

THE ENFORCEABILITY OF CLASS ACTION WAIVERS IN CONSUMER AGREEMENTS

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In recent years, class action waivers contained in arbitration provisions have become controversial. *Dale v. Comcast Corp.*, -- F.3d --, 2007 WL 2471222 (11th Cir. September 4, 2007). This dispute has become particularly intense in the wake of the Supreme Court's determination that whether a class action is allowed under an arbitration agreement is a decision for the arbitrator, thus injecting uncertainty as to procedure and outcome for defendants. *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003).

Plaintiffs will normally challenge the enforceability of the arbitration provision itself, as well as the class action waiver. While some courts have been receptive to such arguments, the majority agree that class action waivers are generally enforceable. Notably, while the majority of class action waiver decisions involve arbitration, class action waivers can exist independently of arbitration clauses and may even have stronger arguments for enforcement in such circumstances.

ENFORCEABILITY

Under the Federal Arbitration Act, consumer arbitration provisions (including class action waivers) are enforceable unless the arbitration provision is unconscionable and thus void as a matter of state law. Plaintiffs have also argued that such provisions inappropriately limit certain statutory claims, thus violating legislative intent.

1: Unconscionability.

Plaintiffs often claim that the arbitration provision is unconscionable because the relatively high cost of arbitration (or court proceedings), combined with the relatively low value of certain consumer claims, make the pursuit of a remedy under such contracts economically

infeasible. While the law varies from state to state, in most jurisdictions a contract must be both substantively and procedurally unconscionable to be unenforceable. *See Gillman v. Chase Manhattan Bank, N.A.*, 73 N.Y.2d 1 (N.Y. 1988). A provision may be substantively unconscionable when it is so grossly unfair that no reasonable person would accept it, and may be procedurally unconscionable when the weaker party has no bargaining power at all and no alternative but to enter the contract.

Plaintiffs often assert that preprinted, standard consumer contracts are contracts of adhesion and therefore procedurally unconscionable. Plaintiffs emphasize the economic disparity between the consumer customer and the seller, and the absence of meaningful bargaining. Nonetheless, such standard contracts often survive scrutiny.

First, most courts acknowledge that consumers usually do not have to contract with a company; they are free to go elsewhere or without. Furthermore, while the market does much of the bargaining, the consumer achieves a certain price in exchange for accepting the company's goods or services on certain conditions; this is *quid pro quo*. Therefore, many courts are reluctant to deem all standard contracts procedurally unconscionable.

Moreover, it is well settled that a contract of adhesion is not necessarily unconscionable.¹ Courts routinely enforce adhesion contracts, including arbitration agreements contained in adhesion contracts.² For an adhesion contract to be unenforceable, the party wishing to escape its enforcement must show that (1) terms of the contract are grossly favorable to a party that has (2) overwhelming bargaining power. Substantive unconscionability must shock the conscience. As the Alabama Supreme Court puts it, the contract must be "such as no man in his sense and not under delusion would make on the one hand, and no honest and fair man would accept on the other." *Sears Termite & Pest Control, Inc. v. Robinson*, 883 So.2d 153, 158 (Ala. 2003).

Class action waiver provisions in consumer transactions are generally not found unconscionable unless the provision grants *de facto* immunity from liability for the defendant by removing the plaintiff's only economically feasible means of recovery. If the contract provides one or more viable alternative means of enforcement or if a statute provides such a viable method (for instance, a provision enables a plaintiff to recover attorney fees), the waiver provision is generally found permissible.³

2: Can Waive Class Action for Statutory Violations

Plaintiffs may also argue that a class action waiver violates the statutory rights available under certain state and federal laws because it removes an intended, efficient procedural vehicle for vindicating those rights. The Supreme Court has written that when a party waives some procedural right related to a statutory claim, the party "should be held to [the bargain] unless Congress has evidenced an intention to preclude a waiver of judicial remedies for the statutory rights at issue." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991).

Therefore, for a plaintiff to successfully maintain that a class action waiver provision limits her statutory remedies, she would need to show that "Congress intended to preclude parties from contracting away their ability to seek class action relief" under the particular statute, or that such a waiver is "inherently inconsistent with [the act's] enforcement scheme." *Randolph v. Green Tree Fin. Corp.-Alabama*, 244 F.3d 814, 817-18 (11th Cir. 2001).

