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Comment, Constitutional and Statutory Requirements of Notice Under Rule 23(c)(2)

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CONSTITUTIONAL AND STATUTORY REQUIREMENTS OF NOTICE UNDER RULE 23(c)(2)

The respective due process clauses of the 5th[1] *and 14th*[2] *amendments guarantee fair procedures to all litigants in our courts. Class actions, by definition, create several due process problems. A class action is an action brought by an individual on behalf of himself and all other persons similarly situated.*[3] *It is a representative action where the rights of thousands of people may be determined by the suit of one or more individuals from the class.*[4] *To meet the requirements of due process the rights of the absent parties must be protected along with the rights of the litigants before the court.*

While a manuscript was being prepared on this topic and the related topic of the statutory notice requirement of Rule 23 of the Federal Rules of Civil Procedure, the University of Pennsylvania Law Review *published a student comment*[5] *on these topics closely resembling our manuscript and rendering it repetitive. However, an exhaustive symposium on Rule 23 requires a section on the constitutional and statutory notice requirements of the Rule. Accordingly, the following is a digest of the relevant sections of the* Pennsylvania *article. Points of disagreement are indicated in footnotes.*

The Advisory Committee's[6] Notes to Rule 23 cite two Supreme Court decisions dealing with the due process requirements for binding absent members of a class,[7] *Hansberry v. Lee*[8] and *Mullane v. Central Hanover Bank & Trust Co.*[9] In *Hansberry*, a suit was brought to enjoin the breach of a restrictive covenant. The defendants claimed that the covenant had never become effective since it had not been signed by the requisite number of property owners. Although the defendants could prove their assertion, the Illinois court granted the injunction[10] because it had been stipulated in an earlier class action that the requisite number of property owners had signed

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1 U.S. Const. amend. V.

2 U.S. Const. amend. XIV, § 1.

3 Black's Law Dictionary 315 (4th ed. 1968).

The due process requirements of the Constitution are equally applicable to all types of class actions. However, stricter standards may be established by Rule 23 with regard to particular types of class actions.

4 Binding absent members does not appear to present a constitutional problem so long as their interests are protected. As Judge Frankel pointed out in commenting on Rule 23, "It is not really unprecedented . . . to conclude in one fair proceeding the interests of people who do not participate in person or by counsel." Frankel, Some Preliminary Observations Concerning Civil Rule 23, 43 F.R.D. 39, 46 (1967). For example, in addition to class actions, absent parties are bound by in rem proceedings, statutes of limitations, the doctrine of laches, and the doctrine of stare decisis.

5 Comment, Adequate Representation, Notice and the New Class Action Rule: Effectuating Remedies Provided by the Securities Laws, 116 U. Pa. L. Rev. 889 (1968).

6 The Advisory Committee drafted the Federal Rules of Civil Procedure and submitted them to the Supreme Court for approval. The Notes of the Advisory Committee help to explain the meaning and intended application of the Rules.

7 39 F.R.D. 98, 106-07 (1966).

8 311 U.S. 32 (1940).

9 339 U.S. 306 (1950).

10 Lee v. Hansberry, 372 Ill. 369, 24 N.E.2d 37 (1939).

the covenant.[11] The court considered the present defendants bound by the earlier class action even though the finding in the earlier action was erroneous. Only by a direct attack on the prior judgment could the findings of the court be set aside.[12]

The United States Supreme Court reversed on the ground that the interests of the representatives in the first case were not the same as the interests of the defendants in the present action and, hence, that the present defendants were deprived of due process in the first action. In considering the requirements of due process the Court never mentioned a requirement of notice. Rather, it was concerned with the identity of interests of the representatives and the rest of the class and with the basic fairness of the representative's actions.[13] A fundamentally fair proceeding that protected the absent parties was all that the Supreme Court required. While the Advisory Committee cited *Hansberry* for the proposition that notice must be given in actions brought under subdivision (b)(3), it is not clear that such notice is required by the opinion.

