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### As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?

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## AS MANDATORY BINDING ARBITRATION MEETS THE CLASS ACTION, WILL THE CLASS ACTION SURVIVE?

JEAN R. STERNLIGHT\*

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## INTRODUCTION

It is no secret that banks, insurance companies, and other potential corporate defendants do not like class actions.<sup>1</sup> Today, such potential defendants, in a broad array of industries, hope that they have found a surreptitious way to defeat the feared class action: mandatory binding arbitration.<sup>2</sup> These companies and their attorneys assert that they may use contracts of adhesion<sup>3</sup> to compel consumers, employees, and others to arbitrate rather than litigate their claims,<sup>4</sup> and to require that such arbitration must proceed on

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1. There are exceptions to this general rule. At times defendants are said to favor class actions so that they can enter into favorable settlements with collusive plaintiffs' attorneys. See Richard B. Schmitt, *The Deal Makers: Some Firms Embrace the Widely Dreaded Class Action Lawsuit*, WALL ST. J., July 18, 1996, at A1 (explaining that some corporations welcome class actions in order to avoid future lawsuits); see generally DEBORAH R. HENSLER ET AL., CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAIN: EXECUTIVE SUMMARY 15 (1999) (observing that in three of ten studied class actions, "from the moment of filing, defendants seemed about as eager as plaintiff attorneys to settle the litigation against them by means of a class action").

2. Several commentators have urged companies in various industries to adopt mandatory binding arbitration, at least in part to avoid class actions. See, e.g., Edward Wood Dunham, *The Arbitration Clause as Class Action Shield*, 16 FRANCHISE L.J. 141, 142 (1997) (urging franchisors to adopt binding arbitration); Alan S. Kaplinsky & Mark J. Levin, *Excuse Me, But Who's the Predator? Banks Can Use Arbitration Clauses as a Defense*, BUS. L. TODAY, May-June 1998, at 24, 24 [hereinafter Kaplinsky & Levin, *Excuse Me, But Who's the Predator?*] (discussing binding arbitration clauses in banking and consumer loans); Michael R. Pennington, *Every Health Insurer's Litigation Nightmare: A Case Study of How One Class Action Affected the Business of One Insurer*, THE BRIEF, Summer 1999, at 47, 52 (stating that Alabama insurance companies are imposing binding arbitration clauses in an "effort to limit litigation exposure in general, and exposure to class actions in particular"); J.T. Westermeir, *How Arbitration Clauses Can Help Avoid Class Action Damages*, 14 COMPUTER L. STRATEGIST, Sept. 1997, at 1 (discussing use of arbitration clauses by computer manufacturers and internet service providers); John M. Flynt, Comment, *A Solution to Force-Placed Insurance Litigation For Lenders: Disclosure and Arbitration*, 26 CUMB. L. REV. 537, 573 (1996) (proposing solutions to force-placed insurance). For examples of correspondence showing that at least one arbitral organization has relied on the absence of class actions in marketing its services to potential clients, see *infra* note 278.

3. By "contracts of adhesion" I simply mean contracts that are prepared in advance by the drafter and imposed on a take-it-or-leave-it basis. Such contracts may be part of forms, or may appear on the backs of tickets or boxes. Although some have attacked them as unfair, and have argued that they should be presumptively unenforceable, see, e.g., Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173, 1176-80 (1983), most courts have held that the mere fact that a contract is adhesive does not mean that it is void unless it is also unconscionable or unjust. See generally LAWRENCE A. CUNNINGHAM & ARTHUR J. JACOBSON, 3 CORBIN ON CONTRACTS § 559C (Supp. 1999) (discussing various court determinations of what constitutes a contract of adhesion).

4. Courts are often quite willing to enforce arbitration clauses that are imposed as a

an individual rather than class basis. Increasingly, potential defendants are drafting arbitration clauses that explicitly bar class actions, hoping that these will facilitate favorable court rulings.<sup>5</sup>

Thus far, it is not clear whether such strategies will work, at least in the long term. This Article argues that it would be wrong to allow companies to use arbitration clauses to insulate themselves entirely from class action liability, and that courts and legislators should take steps to protect access to class actions.

