IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: PACIFIC SUNWEAR OF CALIFORNIA, INC., a California corporation, *et al.*,[1] Debtors.	Chapter 11 Case No. 16-10882 (LSS) (Jointly Administered)

MEMORANDUM DECISION ON (A) TEMPORARY ALLOWANCE OF CLAIMS FOR VOTING PURPOSES; AND (B) MOTION TO RECONSIDER AND/OR AMEND THE COURT'S JUNE 22, 2016 MEMORANDUM ON CLASS CERTIFICATION

By a previous memorandum opinion dated June 22, 2016,[2] I ruled on a request by Tamaree Beeney and Charles Pfeiffer to file claims against the PacSun estates for alleged violations of California wage and hour laws, which had been asserted prepetition in separate (but subsequently consolidated) lawsuits. Mr. Pfeiffer sought permission to file a claim pursuant to California's Private Attorney General Act (a "PAGA claim"). Ms. Beeney sought to file both a PAGA claim and a class proof of claim in her capacity as a prepetition court-approved class representative. For the reasons set forth in the First PacSun Memorandum, I ruled that court permission was not necessary to file a PAGA claim. On the other hand, I granted Ms. Beeney permission to file a class proof of claim for PacSun's alleged failure to properly compensate employees for rest breaks and security checks. In

[1] The Debtors and the last four digits of their respective federal taxpayer identification numbers are as follows: Pacific Sunwear of California, Inc. (9463-CA); Miraloma Borrower Corporation (0381-DE); and Pacific Sunwear Stores Corp. (5792-CA) (collectively, "PacSun" or the "Debtors"). The Debtors' address is 3450 East Miraloma Avenue, Anaheim, CA 92806.
[2] *In re Pac. Sunwear of Cal., Inc.*, 2016 WL 3564484 (Bankr. D. Del. June 22, 2016) ("First PacSun Memorandum").

doing so, however, I found that Ms. Beeney was an adequate representative solely for absent class members who, like her, hold general unsecured claims. Accordingly, I circumscribed the time period relating to the proof of claim to March 18, 2007 through the 181st day prior to the filing of the bankruptcy petition.

Now, Ms. Beeney asks me to reconsider the First PacSun Memorandum and permit her to represent employees not only for the entire period certified by the state court prepetition (*i.e.*, March 18, 2007 through February 26, 2016), but also for the remainder of the priority period.[3] Alternatively, Ms. Beeney asks for permission to amend her proof of claim to permit Ms. Shin to be added as a class representative of employees whose claims would fall within 180-day priority period of section 507(a)(3) of the Bankruptcy Code.[4]

Several other motions were also filed that relate to the class and PAGA claims. Ms. Beeney and Mr. Pheiffer filed a motion for estimation and temporary allowance of their claims for purposes of voting on the Debtors' plan of reorganization.[5] The Debtors filed a cross-motion to estimate these claims for the same reason.[6] The Debtors additionally filed objections to, and motions to strike the, priority status of the PAGA and class claims.[7] Finally, the Debtors filed an adversary proceeding for a declaratory judgment that neither

[3] *Motion (First Amended) of Class Claimants (A) for Leave to Amend Proof of Claim to Substitute Class Representative or, Alternatively, to Provide Additional Time for Priority Class Representative to File Class Proof of Claim, and (B) for Partial Reconsideration* ("Motion to Amend or Reconsider") [Dkt. No. 563].
[4] United States Bankruptcy Code, 11 U.S.C. §§ 101 *et seq.*
[5] *Motion of Class and PAGA Claimants for Estimation and Temporary Allowance of Claims of Class and PAGA Claimants for Purposes of Accepting or Rejecting the Joint Plan of Reorganization of Pacific Sunwear of California, Inc. and Subsidiary Debtors* ("Estimation Motion") [Dkt. No. 379].
[6] *Debtors' Cross-Motion to Estimate Class of Tamaree Beeney and PAGA Claims of Tamaree Beeney and Charles Pfeiffer for Voting Purposes* ("Cross-Motion") [Dkt. No. 415].
[7] *Debtors' Objection to, and Motion to Strike, Priority Status or Classification for Claim Number 986* [Dkt. No. 509]; *Debtors' Objection to, and Motion to Strike, Priority Status or Classification for Claim Number 989* [Dkt. No. 510].

Ms. Beeney nor Mr. Pfeiffer have any administrative expense claims.[8] In the adversary proceeding, the Debtors filed a motion for summary judgment.[9] Objections and replies have been filed with respect to each of these motions.

On July 18, 2016, I heard argument and accepted evidence. The declarations of Hyo Jeong "Alice" Shin, Steve Fox and Sandy Renteria were admitted into evidence without objection, as was Ms. Shin's deposition. I have also received the permitted post-hearing submissions. Each motion is now ripe for decision.[10] Familiarity with the First PacSun Memorandum is assumed.

Because my decision on the Estimation Motion and Cross-Motion influence my decision on the Motion to Amend or Reconsider, I will address the Estimation Motion and Cross-Motion first.

I. Estimation of Ms. Beeney's and Mr. Pfeiffer's Claims for Voting Purposes

A. Relevant Procedural Background

On May 20, 2016, Ms. Beeney and Mr. Pfeiffer filed their motion for leave to file their proofs of claim. Contemporaneously, they filed a motion for "estimation and temporary allowance" of the class and PAGA claims for purposes of voting on the Debtors' plan.[11] By the Estimation Motion, they seek an order "estimating and temporarily allowing" their claims in an amount equal to the dollar values included in the proofs of claim they then intended to file, if given permission. In the proofs of claim, Ms. Beeney

[8] Adv. Proc. No. 16-51019.

[9] *Plaintiffs' Motion for Summary Judgment* [Adv. Dkt. No. 4].

[10] In this Memorandum, I address all motions other than the summary judgment motion, which will be the subject of a separate ruling.

[11] *Motion of Class and PAGA Claimants for Estimation and Temporary Allowance of Claims of Class and PAGA Claimants for Purposes of Accepting or Rejecting the Joint Plan of Reorganization of Pacific Sunwear of California, Inc. and Subsidiary Debtors* ("Estimation Motion") [Dkt. No. 379].

asserts a prepetition general unsecured "Rest Break Claim" of $5,680,559 and a prepetition general unsecured "Off the Clock Claim" of $6,577,458. The PAGA claim was filed in the aggregate amount of $135,374,113.[12]

On June 2, 2016, the Debtors filed an opposition to the Estimation Motion. The Debtors first incorporated their objection to the motion for leave to file the class and PAGA claims. The Debtors next argued that the Estimation Motion should be denied because it did not suggest a methodology for estimating the claim, but instead simply asked the Court to adopt the to-be-filed claim. The Debtors also argued that the class action and PAGA claims were capped by the allegation in Ms. Beeney's complaint that the aggregate amount of the claims, inclusive of monetary damages, civil penalties and attorneys fees, is less than $5,000,000. Finally, the Debtors attached to their objection two motions to approve class action settlments in other cases filed by the firm representing Ms. Beeney and Mr. Pfeiffer, alleged to be settlements of similar wage and hour class actions. Based on their arguments, the Debtors ask me to value the class claims at $500,000, but in no case greater than $5,000,000, and the PAGA claims at $10,000.

The Debtors also filed a "cross-motion" to estimate the class and PAGA claims for voting purposes.[13] The stated purpose of the cross-motion was to ensure that a hearing would go forward on the Estimation Motion, as it had already been adjourned several times by Ms. Beeney and Mr. Pfeiffer. In the Cross-Motion, the Debtors stated that they had not yet objected to the class claim or the PAGA claim given the pendency of the Estimation Motion and the expense attendant to undertaking such an objection. Ms. Beeney and Mr.

