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Civil Procedure--Class Action--Applicability for Consumer/Common Law Fraud

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was permitted, the instant holding would not affect such an action. Even if the prospective members can be identified without the aid of discovery devices,[28] the political effort and expense of organizing such an association may effectively preclude use of this device. Finally, if state legislation permits, the above-mentioned organization could sue in its own capacity in federal court without any resort to the class action requirements. Although it can sue as an entity, no citizenship has been accorded the unincorporated association;[29] citizenship of *each* member, therefore, would have to be diverse from that of the adverse parties—and total diversity in an interstate organization is rare. Although none of the three options is a cure-all for small claim litigants, each has its peculiar disadvantage. An application of these options to the facts of each new case should aid counsel in selecting the route presenting the fewest difficulties.

Steve Hixson

CIVIL PROCEDURE—CLASS ACTION—APPLICABILITY FOR CONSUMER/COMMON LAW FRAUD.—On July 1, 1969, the Kentucky Rules of Civil Procedure [hereinafter referred to as Civil Rules] were amended to conform to the Federal Rules of Civil Procedure which had been changed in 1966. Civil Rule 23, Class Actions, was one of the rules changed.[1] On July 3, 1969, a class action was filed in Madison Circuit Court

[28] Since the members of the class are often identified by using the discovery rules *after* commencement of the action, resort to advertising would probably be necessary to identify those entitled to join the association—a costly and time consuming proposition.

[29] 3B J. MOORE, FEDERAL PRACTICE ¶ 23.08, at 2510 (2d ed. 1969).

[1] The applicable section to be discussed here is KY. R. CIV. P. 23.02(3), the section that followed the old "spurious" class action concept. KY. R. CIV. P. 23.02(3) provides:

> An action may be maintained as a class action if the prerequisites of Rule 23.01 are satisfied, and in addition . . . (3) the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (a) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (b) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (c) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (d) the difficulties likely to be encountered in the management of a class action.

A complete analysis of KY. R. CIV. P. 23 is beyond the scope of this comment and the 23.02(3) provision will be considered as the controlling part of the rule for this discussion. It should be noted however that other provisions of KY. R. CIV. P. 23 must be satisfied before the 23.02(3) provision becomes an issue.

against General Motors Corporation. The complaint alleged that General Motors had fraudulently inflated "sticker prices" on new cars sold in Kentucky since 1958 and that plaintiff and all other buyers of General Motors cars since 1958 were injured by this fraudulent action. $139,000,000 actual damages and $347,500,000 punitive damages were asked.[2] Pursuant to Civil Rule 23.03, a hearing must be held as soon as practical to determine if the suit should continue as a class action. The issue to be determined here is whether a class suit should be maintained in Kentucky for a consumer/common law fraud action. *Dayton v. General Motors Corporation,* Civil No. 5693 (Madison Cir. Ct., Ky., filed July 3, 1969).

The essential elements of common law fraud in Kentucky are material representation, falsity, recklessness, intention, reliance, deception, and injury.[3] In order for Civil Rule 23.02(3) to be applicable, there must be common questions of law and fact which predominate over questions affecting individual members of the class.[4] It is the court's responsibility to determine whether a class action in a particular case is the fairest and most efficient method to employ.[5] The common questions involved in common law fraud brought by a consumer on behalf of a class would be the representation, falsity, recklessness, deception and intention of the defendant while the individual questions would be reliance and injury.[6] Thus, the judge is faced at the outset with the responsibility of balancing the common against the individual interests and determining whether plaintiff should be permitted to represent the consumer class in his suit. This judicial hurdle was in the minds of the Advisory Committee which drafted the 1966 Amendments to the Federal Rules:

> A fraud perpetrated on numerous persons by the use of similar misrepresentations may be an appealing situation for a class action, and it may remain so despite the need, if liability is found, for separate determination of the damages suffered by individuals within the class. On the other hand, although having some common core, a fraud case may be unsuited for treatment as a class action if there was material variation in the representations made or in the kinds of degrees of reliance by the persons to whom they were addressed.[7]

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[2] Lexington Sunday Herald-Leader, July 6, 1969, at 14, col. 5.
[3] Scott v. Farmer's State Bank, 410 S.W.2d 717 (Ky. 1966).
[4] Ky. R. Civ. P. 23.02(3).
[5] Frankel, *Some Preliminary Observations Concerning Civil Rule 23,* 43 F.R.D. 39 (1967).
[6] Advisory Committee's Notes, *Proposed Amendments to Rules of Civil Procedure,* 39 F.R.D. 69 (1966).
[7] *Id.* at 103.