The companies and attorneys who seek to use arbitration to eliminate class actions contend that plaintiffs, and especially their attorneys, exploit the class action remedy as a way to extort unfair settlements from innocent defendants.<sup>6</sup> In an article aptly entitled *Excuse Me, But Who's the Predator?*, attorneys Alan S. Kaplinsky and Mark J. Levin state:

All of the dangers inherent in an individual consumer lawsuit—the threats of costly and drawn-out litigation,

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contract of adhesion. See *infra* notes 199-210 and accompanying text; see also Jean R. Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Concerns*, 72 TUL. L. REV. 1, 33 (1997) [hereinafter Sternlight, *Rethinking*] (stating that many courts have held "that the mere adhesive nature of a contract does not render it invalid").

5. See, e.g., Christopher R. Drahozal, "Unfair" Arbitration Clauses, 2001 U. ILL. L. REV. (forthcoming 2001) (manuscript at 41, on file with author) (concluding that 16 of 34 arbitration clauses examined in a survey of clauses imposed by franchisors on franchisees proscribed class actions in arbitral proceedings). In *Zawikowski v. Beneficial Nat'l Bank*, No. 98-C-2178, 1999 WL 35304, at \*1 (N.D. Ill. Jan. 11, 1999), the court noted that the company's clause expressly prohibited the filing of a class action without the parties' consent, but did not provide the wording of the clause in its decision. See *id.* at \*2. A clause provided by MBNA states, in part, "No Claim submitted to arbitration is heard by a jury and no Claim may be brought as a class action or as a private attorney general. You will not have the right to act as a class representative or participate as a member of a class of claimants with respect to any Claim." An American Express clause states, in part, "There shall be no right or authority for any Claims to be arbitrated on a class action basis or on bases involving Claims brought in a purported representative capacity on behalf of the general public, other Cardmembers or other persons similarly situated; provided however, that the claimant's individual Claim would be subject to this Arbitration Provision." A clause prepared by J.C. Penney & Monogram Credit Card Bank of Georgia states, *inter alia*, "you will not have the right to participate as a representative or member of any class of claimants pertaining to any Claim subject to arbitration." A clause prepared by H&R Block states "No class actions are permitted without the consent of the parties." (all clauses on file with author).

6. See *infra* notes 123-33 and accompanying text. This Article focuses on plaintiff rather than defendant class actions, as these are by far the more prevalent, both generally and specifically, in the arbitration context.

runaway juries, gargantuan punitive damages awards and adverse publicity—are magnified exponentially when a class of hundreds or thousands of consumers is certified. Faced with these threats, companies often feel pressured to pay substantial amounts in settlement for reasons having nothing to do with the actual merits of the dispute.<sup>7</sup>

This opposition to class actions is common to defendants in many kinds of suits, but particularly includes defendants in mass tort claims, securities fraud claims, and consumer claims.<sup>8</sup> While class action opponents have tried numerous legislative and other strategies to limit or eliminate class actions in various arenas,<sup>9</sup> these measures have still left some defendants feeling vulnerable to the class claim. As attorneys Kaplinsky and Levin put it: “Consumers have been ganging up on banks. But now [referring to binding arbitration] the institutions have found a way to defend themselves.”<sup>10</sup>

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7. Kaplinsky & Levin, *Excuse Me, But Who's the Predator?*, *supra* note 2, at 24. For a general summary of some of the policy controversies surrounding class actions, see HENSLER ET AL., *supra* note 1. See generally Chris Guthrie, *Framing Frivolous Litigation: A Psychological Theory*, 67 U. CHI. L. REV. 163 (2000) (discussing psychological reasons why defendants are likely to be far more interested in settling high-risk litigation than are plaintiffs, and arguing that this disparity gives plaintiffs an advantage in the negotiation process).

8. For example, Lew Goldfarb, Associate General Counsel to Daimler Chrysler Corp., has stated that

Class action lawsuits should be used to resolve legitimate claims and not serve as a rigged lottery for trial lawyers. . . . For too long, trial lawyers have been exploiting class actions, turning these lawsuits into a form of legalized blackmail. They launch frivolous cases because they believe that just the threat of massive class actions filed in many states can coerce a company into settlement.

