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Court of Appeals Decides Class Certification Issue

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The Court of Appeals recently stated a general rule that class certification should be denied only after a motion to certify is made with supporting affidavits, and not on a motion to dismiss on the pleadings. *Maddicks v. Big City Props.*, 2019 WL 5353010 (Ct. App. 2019). What is remarkable about *Maddicks* is that the Court of Appeals and a panel of the First Department mustered only bare majorities to reach this unremarkable conclusion. The fact that three out of seven judges on the Court of Appeals and two out of five judges on the Appellate Division panel opposed this common sense reading of the CPLR's class action rules suggests that the legislative goal in 1975, "to provide a flexible, functional scheme wider and more welcoming than 'the narrow class action legislation which preceded it,'" is still sailing into strong judicial headwinds. Id. at *4.

Let's look at the facts, and then the takeaways.

Facts and Procedural Posture. As summarized by the trial court (New York County Supreme), plaintiffs alleged that defendants or their corporate predecessors owned or operated over 20 apartment buildings and engaged in a common scheme to inflate rents in violation of New York's rent stabilization laws. Defendants were alleged to have used various methods to impose illegal overcharges, including: (1) failing to provide rent-stabilized leases as required in order for the defendants to receive tax incentives under the J-51 program, (2) misrepresenting the value of improvements made to the apartments in order to obtain unwarranted rent increases, (3) failing to register rental information in order to collect more than the correct permissible rent, and (4) inflating the fair market rent on apartments and deregulating such apartments. *Maddicks v. Big City Props.*, 2017 WL 5499213 (Sup. Ct., N.Y. Co., 2017) (Edwards, J.).

The Appellate Division drew from the pleading the additional fact that all 11 buildings at issue on the appeal were managed by one management company, and all eight owners were "allegedly part of one holding company." *Maddicks v. Big City Props.*, 163 A.D.3d 501, 503 (1st Dept. 2018). The Appellate Division found plaintiffs to have pleaded "that the setting of the improper rents in these apartments was *part of a systematic effort* by [the holding company] to avoid compliance with the rent stabilization laws." 163 A.D.3d at 503 (emphasis added). The dissent described this fact as "irrelevant," while the majority viewed it as an allegation that "would support a class action … ." 163 A.D.3d at 503 (majority) & 511 (dissent). The Court of Appeals also found this additional fact notable and, like the Appellate Division, criticized its dissenters for "ignor[ing] this

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point in concluding" that common questions did not predominate. *Maddicks v. Big City Props.*, 2019 WL 5353010 at *1 & n.2 (Ct. App. 2019).

Plaintiffs pleaded their action on behalf of a class against defendants, who moved under CPLR 3211(a)(7) to dismiss not just the class allegations but the entire complaint. The trial court granted the motion, on the grounds that the complaint did not satisfy the requirements of the CPLR's class action rules regarding commonality, typicality and superiority requirements for class certification (CPLR (901(a)(2), (3) & (5)). 2017 WL 5499213 at *3-*4. The Appellate Division reinstated the complaint, and the Court of Appeals affirmed the Appellate Division. The Court of Appeals reviewed the pleading as construed by the Appellate Division, and relied on the "systemic effort" allegation for the conclusion that dismissal by the trial court was in error. *Maddicks*, at *2-*3.

The Appellate Division's Discretion Governs. The court's reliance on "the Appellate Division's analysis of the complaint" and not that of the trial court (id. at *2) points to an unusual aspect of New York practice. The trial court noted that it had "broad discretion to determine whether the putative class meets the standards for class certification." 2017 WL 5499213 at *2. While the determination of compliance with CPLR 901 "ordinarily rests with the sound discretion of the trial court," in New York it is the discretion of the Appellate Division that governs: "The Appellate Division, as a branch of Supreme Court, is vested with the same discretionary power and may exercise that power, even when there has been no abuse of discretion as a matter of law by the nisi prius court." *Small v. Lorillard Tobacco*, 94 N.Y.2d 43, 52-53 (1999). *Small*, like *Maddicks*, had the Court of Appeals reviewing an Appellate Division reversal of a trial court class certification decision, and the question presented was "whether *the Appellate Division* abused its discretion as a matter of law." *Small*, 94 N.Y.2d at 53 (emphasis added). In *Small*, as in *Maddicks*, the Court of Appeals held it did not. Id. at 57.