[12] It is not necessary to determine the amount of the prepetition priority claims because, under the Debtors' plan, they are not impaired and are deemed to vote in favor of the plan.

[13] *Debtors' Cross-Motion to Estimate Class Claims of Tamaree Beeney and PAGA Claims of Tamaree Beeney and Charles Pfeiffer for Voting Purposes* ("Cross-Motion") [Dkt. No. 523].

Pfeiffer objected to the Cross-Motion. They argued that: (i) notwithstanding their Estimation Motion, I cannot estimate their claims for voting purposes because the Debtors failed to file a substantive objection to their claims; as such, the Estimation Motion and Cross-Motion are moot; but (ii) if I were to estimate their claims, the Debtors' proposed figures have no evidentiary basis, whereas their proofs of claim are treated as *prima facie* evidence of their respective amount and validity. No new or different arguments were made at the hearing on these motions.

B. The Court Treats the Dispute as One for Temporary Allowance of a Claim for Voting Purposes

As an initial matter, I am treating the Estimation Motion and Cross-Motion as requests for temporary allowance of the claims only for voting purposes, and not as a request for estimation for all purposes. While the parties and courts often use the term "estimation" for both undertakings, these concepts are not the same nor do they serve the same purpose.[14]

Estimation of claims is governed by section 502(c) of the Bankruptcy Code, which requires that the court estimate "for purpose of allowance under this section" any contingent or unliquidated claim "the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case."[15] Thus, by its very nature, estimation under section 502(c) results in allowing a claim for purposes of the entire case, and is no different than a claim allowed under section 502(a) or (b).[16] No particular procedure is required to estimate

[14] *Stone Hedge Props. v. Phx. Capital Corp. (In re Stone Hedge Props.)*, 191 B.R. 59, 64–65 (Bankr. M.D. Pa. 1995); *In re Innovasystems, Inc.*, 2014 WL 7235527, at *7 (Bankr. D.N.J. Dec. 18, 2014).
[15] 11 U.S.C. § 502(c).
[16] 4 Collier on Bankruptcy ¶ 502.04[3] (Alan Resnick & Henry J. Sommer eds., 16th ed.) (further noting that the Court could limit the allowance if the parties so request, or out of deference to a nonbankruptcy court for the ultimate determination of the claim).

a claim; bankruptcy courts may use whatever method is best suited to the case as long as the procedure is consistent with fundamental bankruptcy policies, which require speed and efficiency.[17] Nevertheless, the Court must estimate the claim "in accordance with the legal rules that will govern the final amount of the claim."[18]

On the other hand, Bankruptcy Rule 3018 provides for the temporary allowance of a claim "in an amount which the court deems proper" for voting purposes only.[19] The policy behind Bankruptcy Rule 3018 "is to prevent possible abuse by plan proponents who might ensure acceptance of a plan by filing last minute objections to the claims of dissenting creditors."[20] Like estimation under section 502, neither the Bankruptcy Code nor the Bankruptcy Rules provide guidance on a methodology to be used, but commend the determination to the court's discretion.[21] Courts tend to look at the debtor's schedules, the proof of claim, and the objection filed to the proof of claim.[22] At least one court has suggested that a determination under Rule 3018 "should ensure that the voting power is commensurate with the creditor's economic interests in the case."[23] Consistent with that notion, some courts have estimated a claim at $0 when the court finds it unlikely that the

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[17] *In re Adelphia Bus. Solutions, Inc.*, 341 B.R. 415, 422 (Bankr. S.D.N.Y. 2003).
[18] *In re Armstrong World Indus., Inc.*, 348 B.R. 111, 123 (D. Del. 2006).
[19] Fed. R. Bankr. P. 3018(a).
[20] *Armstrong v. Rushton (In re Armstrong)*, 294 B.R. 344, 354 (B.A.P. 10th Cir. 2003) (citing *Stone Hedge*, 191 B.R. at 64).
[21] *In re Quigley Co.*, 346 B.R. 647, 653 (Bankr. S.D.N.Y. 2006).
[22] *Stone Hedge*, 191 B.R. at 65.
[23] *Quigley*, 346 B.R. at 654; *see also Innovasystems*, 2014 WL 7235527, at *8–9 (discussing *Matter of Gardinier, Inc.*, 55 B.R. 601 (Bankr. M.D. Fla. 1985) and noting that "[t]he Court considered that the potential size of the claim could allow the creditor to exert undue influence with other creditors in its class under the plan and thus 'scuttle' the proceeding.").

claimant will succeed on the merits.[24] Other courts have similarly assessed the probabilities of success on the merits and discounted the claim appropriately.[25]

Here, the Debtors have not suggested that the prepetition class and PAGA claims must be estimated for all purposes. Accordingly, the Estimation Motion and Cross-Motion will be reviewed under Bankruptcy Rule 3018.

C. Under the Unique Circumstances of this Case, the Debtors' Failure to File an Objection is Not Fatal to Temporarily Allowance for Voting Purposes

The distinction between an estimation motion under section 502(c) and a motion to temporarily allow a claim for voting purposes is relevant to Ms. Beeney and Mr. Pfeiffer's argument that the Estimation Motion and Cross-Motion are moot. They argue that the Estimation Motion was filed protectively or anticipatorily to get a head start on the temporary allowance process.[26] But, no objection was ever filed. Accordingly, they contend that their proofs of claim are deemed allowed, and therefore, they are entitled to vote their claims as stated therein.

I agree with this position as a general proposition. Allowed claims may vote on a plan.[27] A proof of claim is deemed allowed unless a party in interest files an objection.[28] Thus, a claimant may vote on a proposed plan if he has filed a claim and there is no outstanding objection. A necessary corollary is that "a temporary allowance order only arises if there is an objection to a claim."[29]

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[24] *Innovasystems*, 2014 WL 7235527, at *9.
[25] *Id. at* *7.
[26] Reconsideration Hr'g Tr. at 65.
[27] 11 U.S.C. § 1126(a).
[28] 11 U.S.C. § 502(a)
[29] *Armstrong*, 294 B.R. at 354.

The Debtors counter that no objection is necessary to invoke the temporary allowance process with a somewhat tortured reading of Bankruptcy Rule 3018. Bankruptcy Rule 3018(a) provides in relevant part:

> Notwithstanding objection to a claim or interest, the court after notice and hearing may temporarily allow the claim or interest in an amount which the court deems proper for the purpose of accepting or rejecting a plan.[30]

Placing emphasis on the word "notwithstanding," the Debtors argue that reading this provision to require an objection before invoking Rule 3018 would change the meaning of "notwithstanding objection" to "if and only if a party has filed an objection."[31] They also cite *Armstrong* as stating that a creditor may request temporary allowance for multiple, non-exclusive reasons. The *Armstrong* court's nonexclusive reasons, however, all presuppose the filing of an objection (*i.e.*, objection is filed too late to be heard on the merits prior to confirmation; objection is frivolous; objection is questionable).[32] *Armstrong* does not suggest that an objection is unnecessary. Further, given its purpose is to enfranchise—not disenfranchise—creditors, there is no need to invoke the rule unless and until an objection is filed.

Here, however, Ms. Beeney and Mr. Pfeiffer did just that—they filed a motion to temporarily allow their claim before an objection was filed (and, even before they had filed their proofs of claim). In these unique circumstances, given the objection to the Estimation Motion, which asserts grounds for allowing the claims in a lesser amount, as well as the Cross-Motion, I find that these filings function as an objection to the class and PAGA claims. I will not, in this instance, penalize the Debtors, and more importantly, other

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[30] Fed. R. Bankr. P. 3018(a).

