



One Minute Memo®

High Court Holds That State Class Action Limits Are Pre-Empted in Federal Court

A closely divided U.S. Supreme Court held 5-4 that a New York statute barring awards of liquidated damages in class actions is pre-empted when a case is litigated in federal court under the provisions of Rule 23 of the Federal Rules of Civil Procedure. Although the decision, *Shady Grove Orthopedic Associates, P.A. v. Allstate Insurance Co.*, No. 08-1008 (March 31, 2010), addresses technical and arcane issues of procedure and federal pre-emption, it could have a significant practical impact on the litigation of class and collective claims arising under New York law (or similar laws in other states), especially in the wage-hour area, by increasing the measure of potential remedies in such cases and making federal court a more favorable forum for plaintiffs' counsel.

Section 901(b) of the New York Civil Practice Law and Rules (CPLR) provides: "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." Various other New York statutes—including the New York Labor Law (NYLL)—provide for awards of liquidated damages to successful plaintiffs. New York courts have held that liquidated damages under such statutes trigger the provisions of section 901(b), and therefore cannot be recovered in a class action. In recognition of this rule, plaintiffs bringing putative class actions arising under statutes that award liquidated damages typically have waived their right to receive such damages so that they can prosecute their claims on a classwide basis.

The Court held that Rule 23 preempts CPLR 901 for class actions pending in federal court. Because both provisions set forth the conditions under which "a class action may proceed for a given suit," and because Rule 23 "automatically applies 'in all civil actions and proceedings in the United States district courts'" (quoting Fed.R.Civ.P. 1; emphasis in original), the Court held that the restrictions embodied in CPLR 901 are inapplicable in federal court.

The impact of the decision, particularly in putative class claims under the NYLL, may be felt immediately. Section 663.1 of the NYLL provides that where an employee is wrongfully deprived of wages, and the employer fails to prove that it had "a good faith basis to believe that its underpayment of wages was in compliance with the law," the employee may obtain "an additional amount as liquidated damages equal to twenty-five percent of the total of such underpayments found to be due the employee." To the extent that NYLL claims are asserted in federal court, whether in conjunction with claims under federal law or pursuant to an independent basis for federal jurisdiction, plaintiffs will no longer be required to waive their claim to the 25% liquidated damages award as the price of seeking class action certification.

While Shady Grove did not involve an employment claim, and the case's ultimate significance cannot be known until it is applied in specific cases and circumstances, the effect of the case may be to increase an employer's monetary exposure by 25% for all years during which the NYLL provides the grounds for relief. For the same reason, plaintiffs may be more amenable to bringing putative class claims in federal court.

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