CLASS ACTION ARBITRATION

by

Alfred G. Feliu[1]

EDITOR'S NOTE**: The question of whether employee dispute management programs can or should include putative waivers of class or collective actions was emotionally debated in the CPR Employment Disputes Committee. The CPR Employment Dispute Arbitration Procedure includes a provision, at Section 2.7, that can be included if there is an intention to attempt to effect such a waiver.* ***The inclusion of this optional section in the model Procedure is not an endorsement by CPR or by all Committee members of waiver of class or collective actions.)

Class action arbitration brings together the perceived efficiencies of class actions in multi-party litigation and in arbitration, an increasingly favored means of dispute resolution. The marriage of these two means of dispute resolution has not, however, been uniformly applauded. Many legal and practical issues remain that cloud the atmosphere for class action arbitration. The future and practical application of class action arbitration thus remains decidedly uncertain.

Key to the discussion of class action arbitration is the intent of the parties, and the language employed in the arbitration agreement to express that intent. Three basic options are available. The parties can clearly state in the agreement that class claims may be adjudicated in the arbitration context; the agreement can clearly reject the class action

[1] Alfred G. Feliu is a partner in the firm Vandenberg and Feliu LLP in New York City.

option; or the agreement can be silent or ambiguous on the point. Before the rights of parties in each of these situations can be evaluated, however, a more basic question must be asked – can class claims be arbitrated at all?

Legal Landscape

Few of the key legal issues related to the arbitration of class claims have been definitively resolved. Even the most basic question – can class actions be heard in the arbitral context? – lacks an authoritative answer. That having been said, there is strong support for the view that courts will support the arbitration of class actions, where the parties' agreement clearly allows for it.

Moreover, even in the absence of clear sanctioning, courts seem inclined to authorize the arbitration of class claims. Most notably, the Supreme Court in *Green Tree Financial Corp. v. Bazzle*, 123 S. Ct. 2402 (2003), impliedly recognized the viability of class action arbitration. The court ruled that the question whether the parties' agreement allowed for class actions was for the arbitrator, not the court, to decide in the first instance. In doing so, the Court gave no hint that arbitrators lacked the authority to hear and decide class actions when authorized by the parties to do so.

A brief overview of the legal landscape follows.

1. The *Bazzle* Decision

In *Bazzle*, the respondent landowners had secured loans from a commercial lender, Green Tree. The loan documents included a mandatory arbitration agreement which provided that "all disputes, claims, or controversies arising from or relating to [the loan agreement] . . . [were to] be resolved by binding arbitration by one arbitrator selected by [Green Tree] with consent of [respondents]." Green Tree apparently failed to

provide certain documentation with the loan forms required by South Carolina law and respondents commenced two separate court actions on behalf of themselves and other putative class members. Green Tree moved to compel arbitration. In one case, the court certified the class and compelled arbitration of the class claims. In the second case, arbitration was compelled on appeal. In both cases, the same arbitrator conducted class-wide arbitrations and found for respondents. In doing so, the arbitrator awarded nearly $11 million in damages in the first case, and over $9 million in the second.

On appeal, the South Carolina Supreme Court upheld both awards. The court reasoned that class-wide arbitration was appropriate, even if the relevant arbitration provision was silent, where equity and efficiency would be served and the parties would not be prejudiced as a result. The court was concerned that consumers would be denied any practical means of relief if they were required to arbitrate claims of nominal monetary value.

The United States Supreme Court vacated the judgment. Four justices (with a fifth justice concurring in the judgment) ruled that whether the arbitration provision, which was silent on the question of class arbitration, encompassed class claims was for the arbitrator to decide in the first instance. The plurality opinion noted that the arbitration clause was broad and submitted to the arbitrator all disputes relating to the loan agreement. The plurality concluded that whether the loan agreement authorized class claims did not concern the overall validity of the arbitration agreement or whether it applied to the underlying dispute, which are questions for the court, but rather concerned questions of contract interpretation and arbitration procedures. In contrast, the dissent read the loan agreement as precluding class claims because it spoke in terms of one

arbitrator selected by the parties (class members who were not class representatives generally would not participate in the selection of the arbitrator) and referred to the respondents as "you," suggesting that only the consumer was subject to the arbitration agreement.

No suggestion was made by any of the justices that arbitrators cannot hear and decide class claims. Rather, the issue was under what circumstances arbitrators can do so.