Mullane is cited also for the proposition that notice must be given in a (b)(3) action.[14] In *Mullane*, the plaintiffs challenged the adequacy of the notice required under a New York banking statute.[15] The statute allowed banks to commingle the assets of several trust funds into a single investment trust. An accounting had to be submitted for court approval three times a year.[16] At these accountings the statute required the presence of separate attorneys to represent the people interested in the income of the fund and those interested in the principal.[17] If the court approved the accounting, all claims against the trustee for improper management during the term of the accounting were terminated.[18] The statute required notice by publication in a court-selected newspaper once a week for the four weeks preceding the accounting. The notice had to include only the name of the bank, the date of the fund's inception and a list of all participating trusts, estates or funds.[19] A list of the interested persons was not required. This minimal notice was the provision of the statute attacked in *Mullane*.

The interests of the attorneys serving as guardians *ad litem* in *Mullane* were quite different from the interests of the representatives in a class action. The guardian *ad litem* acts without the advice or assistance of any client. His fee is court-established and not predicated on success. Thus, his main concern may become the quick and perfunctory performance of his court-assigned duties. On the contrary, in a class action, where the attorney is paid on a contingent fee basis, the interests of the attorney and the interests of

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11 Burke v. Kleiman, 277 Ill. App. 519 (1934).

12 372 Ill. at 373, 24 N.E.2d at 39.

13 311 U.S. at 43.

14 39 F.R.D. at 107.

15 N.Y. Bank. Law § 100-c (McKinney 1950).

16 Id. § 100-c(10).

17 Id. § 100-c(11).

18 339 U.S. at 311.

19 N.Y. Bank. Law § 100-c(9) (McKinney 1950).

the absentees are identical. If the class prevails the attorney collects his fee; if the class loses the attorney goes uncompensated.[20]

This divergence of interests in the guardian *ad litem* procedure may have persuaded the Court in *Mullane* to ensure that some of the beneficiaries received actual notice of the proceedings. The Court required that mailed notice be sent to those beneficiaries whose names and addresses were known and with whom the bank regularly communicated.[21] The Advisory Committee interpreted this holding to require individual notice to all absent members of a class who could be identified through reasonable effort.

The facts of *Mullane* neither compel nor suggest such an interpretation. In *Mullane*, the Court was faced with a case where the following factors were present: (1) a possible conflict of interest; (2) a small number of beneficiaries; (3) an existing mailing list; and (4) notice published in the back pages of a newspaper. These factors are not present in the typical class action.

Of greater relevance to the class action situation is the Court's treatment of the notice required to be directed to unknown and conjectural beneficiaries. Here the statutory standard of notice by publication was sanctioned even though the Court recognized that such notice was likely to be ineffective.[22] The Court balanced the expense required to discover the names and addresses of the unknown absentees against the character of the proceedings and the nature of the interests involved.[23] It concluded that the burdens of notifying unknown absentees would outweigh the benefits of the common trust fund device.[24]

In addition to these practical considerations the Court recognized that personal notice to those on the mailing list would in effect turn the guardian *ad litem* procedure into a representative action.[25] The interests of the notified beneficiaries would be identical with the interests of the absentees.[26] An identity of interests would insure the adequate protection of the interests of the absent beneficiaries. The Court stated that "[n]otice reasonably certain to reach most of those interested in objecting is likely to safeguard the interests of all, since any objection sustained would inure to the benefit of all."[27]

It is therefore difficult to accept as correct the Advisory Committee's interpretation of *Mullane* as requiring individual notice in a class action suit. On the contrary, the language in *Mullane* tends to indicate that notice need not be sent to absent class members so long as their representatives adequately protect their interests. Thus, there does not seem to be a constitutional requirement of individual notice in class actions.[28]

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[20] See Dolgow v. Anderson, 43 F.R.D. 472, 494-95 (E.D.N.Y. 1968).

[21] 339 U.S. at 318.

[22] Id. at 317.

[23] Id.

[24] Id. at 318.

