov/public-statements/1983/10/ftc-policy-statement-deception [hereinafter *Deception Policy*].

prospective consumers.[14] The litigation of health claims focused on in this Note revolves around the second step's inquiry into a statement's accuracy and level of substantiation. [15]

The FTC's standards set out in the *Substantiation Policy*, which outlines the FTC's understanding of what constitutes adequate substantiation for avoiding liability under Section 5, help give more context to the inquiry.[16] The FTC first determines which claims the advertisement conveys.[17] Then, the FTC categorizes the claims as either "efficacy claims" or "establishment claims."[18] Efficacy claims convey a product's supposed benefit or function without mention of scientific proof of the product's effectiveness.[19] Establishment claims, however, expressly or implicitly convey that a product's effectiveness has been proven, perhaps via a reference to scientific studies or by showing a person in a lab coat.[20] Establishment claims can be further classified as either "specific" or "non-specific," depending on the type of substantiation conveyed by the claim.[21] Specific claims indicate a more precise level of substantiation.[22] Non-specific claims, on the other hand, convey a general sense of substantiation through the advertisement's language.[23] An advertisement's claim, whether express or implied, can be characterized as an efficacy claim, specific establishment claim, or non-specific establishment claim.

Because the level of substantiation required hinges on the classification of the claim, the first step of the inquiry may be dispositive of the second step, in which the FTC determines if a claim is unsubstantiated. An advertiser must have a "reasonable basis" of substantiation before disseminating an efficacy claim,

14. *Deception Policy*, *supra* note 13, at 174; Kraft, Inc. v. FTC. 970 F.2d 311, 314 (7th Cir. 1992).

15. *See infra* Part III (discussing the use of the reasonable basis standard in measuring accuracy and substation of claims).

16. *See Substantiation Policy*, *supra* note 13, at 839 (describing the requirements of adequate prior substantiation).

17. The standards for determining whether an advertisement actually conveys a claim are outside the scope of this Note.

18. Thompson Med. Co. v. FTC, 791 F.2d 189, 194 (D.C. Cir. 1986).

19. Removatron Int'l Corp. v. FTC, 884 F.2d 1489, 1492 n.3 (1st Cir. 1989).

20. *Thompson Med. Co.* 791 F.2d at 194.

21. *Removatron*, 884 F.2d at 1492 n. 3.

22. *Id.*

23. *Removatron*, 884 F.2d at 1492 n. 3 (examples of language used in non-specific establishment claims include 'tests prove' or 'studies show").

regardless of the advertiser's intent to convey the claim.[24] As originally set out in the FTC's decision in *Pfizer*[25] and later adopted in the *Substantiation Policy*, a "reasonable basis" is determined by considering six factors: (1) the type of product, (2) the type of claim, (3) the benefit of a truthful claim, (4) the ease of developing substantiation for the claim, (5) the consequences of a false claim, and (6) the amount of substantiation experts in the field would consider reasonable.[26]

Establishment claims, however, are not examined under the *Pfizer* factors. Rather, the "advertiser must possess the specific substantiation claimed"[27] for specific establishment claims and "evidence sufficient to satisfy the relevant scientific community of the claim's truth" for non-specific establishment claims.[28] Each classification requires some level of substantiation and thus, an advertiser who disseminates a claim without some level of prior substantiation is exposed to liability under Section 5.[29]

The requirement for substantiation is clear, but what type and quantity of scientific research an advertiser must have to satisfy the requirement is significantly less clear. In fact, it has proven difficult to translate the FTC's broad standards into a solid platform on which it is comfortable for advertisers to rely. Especially in the context of health claims, which combine a difficulty to substantiate with their inherent appeal to consumers, advertisers may take liberties with their advertisement claims and the supporting science.

A better meaning of a reasonable basis emerged because of the FTC's application of the standard over many decades.[30] However, as explained in the following section, the FTC decided to change the rules without informing anyone by altering the

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24. Pfizer Inc. 81 F.T.C. 23, 30 (1972); *see Substantiation Policy*, *supra* note 13, at 174 (reaffirming the FTC's commitment to requiring advertising substantiation with a reasonable basis for claims).

25. *Pfizer Inc.* 81 F.T.C. at 30.

26. *Id.*

27. Thompson Med. Co. v. FTC, 791 F.2d 189, 194 (D.C. Cir. 1986).

28. Bristol–Myers Co. 102 F.T.C. 21, 321 (1983), *aff'd*, 738 F.2d 554 (2d Cir. 1984).

29. *See Substantiation Policy*, *supra* note 13, at 839 ("Therefore, a firm's failure to possess and rely upon a reasonable basis for objective claims constitutes an unfair and deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act. ').