2. Court's Recognition of Class Arbitrations

A number of courts have expressly recognized the ability of arbitrators to hear and determine class actions. See e.g. *Blue Cross of California v. Superior Court,* 67 Cal.App.4th 42, 65 (1998), *cert. denied,* 527 U.S. 1003 (1999); *Lewis v. Prudential Bache Securities, Inc.*, 179 Cal.App.3d 935, 945-46 (1986); *Izzi v. Mesquite Country Club,* 186 Cal.App.3d 1309, 1321-22 (1986).

The Seventh Circuit has ruled that it will only permit class action arbitrations where the parties have expressly provided for such actions in their arbitration agreement. *Champ v. Siegel Trading Co.*, 55 F.3d 269 (7th Cir. 1995).

3. Can An Employer Preclude Class Arbitrations?

In recent years, some employers have included provisions in their arbitration agreements that purport to bar class actions. These clauses are sometimes referred to as "class action shield" provisions. Courts are divided as to their enforceability.

For example, the Fourth Circuit rejected a challenge to a class action shield provision on unconscionability grounds in a Fair Labor Standards Act case. *Adkins v. Labor Ready, Inc.*,303 F.3d 496 (4th Cir. 2002). In *Adkins*, the court found no support in the FLSA for the view that class actions thereunder were unwaivable or would "defeat

the strong congressional preference for an arbitral forum." Id. at 503. Similarly, in *Snowden v. Checkpoint Check Cashing*, 290 F.3d 631 (4th Cir.), *cert. denied*, 537 U.S. 1087 (2002), the court rejected the argument that a bar against class arbitrations was unconscionable given the small amount of damages involved, where the applicable statute provided for recovery of attorneys' fees by the prevailing party.

In contrast, a number of federal and state courts in California have ruled that it is unconscionable for an employer to bar class actions in its arbitration agreements. The California Supreme Court began the discussion in *Keating v. Southland Corp.*, 31 Cal.3d 584 (1982), *reversed on other grounds*, 465 U.S. 1 (1984), where it recognized the power of a court to order class arbitration, but questioned whether arbitration of class claims might prejudice the legitimate interests of the parties. The court reasoned: "Arbitration proceedings may well provide certain offsetting advantages through savings of time and expense; but, depending upon the nature of the issues and the evidence to be presented, it is at least doubtful that such advantages could compensate for the unfairness inherent in forcing hundreds or perhaps thousands of individuals asserting claims involving common issues of act and law to litigate them in separate proceedings against a party with vastly superior resources." 31 Cal.3d at 609. The court went on to say that if "an arbitration clause may be used to insulate the drafter of an adhesive contract from any form of class proceeding, effectively foreclosing many individual claims, it may well be oppressive and may defeat the expectations of the nondrafting party." Id. at 610. The court remanded the case to the lower courts to address these issues.

In the years subsequent to the *Keating* decision, California courts have generally warmed to the notion of class arbitrations and have struck down arbitration agreements

that preclude class claims. See *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003) (bar against class claims in arbitration agreement unconscionable because it was not bilateral as AT&T is not likely to bring class actions against its own customers), *Szetela v. Discover Bank*, 97 Cal.App.4th 1094, 1101 (2002). See also *Luna v. Household Fin. Corp. III*, 236 F.Supp.2d 1166, 1178-79 (W.D.Wash.2002).

Practical Considerations

Employers are well-advised to consider the issue of class arbitrations carefully when drafting arbitration agreements and provisions. There is no excuse for making this issue an afterthought, given the serious implications of such an oversight. Unfortunately, whether to provide for class arbitrations is not an easy decision, and involves sorting out conflicting considerations.

Most employers view class actions as litigation landmines. The question then becomes, if such an action were to be filed, is it in the best interest of the company to have the action heard in court or by an arbitrator or arbitration panel? Many employers will presumably choose to have such cases heard in court where greater appeal rights permit the possibility of remedying an error of law made at the trial level. That analysis would argue for including a class action shield provision that prohibits class arbitrations in the employer's arbitration agreement. However, as demonstrated by the federal and state courts in California, the enforceability of class action shield provisions is in question. On the other hand, the prospect of a class claim's being adjudicated before an arbitrator rather than a court may discourage some prospective class members from filing such a claim in the first place.

A second concern in drafting an arbitration provision is the allocation of

responsibility for deciding whether a class action is covered by the arbitration agreement. A silent or ambiguous arbitration agreement would allow that question to become a preliminary legal skirmish that could waste precious time and financial resources. The drafters of the arbitration agreement at a minimum should expressly provide that all procedural questions are either for the court or the arbitrator to decide.

Finally, the drafter of a corporate arbitration agreement must be cognizant of applicable state law on the question of class arbitration. Also, consideration must be given to applicable state law on the questions of substantive and procedural unconscionability to minimize the risk of a later challenge.