[31] *Debtors' Reply in Support of Cross-Motion to Estimate Class Claims of Tamaree Beeney and PAGA Claims of Tamaree Beeney and Charles Pfeiffer for Voting Purposes* ¶ 5 [Dkt. No. 560].

[32] *See Armstrong*, 294 B.R. at 354.

creditors entitled to vote, because Mr. Pfeiffer and Ms. Beeney invoked a process they no longer believe is appropriate, but upon which others may have relied.

D. For Voting Purposes, the Class Claim Shall Be Temporarily Allowed at $5,000,000 and the PAGA Claim Shall Be Temporarily Allowed at $100,000

The actual evidence before the Court is limited. Ms. Beeney and Mr. Pfeiffer rely on their proofs of claim, which they assert constitute *prima facie* evidence of the validity and amount of their claims pursuant to Bankruptcy Rule 3001. The proofs of claim contain detailed mathematical calculations for each category of alleged wage and hour violation based on the total number of work weeks, pay periods, or shifts as applicable and the applicable hourly rate. For example, Ms. Beeney asserts that the Debtors' off-the-clock bag searches result in a class claim of $6,577,458, based on the assumption that each absent class member was required to work 30 minutes per week off the clock at an hourly rate of $9.01, with 1,460,035 work weeks (*i.e.*, 1,460,035 work weeks x $9.01 hourly rate x .5 hours). The PAGA claim for off-the-clock work is asserted to be $40,544,300 (405,443 pay periods x $100 PAGA fine). Various assumptions and extrapolations are made as set forth in the proofs of claim, which are clearly based on an expert's analysis of the claims. The Debtors did not submit competing expert evidence,[33] or any evidence or argument for that matter, critiquing the analysis supplied by the claimants. And, while they initially questioned the *prima facie* validity of the proofs of claim, at argument, they conceded that point solely in connection with these motions.[34]

[33] It appears the Debtors retained an expert in the California action who provided differing figures to Judge Berle in connection with certification of the class. California Certification Hr'g Tr. At 33:17–19, Nov. 24, 2015 (Ex. D. to Dkt. No. 414).
[34] Reconsideration Hr'g Tr. at 71, 88.

The Debtors' request to temporarily allow the class claim at $500,000, but in no event at more than $5,000,000, is based on the following: (i) the complaint filed by Ms. Beeney in California state court established the aggregate amount in controversy (for both the class and PAGA claims) at less than $5,000,000, and the class should therefore be estopped from asserting a greater claim; (ii) the settlement examples from two unrelated cases before the California Superior Court filed by counsel representing Ms. Beeney and Mr. Pfeiffer in this action, each of which seeks to settle for hundreds of thousands of dollars, not millions; (iii) the rest break claims are tenuous because the employee manual given to managers always contained the correct policy and the employee handbook was corrected as of January 1, 2014; (iv) the recent decision out of the United States District Court for the Northern District of California effectively precludes the security check claims; and (v) the discretion given to courts by the PAGA statute to prevent an award from being "unfair, arbitrary and oppressive, or confiscatory" suggests a nominal PAGA award in this case.

Courts disagree about which party has the burden of proof in a Rule 3018 proceeding. Just as there is no guidance in the Bankruptcy Code on how to determine the proper amount of the claim, there is no guidance on the burden of proof in such a proceeding.[35] As the *Armstrong* court observed, some courts place the burden on the objector while others place it on the claimant.[36] I agree with the court in *Stone Hedge Properties v. Phoenix Capital Corp*[37] that because a Rule 3018 proceeding is meant to enfranchise claimants, there is an inconsistency in using the burden of proof rules that apply to

[35] *Armstrong*, 294 B.R. at 354.
[36] *Id.* (citing *In re Zolner*, 173 B.R. 629, 633–36 (Bankr. N.D. Ill. 1994) (burden of proof is on the claimant), *aff'd*, 249 B.R. 287 (N.D. Ill. 2000) and *Stone Hedge*, 191 B.R. at 64–65 (suggesting that burden of proof may be on objector)).
[37] 191 B.R. 59 (Bankr. M.D. Pa. 1995).

objections to claims.[38] I need not decide this issue, however, because legal analysis rather than evidence fuels my decision in this case.

(i) Because the Class Has Been Certified, There Is a Potential that It Is Capped by the Limitation in the Complaint

In the jurisdiction and venue section of her *First Amended Class Action Complaint* filed on May 6, 2011, in the Superior Court of the State of California for the County of Orange, Ms. Beeney alleges:

> This class action is brought pursuant to California Code of Civil Procedure section 382. The monetary damages and restitution sought by Plaintiffs exceeds the minimal jurisdiction limits of the Superior Court and will be established accordingly to proof at trial. The amount in controversy for each class representative, including claims for compensatory damages and pro rata share of attorneys' fees, is less than seventy-five thousand dollars ($75,000). However, Plaintiffs allege on information and belief, that the aggregate amount in controversy for the proposed class action, including monetary damages, civil penalties, injunctive relief, restitution and attorneys' fees requested by Plaintiffs, is less than five million dollars ($5,000,000), exclusive of interests and costs.[39]

It is clear on the face of these allegations that they are intended to establish the jurisdiction of the Superior Court. It is also clear, as the Debtors contend, that the $5,000,000 figure was not pulled out of thin air. The Class Action Fairness Act grants federal courts original jurisdiction over "any civil action in which the matter in controversy exceeds the sum or value of $5,000,000, exclusive of interest and costs" if the case is pled as a class action and there is minimal diversity.[40] The purpose of the statute is to "expand substantially federal court jurisdiction over class actions."[41]

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[38] *Id.* at 65.
[39] First Amended Class Action Complaint ¶ 1 (Ex. A to Dkt. No. 414).
[40] 28 U.S.C. § 1332(d)(2).
[41] *Morgan v. Gay*, 471 F.3d 469, 472 (3d Cir. 2006). In her post-hearing submission, Ms. Beeney asserts, for the first time, that her class action is a "local controversy" which she contends falls within the exception to CAFA's preference for federal jurisdiction. *See* 28 U.S.C. § 1332(d)(4).

The Debtors argue, based on *Morgan v. Gay*,[42] that Ms. Beeney and all absent class members are bound by their self-imposed $5,000,000 cap. *Morgan* discusses the rather unusual, but apparently not atypical, scenario in which the defendant asserts that the claims against it aggregate more than the plaintiff alleges so federal jurisdiction can be established. That scenario typically involves the following sequence of events: plaintiff first files a class action in state court asserting damages of less than $5,000,000, defendant then removes the action to federal court stating that damages exceed $5,000,000, and lastly plaintiff files a remand motion. The question the Third Circuit addressed in *Morgan* was whether the plaintiff's pleading was dispositive on the amount in controversy for jurisdiction purposes. The Third Circuit held it was not. But, given the "broad good faith requirement in a plaintiff's complaint with respect to the amount in controversy," the Third Circuit held that in order to remove a case to federal court the defendant had to prove "to a legal certainty" that the amount in controversy was over the statutory minimum.[43] In essence, the Third Circuit found that a defendant was not bound by the plaintiff's allegation of the amount in controversy.

In what is most likely *dicta*, the Third Circuit then addressed whether the plaintiff in the remanded state court class action could ever recover more damages than the $5,000,000 limitation in the complaint. It recognized a tension between cases such as the U.S. Supreme Court's decision in *St. Paul Mercury Indemnity Co. v. Red Cab Co.*,[44] which holds that a plaintiff is the master of his own complaint and recognizes a broad good faith requirement

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While this may be true, she does not suggest that the $5,000,000 aggregate amount in controversy was not pled to avoid CAFA jurisdiction nor does she identify a state-based reason for the allegation.

[42] 471 F.3d 469 (3d Cir. 2006).