*Automaker Sues Attorneys for Filing “Frivolous” Class Actions*, Andrews’ Prof. Liab. Litig. Rep., Jan. 2000, available in WL, File 9 No. 5 ANPLLR3; see also *Mass Tort Litigation Fever Running High: Practitioners Say There Is No Apparent Cure to This Societal Problem*, ILL. LEGAL TIMES, Jan. 1996, available in LEXIS, News Library, Illinois Legal Times File (discussing the snowballing of mass tort class actions since the asbestos cases); Pennington, *supra* note 2, at 52 (arguing that fraud class action brought against medical insurer Liberty National had a severe and unfair detrimental impact on that company). For other articles discussing allegedly exploitative lawsuits, see *infra* note 129.

9. See *infra* notes 131-33 and accompanying text for a brief discussion of proposed reforms to Federal Rule of Civil Procedure 23 itself, and a discussion of securities and “tort reform” legislation geared to limit plaintiffs’ use of class actions.

10. Kaplinsky & Levin, *Excuse Me, But Who's the Predator?*, *supra* note 2, at 24. In this article Kaplinsky and Levin urge “[l]enders that have not yet implemented arbitration programs” to “promptly consider doing so, since each day that passes brings with it the risk

When corporate defendants, their attorneys, arbitral organizations, and other commentators sing the praises of arbitration to the public at large, they generally do not highlight the impact of arbitration on class actions. Instead, they make claims to the effect that arbitration is quicker, cheaper, and better for all concerned, and that consumers and employees will benefit just as much as will the companies that are imposing the arbitration clauses.<sup>11</sup> In

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of additional multimillion-dollar class action lawsuits that might have been avoided had arbitration procedures been in place." *Id.* at 28; see also Dunham, *supra* note 2, at 142 ("An arbitration clause may not be an invincible shield against class action litigation, but it is surely one of the strongest pieces of armor available to the franchisor."); Alan S. Kaplinsky & Mark J. Levin, *Anatomy of an Arbitration Clause: Drafting and Implementation Issues Which Should Be Considered by a Consumer Lender*, 1102 PRACTISING L. INST. 513, 532 (1999) (stating that lenders "who in recent years have been assaulted by a barrage of consumer class action lawsuits" should be interested in the fact that arbitrations are not permitted to proceed on a class action basis); Alan S. Kaplinsky, *Arbitration and Class Actions—A Contradiction in Terms*, 1113 PRACTISING L. INST. 619 (1999) [hereinafter Kaplinsky, *Arbitration and Class Actions*] (arguing that disputes which are arbitrable may not proceed by way of class action, either in court or in arbitration, unless the arbitration agreement expressly allows for arbitration); Alan S. Kaplinsky & Mark J. Levin, *Drafting and Implementing of a Consumer Loan Arbitration Clause*, 51 CONSUMER FIN. L.Q. REP. 295, 295 (1997) (stating that although lenders have recently been targeted by numerous class action suits which they are frequently pressured to settle in order to avoid the threat of costly and expensive litigation "having nothing to do with the actual merits of the dispute," arbitration can be a "powerful deterrent to frivolous lawsuits" in part because class actions "usually are not permitted"); Westermeyer, *supra* note 2, at 3 (suggesting that computer manufacturers and internet service providers use contracts of adhesion—for example, in enclosures, shrink-wrap, or Web-wrap—to impose arbitration agreements on their customers in order to avoid class actions); Flynt, *supra* note 2, at 573 (urging that lenders who employ "force-placed insurance," whereby buyers are compelled to purchase expensive insurance to collateralize loans, require arbitration as a means of limiting class action challenges to such programs); Caroline E. Mayer, *Hidden in Fine Print: "You Can't Sue Us": Arbitration Clauses Block Consumers from Taking Companies to Court*, WASH. POST, May 22, 1999, at A1 [hereinafter Mayer, *Hidden in Fine Print*] (quoting an official at the arbitral organization National Arbitration Forum as stating in a letter to a corporate attorney, "[t]he only thing which will prevent 'Year 2000' class actions is an arbitration clause in every contract, note and security agreement").