The new Federal Rule 23(b)(3) found immediate acceptance in fraud cases involving violations of federal securities regulations.[8] The individual questions of reliance[9] and damages[10] did not keep the courts from permitting the class actions to continue.[11] Those questions did, however, require the courts to speculate on what methods would be employed to deal with them.[12] The problem of how to prove individual reliance in a class suit has received the most attention and the solutions offered vary from using the devices of split trials[13] and separate proceedings[14] to changing the substantive law of fraud and not requiring reliance.[15] While there have been no cases[16]

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[8] *See generally* 10 FED. RULES SERV.2d 23b.3 (1967); 11 FED. RULES SERV. 2d 23b.3 (1968); 12 FED. RULES SERV.2d 23b.3 (1969).

[9] Professor Moore says that individual questions with respect to reliance have not defeated the class status of fraud cases; that reliance is often one of the factors remanded to the separate proceedings on individual recovery, and that, substantively, it may be relatively immaterial once the form of fraud giving rise to liability is determined. Greater difficulty has been acknowledged where the representations themselves varied as to different members of the class. 3B J. MOORE, FEDERAL PRACTICE ¶ 23.45[2] (2d ed. 1969).

[10] Dolgow v. Anderson, 43 F.R.D. 472 (E.D.N.Y. 1968). The court said:

> . . . [D]efendants argue that each member of the class would have to prove reliance, compliance with the statute of limitations, and damages, and thus the common questions cannot be said to predominate over those affecting individual members. To 'acknowledge the defendant's position at this point would be, in effect, an emasculation of the vitality and pliability of the amended rule. . . .' The common issues need not be dispositive of the entire litigation. The fact that questions peculiar to each individual member of the class may remain after the common questions have been resolved does not indicate the conclusion that a class action is not permissible. *Id.* at 490.

[11] Eisen v. Carlisle & Jacquelin, 391 F.2d 555 (2d Cir. 1968).

> Suits alleging violations of Section 10(b) of the Securities Exchange Act, though often involving separate considerations of the elements of misrepresentation and reliance as they affect individual members, have also been accorded treatment as class actions under the new rule. *Id.* at 565.

[12] Green v. Wolf Corp., 406 F.2d 291 (2d Cir. 1968). The court said that if the trial court determines that individual reliance is an essential element of the proof, it can order separate trials on that particular issue, as well as on the question of damages, if necessary.

[13] Judge Frankel commenting on the Federal Rule 23 said:

> The effective administration of (b)(3) actions will probably require wide use of the already familiar device of split trials. And I submit that a lively awareness of this sensible device should serve to postpone or minimize some of the excessively frightening complications that seem overwhelming from a threshold view of the case. Frankel, *supra* note 5, at 47.

[14] J. MOORE, *supra* note 9, ¶ 23.45.

[15] Dolgow v. Anderson, 43 F.R.D. 472 (E.D.N.Y. 1968). The feeling of the majority was that reliance in a stock fraud case is presumed from the fact that an individual purchased the stock.

> Moreover, plaintiffs may not even have to prove individual reliance —the only issue that may prove troublesome. They are contending that purchase of Monsanto stock at a price which was affected by defendant's improper activities constitutes sufficient reliance. *Id.* at 491.

[16] W. BARRON & A. HOLTZOFF, FEDERAL PRACTICE AND PROCEDURE § 562 (1961, Supp. 1968).

dealing with common law fraud in a consumer products situation like the instant case, the issue did arise in a stock fraud case[17] brought before a federal district court in New York. In dismissing the class action the court said:

> Reliance by each person claiming to be a member of the class must be proven in . . . common law fraud actions. Thus, each claim would turn on whether the particular member of the class actually relied upon Abele's statement . . . and whether such reliance was reasonable under the special circumstances surrounding the acts of each plaintiff.[18]

Thus, it is questionable whether common law fraud is a proper subject for a class suit in federal court.[19] With the acceptance of securities fraud class actions in federal courts,[20] what should be Kentucky's approach to the consumer/common law fraud class action? This question may be answered by considering the following three points.