30. *See* Maureen K. Ohlhausen, *100 Is the New 30: Recommendations for the FTC's Next 100 Years*, 21 GEO. MASON L. REV. 1131, 1141 (2014) (discussing the history and guidance provided by the reasonable basis standard).

requirements for meeting the reasonable basis standard in recent years.

III. LEVEL OF SUBSTANTIATION: THE RETREAT FROM THE "REASONABLE BASIS" STANDARD

The FTC's 1972 decision in *Pfizer* was the beginning of the requirement that an advertiser possess a "reasonable basis" for advertising claims.[31] This standard, along with the *Pfizer* factors, was reiterated in the 1983 *Substantiation Statement*.[32] In the 1990's, the FTC promulgated additional policy statements focused specifically on health claims made by food and supplement advertisers.[33] These subsequent policy statements have elaborated the reasonable basis standard in the health claim context, thereby providing a better understanding of what the FTC considers sufficient prior substantiation.[34] For example, the *Food Policy Statement* states that the requisite level of substantiation for health claims as "usually require[s] competent and reliable scientific evidence" where "scientific evidence consist[s] of tests, analyses, research, studies or other evidence conducted using procedures generally accepted in the relevant profession. "[35] Then in the *Supplement Policy Statement*, the FTC included more detail about the various levels of substantiation.[36] For example, the *Supplement Policy Statement* stated, "[a]s a general rule, well-controlled human clinical studies are the most reliable form of evidence."[37] While these statements have provided greater guidance to the industry, the FTC kept the substantiation standard flexible and rooted in a case-by-case "reasonable basis" analysis, rather than applying a more rigid standard with pre-prescribed types of tests for certain classes of

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31. J. Howard Beales III, et al. *In Defense of the Pfizer Factors* 1 (George Mason Univ. Law & Econ. Research Paper No. 12-49, May 2012), http://www.law.gmu.edu/assets/files/publications/working_papers/1249InDefenseofPfizer.pdf.

32. *See Substantiation Policy*, *supra* note 13, at 839.

33. In addition to the *Supplement Policy Statement*, *supra* note 4, the FTC's 1994 *Enforcement Policy Statement on Food Advertising* is relevant to the issues discussed in this Note. *Enforcement Policy Statement on Food Advertising*, FTC (May 13, 1994), http://www.ftc.gov/bcp/policystmt/ad-food.shtm [hereinafter *Food Policy Statement*].

34. *See Supplement Policy Statement*, *supra* note 4, at 8–9 (elaborating on the reasonable basis standard).

35. *See Food Policy Statement*, *supra* note 34.

36. *Supplement Policy Statement*, *supra* note 4, at 8–9.

37. *Id.* at 10.

products or claims.[38] After decades of application of the reasonable basis standard, express advancement, and clarification through FTC policy statements, the reasonable basis standard became the expectation within the industry.[39] Additionally, the guidelines, anchored in the reasonable basis standard, have not been repealed or supplemented to indicate any material alteration in the requisite level of substantiation.[40]

Thus, as the FTC changed course over the past several years in favor of a standard requiring two RCTs, concern arose that a change in expectations would lead to less frequent use of beneficial health claims by advertisers.[41] Recent FTC orders have frequently required that an advertiser possess two RCTs before disseminating a health-related claim, akin to the level of substantiation required for FDA drug approval.[42] Additionally, some consent orders entered into by food and supplement industry incumbents have gone as far as requiring pre-approval by the FDA itself before disseminating certain claims.[43] This shift to a more stringent, two-RCT standard has found members of the industry surprised and frustrated with the change in policy by the FTC. Even former FTC Chairman Timothy Muris has argued that the FTC has "lost its way" in how it regulates advertisements.[44]

While these more recent orders often use the language connected with the reasonable basis standard, using language such as "competent and reliable scientific evidence," the orders also incorporate a rigid two-RCT standard.[45] Incorporating the specific testing requirements in the reasonable basis standard eliminates the inherent flexibility of the prior substantiation doctrine, which has

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38. Beales, *supra* note 32, at 2.

39. *Id.* at 1.

40. Ohlhausen, *supra* note 31, at 1141 (noting that recent Commission orders 'seem to have adopted' a two-RCT standard for health claims).

41. *Id.* at 1142 (discussing the changing expectations of advertisers and harm caused to consumers). *See* Randal Shaheen & Amy Mudge, *Has the FTC Changed the Game on Advertising Substantiation?* 25 ANTITRUST 65, 65–66 (Fall 2010) (examining the history of the reasonable basis standard).

42. Beales, *supra* note 32, at 3.

43. *Id.* (citing *In re* Nestlé Healthcare Nutrition, Inc. 92–3087, 2010 WL 2811203, at *3 (F.T.C. July 14, 2010)).