11. See, e.g., Mayer, *Hidden in Fine Print*, *supra* note 10, at A1 (quoting American Express spokeswoman Emily Porter as defending company's move to require customers to arbitrate rather than litigate disputes against the company, stating that their purpose was "to find an efficient and convenient way to resolve disputes more quickly than the court system, which can be burdensome in time and money both for [the] company and [its] customers"); Caroline E. Mayer, *Win Some, Lose Rarely? Arbitration Forum's Ruling Called One-Sided*, WASH. POST, Mar. 1, 2000, at E1 [hereinafter Mayer, *Win Some, Lose Rarely?*] ("Businesses such as First USA say that for everyone involved, arbitration is faster, more efficient and cheaper than litigation."); Richard C. Reuben, *Banking on ADR*, CAL. LAWYER, Sept. 1992, at 17, 18 [hereinafter Reuben, *Banking on ADR*] (discussing two California banks' adoption of mandatory arbitration programs with respect to customer claims and observing that the banks have defended the programs as less expensive and time consuming than

private, however, and in their own industry publications, defense counsel and other arbitration advocates readily observe that arbitration can be used to deter the filing of a class action suit, or secure dismissal of a class action that was nonetheless brought.<sup>12</sup> The potential defendants know that because many claims are not viable if brought individually, plaintiffs will often drop or fail to initiate claims once it is clear that class relief is unavailable.<sup>13</sup> The potential defendants also believe that, should plaintiffs choose to pursue individual claims in arbitration, defendants' exposure still will be much lower than it would have been in class action litigation.<sup>14</sup>

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litigation). Reuben quotes a bank official as stating that customers "will have their grievances addressed without having to pay the high court costs and attorneys fees." *Id.* He also quotes the general counsel of a major arbitration organization as stating: "We find that ADR is well-liked by both sides of most disputes, because it is quicker and less expensive than litigation." *Id.* (quoting James J. Welsh, general counsel of JAMS).

12. See, e.g., Kaplinsky, *Arbitration and Class Actions*, *supra* note 10 (summarizing laws that support the use of arbitration to eliminate class actions); Hal Davis, *Banks Follow Brokerages: Arbitrate Yes, Litigate No: Plaintiffs' Attorneys Say Forcing Consumers to Arbitrate Disputes Will Eliminate Class Actions and Is Unfair*, NAT'L L.J., Sept. 12, 1994, at B1 (quoting plaintiff's attorney and consumer advocate Patricia Sturdevant as stating that the "real intent [behind Bank of America's adoption of mandatory binding arbitration of customer claims] was to eliminate class action challenges"); Kaplinsky & Levin, *Excuse Me, But Who's the Predator?*, *supra* note 2, at 24 ("[L]enders have discovered that the potential for class action litigation is significantly reduced if the consumers have agreed to arbitrate their disputes with the lenders."); Reuben, *Banking on ADR*, *supra* note 11, at 18 (noting that many critics of California banks' adoption of mandatory binding arbitration suggested that the plans "are driven by an interest in short-circuiting high-stakes class action litigation and hefty punitive-damage awards," and further observing that banks adopting such programs "have recently been stung by multi-million-dollar court losses involving deposit fees and credit card fees"). For a general discussion of the corporate strategy underlying the decision by some banks and companies to impose mandatory binding arbitration, see RALPH NADER & WESLEY J. SMITH, *NO CONTEST: CORPORATE LAWYERS AND THE PERVERSION OF JUSTICE IN AMERICA* 300-08 (1996) (discussing Bank of America's collateral involvement in another arbitration case in order to protect its stake in *Badie v. Bank of America*, No. 944916 (Cal. Super. Ct. Aug. 18, 1994), *aff'd*, 67 Cal. App. 4th 779 (Cal. Ct. App. 1998)).

13. Specifically, the named plaintiffs may drop their claims, and the non-named plaintiffs may never file claims. See Dunham, *supra* note 2, at 142; see also Kaplinsky & Levin, *Excuse Me, But Who's the Predator?*, *supra* note 2, at 26 ("Stripped of the threat of a class action, plaintiffs' lawyers have much less incentive to sue."). Statistics produced by credit card company First USA show that since it implemented its mandatory arbitration clause in early 1998, only four consumers have filed arbitration claims against the company. See Mayer, *Win Some, Lose Rarely?*, *supra* note 11, at E1. In contrast, First USA itself filed 51,622 arbitration claims against consumers in the same period. See *id.* Consumers' lawyers report that the disparity is due to economics, in that consumer claims typically are not viable except on a class basis. See *id.*

