Essay: FOREIGN CITIZENS IN TRANSNATIONAL CLASS ACTIONS

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When, if ever, should foreign citizens be included as members of American class actions? The question is not a new one. Judge Friendly first raised it thirty-five years ago, in *Bersch v. Drexel Firestone, Inc.*[1] Since *Bersch*, courts have tied the answer to res judicata and the recognition of judgments: If a court in the country of which putative class members are citizens will not recognize the judgment of an American court, then the court should exclude those citizens from the class action. *Bersch*'s reasoning was twofold. First, class actions impose unnecessary burdens on our district courts when foreign courts are free to disregard the American judgments. Second, if a foreign class member can bind the defendant to a result that favors the class member but a defendant cannot bind the foreign class member to a result that favors the defendant, the class action unfairly acts as a one-way ratchet that always operates to the detriment of the defendant. This reasoning is the foundation for the existing consensus that the superiority element of Rule 23(b)(3) is not satisfied if a class action includes foreign citizens who hail from nonrecognizing countries.[2]

We argue that the existing consensus is wrong for a simple reason: It assumes that foreign class members will inevitably sue in their home country. In recent years, however, mass-aggregation devices, some of which will entertain the claims of foreigners, have proliferated around the world. Thus, British subjects dissatisfied with an American class judgment or settlement might attempt to relitigate the claim in an aggregate proceeding conducted in a non-British forum that does not recognize the American outcome. Moreover, if the claim is individually viable, a foreign class member who is dissatisfied with the American class judgment or settlement has reason to press the claim in a hospitable foreign forum. It is the generic risk of class members' relitigation in a foreign forum—not the risk of foreign citizens' relitigation in their home country—that raises the concerns Judge Friendly identified. Excluding citizens from nonrecognizing countries is a poor cure for this problem.

It is time, therefore, to reconsider the circumstances in which foreign citizens can become members of an American class action. Using standard tools of economic analysis, we make two arguments. First, we argue that the weight *Bersch* and *Vivendi* place on

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1 519 F.2d 974 (2d Cir. 1975).

2 The doctrinal hook that courts usually use to exclude foreign members from nonrecognizing countries is the "superiority" element of Rule 23(b)(3). In the words of the most noteworthy recent case, *In re Vivendi Universal, S.A. Securities Litigation*, "res judicata concerns have been appropriately grafted onto the superiority inquiry"242 F.R.D. 76, 95 (S.D.N.Y. 2007). *See also* Kern v. Siemens Corp., 393 F.3d 120, 129 n.8 (2d Cir. 2004) (noting "significant doubts" about the superiority of a class action that included Austrian citizens when Austrian courts would not bind these citizens to an American class judgment).

(non)recognition is too great. Because *Bersch* and *Vivendi* seek to avoid relitigation in foreign tribunals, the logical starting point is to analyze the incentives that foreign citizens have to file either an initial or a subsequent foreign proceeding. This analysis discloses that any rule including and excluding foreign citizens yields certain benefits and generates certain costs. A foreign country's (non)recognition of the American outcome is relevant in determining these benefits and costs, but it plays only a small role. Indeed, to maximize benefits, it often makes sense to include as class members citizens from countries that *would not* recognize an American class judgment or settlement; and it is sometimes necessary to exclude citizens from countries that *would* recognize an American class judgment or settlement.

Second, we argue that, in most real-world applications, the *Bersch-Vivendi* rule is more costly (i.e., less efficient) than other rules regarding the inclusion or exclusion of foreign citizens.[3] Indeed, although no rule regarding foreign class membership is costless, we can specify the rule that is most efficient in theory: American courts should include foreign citizens as long as the benefit that these citizens receive from the American class action exceeds their expected net benefit from subsequent foreign litigation, and conversely should exclude foreign citizens whose expected net benefit in a subsequent foreign proceeding exceeds the benefit they receive in the American proceeding. Because of the informational difficulties in applying this rule and other alternatives to the *Bersch-Vivendi* rule, however, we conclude by suggesting that American courts should use a series of presumptions that, taken together, capture most of the benefits of the ideal rule.

Our analysis emphasizes that any approach to the inclusion or exclusion of foreign citizens must begin by considering the incentive that foreign citizens do, or do not, have to relitigate in a foreign forum. If foreign citizens have an incentive to relitigate, then their inclusion generates costs than can be avoided by their exclusion; on the other hand, if foreign citizens have no incentive to relitigate, the feared costs will not materialize, and problems of undercompensation and underdeterrence arise. In either event, the starting point for determining the benefits and costs of various rules for inclusion or exclusion is the incentive to litigate. In determining this incentive, the factors include the stakes of the litigation, the existence of foreign forums that will not recognize the American class judgment or settlement, the likelihood of recovery in such foreign forums, the capacity of such forums to resolve efficiently the claims presented to it, and the likelihood and efficiency of the American class action to achieve a recovery for included foreign citizens.