44. Ohlhausen, *supra* note 31, at 1143 (citing Timothy J. Muris, Chairman, FTC, Keynote Panel at the George Mason Law Review and Law & Economics Center Antitrust Symposium: The FTC: 100 Years of Antitrust and Competition Policy (Feb. 13, 2014, 48:18), http://vimeo.com/86788315).

45. *See Nestlé Healthcare*, 2010 WL 2811203, at *11 (finding that 'competent and reliable scientific evidence means at least two adequate and well-controlled human clinical studies").

historically allowed for the substantiation to be tailored to the specific claim.

Given the severe penalties under Section 5 for deception,[46] this shift in the FTC's substantiation requirement, unaccompanied by any new policy statements, may subject advertisers to substantial liability for not possessing adequate research for each claim.[47] POM, a company built around promoting its products' health benefits, decided to challenge the FTC's new approach in the federal courts.[48]

IV POM WONDERFUL V. FTC: CUTTING SHORT THE FTC'S NEW APPROACH TO PRIOR SUBSTANTIATION

When POM argued that the First Amendment prohibited the FTC from requiring POM to cite two RCTs before continuing to disseminate disease-related claims in its advertisements, it was thought that the food and supplement industry would garner an understanding of the FTC's position on substantiation at a minimum and, hopefully, see the demise of the two-RCT requirement.[49] After taking almost a year to decide, the court handed down a decision that was all that an advertiser could have hoped for: a construction of the commercial speech doctrine under the First Amendment that prohibits a two RCT prior-substantiation standard except in "narrow circumstances based on particularized concerns."[50]

In rejecting the FTC's rationale for imposing a two-RCT requirement for POM, the court was not convinced that an advertiser's history of intentionally deceiving consumers had any

46. Once an advertiser is found to have violated Section 5 they are exposed to an array of liabilities, including: cease-and-desist order with daily penalties, fencing in relief, periodic compliance reports, monetary restitution, and corrective advertising. Company officers in their personal capacity and third party intermediaries can also be subject to these penalties. Anne Maher & Lesley Fair, *The FTC's Regulation of Advertising*, 65 Food & Drug L.J. 589, 615–18 (2010). Recent cases have indicated that the FTC is imposing stricter penalties now than they have in the past, such as seeking damages in administrative orders for failing to have the requisite substantiation. Beales, *supra* note 32, at 4.

47. Elaine Watson, *Will POM Wonderful Case Finally Clear Up Confusion Over What Evidence Is Needed to Support Ad Claims?*, FOOD NAVIGATOR–USA (Dec. 7, 2012), http://www.foodnavigator-usa.com/Regulation/Will-POM-Wonderful-case-finally-clear-up-confusion-over-what-evidence-is-needed-to-support-ad-claims.

48. *See infra* Part III (discussing POM Wonderful's commercial speech challenge to the Commission's Order).

49. Watson, *supra* note 48.

50. POM Wonderful, LLC v. FTC, 777 F.3d 478, 504–05 (D.C. Cir. 2015).

importance to the analysis.[51] Further, the court was not convinced that a need for independent validation through a second RCT justified the restriction.[52] In reaching this conclusion, the court relied on two implicit presumptions: (1) the scientific community is able to determine if the results of a single RCT are reliable and accurate without the need for a second RCT, and (2) there is full and known disclosure of relevant scientific evidence.[53]

If these presumptions are false, then consumers, the FTC, and the scientific community still may not be able to verify the validity of a claim. In such an event, requiring an additional RCT increases the probability that a claim is valid by replicating results when the scientific community is unable to ensure validity, and by forcing more disclosure when there is reason to believe information is being withheld. Due to the litany of techniques at the disposal of a company funding research, the frequency with which the court's presumptions are false may be great enough to warrant a construction of the commercial speech doctrine that does not restrict the imposition of a second RCT to "narrow circumstances based on particularized concerns."[54] A broader construction would enable the FTC to protect consumers by ensuring the accuracy of information in the market.

A. The Background, the Commission's Order. and the First Amendment Challenge

POM, a producer and marketer of pomegranate-based products, disseminated ads from 2003 to 2010 conveying implied and express claims that its products could treat, prevent, or reduce the risk of heart disease, prostate cancer, and erectile dysfunction.[55] The FTC filed a complaint alleging that forty-three advertisements contained false, misleading, or unsubstantiated claims in violation of Section 5 of the FTC Act.[56] After appeal by both parties from an administrative law judge (ALJ) finding that nineteen of the ads violated Section 5, the full Commission affirmed the ALJ's decision, with four of the five Commissioners finding that thirty-six of POM's ads were false, misleading, or unsubstantiated.[57]

51. *Id.* at 505.
52. *Id.* at 502.
53. *Id.* at 502–03.
54. *Id.* at 504.
55. *POM Wonderful*, 777 F.3d at 483.
56. *Id.* at 488.
57. *Id.* at 488–89.