First, there are the practical problems that will arise in the administration of such suits. Professor Moore feels that these challenges should not defeat a class action unless they are of such a magnitude that their cost will erase any recovery.[21] Perhaps the factual and evidentiary problems of damages and, in particular, reliance in the common law fraud class action fall into Moore's category. Consider Judge Medina's opinion in *Eisen v. Carlisle & Jacquelin*[22] in which he speculated on issues that trial courts would face in determining whether a class action should proceed. "There may conceivably be questions of jurisdiction or venue, as well as of demands for a jury trial."[23] If a defendant in a common law fraud case can demand a jury trial,[24] what is to prevent a defendant in a common law fraud class action from demanding the same procedural right with respect

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[17] Berger v. Purolator Products, Inc., 41 F.R.D. 542 (S.D.N.Y. 1966).

[18] *Id.* at 545.

[19] *See* Rice, *Remedies, Enforcement Procedures and the Duality of Consumer Transaction Problems*, 48 BOSTON U.L. REV. 559 (1968).

[20] There is apparently some difference between securities fraud and common law fraud other than the obvious federal question involved in the former. See Texas Continental Life Ins. Co. v. Bankers Bond Co., 187 F. Supp. 14 (W.D. Ky. 1960), *rev'd on other grounds*, 307 F.2d 242 (6th Cir. 1962), wherein the court alluded to this difference:

> Sec. 10(b) of the Act of 1934 . . . creates a remedy in addition to the common-law right of action for fraud by describing the proposed conduct as unlawful. . . . The statute contemplates a new right of action for . . . constructive fraud which grows out of the failure to make a full and complete disclosure. *Id* at 23.

[21] 3B J. MOORE, *supra* note 9, ¶ 23.45, at 893.

[22] 391 F.2d 555 (2d Cir. 1968).

[23] *Id.* at 567.

[24] KY. R. CIV. P. 38.01.

to damages and reliance.[25] While there may be no present answer for the practical problems that may arise once a class action is commenced, proponents of the rule can point to the trial judge as having the power and authority to fashion a remedy that will solve the problems.[26]

The second point is the desirability of allowing a consumer/common law fraud class action. Granting that solutions to the practical problems might be formulated by the judge, is this allocation of power a desirable consequence?[27] Certainly the concept of an adversary system must defer to the initiative of judges burdened with the responsibility of creating new judicial machinery to handle practical problems.[28] Aside from the undesirable effects of increased judicial power, there are other consequences which grow from allowing this type of class action. In its supplemental report, the Committee on Federal Rules of Civil Procedure for the Ninth Circuit said in reference to the amended Rule 23:

> Litigation will generally be encouraged; the incentive to settle, diminished. . . . Moreover, under the mandate of (b)(3), courts are empowered to entertain class actions where the common questions predominate over questions peculiar to individual members. Accordingly, the litigation stimulated by a favorable class judgment may bring to the bar issues involving far more attention than were questions of damages. Thus to the extent separate suits would never have been prosecuted, or settled out of court instead, the courts may find themselves saddled with more litigation as a result of the proposed changes in Rule 23(a). The new Rule may make many suits grow where there was just one.[29]

The consequences of class actions in such a fraud case might make the action undesirable. But if consumers cannot bring class actions to

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[25] One solution could be to maintain a separate jury to determine the issues mentioned and to herd the plaintiffs before it, appointing a commissioner to preside over the proceedings. But considering the number of claims and the time necessary to try them, the cost of this alternative would be extremely high.

[26] *See* Comment, *Adequate Representation, Notice and the New Class Action Rule: Effectuating Remedies Provided by the Securities Laws,* 116 U. PA. L. REV. 888 (1968).

[27] Justice Black, commenting on the new Federal Rules, said that the amendments place too much power in the hands of the trial judge and that the rules might almost as well simply provide that class suits can be maintained either for or against particular groups whenever in the discretion of a judge he thinks it is wise. Statement by Mr. Justice Black, 39 F.R.D. 272 (1966).