[43] *Id.* at 474.

[44] 303 U.S. 283 (1938).

with respect to a jurisdictional limits allegation, and Rule 54(c) and state analogues that may permit a plaintiff to obtain relief beyond that demanded in his pleadings. Looking at the relevant state law, which cautioned that "a verdict in excess of the demand is not prohibited unless it would clearly prejudice the opposing party[,]" the Third Circuit cautioned that such a verdict "could well be deemed prejudicial to the party that sought removal to federal court when the party seeking remand uses a damages limitation provision to avoid federal court."[45]

Ms. Beeney responds by arguing that *Morgan* is inapposite because the Debtors never sought to remove the Beeney class action, and thus could not be prejudiced by having been on the losing side of a remand motion. She points out that under California law, a plaintiff is not limited to the amount in controversy pled in the complaint.[46] But, at argument, Ms. Beeney referred me to the U.S. Supreme Court's decision in *Standard Fire Insurance Co. v. Knowles*,[47] which holds that absent class members are not bound by a statement in a complaint limiting aggregate damages to less than $5,000,000[48] because a plaintiff filing a class action complaint "cannot legally bind members of the proposed class before the class is certified."[49] The Supreme Court reasoned that a non-named party is not party to a class action before it is certified. Because the Court examines the case at the time it was filed in state court for jurisdiction purposes, the plaintiff "lacked the authority to concede the amount-in-controversy issue for the absent class members."[50]

[45] *Morgan v. Gay*, 471 F.3d at 477.
[46] *Patel v. Nike Retail Servs.*, 58 F. Supp. 3d 1032, 1036 (N.D. Cal. 2014) (citing *Damele v. Mack Trucks, Inc.*, 219 Cal. App. 3d 29, 41–42 (1990)).
[47] 133 S. Ct. 1345 (2013).
[48] The complaint also attached an affidavit stipulation to the same effect. *Id.* at 1347.
[49] *Id.*
[50] *Id.*

Recognizing that the law of class actions is complicated and nuanced, I asked the parties to address in their post-hearing submissions whether Judge Berle's certification of the class now bound the absent class members to the $5,000,000 cap in the Beeney complaint. Neither party provided a case directly on point (and, perhaps none exists). But, the Debtors do refer me to portions of the *Knowles* decision that suggest a binding effect. For example, the Supreme Court acknowledged that a class action might not be certified because of the existence of a limiting damages provision in the complaint or that a court might condition certification on the removal of any such provision.[51] The Supreme Court also suggested that a proposed class representative may be inadequate because he imposes an artificial cap in the complaint.[52] Finally, the Supreme Court set up a syllogistic counterargument to its conclusion, which includes within it the step that "if the state court eventually certifies the class, the stipulation will bind those who choose to remain as class members."[53]

Without evidence regarding the five-year history of the state court action, I am not prepared to say that the Debtors are prejudiced if the damages in the class action exceed $5,000,000, but, given the holding and discussion in *Knowles* as well as Judge Berle's certification of the class without excising the limitation from the complaint, there is a high possibility the claims would be capped at $5,000,000. As the Debtors point out, the $5,000,000 figure included all claims, not just those that were ultimately certified. And, as recognized in *Red Cab* and acknowledged by plaintiffs at argument,[54] there is a good faith component to an amount in controversy statement, if a plaintiff chooses to make one.

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[51] *Id.*
[52] *Id.*
[53] *Id.*
[54] Reconsideration Hr'g Tr. at 92.

(ii) The Court Will Not Consider the Debtors' Submission of Settlements in Other Class Actions

In an effort to minimize the class and PAGA claims, the Debtors attached to their filings two settlement approval motions ("Settlement Motions") from other class actions asserting California wage and hour violations and seeking both damages and penalties under the PAGA. These Settlement Motions were filed by Capstone Law APC, the same firm the Debtors assert represent Ms. Beeney and Mr. Pfeiffer in the California state court. The Debtors argue that I may take judicial notice of these settlements because "they are reflected in the pleadings on file in courts of competent jurisdiction."[55]

At the reconsideration hearing, the Debtors moved the Settlement Motions into evidence, drawing opposition from Ms. Beeney and Mr. Pfieffer. They asserted multiple grounds to exclude the Settlement Motions, including lack of foundation, no indicia of reliability, and no way to evaluate, objectively, the statements in the Settlement Motions. They posited that the only way I could consider the Settlement Motions would be in the context of expert testimony.

I agree with Ms. Beeny and Mr. Pfeiffer. The Settlement Motions, absent testimony to explain the similarities and differences between the circumstances in those cases and the circumstances here is simply unhelpful. Moreover, the only basis the Debtors offered for their admission into evidence was judicial notice. The Debtors cite *Southmark Prime Plus, L.P. v. Falzone*[56] for the proposition that a court may take judicial notice of the contents of records from another jurisdiction.[57] While undoubtedly true, the district court also

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[55] *Debtors' Opposition to Motion of Class and PAGA Claimants for Estimation and Temporary Allowance* ¶ 12 ("Opposition to Estimation") [Dkt. No. 415].
[56] 776 F. Supp. 888 (D. Del. 1991).
[57] Opposition to Estimation ¶ 12.

recognized that "[a] judicially noticed fact must be one not subject to reasonable dispute in that it is . . . (2) capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned."[58] The Debtors ask me to take judicial notice of "facts" (*i.e.*, the claims being the settled, the aggregated asserted amounts of those claims, and the settlement amounts) to draw a conclusion that the claims before me should be set at similar amounts. These are not the types of "facts" that courts take judicial notice of, and I decline to do so even in the arguably more liberal context of this proceeding. Accordingly, the Settlement Motions will not factor into my decision.

(iii) The Debtors Have Not Presented Any Evidence on Which to Reduce the Rest Break Claims

Without much elaboration, the Debtors argue that a downward departure from the settlements embodied in the Settlement Motions is warranted because the certified rest break claims are tenuous, given that the employee manual distributed to managers always contained the correct policy and the employee handbook was corrected as of January 1, 2014. That change is not dispositive for the prepetition class, which spans eight years. Further, the Debtors have not submitted any information, or even an alternative mathematical calculation, that cuts off the class claim at January 1, 2014. Accordingly, there is no basis to discount Ms. Beeney's claims because of the "tenuous" nature of the rest break claims.

(iv) *Frlekin v. Apple Inc.* Causes Significant Challenges to Recovery on the Off-the-Clock Claims

On November 7, 2015, the United States District Court for the Northern District of California decided cross motions for summary judgment in the case of *Frlekin v. Apple*,[59] a

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[58] *Falzone*, 776 F. Supp. at 892 (quoting Fed. R. Evid. 201(b)(2)).
[59] 2015 WL 6851424 (N.D. Cal. Nov. 7, 2015).

class action suit alleging violation of California's wage and hour laws. Employees of Apple retail stores located in California were subject to both bag and technology searches to ensure against theft. The searches occurred whenever an employee left the store premises carrying a bag, purse, backpack or an Apple product, such as an iPhone. As here, the named plaintiffs in the class action sought compensation for the time spent waiting for the searches to be performed. As part of the class certification, the named plaintiffs agreed to limit the reasons for bringing bags to work. The class, as certified, was authorized to bring claims "based on the most common scenario, that is, an employee who voluntarily brought a bag to work purely for personal convenience."[60] On summary judgment, then, the issue was "whether the time spent waiting for the exit searches to be completed deserved compensation under California law."[61]

California law requires employees to be paid for all hours worked, which is defined as "the time during which an employe[e] is subject to the control of an employer, and includes all the time that the employee is suffered or permitted to work, whether or not required to do so."[62] The court addressed these two independent bases with respect to the off-the-clock bag searches and found them wanting.