The Commission's order prohibited POM from making any representation that any of its food, drug, or dietary supplement were "effective in the diagnosis, cure, mitigation, treatment, or prevention of any disease" unless supported by "competent and reliable scientific evidence that, when considered in light of the entire body of relevant and reliable scientific evidence, is sufficient to substantiate that the representation is true."[58] The order further explained that, "competent and reliable scientific evidence shall consist of at least two randomized and controlled human clinical trials."[59] However, unlike disease claims, the order did not incorporate the requirement of a second RCT in the "competent and scientific evidence" standard of "health benefits" claims.[60]

POM argued, among other things, that the Commission's order violated the First Amendment commercial speech doctrine because it was broader than necessary to achieve the government's interest of preventing consumer confusion.[61] Specifically, it was alleged that the Commission could have advanced the government's interest by imposing more narrow remedies, such as the competent and reliable scientific evidence standard without the language incorporating a two-RCT requirement.[62] Although POM was unsuccessful in its other arguments, the D.C. Circuit accepted this part of its First Amendment contention.[63]

B. The D.C. Circuit Left Open the Issue of When a Second RCT is Justified

Although the circuit court determined that a two-RCT requirement for disease claims was improper under the facts of this specific case, it did not explain under what circumstances a two-RCT requirement would be appropriate.[64] In reaching its decision that a two-RCT requirement was improper, the court applied the *Central Hudson*[65] test, which states that the FTC has the burden of showing

58. *Id.* at 489.
59. *Id.*
60. *Id.*
61. Final Brief for Petitioner at 48, *POM Wonderful*, 777 F.3d 478 (No. 13-1060).
62. *Id.* at 50.
63. *POM Wonderful*, 777 F.3d at 503.
64. *Id.*
65. *Id.* at 501.

that the challenged restriction on commercial speech is "not more extensive than necessary" to serve the governmental interest.[66]

The court rejected the FTC's argument that the two-RCT requirement was consistent with the precedent of both the court and the FTC, was required to validate potentially defective studies, and acted as a barrier against advertisers intentionally deceiving consumers.[67] The court reasoning appears to be more akin to the least restrictive means prong of a strict scrutiny analysis rather than the intermediate level of scrutiny affiliated with the commercial speech doctrine under *Central Hudson*.[68] In so doing, the court cabined the use of the two-RCT standard to "narrow circumstances based on particularized concerns."[69] The court did not clearly establish what constitutes particularized concerns. However, through the court's rejection of the FTC's justifications for requiring a second RCT in this case, a rough understanding of what is not sufficient to constitute a particularized concern is established.

1. The Two-RCT Standard is Cabined to "Particularized Concerns"

Looking to its own precedent, the court noted that it had previously recognized that the "FTC has usually required two well-controlled clinical tests" before allowing certain establishment claims to be disseminated.[70] However, the cases imposing the two-RCT requirement all "involved a highly specific type of representation: establishment claims about the comparative efficacy of over-the-counter analgesics."[71] Such cases involved the subjective nature of pain, which was further magnified by the comparative nature of the claim, and the FDA's specialists on analgesics specifically recommended that two RCTs be required.[72] Thus, the court in *POM Wonderful* explained that judicial precedent allowed a second RCT requirement "only in narrow circumstances

66. Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of N.Y 447 U.S. 557, 566 (1980).

67. *POM Wonderful*, 777 F.3d at 503–06.

68. *See id.* (finding the commissioner's order 'fails *Central Hudson* scrutiny insofar as it categorically requires two RCT's for all disease-related claims"); *see also Cent. Hudson*, 447 U.S. at 566 (requiring that the means by which a commission seeks to further its asserted interest 'is not more extensive than it is necessary to serve that interest").

69. *POM Wonderful*, 777 F.3d at 504.

70. *Id.* at 503.