14. As one banker put it, "One outrageous \$40 million verdict can sour your whole year."

Attorney Edward Wood Dunham bluntly describes this strategy in his article, *The Arbitration Clause as Class Action Shield*.<sup>15</sup> He states:

The nine-figure jury verdict in the *Meineke Discount Muffler* class action is a bracing reminder that franchising is full of potentially catastrophic litigation risks. The verdict will almost certainly spawn a new generation of class action suits against franchisors, with particular emphasis on alleged mismanagement of franchisee advertising payments. Franchisors with an arbitration clause in their franchise agreements have an effective tool for managing these new class action risks.<sup>16</sup>

He frankly goes on to explain:

Absent unusual circumstances . . . the franchisor with an arbitration clause should be able to require each franchisee in the potential class to pursue individual claims in a separate arbitration. Since many (and perhaps most) of the putative class members may never do that, and because arbitrators typically do not issue runaway awards, strict enforcement of an arbitration clause should enable the franchisor to dramatically reduce its aggregate exposure.<sup>17</sup>

If successful, the strategy urged by Dunham and others would permit any company that has an ongoing relationship with a potential plaintiff—such as an insurer, manufacturer, cruise ship or HMO—to use a contract of adhesion to require that person, typically unknowingly,<sup>18</sup> to arbitrate rather than litigate, and to

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Davis, *supra* note 12, at B1 (quoting Bank of America Assistant General Counsel Arne Wagner).

15. See Dunham, *supra* note 2. Mr. Dunham is one of the attorneys who has represented Doctor's Associates, the franchisor for Subway Sandwich shops, in a series of important arbitration cases. See, e.g., *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 688 (1996) (holding that the FAA preempted a Montana statute's notice requirement with respect to arbitration clauses); *Doctor's Assocs., Inc. v. Distajo*, 107 F.3d 126, 139 (2d Cir. 1997) (upholding injunctions against state courts to support arbitration); *Doctor's Assocs., Inc. v. Stuart*, 85 F.3d 975, 985 (2d Cir. 1996) (upholding district court decision ordering arbitration and granting preliminary injunction against state court); *Doctor's Assocs., Inc. v. Hollingsworth*, 949 F. Supp. 77, 86 (D. Conn. 1996) (granting motion to compel arbitration and issuing injunction to prevent state court litigation).

16. Dunham, *supra* note 2, at 141 (footnotes omitted).

17. *Id.*

18. Consumers and employees who become parties to arbitration agreements typically

explicitly bar that person from proceeding by way of class action.<sup>19</sup> One might call this the “do it yourself” approach to law reform: the company need not convince any legislature to pass revised laws, nor persuade any judicial body to change court rules, but rather merely choose to eliminate the pesky class action on its own. If companies attempted to take direct and obvious legislative or even contractual steps to eliminate class actions, they would likely encounter substantial resistance, even in this era of “tort reform,” from those who credit class actions for many important achievements. By contrast, using arbitration to eliminate class actions is advantageous for class action opponents in part because it is surreptitious.

In the most extreme version of this defense, some companies seek to use arbitration to defeat class actions by issuing a mandatory arbitration provision *after* the filing of the class action.<sup>20</sup> Subsequent to the filing of the lawsuit that was designated as a class action, but prior to the court’s certification of the class,<sup>21</sup> defendants in several cases have sought to impose binding arbitration on the putative class members and then challenged the

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have no idea that they are waiving their right to proceed by way of class action. *See* Joan Lowy, *Consumers Are Losing the Right To Sue Without Knowing It*, Scripps Howard News Service, May 2, 2000, available in LEXIS, News Group File.

19. Potential defendants who lack an ongoing relationship with the potential plaintiff, such as those who may be sued in many personal injury suits, would not find it as easy to use a binding arbitration agreement to evade a class action. For example, the Union Carbide company could not feasibly have required all the residents of Bhopal, India to sign an arbitration clause so that when the plant released poison gases the plaintiffs would lose their right to pursue class relief. *See generally In re Union Carbide Corp. Gas Plant Disaster at Bhopal, India*, 634 F. Supp. 842 (S.D.N.Y. 1986), *aff’d*, 809 F.2d 195, 206 (2d Cir. 1987) (describing facts of alleged toxic gas leak and granting dismissal of lawsuit based on forum non conveniens).