The first basis—that the employee was subject to the control of the employer—has two prongs: (i) the employer restrained the employee's action during the activity; and (ii) the activity was mandatory, not optional. As to the first prong, the Court easily concluded it was met because if an employee wished to leave an Apple store, he was subject to a bag

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[60] *Apple*, 2015 WL 6851424, at *2. Any class members with special needs could intervene, but none did. *Id.*
[61] *Id.* at *1.
[62] *Id.* at *3.

search.[63] But, as the Court explained, the second prong was not met because the employee could choose not to bring a bag to work. The Court found that if an employee had a real choice over whether to engage in the conduct, as opposed to an illusory choice, then the activity was optional, not mandatory. As applied to Apple, the evidence was clear that some employees did not bring bags to the store, and, therefore, did not undergo searches when they left the store. With a class limited to those who voluntarily brought a bag to work for their own convenience, the court found nothing illusory about the choice.[64]

As for the second basis—that the employee is suffered or permitted to work—the court held that waiting to be searched was not compensable, observing that "[o]ur plaintiffs merely passively endured the time it took for their managers or security guards to complete the peripheral activity of a search. Neither the searches nor waiting for them to be completed had any relationship to their job responsibilities."[65] In making this decision, the court took guidance from the U.S. Supreme Court's decision in *Integrity Staffing Solutions, Inc. v. Busk*,[66] which held for purposes of the Fair Labor Standards Act that preliminary and postliminal activities are only compensable if the activities are an "integral and indispensable" part of an employee's duties.[67]

While the Debtors argue that *Apple* is directly on point, Ms. Beeney and Mr. Pfeiffer try to distinguish the case legally and factually. First, they argue that a close reading of *Apple* shows that the issue is not whether the choice to bring a bag is voluntary, but whether the search itself is voluntary. This is a misreading of *Apple*, which, based on the class

[63] *Id.*
[64] *Id.* at *6.
[65] *Id.* at *11.
[66] 135 S. Ct. 513 (2014).
[67] *Apple*, 2015 WL 6851424, at *10.

certified, necessarily focused on the employee's choice to bring a bag. Second, they distinguish *Apple* factually by arguing that the Debtors' employees were searched regardless of whether they carried a bag. This argument is new, and when pressed at argument to identify the nature of a search unrelated to a bag check, counsel could not.[68] Regardless, common experience shows that most employees bring bags to work voluntarily. Finally, Ms. Beeney and Mr. Pfeiffer argue that I should ignore the *Apple* case altogether, as Judge Berle "was not convinced by the Debtors['] first effort to use *Apple* to get rid of the bag check claim."[69] As Judge Berle stated, however, he was not attempting to ascertain the merits of the claim, only whether Ms. Beeney met the class action requisites; thus, this argument is not persuasive.[70]

Based on a review of *Apple* and the arguments of counsel, claims based on the searches of bags, backpacks or the like brought voluntarily to a PacSun store are likely foreclosed. While there may have been other types of exit searches conducted, to date, Ms. Beeney and Mr. Pfeiffer have not satisfied me that such claims exist.

(v) PAGA Provides Discretion to Ensure that Any Penalties Are Not Unfair, Arbitrary and Oppressive, or Confiscatory.

The PAGA provides that in actions brought by aggrieved employees as private attorney generals for the state of California "a court may award a lesser amount than the maximum civil penalty amount specified by this part if, based on the facts and circumstances of the particular case, to do otherwise would result in an award that is unjust,

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[68] Counsel pointed to the deposition of Ms. Shin, who, in response to somewhat leading questioning from her counsel, testified that male colleagues, to the best of her knowledge, underwent a security check regardless of whether they brought a backpack or not. Shin Dep. at 62, July 14, 2016 (Ex. C. to Dkt. No. 572).
[69] Reconsideration Hr'g Tr. at 56.
[70] California Certification Hr'g Tr. at 28.

arbitrary and oppressive, or confiscatory."[71] The statute, itself, does not give any guidance on what facts or circumstances would warrant a reduction and neither did any of the parties to this case.

In his proofs of claim, Mr. Pfeiffer asserts PAGA claims in the aggregate amount of $135,374,113.[72] With respect to the Estimation Motion and Cross-Motion, other than the objections based on the Settlement Motions, which I am not considering, the only other argument made is that I should use the discretion given by the statue to ensure that the award is not unjust, arbitrary and oppressive, or confiscatory.

Permitting the PAGA Claim to be voted in its full amount would not be arbitrary because it is based on the calculations made in the proofs of claim, which, while they contain assumptions and extrapolations, have not been specifically challenged by the Debtors. I do find, however, that given the court's duty to divine the "proper" amount of the claim for voting purposes, awarding the full amount of this penalty claim would give the PAGA claim an outsized influence over the plan process.

(vi) The Proper Amount of the Class and PAGA Claims for Voting Purposes

The Debtors did not provide any evidence of the size of other creditors' claims in the general unsecured class at the hearing on the Estimation Motion and Cross-Motion. A review of the previously approved disclosure statement[73] reveals that the Debtors estimated the claims in the general unsecured class to be between $11 million and $22 million without

[71] PAGA § 2699(e)(2).
[72] The claim breaks down as follows: Rest Break Claims: $18,654,759; Off-the-Clock Claims: $47,121,758; Meal Period Claims: $4,880,300; Business Expense Claims: $8,108,900; Vacation Claims: $578,800; On-Call Claims: $20,272,150; §203 Penalties: $35,374,113.
[73] *Disclosure Statement for the Joint Plan of Reorganization of Pacific Sunwear of California Inc. and Subsidiary Debtors* [Dkt. No. 521].

including the class and PAGA claims. Taking into account the legal arguments that have been made as well as the evidence presented, I find on the record made that the class claim will be temporarily allowed in the amount of $5,000,000 for voting purposes only. Because the employee claims will have a voice through the class claim, and given the statutory permission to ensure the claims are not unjust or confiscatory, the PAGA Claim, which is punitive in nature, will be temporarily allowed in the amount of $100,000 for voting purposes only.

II. While I Will Entertain Reconsideration of the First PacSun Memorandum, I Find No Basis to Change that Decision.

Ms. Beeney asks me to reconsider my previous ruling that she is not an adequate representative of any absent class members other than those, like her, who hold general unsecured claims. Ms. Beeney cites to Federal Rule of Civil Procedure 59(e), made applicable by Bankruptcy Rule 9023, which permits alteration or amendment of a judgment based on (i) an intervening change in the law; (2) the availability of new evidence; or (3) the need to correct a clear error of law or to prevent manifest injustice. While she does not state which section is applicable, process of elimination (there is no citation to intervening law or new evidence) points to "preventing manifest injustice."

My ruling in the First PacSun Memorandum that Ms. Beeney cannot adequately represent absent class members who may hold priority claims was based on the Third Circuit's decision in *Dewey v. Volkswagen Aktiengesellschaft*,[74] which was cited by the Debtors, but, quite candidly, was not a focus at the original argument. Accordingly, at the July 18 hearing, I permitted Ms. Beeney's counsel to address the First PacSun Memorandum,

[74] 681 F.3d 170 (3d Cir. 2012).

including *Dewey*. Having now considered her arguments, I have no reason to change or revise my original conclusion.

In her papers and at argument, Ms. Beeney did not cite any case law that suggests that *Dewey* is not binding, applicable authority or that I applied it incorrectly as a matter of law. Rather, Ms. Beeney makes four different arguments: (i) the structural conflict that I found exists in this case is merely a "potential conflict which may never materialize;" (ii) my decision presupposes that Ms. Beeney will breach her fiduciary duty to the absent class members; (iii) the so-called "Straddle Employees"—those whose dates of employment are both before and after, the priority class period cutoff of October 10, 2016—will act as "natural watchdogs" against any improper treatment of one class over another; and (iv) that my decision unfairly, and retroactively, creates a forfeiture of a subset of claims in the state certified class. I will address these arguments in order.