71. *Id.*

72. *Id.*

based on particularized concerns," but not in the broad attempt to prevent companies from misleading consumers.[73]

Turning to the FTC's past orders imposing two RCTs, the court was again not satisfied that the FTC had imposed two RCTs in a way that justified its use under the broad reasoning of consumer protection. The court noted that having looked at all the orders cited by the FTC, not one explained why two RCTs were required to prevent the claims at issue from being misleading.[74] Some of the previous consent orders had applied the two-RCT requirement for some claims but not others.[75] Others still had imposed less support than even a single RCT for some claims[76] Further, the Commission had even allowed a single RCT after an ALJ imposed a two-RCT requirement.[77] Considering these previous orders, the court explained that the precedent of the FTC matched its own; two RCTs were only "selectively imposed in specific circumstances based on particular concerns."[78]

From the discussion of precedent, it is apparent that when the FTC wants to restrict speech with a two-RCT standard there must be some characteristic that is unique and particular about the restricted claim requiring something above and beyond a single RCT It is not clear, however, when these unique and particularized concerns rise to a level sufficient to warrant this heightened restriction. But, given the specificity with which the court explained when the requirement was justified in past situations and the repeated use and emphasis on "particular concerns," it is likely the scope of situations that sufficiently warrant two RCTs is very narrow, perhaps so narrow as to only include claims comparing the subjective effects of certain medication. But certainly, a broad concern about consumer protection from being misled is not an adequate concern to warrant a restriction on claims absent two RCTs.

While the court did not explain exactly where the line for the two-RCT standard exists, the facts of POM Wonderful were such that, in finding a second RCT unwarranted, the court provided an understanding of how far an advertiser can go and still escape the heightened restriction. The record included a litany of facts

73. *Id.* at 504.

74. *Id.*

75. *Id.*

76. *Id.*

77. *POM Wonderful*, 777 F.3d at 504.

78. *Id.*

indicating a planned deception of consumers.[79] This signals a need for the FTC to use its power to the fullest extent possible to prevent deception. But, in addressing the findings made by the Commission in the order against POM, the court made clear that FTC's concerns were insufficient to warrant a second RCT[80] Notably, these concerns are present in many deceptive advertisement cases and are applicable to a wide variety of situations outside that of disease claims.

2. Concern for the Validity of a Single RCT is Not a Particularized Concern

Expert testimony in the *POM* case offered the explanation that a second RCT was required because of the possibility of a defect in a proffered single RCT, such as a chance inaccuracy or a unique study sample.[81] In such an event, a second RCT would have the effect of providing an independently replicated result, thereby providing a mechanism to ensure consistent and accurate results.[82] In rejecting this concern as being adequate, the court reasoned that a RCT that satisfies the order must meet the "competent and reliable scientific evidence" standard, which, per the order, requires the study to be "generally accepted in the profession to yield accurate and reliable results."[83] Thus, because the scientific profession would not accept that a flawed RCT yielded accurate results, it would not meet the order requiring only one RCT[84] The imposition of a second RCT then is simply a greater restriction on speech than required to achieve the government's interest. While the FTC thought the possibility of defective studies warranted additional restrictions as a means of ensuring the protection of consumers,[85] it apparently does not fall within the particular circumstances required by the court.

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79. *Id.* at 484–88 (discussing POM's intentional reliance upon poorly conducted studies providing favorable results in their advertisements while failing to mention more reliable studies showing unfavorable results for a multitude of claims over many years).

80. *See infra* section IV.B.2–3 (discussing the court's rejection of the FTC's justification for imposing a second RCT requirement in this case).

81. *POM Wonderful*, 777 F.3d at 504.

82. *Id.*

83. *Id.*

84. *Id.*

85. Brief of Respondent at 76–77, *POM Wonderful*, 777 F.3d 478 (No. 13-1060).

3. A History of Intentional Deception is Not a Particularized Concern

While addressing the FTC's final justification for the two-RCT requirement, the court made clear that an advertiser's deceptive history or intentional dissemination of deceptive claims does not adequately satisfy the FTC burden of justifying the restriction on speech.[86] The FTC had argued that POM "demonstrated [a] propensity to misrepresent to [its] advantage the strength and outcomes of scientific research," and "[had] engaged in a deliberate and consistent course of conduct;"[87] therefore, a second RCT would act as a safeguard against future misrepresentations and provide greater confirmation of validity.[88]

The court rejected FTC's justification for two reasons. First, the court explained that every defendant to an FTC order has been found to have engaged in some form of deceptive advertisement,[89] as there would not be liability otherwise. Therefore, a defendant's history does not justify imposing a second RCT, as the requirement would apply in every case.[90] Second, the court reasoned that because the order requires claims to be based on "competent and reliable scientific evidence that, *when considered in light of the entire body of relevant and reliable scientific evidence*, is sufficient to substantiate that the representation is true," the second RCT was unnecessary to prevent the dissemination of unsupported favorable research results.[91] Therefore, the court noted that it was unclear what a second RCT provided above and beyond what was already provided for in the order. [92]

Notably, the court recognized that POM had selectively chosen which research to represent in its advertisements. Further, the court went on to state that "[t]he Commission [did] not explain how the two-RCT requirement is reasonably linked to the particular history of petitioners' wrongdoing."[93] This indicates that not only is a history of deception not a particularized concern, but also that a history of intentional deception through manipulating scientific evidence is also not a particularized concern justifying a two-RCT

86. *POM Wonderful*, 777 F.3d at 505.
87. *Id.*
88. Brief of Respondent, *supra* note 86, at 77.
89, *POM Wonderful*, 777 F.3d at 505.
90. *Id.*
91. *Id.*
92. *Id.*
93. *Id.*

requirement. Because the prior substantiation doctrine is at its core concerned with ensuring some level of accurate scientific evidence, it is difficult to imagine a situation that warrants the high barrier of a second RCT if intentionally manipulating scientific research does not.