A plaintiff is usually unable to make such a showing because consumer protection acts are often silent as to the class action mechanism and additionally provide incentives to litigants and lawyers to pursue claims (such as fee-shifting and treble damages). Moreover, companies often agree to pay arbitration initiation costs in the contract. Most importantly, arbitrators (and judges) typically have the discretion to allocate costs as he sees fit in accordance with applicable law and can shift costs away from the consumer.

Consumer class action waivers in Alabama

One of the seminal consumer class arbitration waiver cases in Alabama is *Leonard v. Terminix International Co.*, where a plaintiff argued, among other things, that such a waiver made arbitration of its contractual claims “inaccessible.” 854 So. 2d 529, 534 (2002). A divided Alabama Supreme Court agreed that the particular provision at issue, under those particular facts, was not enforceable.

The Court distinguished its reasoning from the broader argument that mere economic hardship might render an arbitration clause unconscionable for certain consumers. The issue was not whether the Terminix contract was burdensome on the plaintiffs, but whether “economic feasibility precluded presentation of the claims” for any potential claimant. *Id.* at 537. Because the case involved an adhesion contract which limited the recovery of “indirect, special, and consequential damages,” required arbitration, and precluded class action treatment, it essentially “restrict[ed] the [plaintiffs] to a forum where the expense of pursuing their claim far exceed[ed] the amount in controversy.” *Id.* at 539. Further, the Terminix contract was silent as to who should pay arbitration costs. Thus, the Court found the class action waiver restriction unconscionable.

While *Leonard v. Terminix* opened the door for unconscionability in Alabama, its holding should be viewed through its particular facts, particularly with the 5-4 split on the Court. Further, the Court reaffirmed its holding that mere economic hardship did not constitute substantive unconscionability. The holding leaves room for other Alabama courts to enforce less restrictive class action waivers in line with other cases such as *Med. Ctr. Cars Inc. v. Smith*, 727 So. 2d 9 (Ala. 1998). For instance, in *Billips v. Bankfirst*, a consumer credit card holder argued that the arbitration clauses in her card member agreements were unenforceable. *Billips v. Bankfirst*, 294 F. Supp. 2d 1265 (M.D.Ala. 2003). The court held that the case was

distinguishable from *Leonard v. Terminix* because the defendant bank agreed to pay the fees associated with the plaintiff's initiating the arbitration, because the federal statute under which the plaintiff brought the suit awarded costs and attorney's fees, and because the contract did not limit the damages available to the plaintiff. *Billips*, 294 F. Supp. 2d at 1276. The court enforced the waiver, and its reasoning was reaffirmed in a very similar case *Battels v. Discover Bank*, in 2004. *See also Taylor v. Citibank USA, N.A.*, 292 F.Supp.2d 1333, 1345 (M.D.Ala. 2003) (distinguishing *Terminix*).

Consumer Class Action Waivers in the 11th Circuit

The Eleventh Circuit has upheld class action waivers challenged as unconscionable. The court acknowledged that a party can avoid arbitration on the basis of costs if she can demonstrate "that she faces such 'high costs' if compelled to arbitrate her claim . . . that she is effectually precluded from vindicating [her federal statutory] rights in the arbitral form." *Musnick v. King Motor Co.*, 325 F.3d 1255, 1260 (11th Cir. 2003).

Likewise in *Jenkins v. First American Cash Advance of Georgia, LLC*, 400 F.3d 868 (11th Cir. 2005), the Eleventh Circuit upheld a class action waiver, reversing the district court. The *Jenkins* court held that the provision was not unconscionable (the claim had been brought by two borrowers against payday lenders). The court noted that class action provisions to arbitration agreements are not *per se* invalid or unenforceable in a number of other federal circuits. *Id.* at 877. It also disagreed with the contention that the plaintiffs would not be able to find legal representation without the class action vehicle. *Id.* at 878.

However, recently the Eleventh Circuit invalidated an arbitration agreement that contained a class arbitration waiver. In *Dale v. Comcast Corp.*, -- F.3d --, 2007 WL 2471222 (11th Cir. September 4, 2007), the Eleventh Circuit stated that the enforceability of class arbitration waivers must be analyzed on a case-by-case basis, factoring in the fairness of the

provision, the cost of bringing a claim versus possible recovery, whether attorney fees and costs are recoverable, the effect of the waiver on the company's behavior, and other public policy considerations. *Id.* at *6. The Court distinguished its prior decisions enforcing agreements containing class arbitration waivers, noting that in each of the earlier cases, plaintiffs could recover attorney fees and costs if plaintiffs prevailed on the underlying claims. *Id.* at *4. In *Dale*, plaintiffs would have been foreclosed from recovering attorney fees if their low value claims were pursued in arbitration on an individual basis. *Id.* at *5. The Eleventh Circuit found that plaintiffs' inability to recover attorney fees effectively precluded the plaintiffs from suing the defendant on an individual basis and enabled the defendant to engage in the alleged conduct unchecked by the market. *Id.* at *5-7.