[25] Id. at 319.

[26] Id.

[27] Id.

[28] Interpreting *Mullane* to require no notice in a class action seems to ignore the result reached in that case. Mailed notice was required as to those beneficiaries who were known; publication was required as to those who were unknown. Thus, some form

While due process may not require any notice to absentees in a class action, the statutory requirements of Rule 23 must be complied with. Subdivision (c)(2) states that "[i]n any class action maintained under subdivision (b)(3), the court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort."[29]

This subdivision could prove to be the greatest impediment to the prosecution of class actions. The interpretation of this section is left largely in the hands of the trial judge, since the Advisory Committee's Notes are not very illuminating.[30] It will fall upon the trial judge to decide "the best notice practicable" and how great an effort need be made to identify individual members of the class. While the notice need not meet the rigorous procedures for service of process,[31] some minimal notice is essential. Subdivision (c)(2) appears to strike a balance between a desire to inform class members and the expense and effort needed to notify them individually.

While one would expect a balancing test to be applied in order to determine the required notice under subdivision (c)(2), the first court to consider this problem did not apply such a test. In *Eisen v. Carlisle and Jacquelin*,[32] individual notice was considered mandatory under (c)(2) despite the presence of competing interests. In *Eisen*, an action was brought on behalf of all the odd-lot traders on the New York Stock Exchange during a six-year period. Estimates of the size of the class ranged from hundreds of thousands to 3,750,000.[33] Requiring individual notice to all the members would be so costly, both in terms of investigation and mailing costs, that a class suit would be prohibitively expensive.

However, Judge Tyler refused to allow notice by publication on the grounds that both Rule 23 and due process required individual notice to all members who could be identified. Ignoring the statutory language of "best notice practicable" and "reasonable effort" the court held that the action could not be maintained because of the inherent financial limitations presented.[34] The implication of the *Eisen* decision is that class actions may be

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of notice was required to be directed to all beneficiaries. It cannot be said that the court would have upheld a statute that required mailed notice to known beneficiaries, while it completely ignored those who were unknown.

Under *Mullane*, it seems that some form of notice is constitutionally required in all class action cases. The particular form of notice will have to be determined on a case-by-case basis with the prime factors for consideration being the cohesiveness of the class, the adequacy of the representation, and the practical consequences of requiring individual notice. As the cohesiveness of the class and the adequacy of the representation increase, the need for individual notice will decrease. Similarly, as the cost of individual notice increases to the point where it will make the use of the class action suit financially impossible, other methods of notification will become more attractive.

This type of approach was adopted by the Advisory Committee in its Notes to subdivision (d)(2), the section dealing with discretionary notice. 39 F.R.D. at 106-07.

[29] Fed. R. Civ. P. 23(c)(2).

[30] See 39 F.R.D. at 104-05.

[31] Id. at 107.

[32] 41 F.R.D. 147 (S.D.N.Y. 1966), rev'd on other grounds, 391 F.2d 555 (2d Cir 1968).

[33] Id. at 151.

[34] Id. at 151-52.

foreclosed in cases where there are large numbers of small claimants since the representatives will probably not be able to afford the cost of notifying absent members.

This result would be particularly disturbing since this type of large class is most likely to be spawned by a violation of either the federal securities laws or the federal antitrust laws. In both these areas there has been a determination by Congress that private enforcement of these statutes is vital to the general scheme of enforcement enacted.[35] Yet, the class action device may be the only way that private enforcement can be effectuated when the injured parties are numerous and each claim is monetarily small. Thus, to deprive the small claimant of the use of the class action may be to defeat a vital part of the enforcement provisions of the securities and antitrust laws.

The court in *Eisen* seemed to be more concerned with the requirements of due process and hence attributed less importance to the language of subdivision (c)(2).[36] As has been noted, the Supreme Court has not required individual notice in all cases in order to assure due process. The due process standard is one of flexibility and under *Mullane* it is quite possible that publication would be sanctioned in an *Eisen*-type case.