20. They resort to this approach because, despite some defense attorneys’ efforts to urge all potential defendants to impose binding arbitration on their customers or employees prior to the filing of a class action, some companies are not so farsighted. Full analysis of the legitimacy of this post-filing attempt to impose arbitration exceeds the scope of this Article, but it will briefly discuss the few decisions which have been issued in this area, all of which have foreclosed the company from imposing binding arbitration after the fact. *See infra* notes 289-308 and accompanying text.

21. Until suits which have been filed as class actions actually have been certified to proceed as a class, they are only “putative” class actions. This author is aware of just one case in which, subsequent to certification of a suit as a class action, the defendant sought to derail the suit by imposing binding arbitration on the class members. *See H&R Block, Inc. v. Haese*, No. 13-97-673-CV, 2000 WL 924805, at \*3-4 (Tex. App. June 29, 2000) (affirming in relevant part trial court’s order precluding defendant from imposing mandatory arbitration, subsequent to certification of class action).



legitimacy of the class suit on that basis.<sup>22</sup> Still, courts have not yet condoned this practice.<sup>23</sup>

As one might expect, consumer and employee advocates have vigorously opposed companies' attempts to use arbitration to foreclose class actions, either before or after the filing of the putative class action, arguing that class actions are imperative to protect essential rights, and that companies should not be permitted to use adhesion contracts to eviscerate this important procedural mechanism. They observe that class actions historically have proved critical to the protection of rights of employees, consumers, medical patients, racial or ethnic minorities, and others who lack the resources to litigate individual claims.<sup>24</sup> They urge that using arbitration to eliminate class actions will relegate

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22. See *infra* notes 289-308 and accompanying text. The practice has been publicly endorsed by at least one defense attorney. See Kaplinsky, *Arbitration and Class Actions*, *supra* note 10, at 639-40:

[T]here would seem to be no impediment restricting a credit card issuer from implementing an arbitration program by sending change-in-terms notices to members of the putative class. There would also seem to be no reason why an issuer would need to disclose in its notice any pending putative class action lawsuits. Finally, there would also seem to be no impediment restricting a lender from including in a new closed-end loan an arbitration clause which covers disputes which are the subject of a pending class action lawsuit which has not been certified.

If few people opt-out of the change, the class action then may not be certifiable based on its failure to satisfy the numerosity requirement. At a minimum, the size of the class will be reduced.

*Id.* A bit later in the article, however, the author proposes a somewhat more conservative approach, stating that in light of the fact that several courts have upheld challenges to attempts to impose arbitration on putative class members, "a lender may want to carve-out of its arbitration clause any claims asserted in any pending lawsuits, including class actions which have not yet been certified." *Id.* at 642.

23. See *infra* notes 289-308 and accompanying text.

24. See, e.g., *Brown v. Board of Educ.*, 347 U.S. 483 (1954) (holding, in class action, that school segregation violates the Equal Protection Clause); *Youngberg v. Bank of Am.*, 119 F.3d 6 (9th Cir. 1997) (discussing class action brought against bank for overcharging \$24 million in transactional fees); *Ridgeway v. Flagstar Corp.*, Nos. C 93-20202 JW, C 93-20208 JW, 1994 WL 525553, at \*1 (N.D. Cal. Sept. 22, 1994) (approving \$27 million consent decree in class action brought against Denny's for failing to serve African American customers); *Martarella v. Kelley*, 349 F. Supp. 575 (S.D.N.Y. 1972) (holding, in class action, that detention facility for persons in need of supervision violated the Eighth Amendment because the facility failed to provide adequate rehabilitative programs); *Avery v. State Farm Mut. Auto. Ins. Co.*, No. 97-L-114, 1999 WL 955543, at \*1 (Ill. Cir. Ct. Oct. 8, 1999) (approving jury verdict of over \$456 million in class action brought by State Farm customers who had been given nonfactory authorized replacement parts). For discussion of the arguments made in defense of class actions in further detail, see *infra* notes 90-108 and accompanying text.

consumers and others to a forum in which they cannot achieve a just result, and may potentially prevent such claimants from pursuing valid claims.<sup>25</sup> Specifically, these plaintiffs' advocates urge that many cases may not be resolved economically on an individual basis, even though the defendant has allegedly engaged in illegal conduct causing substantial economic harm to a group of persons.<sup>26</sup> Thus, they assert that class actions must, at a minimum, be permitted in arbitration, if not in litigation.<sup>27</sup>

To support the point that some claims are viable only if brought as class actions, defenders of class actions might cite numerous cases that have already arisen in the arbitration context.<sup>28</sup> For

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25. See, e.g., Davis, *supra* note 12, at B1 (citing comments of Patricia Sturdevant, who represented Californian Trial Lawyers Association and Consumer Action in a lawsuit challenging the validity of arbitration for bank customers).