First, Ms. Beeney urges that I reverse my decision and address the adequacy of representation requirement "in real-time—when and if such conflict issues actually materialize."[75] She contends that a conflict may never arise because, for example, this matter may be litigated rather than settled, as evidenced by the five years of litigation that preceded the filing of the petition.[76] In making this argument, Ms. Beeney misapprehends

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[75] Motion to Amend or Reconsider ¶ 10.

[76] *Id.* Ms. Beeney states that the most likely outcome—a litigated outcome—was unaccounted for in the First PacSun Memorandum. The possibility of a litigated outcome, while theoretically possible, is not practicable in the context of this case. As reflected in the other motions before me, the looming confirmation hearing makes it necessary to either estimate or resolve any administrative or priority claims, which must be paid in full in order to confirm a plan. 11 U.S.C. § 1129(a)(9). Further, while the Debtors' current plan provides for holders of "Qualified Unsecured Trade Claims" (which, by definition, do not include the alleged class claims) to receive a 100% recovery, holders of general unsecured claims are limited to their share of $400,000. Assuming for the sake of argument that the current plan is confirmable and confirmed (on which I make no comment), it seems unlikely that the class claim would be litigated.

the structural conflict inherent in the prepetition class now that the Debtors have filed their bankruptcy cases. As explained in the First PacSun Memorandum, because section 1129(a)(9)(B) requires payment in full of claims having priority under the Bankruptcy Code, there is a fundamental conflict between those claimants and the holders of general unsecured claims. And, as the *Dewey* court emphasized, it is irrelevant whether the proposed settlement actually leaves the weaker positioned class members unharmed; the point is that the structural protection that is the foundation of Rule 23(a)(4) must be met throughout the process of bargaining for settlement.

Since the First PacSun Memorandum, the United States Court of Appeals for the Second Circuit in *In re Payment Card Interchange Fee & Merchant Discount Antitrust Litigation*,[77] refused to certify a class and approve a proposed settlement of litigation spanning ten years because of the inadequacy of the class representatives. Agreeing with the Third Circuit, but stating the principle differently, the Second Circuit explained:

> Adequacy must be determined independently of the general fairness review of the settlement; the fact that the settlement may have overall benefits for all class members is not the "focus" in "the determination whether proposed classes are sufficiently cohesive to warrant adjudication."[78]

Waiting for a final resolution as Ms. Beeney suggests does not cure any fundamental intra-class conflict. Moreover, I do not find it efficient in the context of this case to essentially preclude settlement discussions with the Debtors because of an inadequate representative.

It is also clear that because Ms. Beeney is no longer an adequate representative for all absent class members, I could have simply denied the filing of any class proof of claim à là *Dewey* and *Payment Card Interchange*. Instead, I permitted the filing of a class claim for those

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[77] 2016 WL 356719 (2d Cir. June 30, 2016).

[78] *Id.* at *5 (quoting *Denney v. Deutsche Bank AG*, 443 F. 3d 253, 268 (2d Cir. 2006)).

absent class members who would, if their claims are valid, hold general unsecured claims.[79] That ruling permits Ms. Beeney to file a class proof of claim covering a period of 8 years and seven months; it excludes claims covering only a four month period, albeit the priority period. Under these circumstances, to borrow from the Second Circuit, the only interest that may be served by this request under the circumstances is that of class counsel.[80]

Dewey and *Payment Card Interchange* also dispense with Ms. Beeney's arguments that my decision presupposes that Ms. Beeney will breach her fiduciary duty to the absent class members and that the existence of Straddle Employees solves any fundamental intra-class conflict. I do not, as Ms. Beeney would have me do, look to bankruptcy law to determine whether Ms. Beeney is an adequate representative; I look to Rule 23. Interpreting Rule 23, the Second Circuit, citing United States Supreme Court decisions as well as its own, specifically rejects the argument that class representatives who hold claims in more than one subgroup can adequately represent any one of those subgroups. It explains: such class representatives will have the incentive to maximize their own total recovery rather than the recovery of any single group.[81]

Finally, Ms. Beeney argues that my decision unfairly, and retroactively, creates a forfeiture of a subset of claims in the state certified class. Ms. Beeney contends that neither she nor Judge Berle could have anticipated the bankruptcy filing, and thus my ruling is

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[79] Ms. Beeney suggests that Judge Berle's order and, thus, my order, may already permit the filing of priority proofs of claim for Straddle Employees. To avoid any such unintended result, I will amend my June 22, 2016 order to clarify that Ms. Beeney may only file a general unsecured claim on behalf of her class.

[80] *Payment Card Interchange*, 2016 WL3563719, at *8.

[81] *Payment Card Interchange*, 2016 WL 3563719, at *7 (citing *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 627 (1997), *Ortiz v. Fibreboard Corp.*, 527 U.S. 815 (1999), and *In re Literary Works in Elec. Databases Copyright Litig.*, 654 F.3d 242 (2d Cir. 2011)); *see also Dewey*, 681 F. 3d at 189–90 (suggesting that one of the ways to satisfy Rule 23(a)(4) is to divide the class into two subclasses each with representative plaintiffs).

"untenable and unfair . . . because the perceived conflict can only possibly be known *six months after it first arises*" creating a race to find a substitute representative prior to a bar date and a "highly-elevated [] risk of forfeiture."[82] While this may be true, it is not unique to bankruptcy. What Ms. Beeney ignores is that neither class certification nor approval of a class representative is set in stone.

There is no absolute right to proceed by class action, which is an exception to the general rule that parties assert and litigate their own claims.[83] To certify a class, therefore, all of the Rule 23(a) requisites and one of the Rule 23(b) criteria must be satisfied. A necessary corollary to certification is the court's duty to monitor the litigation to ensure that the requisites are maintained throughout the case.[84] A judge must "define, redefine, subclass, and decertify as appropriate in response to the progression of the case from assertion to facts."[85] So, for example, if during the course of the litigation, the size of the class is reduced because class members opt out, or evidence revealed in discovery narrows the class such that joinder is now possible, the class may be decertified.[86] Or, if evidence

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[82] Motion to Amend or Reconsider ¶ 44–45.
[83] *Wal-Mart Stores Inc. v. Dukes*, 564 U.S. 338, 348 (2011) ("The class action is 'an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only.'" (quoting *Califano v. Yamasaki,* 442 U.S. 682, 700–01, (1979)).
[84] Newberg on Class Actions § 7:37 (5th ed. 2011).
[85] *Richardson v. Byrd*, 709 F.2d 1016, 1019 (5th Cir. 1983). I recognize that *Byrd* was decided under a previous version of Rule 23, but, as other courts, I find the holding still applicable. *See, e.g.*, *Lightfoot v. District of Columbia*, 246 F.R.D. 326, 334 n.6 (D.D.C. 2007); *See also*, *Alberton v. Commonwealth Land Title Ins. Co.*, 299 F.R.D. 109 (2014) (reviewing certification standards six years after original certification due to the significant changes in the governing procedural and substantive law, and decertifying two subclasses). Judge Berle recognized his duty as a state court judge to ensure that the class action requisites are maintained during the course of the case. He specifically acknowledged that his ruling was without prejudice to decertification under certain circumstances, which included failure to establish the validity of her expert's statistical sampling and whether that analysis was appropriate in the case. First PacSun Memorandum *1.
[86] Newberg on Class Actions § 7:38.

garnered during discovery reveals new information about the class claims such that common law and facts no longer exist, a class may likewise be decertified.[87]