In any event, the financial ability to send out mailed notice should not be a condition precedent to maintaining a class action if all the other standards of Rule 23 are met. As was pointed out in *Dolgow v. Anderson*, "[I]t would be anomalous to say that . . . litigation may proceed as a class action and then lay down a condition which could never be met."[37] Courts should interpret (c)(2) so that the best notice possible within the bounds of reasonable effort is ordered. Individual notice should be required only when it would not preclude the maintenance of the action. In cases involving large numbers of small claimants something short of personal notice is the "best notice practicable."[38]

The alternative to individual notice is not necessarily notice by publication. In addition to individual notice and notice by publication the court might order individual notice to those members appearing on an existing mailing list, individual notice to a random sample of absent members, individual notice to those members whose financial stake in the outcome of the case exceeds a certain limit, or a combination of the above.

At the same time, the financial burden of sending the notice may be shifted away from the plaintiff. While it has been generally assumed that the

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[35] Securities Act of 1933, §§ 11-12, 15 U.S.C. §§ 77(k)-(*l*) (1964); Securities Exchange Act of 1934, §§ 9(e), 16(b), 18, 15 U.S.C. §§ 78 i(e), p(b), r (1964); Clayton Act §§ 4-5, 15 U.S.C. §§ 15-16 (1964).

[36] See 41 F.R.D. at 151.

[37] 43 F.R.D. at 500.

[38] Combining this interpretation of the notice required under (c)(2) with the constitutional notice requirements of due process (see note 28, supra), it appears that there is only one notice requirement for all class actions. Both (c)(2) and due process require some notice. Both indicate a preference for individual notice. Yet, both allow notice by publication if individual notice is not practicable. Thus, the courts must make the same pragmatic analysis to resolve both the notice requirements of due process and the notice requirements of (c)(2).

plaintiff should bear the expense of the notice,[39] this result is not required by the statute. Section (c)(2) says that "the court shall direct . . . notice"[40] and it has been suggested that the court's postal mailing privilege be used to defray this expense.[41] It has also been suggested that a corporate defendant may be required to finance the notice in certain cases on the basis of (1) its fiduciary duty to its present stockholders; (2) its interest in having everyone bound by the decree; and (3) its ability to bear the expense.[42]

The selection of a particular form of notice should depend on an analysis of the particular facts of the case. Among the relevant factors to be considered are (1) a comparison of the cost of any particular form of notice with the total damages sought; (2) whether any members of the class have an especially large stake in the outcome of the case; (3) the likelihood of many members who will want to opt out; and (4) whether the suit will ever be brought if not allowed to proceed as a class action. Upon analysis of these factors the court can tailor the notice required to the needs of the particular case.

This analytical process can be illustrated by reference to the type of class action brought in *Eisen*. The class is composed of many members, each of whom has a small claim. It is, therefore, unlikely that many members will want to be excluded from the class and also unlikely that the suit will be brought unless the class action device is employed. In such a situation notice by publication would seem appropriate, with the court specifying national media such as the *Wall Street Journal* or *New York Times*.

The only alternative to this balancing test is a strict construction of the notice requirement of (c)(2). Such a construction would deny the class action device to many worthy litigants. It is submitted that such a denial of the use of the class action would constitute a greater injustice, to both class members and the public interest, than would the denial of notice to some absentees.

Since neither the constitutional requirements of due process nor the statutory requirements of Rule 23, subdivision (c)(2), demand individual notice to absentees, all that seems to be required for a smoothly functioning class action rule is enlightened interpretation by the courts.

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[39] See, Richland v. Cheatham, 272 F. Supp. 148, 156 (S.D.N.Y. 1967); cf. Fischer v. Kletz, 41 F.R.D. 377, 386 (S.D.N.Y. 1966).

[40] Fed. R. Civ. P. 23(c)(2).

[41] Dolgow v. Anderson, 43 F.R.D. 472, 498 (E.D.N.Y. 1968).

[42] Id. at 498-500.