[28] 116 U. PA. L. REV., *supra* note 26, at 923. The author asserts that if the new class action rule is to achieve its full potential as a device for prosecuting many socially worthwhile suits, a new and consistent attitude by the judiciary is required. The courts must understand that it is incumbent upon them to facilitate the bringing of these suits by giving the rules a liberal interpretation.

[29] COMMITTEE ON FEDERAL RULES OF CIVIL PROCEDURE JUDICIAL CONFERENCE—NINTH CIRCUIT, SUPPLEMENTAL REPORT, 37 F.R.D. 71, 81 (1965).

recover from and prevent common law fraud, how can Kentucky consumers protect themselves?[30]

This requirement for consumer protection raises the third point, whether a need exists for a consumer/common law fraud class action in Kentucky.[31] The federal courts have recognized that the class action is not a judicial device but rather an administrative one.[32] And they have apparently felt compelled to enter into some administrative areas such as securities fraud in order to reinforce whatever administrative remedy exists.[33] The problems of these actions' practicality and desirability are skirted in an attempt to redress the consumer's grievances.[34] This may serve the purpose initially, but the concept of the courts as a collection agency for consumer fraud claimants doesn't lend itself to a permanent solution to the problem.[35] Eventually administrative agencies will be developed and consumer protection cases will be handled by administrative machinery designed for such cases.[36] Kentucky would be well advised not to permit class actions in consumer/common law fraud cases, but rather to protect consumers through legislation and agencies to enforce it.

Judge Cardozo said, "A fruitful parent of injustice is the tyranny of concepts. They are tyrants rather than servants when treated as

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[30] Eisen v. Carlisle & Jacquelin, 391 F.2d 555 (2d Cir. 1968). This problem was on Judge Medina's mind in *Eisen* when he said, "[I]n the present case there is apparently no public administrative body that could ensure repayment, so the responsibility must ultimately rest on the judicial system." *Id.* at 567.

[31] The recent Supreme Court case of *Snyder v. Harris,* 394 U.S. 332 (1969) has apparently relegated the Rule 23(b)(3) class action to the state courts by denying the plaintiffs in that class action case the diversity jurisdiction of the federal courts because the individual claims were less than $10,000.

[32] Professor Moore points this out when he says:

> To an increasing extent, the representative lawsuit under revised Rule 23 has developed into a quasi-administrative proceeding, conducted by the judge. This departure from the traditional view of litigation as a strict adversary proceeding calls for a revised attitude toward the parties and their advocates. 3B J. MOORE, *supra* note 9, at 901.

[33] *Id.* at 766 n. 54. ". . . [O]ne of the primary reasons [for the courts'] liberal allowance of private securities fraud suits as class actions is the fact that the SEC itself cannot police all the corporate and security dealers in the country. . . ." *Id.*

[34] *See* Dolgow v. Anderson, 43 F.R.D. 472 (E.D.N.Y. 1968).

[35] *See* 3B J. MOORE, *supra* note 9, ¶ 23.45, at 881 n.5, where Moore says:

> Thus, for example, while federal courts probably must assume the burden for the time being, the impropriety of their operating as collection agencies for small securities fraud claimants points to the need for a more appropriate agency to be created. *Id.*

[36] *But see* Dole, *The Emergence of Deceptive Advertising as a Group Tort: A Possible Consequence of the 1966 Federal Rule Amendment with Respect to Class Actions,* 62 NW. U.L. REV. 661, 682 (1967). The author suggests that relegation of the policing of deceptive advertising to the Federal Trade Commission and kindred public agencies would be an alternative to a (b)(3) class action, but that this approach would make relief contingent on the vagaries of public budgets and staffs.

real existences and developed with merciless disregard of consequences to the limit of their logic."[37] The Civil Rule 23.02(3) class action is such a concept. It represents an effort by judicial theoreticians who feel that all social problems can be solved by the courts, to provide a procedural device to accomplish their purpose. The federal courts have already begun limiting this class action rule.[38] Kentucky should not pick up the quixotic sword and dash off after the windmills. While there may be instances where a Civil Rule 23.02(3) class action would be the best method to use, the case of a consumer/common law fraud is not such an instance.

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[37] B. CARDOZO, THE PARADOXES OF LEGAL SCIENCE 61 (1930).
[38] *See* note 31 *supra.*