Lack of adequate representation is also a basis for decertifying a class.[88] In *Birmingham Steel Corp. v. Tennessee Valley Authority*,[89] a case cited by Ms. Beeney, Birmingham Steel brought a class action on behalf of a group of 400 large-volume industrial consumers against Tennessee Valley Authority. On December 5, 2000, the district court certified the class action with Birmingham Steel as the class representative. The class notice sent to members provided that the class did not include any member in a bankruptcy proceeding. In or around June 2002, Birmingham Steel filed a voluntary bankruptcy proceeding. Shortly thereafter, Tennessee Valley Authority moved to decertify the class. After argument, the district court decertified the class finding that Birmingham Steel was no longer an adequate representative because it was no longer a member of the class.[90] On appeal, the Eleventh Circuit remanded with instructions to allow a "reasonable period of time for a member of the class to intervene or to be substituted as the class representative[,]" failing which, the district court could decertify the class action.[91]

Here, while the class was certified only two months prior to the Debtors' bankruptcy filings, the commencement of bankruptcy with the attendant application of the Bankruptcy Code changed the playing field such that Ms. Beeney is no longer adequate to represent the entire state certified class. While that may seem unfair, it is no different than non-bankruptcy cases where the facts or law develop in a way such that Rule 23 is no longer

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[87] *Id.* (citing *Anderson v. Boeing Co.*, 2006 WL 2990383, at *4 (N.D. Okla. 2006)).
[88] *Id.* § 7:38.
[89] 353 F.3d 1331 (11th Cir. 2003).
[90] *Id.* at 1334.
[91] *Id.* at 1343.

satisfied. Nor is there a forfeiture of any wage and hour claims arising between October 10, 2015, and February 26, 2016 because each person in that priority period will have an opportunity to file his or her own proof of claim, and claimants with priority claims after February 26, 2016 did not have the benefit of the tolling of the statute of limitations. Accordingly, I find no basis to reconsider the First PacSun Memorandum.

III. Ms. Shin Will Not Be Permitted to File Proof of Claim on Behalf of a Class of Priority Claimants

Since the First PacSun Memorandum, Ms. Beeney's counsel, ostensibly on her behalf, has been busy attempting to find a substitute and/or additional class representative to represent those absent class members who would hold priority claims. Ms. Beeney argues that Ms. Shin should be permitted to substitute in or file a late proof of claim because the First PacSun Memorandum was an unforeseeable event that constitutes excusable neglect and there is no prejudice to the Debtors because Ms. Beeney's timely filed proof of claim included claims arising in the priority period. She also argues that I should not analyze whether Ms. Shin is an adequate representative of the class or consider any matter that may have been placed in front of Judge Berle prior to certification as the Debtors did not ask Judge Berle to reconsider his decision nor did the Debtors appeal it.

The Debtors oppose the motion arguing that: (i) excusable neglect cannot exist because Ms. Shin and others with claims in the priority period were served with the bar date notice and did not file their own proofs of claim; (ii) I must perform a complete analysis of the priority claims, including not only whether the class comports with Rule 23, but whether I should exercise my authority to apply Rule 23 with respect to the priority period claims; (iii) that factual differences exist which preclude class certification of a priority period class; and (iv) in any event, Ms. Shin is not an adequate representative of the priority class.

As an initial matter, to the extent excusable neglect is a factor in this analysis, I agree with Ms. Beeney that it is met on the circumstances of this case. Ms. Beeney sought permission to file a class proof of claim, and timely filed such a claim. It is only my decision that she is not an adequate representative for claims in the priority period that created the possibility of an untimely proof of claim. The Debtors are incorrect in their position that Ms. Shin's failure to file an individual claim is the operative question. Rather, the question is whether I should permit Ms. Shin to file a class claim. This position is also consistent with the non-bankruptcy law cited by Ms. Beeney[92] and not contradicted by the Debtors. As stated in *Tennessee Valley Authority*, once certified, "a class acquires a legal status separate from that of the named plaintiffs[,]"[93] and thus a deficiency in the class representative does not necessarily call for dismissal of the action if another member of the class can serve as an adequate representative.[94] Under the circumstances of this case, therefore, Ms. Shin, if all other requisites are met, will be permitted to file a proof of claim on behalf of the class that attained a separate legal status.

Given my duty, however, to ensure that a class action at all times comports with Rule 23, I agree with the Debtors that I must review both the proposed class and the class representative for compliance with that rule. Further, because this is a bankruptcy proceeding I must determine in the first instance whether I should apply Rule 23.

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[92] Motion to Amend and Reconsider ¶ 29.

[93] *Tenn. Valley Auth.*, 353 F.3d at 1336 (citing *Lynch v. Baxley*, 651 F.2d 387, 388 (5th Cir. Unit B July 1981)).

[94] *Id.*

A. I Will Decline to Apply Rule 23 to the Off-the-Clock Search Claims Because to Do So Will Adversely Affect the Administration of the Estate

As discussed in the First PacSun Memorandum, whether to apply Rule 23 once a bankruptcy case has commenced is within the court's discretion.[95] The court's consideration should include an analysis of the three factors articulated in *Musicland*:[96] (i) whether the class was certified prepetition; (2) whether the members of the putative class received notice of the bar date; and (3) whether class certification will adversely affect the administration of the estate.[97]

Application of the *Musicland* factors to the purported priority class differs in at least two respects from the analysis applied to the general unsecured class. First, the entire priority class was not certified prepetition as the state certified class term ended approximately five weeks prior to the filing of the petition. Second, each potential priority claimant received actual notice of the bar date, and thus had an opportunity to file an individual proof of claim. As set forth in the Declaration of Benjamin J. Steele, "only seven proofs of claim have been filed by natural persons in California that assert entitlement to any type of priority."[98]

As for the impact on the administration of the estates, the Debtors argue that the passing of the bar date fundamentally changes the analysis of this factor. Relying on *Musicland,* the Debtors contend that this weighs against the applicability of Rule 23. Several

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[95] First PacSun Memorandum, 2016 WL 3564484, at *5.
[96] *In re Musicland Holding Corp.*, 362 B.R. 644 (Bankr. S.D.N.Y. 2007).
[97] *Id.* at 654–55.
[98] Steel Declaration ¶ 5. Mr. Steele is a Vice President of Prime Clerk, the claims agent appointed in these cases. While it is conceivable that the Debtors' former or current California employees currently live outside of California, it is unlikely that that would add appreciably to the total priority claims filed. Further, although it does not appear that the Steel Declaration was admitted into evidence, Ms. Beeney did not question this point.

courts, however, have recognized that the class action tolling rule[99] applies in bankruptcy, such that if a self-described class representative timely filed a class proof of claim (or an adversary proceeding) and the court declines to allow it, a reasonable bar date should be set to allow claimants—who would have fallen into the class—time to file individual claims.[100] This is the case notwithstanding that these claimants were sent the bar date notice.[101]

Looking solely at these arguments, I would apply Rule 23 to the portion of the priority period that was included in the state certified class action. The Debtors would not be prejudiced because they have been on notice of the class action claims for years. I would not, however, find it appropriate to apply Rule 23 with respect to the priority period after February 26, 2016, the end of the class period certified by Judge Berle.[102]

At the July 18 hearing, in response to argument by Ms. Beeney's counsel about continuing violations, I asked two questions: (i) whether a state court would entertain continuing violations as part of a preexisting certified class and (ii) what are Ms. Beeney's obligations with respect to claims outside the class period. I also permitted post-hearing submissions on that issue. Neither of the parties cited a case directly on point (and there may be none). But, the parties seem to agree that some further action would be necessary before claims arising after the class period could proceed in state court[103]—whether that

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[99] *See, e.g., In re Kaiser Grp. Int'l, Inc.*, 278 B.R. 58, 63-64 (Bankr. D. Del. 2002) ("[T]he filing of a class action tolls the statute of limitations otherwise applicable to all class members in their individual capacities. (citing Bailey v. Sullivan, 885 F.2d 52, 65 (3d Cir. 1989)).