In addition to the incentive to litigate, two other factors have also emerged as significant in evaluating various alternatives for inclusion and exclusion. The first is the effect of excluding some foreign citizens on the value of the claims of those remaining in the American class action. If the risk of incurring costs associated with relitigation is low, and if the value of the American class action for remaining class members will collapse without those foreign citizens who might relitigate, there is reason to include the foreign citizens in the class despite the potential costs associated with relitigation. Conversely, if therisk of incurring costs of relitigation is high, and the exclusion of foreign citizens with an incentive to litigate has little effect on the value of the remaining claims, exclusion is more likely to be appropriate.

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[3] Throughout our analysis, we assume that a class including foreign citizens meets all other requirements for class certification. Additionally, we focus the analysis on Rule 23(b)(3) class actions (and not Rule 23(b)(1) or -(b)(2) class actions) because most class actions are (b)(3) damages class actions.

Second, the administrability of a rule is critical. We call the "ideal" rule described above (i.e., the rule that minimizes costs in most circumstances) the "incentive rule," but there are enormous informational difficulties in applying this rule in most real-world settings. The incentive rule is practical only when the benefits of the American class action are known and the expected benefits of a foreign proceeding are easily ascertained. Thus, we suggest a series of rebuttable presumptions that track the results of the incentive rule but avoid many of its informational demands.

Taking these factors into account, we propose that American courts determine the status of foreign citizens in American class actions through a series of steps that are simple to administer and approximate the results that an incentive rule would achieve:

1. A court should presumptively include foreign citizens when they assert small-stakes claims (i.e., claims that would not be viable in an American court if pursued individually).
2. A defendant can overcome the presumption of inclusion by identifying foreign citizens for whom there exist one or more foreign forums (including arbitral forums) that (a) are open to these citizens, (b) do not recognize an American class judgment or settlement, (c) provide cost-effective procedures for resolving small-stakes cases, and (d) employ rules of substantive, procedural, or remedial law that are likely to result in a more favorable outcome for the foreign citizens than the rules employed in the American court will produce.
3. The court can nonetheless include those foreign citizens who meet the criteria in (2) when:
    a. The foreign citizens expressly consent to be bound by the American class judgment or settlement; or
    b. The foreign citizens are unlikely to pursue their claims in the identified foreign forum(s), and the expected loss in value in the American class action from the exclusion of these citizens outweighs the expected costs of relitigation if these citizens are included.
4. The court should presumptively exclude foreign citizens whose claims would be viable as individual suits in an American court. The class representative(s) can overcome this presumption for some or all foreign citizens by showing that:
    a. The foreign citizens expressly consent to be bound by the American class judgment or settlement; or
    b. No foreign forum open to those citizens will refuse to recognize the American class judgment or settlement.

At the most basic level, these presumptions divide small-stakes cases from large-stakes cases. The reason is simple. The principal concern driving the exclusion of foreign citizens is the fear of relitigation. Relitigation is more likely when the claims are valuable enough to pursue in a foreign forum; it is less likely when the claims do not have sufficient value to bring in a foreign forum. Therefore, we begin with a presumption that claims valuable enough to bring independently in an American court should be excluded, because these are the cases for which there exists an evident incentive to relitigate in the event of an unfavorable American judgment or settlement. Conversely, we begin with the presumption that cases too small to bring independently in an American court are also too small to bring

in a foreign forum. The lack of an incentive to relitigate eliminates concern for incurring relitigation costs. On the other hand, the exclusion of these claims from the American class action results in undercompensation of these foreign citizens.

Both presumptions—the presumption of including small-stakes foreign claims and the presumption of excluding large-stakes foreign claims—are rebuttable. Defendants can overcome the presumption to include small-stakes foreign claims by pointing to one or more specific foreign forums that are "hospitable" to these claims. Hospitability first requires a showing that the foreign forum will be able to hear the claims (i.e., jurisdictional, venue, and comity concerns pose no barrier to resolving the claims). It also requires a showing that the foreign forum has a collective-action mechanism akin to the American class action; if it does not, there is little realistic chance that the small-stakes cases will in fact be relitigated.

Relatedly, hospitability requires that the foreign forum's substantive, procedural, or remedial rules provide an incentive to relitigate. Because the claims are small-stakes in nature, there is no incentive to relitigate them in a foreign forum unless the rules of the foreign forum provide some advantage unavailable in the American case (e.g., they are more cost-effective to bring on a collective basis or foreign law makes them large enough in size that, although regarded as small-stakes cases in the United States, they are large-stakes cases in the foreign forum). If the substantive law, procedures, and remedies are basically the same as they are in the American class action, the American court can logically conclude that the expected outcome in the two proceedings (the American and the foreign) would be comparable; in this case, there is little likelihood that relitigation will occur.