Dale raises several questions, including how to apply the case-by-case analysis, whether this is intended to be a new standard, and whether the *Dale* court is applying a different standard to arbitration clauses than to other provisions of the contract.⁴

Conclusions and Consumer Class Action Waivers Nationally

Most jurisdictions have upheld class action waivers in consumer transactions, in at least some circumstances, usually applying the standards set forth above. These include (among others) Colorado, Delaware, Illinois, New Jersey, New York, North Carolina, Kansas, Tennessee, Washington, and the Third, Fourth, Fifth, Sixth, Seventh, and Eleventh Federal Circuits.

Nevertheless, some jurisdictions, such as New Jersey and California, have found the waivers unconscionability under more broad circumstances. *E.g.*, *Shroyer v. New Cingular Wireless Services, Inc.*, 2007 WL 2332068 (9th Cir. August 17, 2007); *Oestreicher v. Alienware Corp.*, 2007 WL 2302490 (N.D.Cal. Aug. 10, 2007); *but see Delta Funding Corp. v. Harris*, 912 A.2d 104 (N.J. 2006) (waivers are not invalid per se). However, California was willing to apply

Delaware law under a choice-of-law analysis, even though that law possibly contradicted California's. *Discover Bank v. Superior Court*, 36 Cal. Rpt. 3d 456 (Cal. Ct. App. 2005). The court reasoned that the only defendant resided in Delaware, a Delaware statute mandated that its laws apply to disputes between Delaware banks and their cardholders, and the claims asserted against the bank were all under Delaware law. *Id.*

¹ See, e.g., *Roberson v. Money Tree*, 954 F.Supp. 1519 (M.D. Ala. 1997).

² See, e.g., *id.*; *Spurlock v. Life Ins. Co of Virginia*, 2000 WL 1785300 (M.D. Ala. 2000); *Goodwin v. Ford Motor Credit Co.*, 970 F. Supp. 1007 (M.D. Ala. 1997); *Kelly v. UHC Mgmt Co.*, 967 F. Supp. 1240 (N.D. Ala. 1997).

³ *Caley v. Gulfstream Aerospace Corp.*, 428 F.3d 1359 (11th Cir. 2005); *Jenkins v. First American Cash Advance of Georgia, LLC*, 400 F. 3d 868 (11th Cir. 2005); *Randolph v. Green Tree Fin. Corp.*, 244 F. 3d 814 (11th Cir. 2001); *Gipson v. Cross Country Bank*, 294 F. Supp. 2d 1251 (M.D. Ala. 2003)(arbitration clause was not rendered unenforceable by inclusion of provision barring class actions, and class action bar was not unconscionable under state law under those facts); *Taylor v. Citibank USA, N.A.*, 292 F. Supp. 2d 1333 (M.D. Ala. 2003)(same); *Billups v. Bankfirst*, 294 F. Supp. 2d 1265 (M.D. Ala. 2003)(same); *Pitchford v. AmSouth Bank*, 285 F. Supp. 2d 1286 (M.D. Ala. 2003)(arbitration provision in motor vehicle financing agreement was not unconscionable due to fact that it prohibited borrowers from bringing class action, where initial costs of arbitration were to be paid by lender, and borrowers would be entitled to attorney fees and costs under ECOA if they prevailed); *but see Dale v. Comcast Corp.*, -- F.3d --, 2007 WL 2471222 (11th Cir. September 4, 2007)(arbitration agreement precluding class action unconscionable); *Leonard v. Terminix International Co.*, 2002 WL 31341084 (Ala.2002)(arbitration agreement precluding class actions unconscionable).

⁴ E.g., *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 281 (1995) ("States may regulate contracts, including arbitration clauses, under general contract law principles"); *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 477 (1989) ("state law may nonetheless be pre-empted to the extent it actually conflicts with federal law – that is, to the extent that it 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'). Notably, when viewed outside of the context of arbitration, a party's waiver of a procedural advantage is generally treated with less scrutiny, with courts generally finding that parties can agree to waive class actions treatment and even jury trials.