C. *Implicit Presumptions Behind the Court's Reasoning*

In reaching the conclusion that the circumstances presented in POM did not fall within the particular circumstances that can justify the use of a second RCT, the court implicitly makes several presumptions regarding the scientific community's knowledge. If these presumptions are false, then the court's holding significantly cuts against the governmental interest in consumer protection because the two-RCT requirement would be an important mechanism for ensuring the validity of a claim where an order's less extensive restrictions have failed.

First, the court presumes that the scientific community will not accept a single RCT that does not yield accurate. This presumption is implied from the court's reasoning that a second RCT is not justified because the FTC requires "competent and reliable scientific evidence that is sufficient to substantiate that the representation is true," which must itself be "generally accepted in the profession to yield accurate and reliable results."[94] The example of a flawed RCT provided by experts, and rejected by the court, was one flawed due to chance or a unique study sample.[95] Without a presumption that the scientific community is able to distinguish between a flawed RCT with a skewed sample and a reliable RCT, a second RCT is not an additional burden that fails to advance the governmental interest in preventing false information from deceiving consumers. Rather, it is a means of detecting error where the scientific community is not able to do so.

The second presumption implicit in the court's reasoning is that the entirety of scientific information is known. This presumption stems from the court's reasoning that a second RCT is not justified in preventing an advertiser from selectively relying on favorable studies because the FTC requires scientific evidence that is "*considered in light of the entire body of relevant and reliable scientific evidence*."[96] If all studies were in fact not known by the scientific community,

94. *POM Wonderful*, 777 F.3d at 504 (quoting Order at *15, POM Wonderful LLC, No. 9344, 2010 WL 3799084 (F.T.C. Jan. 10, 2013)).
95. *Id.*
96. *Id.* at 505.

then a single RCT may be nothing more than a single flawed favorable result from among a multitude of unfavorable accurate results. In such a situation, a second RCT would not be a burden in addition to the restriction already imposed by the order. Rather, it would be a mechanism imposing a hurdle that would curtail an advertiser's ability to intentionally select favorable results, thereby forcing greater disclosure by the advertiser when there is not a mechanism for the scientific community to consider the evidence known only to the advertiser.

While these presumptions may not always be false, the two-RCT requirement can be seen as a verification imposed as a last resort when the FTC has reason to believe the presumptions are false. In such a situation, the two-RCT requirement would not be more extensive than necessary to serve the governmental interest because the less extensive restrictions of the order would likely fail.[97] As discussed in the proceeding section, the frequency with which these presumptions are false is potentially great enough to warrant the use of a second RCT in a broader set of situations than the court has deemed valid under the commercial speech doctrine.

V REASONS TO DOUBT THE COURT'S PRESUMPTIONS: RESEARCH MANIPULATION AND NONDISCLOSURE

The presumptions underlying the court's reasoning for holding a second RCT restriction as more extensive than necessary are potentially false in many circumstances due to various ways the scientific process can be manipulated to advance outcome–oriented research.[98] If an economically interested party is able to either (1) make unreliable results acceptable to the scientific community or (2) control the body of relevant scientific evidence, then the court's presumptions will be false. The former can be accomplished through an advertiser's manipulation of a study, unbeknownst to outsiders,

97. It is irrelevant for this analysis whether or not there is a more optimal way than a second RCT of increasing the probability of accuracy, as the court measured the extensiveness of a second RCT restriction against the less extensive 'base line' restrictions imposed by the order. It was not compared to some other less extensive test that is also capable of ensuring validity. Thus, this Note does not need to argue that a second RCT is necessary, it only needs to address if a second RCT advances the governmental interest in a way not provided for in the Order when the court's presumptions are false.

98. *See infra* part V.A–B. (discussing the potential opportunities an advertiser possesses when funding research to determine the outcome and hide unfavorable outcomes).

and the latter can be accomplished through an advertiser's ability to exercise control over the results of a study. When an advertiser accomplishes this, it will be able to evade liability if the FTC has no mechanism other than requiring a second RCT that is able to function as a supplement for the scientific community and ensure greater disclosure of evidence. Thus, if it is true that an advertiser is able to control the scientific process to their advantage in many cases and if there are no other mechanisms that are capable of advancing the governmental interest of protecting consumers in way that a second RCT can, then the FTC needs to be able to impose a two-RCT requirement in a broader scope of situations than articulated by the D.C. Circuit.

