

COURTS REFUSE TO GIVE FULL FAITH AND CREDIT TO NATIONWIDE PRODUCTS SETTLEMENT

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To Our Clients and Friends:

For class action defendants, winning final approval for a nationwide settlement, and then defending that approval on appeal, may not be the end of the process. If the settlement was consummated in a state court, judges in other states can refuse to give it full faith and credit. Although this kind of collateral review is supposed to be quite narrow, the treatment that three different state courts have given to a nationwide products liability settlement to which the Tennessee court system granted final approval in 2005 shows that full faith and credit is by no means a given.

The Tennessee settlement involved Dryvit Systems, Inc., a manufacturer of synthetic stucco that allegedly damaged the homes to which it was applied. Dryvit faced numerous lawsuits and, in April 2002, it agreed to settle claims on a nationwide basis. It negotiated the settlement with counsel for plaintiffs who had brought a case in Tennessee on behalf of Tennessee residents only, but who agreed to amend their complaint to state claims on behalf of a nationwide class in order to facilitate the nationwide settlement. (In an oversight that became important later, however, the Tennessee plaintiffs did not actually file a conforming amended complaint until after 2005, after the settlement had received final approval.)

After the Tennessee court granted preliminary approval to the settlement, and notice issued by publication and by mail to 85,000 homeowners known to have used Dryvit's product, several South Carolina residents filed a new class action. Almost immediately, and without any discovery, the South Carolina judge certified a class of South Carolina residents and issued an order purporting to opt all of them out of the nationwide settlement class. There is case law holding that opt-outs must be made on an individual basis, and that this kind of "representative" opting-out is ineffective. Dryvit, however, appears not to have even brought the South Carolina order to the Tennessee court's attention, much less argued against its effectiveness.

The Tennessee settlement took three years to win final approval. The trial judge initially approved it after two fairness hearings in October and December 2002, but there were several appeals, and an appellate court reversed and remanded, requiring the trial court to consider additional issues, and then reversed and remanded again when it believed the trial court did not carry out its prior ruling. *See Posey v. Dryvit Systems, Inc.*, 2004 WL 572348 (Tenn. Ct. App. Mar. 22, 2004), and 2005 WL 17426 (Jan. 4, 2005). The trial judge approved the settlement again in April 2005, and there were no further appeals.

Despite the three-year delay, the Tennessee case was the first case against Dryvit to become final. The certified class action in South Carolina did not advance because Dryvit entered into individual cash settlements with the named plaintiffs in that case and promised fee payments to the plaintiffs' counsel, both contingent upon the *Posey* settlement becoming final and causing the South Carolina case to be dismissed as *res judicata*. Actions in other states apparently did not reach the certification stage.

After *Posey* won final approval, Dryvit sought to use it to dismiss the South Carolina action. The original plaintiffs agreed, but other class members intervened and objected. When Dryvit sought to dismiss other cases in Ohio and New Jersey, those plaintiffs objected, too, asking courts in those states not to give the Tennessee decision full faith and credit. These litigants focused on the very low claims rate in the Tennessee settlement and argued that the notice program was ineffective. They also focused on the Tennessee plaintiffs' failure to file an amended complaint stating claims on behalf of a nationwide class, arguing that without this complaint, the Tennessee court lacked jurisdiction to enter a nationwide settlement. The South Carolina plaintiffs additionally argued that they had been opted out of the settlement by the South Carolina court's initial certification order, and that the private settlements between Dryvit and the South Carolina named plaintiffs were collusive and should preclude Dryvit from relying on the Tennessee judgment.

In March 2007, the Ohio Court of Appeals denied summary judgment on the question of whether the Tennessee settlement should be given full faith and credit. It reached this decision primarily on the basis of the missing amended complaint. *See Bishop v. Dryvit Systems, Inc.*, 2007 WL 646252, at *4 (Ohio Ct. App. Mar. 5, 2007) ("In light of the unusual procedural posture of the *Posey* case, Dryvit's failure to present evidence of a filed second amended complaint identifying a nationwide class, and the Tennessee appellate court's scrutiny of the *Posey* trial court, it is unclear whether a nationwide class has ever been properly certified in *Posey* and, as a result, whether appellants are precluded from bringing their claims against Dryvit."). In August 2008, the New Jersey Supreme Court reached the opposite result. Although it found that Dryvit violated court rules by failing to notify the New Jersey plaintiff of the contemplated nationwide settlement in Tennessee, the New Jersey plaintiff still had an opportunity to opt out of the Tennessee settlement, and the Court held that if he wanted to escape the consequences of his failure to have done so, he would need to present his arguments to a Tennessee court. *See Simmermon v. Dryvit Systems, Inc.*, 953 A.2d 478 (N.J. 2008).

In an unpublished January 2009 decision, a South Carolina judge agreed with all three of the intervenors' arguments and refused to dismiss the South Carolina case against Dryvit. The court focused considerable attention on the settlements Dryvit reached with the original named plaintiffs, stating that "[e]ven though Dryvit has repeatedly asserted that it only

settled the individual claims, an inference exists that the individual settlements were made because of the ‘class’ status of the representatives and meant to stifle the obligations imposed on class representatives found in [South Carolina rules] of prosecuting the action vigorously on behalf of the class.” *Treon v. Dryvit Systems, Inc.*, Civ. No. 2002-CR-07-1377 (S.C. Common Pleas, 14th Circuit, slip. op., Jan. 13, 2009).

The main lesson to be learned from these decisions comes from the fact that they exist at all: Even after a hard-fought approval process and success against objectors on appeal, a class action settlement can still be collaterally attacked in sister states. Not only must defendants ensure compliance with all procedural requirements in the settlement state, but also should remember at each stage of the settlement process that other courts may scrutinize all aspects of the settlement — including the manner in which it was negotiated — at a later time.

Please do not hesitate to contact us with any questions.

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