Finally, hospitability also requires a demonstration that any identified foreign forums meeting the other criteria will not recognize the American judgment. To this limited extent, the concern for nonrecognition that underlay the *Bersch-Vivendi* rule affects the proper approach to inclusion and exclusion of foreign citizens.

Our expectation is that defendants will rarely overcome the presumption favoring inclusion of small-stake foreign claims. Most foreign forums with cost-effective collective-action processes are also likely to recognize an American class judgment or settlement. In the event that the defendants succeed, however, the pendulum swings back in favor of exclusion because of the high risk of relitigation. The third step, however, describes three circumstances in which the court can decline to exclude foreign citizens despite this risk.

The first circumstance (step 3(a)) raises the possibility that foreign citizens might consent to be bound by the American judgment. Consent is a factor strongly favoring inclusion in the American action, but it is unlikely that, in small-stakes cases, many foreign plaintiffs will provide consent.

The second circumstance (step 3(b)) calls attention to the reality that, even if a foreign forum is hospitable to hearing the claims of excluded foreign citizens, these citizens might not sue in that forum. The failure to sue causes a loss to the foreign citizens who will not sue (or at least will not recover as much) in an overseas forum. The exclusion of foreign citizens can also result in a loss in the value of the claims that remain in the American class action. Together, these two losses might be greater than the savings from avoided relitigation. If so, the claims for which the costs of exclusion are greater than their savings should be included in the American class action.

Admittedly a court must strike this balance on less than perfect information. But the American court can get some guidance by examining the nature of the foreign process. For instance, a critical issue is whether the foreign forum employs a class-action-like approach in which a class representative can press claims on behalf of others, or whether the forum requires claimants to take affirmative, opt-in steps to present their claims. If the latter, then the theoretical openness of a forum in, say, Abu Dhabi means little to claimants from Britain; it is unlikely that they will press their claims in such a distant forum. And if they are not likely to press their claims, then the cost of their undercompensation is weightier than the cost of their (unlikely) relitigation. Therefore, in applying this factor, it is important for a court to be realistic about the likelihood that potentially excluded citizens will pursue claims in the hospitable forum that the defendants have identified.

In applying the two limits stated in the third step, a court might be able to address inclusion and exclusion surgically. For instance, in the example above, the court might choose to include British citizens but exclude all citizens from Abu Dhabi other than those who expressly consented to be bound by the American class judgment or settlement. Likewise, if the court already knows the value of the American class judgment or settlement for certain foreign citizens (as, for instance, with some settlement class actions), it might be able to determine the likelihood of relitigation based on this recovery. In other cases, however, the court might need to apply a flat rule, either including or excluding all foreign citizens. The upshot of the third step—especially step 3(b)—is that a court can apply whichever specific rule matches up best with the facts.

The fourth step establishes an opposite presumption of exclusion for foreign citizens with large-stakes claims. The reason is again evident. If a case is regarded as large-stakes in an American court, it is likely viable as an independent action in a foreign forum as well. Because these cases pose the greatest risk of relitigation, they are prime candidates for exclusion. But there may be less here than meets the eye. Although American courts have interpreted Rule 23 to allow class treatment of small-stakes cases, they have been skeptical of class treatment for claims that are independently viable. Until this interpretation changes, this presumption of exclusion operates only in the rare circumstance when a set of large-stakes claims nonetheless pass through the Rule 23 gauntlet.

The presumption can be overcome. As with small-stakes cases, step 4(a) provides that a foreign citizen's consent to be bound is a relevant reason to include the citizen in the class; and here, given the stakes in the litigation, it is likely that some foreign citizens will have enough interest in their claim to make their preference to be included known to the American court. In such a situation, the attitude of any identified nonrecognizing foreign forums toward such consent—in particular, whether they will enforce the foreign citizen's consent—determines the effect that the American court should give to the consent.

The second circumstance under which the presumption can be overcome (step 4(b)) is narrower than the comparable second circumstance for the opposite presumption (step 3(b)). A class representative must show that none of the identified nonrecognizing foreign forums is open to the foreign citizen. If any such forum is open, the large stakes in the litigation provide an incentive for the foreign citizen to pursue the case in this foreign forum. True, if they had been allowed to participate in the American class action, the citizens might have received more (or at least enough to eliminate the incentive to relitigate), but the risk of relitigation, with its attendant costs, is greatest in this area. A flat rule, rather than a rule allowing the court to balance costs of undercompensation

against costs of relitigation, seems a more realistic way to limit costs in light of the parties' litigation incentives.

The framework that we propose is not costless. We have shaped the rules around the parties' incentives to sue and to relitigate, but we have also structured them to be administratively simple. We have achieved neither objective perfectly. No rule in this area, however, is costless, and the "best" rule in theory is impossible to administer in practice. The framework balances the plaintiffs' interest in adequate compensation, the defendants' interest in finality, the American courts' interest in adminstrability, and the shared international interest in appropriate deterrence.