A. Outcome Oriented Research: Difficulty in Determining Reliable Results from Unreliable Results

It has been recognized that, through the many inherent steps of conducting a scientific study, a study's funder can introduce outcome–determinative bias, allowing favorable rather than reliable or accurate results.[99] While this alone does not render false the court's presumption about the ability of the scientific community to detect unreliable evidence, it has also been recognized that this bias can be so pervasive that it is difficult to detect "even with vigorous scrutiny by sophisticated peers."[100] Coupled with the realization that "research financed by an entity with an economic stake in a regulatory decision or lawsuit is unlikely to be replicated by independent scientists,"[101] it would seem that a single defective RCT, either by intentionally induced bias or by chance, would be well-shielded from being deemed inaccurate or unreliable by the scientific community.

The FTC's desire to require a second RCT in order to independently validate a study can be better understood when viewed against the backdrop of the many possible ways of manipulating and introducing bias into scientific studies, which then become the basis for substantiating health–related claims. From the outset of a study, research protocols must be established, which involves a great deal of discretion.[102] Because of the discretion inherently involved in the protocol setting choice, the chance of

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99. THOMAS O. MCGARITY & WENDY E. WAGNER, BENDING SCIENCE: HOW SPECIAL INTERESTS CORRUPT PUBLIC HEALTH RESEARCH 65 (2008).

100. *Id.*

101. *Id.*

102. *Id.*

obtaining a desired outcome can be greatly increased.[103] The conflict of interest that arises when the design is influenced by a funding entity is often not disclosed, further decreasing the chance of discovery by the scientific community.[104] Even in research fields with much greater oversight than deceptive advertising, such as FDA drug approval, biased study design in not uncommon.[105] After data has been collected it must often be statistically analyzed, a process which involves placing a large degree of judgment in the hands of the company controlling the research.[106] The statistical analysis is then subjected to another source of manipulation as it is interpreted.[107] A manipulated interpretation allows for putting negative data into a positive perspective and can give a favorable meaning to results that might otherwise be unfavorable.[108] The outcome-oriented goal of the research does not stop after the study is completed. Techniques such as ghostwriting and redundant publication can further deceive the scientific community.[109]

B. Controlling the Body of Relevant Scientific Evidence: Nondisclosure Contracts

The court's presumption that an entire body of scientific evidence is a known set of information that can be compared to the research an advertiser uses as the basis for making health claims appears to rest on unstable ground when considered in light of the multitude of techniques at the disposal of an advertiser to cover up unfavorable results. Indeed, the court's reasoning that a second RCT is not required to prevent the reliance on favorable results creates a perverse incentive for a company to prevent the results of any unfavorable study from ever being known by the scientific community.[110] With the incentive in place, law provides the tools required for a study's funder to control access to the study's results.[111]

Nondisclosure contracts are among the most effective means of stopping negative research results from ever being released into

103. *Id.* at 66–68.
104. *Id.* at 66–67.
105. *Id.* at 68.
106. *Id.* at 71–72.
107. MCGARITY & WAGNER, *supra* note 100, at 75.
108. *Id.*
109. *Id.* at 77–79.
110. *Id.* at 101.
111. *Id.* at 109.

the scientific community.[112] In effect, nondisclosure contracts and provisions allow the executives of the company funding the research to have complete control over what, if any, information will be accessible by the scientific community.[113] This control is not limited to the research conducted in house by a company's own employees, as nondisclosure contracts can also extend to control researchers being funded at universities.[114] The effectiveness of these contracts does not stem solely from legal recourse that potentially faces one who breaches, but also from the consequences of lost funding.[115] While a researcher under a nondisclosure contract can challenge the validity of a contract, thereby destroying the company's control of the information, the cost of potentially losing the suit is great enough to effectively deter a challenge because of a researcher's reliance on funding.[116] Additionally, because a company is more likely to conduct research regarding the features specific to its own products, it is unlikely that there will be an additional source of scientific evidence to refute the favorable studies the company decides to release.[117] Due to this effective control, it would be possible for an advertiser to make claims—in light of "all known evidence"—supported only by unreliable scientific evidence. Such an advertiser would be satisfying any order that does not impose some additional burden, such as a second RCT.