Plaintiffs Bear a Heavier Burden on a Motion for Class Certification. The three courts in *Maddicks* had before them only a pleading and not an Article 9 motion for class certification, and it is supporting affidavits in support of class certification that typically provide the court with the facts on which a certification decision is based. All three courts in *Maddicks* agreed that a court could dismiss a class action pleading on a motion to dismiss under CPLR 3211(a)(7), but the appellate courts provided sound reasons why that approach is the exception. The Appellate Division referred several times to the "early stage" of the case at which the certification issue was being addressed: "[T]he dismissal, at this early stage, before an answer was filed and before any discovery occurred, was premature." 163 A.D.3d at 502. The Court of Appeals, while also accepting that a class claim may be dismissed under CPLR 3211(a)(7) (2019 WL 5353010 at *3), explicitly called attention to the different legal standards that apply to a motion to dismiss.

As the court stated, "a motion to dismiss should not be equated to a motion for class certification" (id. at *1), and a class action pleading challenged under CPLR 3211(a)(7) "is to be afforded a liberal construction" with "the facts as alleged [to be accepted] as true," the pleading must be "accord[ed] every possible favorable inference," and the issue presented must be "whether the proponent of the pleading *has* a cause of action, not whether it has *stated* one." 2019 WL 5353010 *3 (court's emphasis, internal citations omitted). In contrast, on a class certification motion, plaintiffs have "the burden of establishing compliance with the statutory requirements, … [g]eneral or conclusory allegations in the pleadings or affidavits are insufficient to sustain this burden, … [and] certification must be founded upon an evidentiary basis." E.g., *Rallis v. City of New York*, 3 A.D.3d 525, 526 (2d Dept. 2004) (denying motion for class certification).

The dissent in the Court of Appeals argued that on a motion to dismiss a class action pleading plaintiffs must make a "showing that plaintiffs could meet each of the CPLR 901(a) prerequisites following class discovery," a burden the dissent thought should be met by "supporting affidavits alleg[ing] such facts" as would establish the CPLR 901(a) prerequisites.

Maddicks, 2019 WL 5353010 at *6. The dissent did not explain, however, why affidavits supplementing *a pleading* should be required on a motion to dismiss. Further, even the authority on which dissent relied noted that the proper approach would be to strike the class allegations rather than a motion to dismiss, and that such motions to strike "should not be the norm" but rather are appropriate only where the defects are apparent "on the face of the complaint and incontrovertible facts." Id., citing J.M. McLaughlin, 1 McLaughlin on Class Actions §3.4 (15th ed. 2018).

The dissent's apparent confusion notwithstanding, the court's holding confirms what should be a common understanding, which is that the burden a moving plaintiff must carry on a motion for class certification is greater than that needed to survive a motion to dismiss. Because of that difference defendants should prefer to wait for plaintiffs' motion rather than seeking dismissal of a class pleading.

Facts Presented Were Not Adequate for a Class Certification Analysis. The record is not clear about why the trial court reached out to dismiss a class action complaint based not on the facts alleging wrongdoing but on the class certification criteria. The dissent in the Court of Appeals raised the specter of pre-certification discovery that "may … lead to significant costs" (2019 WL 5353010 at *6), but it cited no state case where such costs have been problematic, and the majority dismissed the concern as "sheer speculation" (id. at *4, n.10). Costs relating to class certification discovery motion were not mentioned in the opinions of either the Appellate Division or the trial court.

An argument for dismissal was made for certain defendants based on defective substantive pleadings (which was successful and not appealed (163 A.D.3d at 502; 2017 WL 5499213 at *3), but the trial court dismissed the claim against the other named defendants based on its finding that "there is no basis for class action relief." Id. at *4. The court did not address whether the plaintiffs had properly pleaded causes of action on their own behalf individually against this second group of defendants. Instead it held that "since the court dismisses the amended complaint based on these grounds [there being no basis for class action relief], the court need not address the remainder of defendants' arguments," which were the plaintiffs' individual complaints. Id. Even the dissent in the Appellate Division did not address why the individual claims of the named plaintiffs should be dismissed, noting that the trial court "granted the motion to dismiss the complaint in its entirety, apparently on a theory of misjoinder." 163 A.D.3d at 508. No substantive attention seems to have been given to the merits of the underlying claim, but rather only whether it could be pleaded on a class basis.