[100] *In re MF Global Inc.*, 512 B.R. 757, 764–65 (Bankr. S.D.N.Y. 2014); Schuman v. The Connaught Grp. (In re The Connaught Grp.), 491 B.R. 88, 97–98 (Bankr. S.D.N.Y. 2013); *see also* Kaiser Grp. Int'l, 278 B.R. 58, 63–64 (Bankr. D. Del. 2002).

[101] *See Kaiser Grp. Int'l*, 278 B.R. at 63–64; *MF Global*, 512 B.R. at 763–65 (distinguishing *Musicland*, upon which the Debtors rely).

[102] This is but one instance of each party taking the inconsistent position that I should be bound by Judge Berle's decision when it favors them and ignore it when it does not.

[103] Ms. Beeney's post-hearing submission suggests for the first time that the state court certified class may already include claims arising after February 26, 2016. I do not read Judge Berle's order that

would be the filing of a new complaint to cover the portion of the priority period not included in the class definition or some type of motion to extend the class period previously certified. Ms. Beeney has cited me to no law which requires her to take on this burden or that makes her a fiduciary for claimants outside the state certified class period. Further, holding any class claim to the prepetition certified period honors the separate legal status the class attained through certification.

Nonetheless, there is another consideration that compels me to decline to exercise my discretion to apply Rule 23 to the off-the-clock security check claims. Having considered the Estimation Motion and the Cross-Motion, I have concluded that it is highly unlikely that those claims survive *Frlekin v. Apple*. And, while I could be incorrect, given my conclusion, it is clear that permitting the filing of the off-the-clock security check claims will adversely impact the estate. Litigating these claims on a priority basis could delay consideration of the Debtors' plan of reorganization and cause expenditures of fees which these Debtors can ill afford, each of which impacts other parties-in-interest in these cases.

I recognize that courts do not generally consider the merits of the claims when considering certification of a class action. But, when, as here, I have already considered the claims and found them wanting, I find that injecting a priority class claim into these cases "would inappropriately clash with bankruptcy needs and concerns"[104] and, thus, adversely

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way, nor is this new found position consistent with previous positions taken by Ms. Beeney in these cases. Moreover, the cases cited actually support the opposite position, considering the language in those cases that defines the class specifically references future class members. *See J.D. v. Nagin*, 255 F.R.D. 406, 417 (E.D. La. 2009) (certifying a class of "all children who are now or in the future will be confined at the Youth Study Center in New Orleans, Louisiana."); *Morel v. Giuliani*, 927 F. Supp. 622, 632 (S.D.N.Y. 1995) (certifying class consisting of "all residents of New York City who have received, receive, or will receive AFDC, Food Stamp or Home Relief benefits . . . .).

[104] *In re Motors Liquidation Co.*, 447 B.R. 150, 164 (Bankr. S.D.N.Y. 2011).

impact the estate and other creditors. Accordingly, I decline to apply Rule 23 to the off-the-clock security check claims.

B. The Rest Break Claims During The Priority Period Do Not Satisfy Rule 23.

By the First PacSun Memorandum, I permitted Ms. Beeney to file a class proof of claim with respect to her allegations that PacSun's rest break policy and off-the-clock security checks violate California law. Central to my holding was the fact that PacSun was alleged to maintain certain companywide policies contravening state wage and hour laws, such that there were common legal issues to be decided and that legal issues predominated over factual issues.[105] As previously noted, if the Debtors are correct that their policies do not violate California law, no class member will have a claim.

Concerning the rest break policy, my holding was based on the then uncontested fact that PacSun's employee handbook (which differed from the manual given to managers) contained a uniform rest break policy alleged to be facially non-compliant with California law.[106] In support of the Debtors' objection to the Motion to Amend or Reconsider, the Fox Declaration was admitted into evidence. Mr. Fox, the Senior Human Resource Manager of Pacific Sunwear Stores Corp. since 2010, states that the employee handbook was changed on January 1, 2014, to reflect the manual given to managers.[107] As such, the rest break

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[105] First PacSun Memorandum, 2016 WL 3564484, at *7 (with respect to commonality), *8 (with respect to typicality) and *10 (with respect to predominance).

[106] California law requires a rest break for every four hours or "major fraction thereof." The handbook stated that employees are provided: "one 10 minute break for every four hours of work. If you are working a shift of less than 3 ½ hours you will not be entitled to a rest period." Fox Declaration ¶ 5. On the other hand, the manual required store managers to provide one 10-minute break to all employees working 3.5 hours or more, two 10-minute breaks for a shift of 6 hours or more, and three 10-minute breaks for a shift of 10 hours or more. *Id.*

[107] Declaration of Steve Fox in Opposition to *Motion of Class Claimants (A) for Leave to Amend Proof of Claim to Substitute Class Representative or, Alternatively, to Provide Additional Time for Priority Class Representative to File Class Proof of Claim, and (B) for Partial Reconsideration* ("Fox Declaration") [Dkt. No. 563 Ex. G].

policy in the updated handbook is now facially compliant with California law. Neither Ms. Beeney nor Ms. Shin assert otherwise, nor do they argue that the modified handbook was not in effect during the priority period.

The updated handbook changes the Rule 23 analysis. It turns the rest break claims from those based on an allegedly violative companywide policy into those that arise only when a specific store deviates from an otherwise compliant companywide policy. The changed nature of these claims creates an inherently fact-driven inquiry. The change is illustrated not only by the Fox Declaration, but also by Ms. Shin's own testimony. Specifically, Ms. Shin testified that she that she did not take a rest break unless instructed to by her manager.[108] There is no suggestion that other employees similarly relied on a manager to direct them to take breaks. Her allegation indicates the need to look into individualized factual issues, including the practice of each manager and whether other employees felt similarly constrained, neither of which was alleged to be uniform. As such, I find that the rest break allegations for the priority period do not satisfy Rule 23(b) because questions of law or fact do not predominate over questions regarding individual employees.[109] While in individual instances the Debtors may have violated California law on rest breaks, there is not a common question of law on liability during the priority period. Accordingly, I will not permit a class proof of claim based on rest break violations for the priority period.

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[108] Shin Dep. at 32–33. This type of allegation was not previously raised in this Court.
[109] The rest break claims may also fail the "commonality" requirement of Rule 23(a)(ii), even though that standard is usually "easily met." *See* First PacSun Memorandum, 2016 WL 3564484, at *7. This is because now that there is no more common legal question regarding liability, there may be no common question at all. Those claims may also fail the typicality requirement, given the lack of evidence that Ms. Shin's failure to take breaks 10–20% of the time was for reasons typical of others—*i.e.*, lack of managerial approval.

Conclusion

I have previously permitted the filing of a class proof of claim covering a period of 8 years and seven months—from March 18, 2007 through October 10, 2016. For the reasons set forth in this Memorandum, the Court will not permit the filing of a class proof of claim for the period after October 10, 2016. Given this ruling, however, a second bar date notice must go to employees who worked in PacSun's California retail locations from October 11, 2016 through February 26, 2016.

For purposes of voting on the Debtors' plan, the class claim will be temporarily allowed in the amount of $5,000,000 and the PAGA claim will be temporarily allowed in the amount of $100,000.

An appropriate order will enter.

Dated: August 8, 2016
Wilmington, Delaware

LAURIE SELBER SILVERSTEIN
UNITED STATES BANKRUPTCY JUDGE