VI. THE FUTURE OF TWO-RCT LITIGATION: A RECOMMENDED APPROACH TO THE FTC AND CONSUMER PLAINTIFF ATTORNEYS

If the FTC wants to regain its ability to ensure accurate information in the market by imposing a two-RCT requirement in a broader set of circumstances than *POM Wonderful* held permissible, then the best course of action for the FTC may be to reframe its argument to focus on the absolute need of two RCTs, rather than focusing on why a single RCT is inadequate. The difference between these two approaches is that the latter leaves open the possibility of some other means of ensuring validity without a second RCT, whereas the former forecloses that possibility. Because the FTC has

112. *Id.*
113. *Id.* at 112.
114. *Id.* at 109–110.
115. *Id.* at 112.
116. *Id.* at 113.
117. *Id.* at 101.

the burden of justifying the restriction on speech under the *Central Hudson* test, the FTC must dissuade the court from reaching this conclusion. Indeed, there is language in *POM Wonderful* indicating that the court's holding could be cabined to the facts of that case if the FTC is successful in framing the issue.

The court noted that "the Commission went to great lengths to explain why RCTs, rather than less demanding studies, are required to substantiate the sorts of causal claims petitioners asserted in the past. But the Commission stressed that it 'need not, and does not, reach the question of the number of RCTs needed to substantiate the claims made.'"[118] Because the FTC argued that an RCT is the gold standard study compared to all other studies, but failed to argue that a second RCT is necessary to advance the governmental interest, the court was able to easily find that the second RCT was not necessary. While the FTC did offer two reasons for requiring a second RCT that were rejected by the court, the court noted, "[a]s justification the Commission tendered two grounds, *in a brief, five-sentence explanation*."[119] This indicates that had the court been presented with a better argument as to why a second RCT was required, as opposed to any other types of tests, the outcome may have been different.

Thus, it could be that the best route for the FTC going forward is to impose the two-RCT requirement where it feels the greater restriction is necessary to advance the governmental interest. In the litigation that will ensue from imposing this restriction, the FTC should center its argument on exactly what a second RCT provides in certain circumstances to the goal of consumer protection through accurate information, rather than arguing a single RCT is required above some lesser standard. Additionally, the court's language and the extended period of time taken to rule on *POM Wonderful* indicates that courts could be open to this argument and to cabining the *POM Wonderful* holding to the facts of that case.

In the subsequent litigation that will likely ensue from the *POM Wonderful* holding, consumer plaintiff attorneys should be as interested as the FTC is in trying to mitigate the reach of the case because of its possible effect on private suits under state fraud laws. Most states have enacted "baby FTC Acts" that mirror the FTC Act but provide a private cause of action for deceptive claims.[120] While a

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118. POM Wonderful, LLC v. FTC, 777 F.3d 478, 503 (D.C. Cir. 2015).

119. *POM Wonderful*, 777 F.3d at 503 (emphasis added).

120. Patrice Hayden & David Zetoony, *Consumer Protection: Theories for Bringing Civil Actions Against Notarios*, AM. BAR ASS'N 10, http://apps.american

plaintiff bringing suit pursuant to one of these state statutes cannot merely rely on a lack of prior substantiation to show that an advertisement is false or misleading,[121] lowering the level of substantiation required at the federal level will likely precipitate a similar change in state courts. What might have been perceived as deceptive for lack of substantiation by state courts may no longer appear as such. That is, advertising defendants will be sure to persuasively rest their defense upon less stringent federal standards. This may not be a silver bullet for defendants, but it is another hurdle for plaintiffs to overcome. Having a similar goal as the FTC, plaintiff attorneys should assist the FTC in future litigation through amicus briefs and by making it known that consumer protection has suffered at the state level because of the restrictions placed on the FTC by the D.C. Circuit.

VII. CONCLUSION

Advertising substantiation is an area of law where bright line standards seem to do more harm than good, which might explain why the reasonable basis standard has managed to endure through the decades and garner the support of FTC Commissioners, academics, and even advertisers. Standards apply not only to those who are regulated, but also to those that do the regulation. Thus, by removing the ability of the FTC to impose a two-RCT requirement, the D.C. Circuit has created a bright line rule in the prior substantiation doctrine. This prohibition on two RCTs might create as much harm as it was thought would be caused by the shift from the reasonable basis standard to the strict two-RCT standard. The difference, however, is that the standards imposed by the FTC are much more amenable than a D.C. Circuit ruling on the First Amendment. Because the court was potentially unaware of the vast possibility to manipulate the evidence at the basis of health claims in advertising, the FTC should adjust its strategy and litigate on behalf of consumers before the restriction of the two-RCT requirement is also perpetuated for decades.

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bar.org/publicserv/immigration/notario/dcmdva1.pdf (last visited November 7, 2016).

121. Dana Rosenfeld & Daniel Blynn, *The "Prior Substantiation" Doctrine: An Important Check on the Piggyback Class Action*, 26 ANTITRUST 68, 68 (2011).