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The Appellate Division, citing the 60-day rule of CPLR 902 and noting the time for making the certification motion had not occurred, found "it was premature, in this case, for the [trial] court to engage in a detailed analysis of whether the requirements for class certification were met." 163 A.D.3d 501, 502. The court noted several times that it was considering the defendants' motion and the trial court's decision without having a class certification motion before it, and that the predominance of common questions should be addressed after the facts had been "fleshed out once plaintiffs make a motion for class certification and defendants oppose it." 163 A.D.3d at 503.

The Court of Appeals noted another consideration demonstrating that the trial court acted prematurely, which was that CPLR 906 permits a plaintiff to take into account particular facts in moving for "a class action with respect to particular issues" or to have the class "divided into subclasses with each subclass treated as a class." The Court of Appeals also found that dismissal was premature because not giving plaintiffs an opportunity to move for fact-based

subclasses or for certification on specific issues would "effectively nullify CPLR 906, which permits plaintiffs to seek certification with respect to particular issues or certification of subclasses. To dismiss the class action pleading at the pleadings stage, the court concluded, "would be to prematurely dispose of causes that could be severed into individual claims *through the procedures established in CPLR article 9*." 2019 WL 5353010 at *5.

Other Guidance From the Court of Appeals. In the context of affirming reinstatement of the dismissal of this class action complaint, the Court of Appeals offered two additional comments suggesting that facts to be considered under CPLR 901(a) get a different treatment when the context is a motion to dismiss.

The first was the issue of whether, in connection with considering the predominance of common questions, a trial court should look at "the common basis for a damages claim or the degree of damage alleged." Id. at *4. The court expressed sympathy for the plaintiffs' claim that "to focus on idiosyncrasies within the class claims—distinctions that speak to damages, not to liability—*at this juncture* would potentially be to reward bad actors who execute a common method to damage in slightly different ways." Id. (emphasis added). The court's reference to "this juncture" meant prior to moving for class certification under CPLR 901-02, at "this early stage, before an answer was filed and before any discovery occurred … ." Id. at *2 (quoting the Appellate Division decision, 163 A.D.3d at 502). While the court seemed to caution that a motion for class certification may require more detail on the common basis for a damages claim, the court also noted that "individualized proof required on issues such as damages does not preclude a finding that common questions of law or fact predominate over individual questions." 2019 WL 5353010 at *5, quoting *Sanders v. Farady Labs.*, 81 F.R.D. 99, 101 (E.D.N.Y. 1979). The court's emphasis on "this juncture" suggested that a motion for class certification under CPLR Article 9, rather than a motion to dismiss, was the appropriate time to address complex damages issues.

Finally, the Court of Appeals also considered whether time-barred claims of certain class members should warrant dismissal of the pleading and concluded it should not. While acknowledging that "individual class members whose claims are shown to fall outside the relevant statute of limitations are barred from recovery," the court concluded that this did not justify dismissal of a complaint with "allegations of a nucleus of a common scheme of fraud," because to do so "would insulate defendants from class liability." Id.

Conclusion. The Court of Appeals described the "legislative desire" behind the enactment of Article 9 in 1976 as "to provide a flexible, functional scheme wider and more welcoming than 'the narrow class action legislation which preceded it." Id. at *4 (citing *City of New York v. Maul*, 14 N.Y.3d 499, 509 (2010), in turn quoting *Friar v. Vanguard Holding*, 78 A.D.2d 83, 91 (2d Dept. 1980)). In *Maddicks* the court applied pleading standards and affirmed the Appellate Division's reinstatement of the complaint based on a "liberal construction" of the pleading and "allowing plaintiffs the benefit of every possible inference." Id. The court did not conclude that plaintiffs had met their burden under Article 9; it simply that it was just "allowing the action to proceed to the CPLR article 9 stage." Id. at *4.

Because plaintiffs seeking class certification bear a greater burden in moving for certification under CPLR 901-02 than in opposing a motion to dismiss under CPLR 3211(a), defendants are well advised to refrain from challenging class certification on the pleadings unless the defects are plainly apparent on the face of the complaint.