26. See, e.g., *Med Ctr. Cars, Inc. v. Smith*, 727 So. 2d 9 (Ala. 1998). The plaintiffs in this case argued that individual damages were too small for individuals to justify paying a \$500 arbitration fee. See *id.* at 19-20. The defendant was accused of fraudulently selling extended service contracts on automobiles. See *id.* at 11.

27. See *infra* notes 135-95 and accompanying text (discussing virtues and failings of classwide arbitration); *infra* notes 357-72 and accompanying text (suggesting that companies should not be able to foreclose entirely the use of class actions in all cases).

28. It is easy to find other examples in addition to those discussed in the text. In *Randolph v. Green Tree Fin. Corp.*, 991 F. Supp. 1410 (M.D. Ala. 1997), the plaintiff class challenged consumer finance practices which cost each class member approximately \$15 per year. See *id.* at 1415. Although the district court ordered arbitration and denied the plaintiffs' right to proceed by way of class action either in litigation or in arbitration, see *id.* at 1425, the Eleventh Circuit refused to enforce the arbitration clause on the ground that the clause's allocation of costs violated the Truth in Lending Act. See *Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149, 1157-59 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235). Similarly, in *Vernon v. Drexel Burnham & Co.*, 125 Cal. Rptr. 147 (Ct. App. 1975), two plaintiffs attempted to bring a class action for fraud and deceit against brokerage firm Drexel Burnham on behalf of approximately 100,000 people who had purchased securities on margin during a certain time period. See *id.* at 148-49. The court ordered that the class action be resolved through arbitration, and failed to address the question of whether arbitration could or should be resolved as a class action. See *id.* at 152-53. The two named plaintiffs alleged that Drexel had improperly calculated interest charges, that they personally had been damaged in the amount of \$266.82, and that the class as a whole had been overcharged in excess of \$1,000,000. See *id.* at 149. This certainly appears to be a case that would not and could not have been brought, except as a class action. Even though the two named plaintiffs were attorneys, see *id.* at 148, they likely would not have thought it worth their while to pursue their own claims through arbitration to obtain a mere \$133 apiece. Imagining the lowest possible filing fees and arbitrator salaries, and the most seemingly simple facts and law, only an independently wealthy attorney with lots of free time could afford to take on such a claim. Understanding the magnitude of such fees, certainly each of us has chosen not to file larger claims. See generally Richard E. Miller & Austin Sarat, *Grievances, Claims, and Disputes: Assessing the Adversary Culture*, 15 L. & SOC'Y REV. 525, 534-60 (1980-81) (presenting empirical evidence showing that persons choose to litigate only a very small

example, in *Lopez v. Plaza Finance Co.*,<sup>29</sup> the plaintiff filed a class action alleging violations of the Truth in Lending Act ("TILA"), the Illinois Consumer Installment Loan Act, and the Illinois Consumer Fraud Act.<sup>30</sup> Jeremias Lopez claimed that when he took out an installment loan for \$300 to purchase a television, he was also forced to purchase nonfiling insurance for seven dollars, which was not included in the finance charge.<sup>31</sup> The *Lopez* opinion does not reflect whether the plaintiff sought return of the entire seven dollars, or only a portion thereof. Either way, certainly few rational plaintiffs or attorneys would seek individual relief on such a small claim, whether through arbitration or litigation, even given the possibility of recovering an additional \$200 for statutory damages, or costs and attorney fees.<sup>32</sup> While recognizing that the plaintiff would be unable to bring the claim without the class action, and that this would mean plaintiffs' rights under TILA would go unenforced,<sup>33</sup> the federal district court nonetheless found this ground insufficient to prevent it from ordering the dispute to individual arbitration.<sup>34</sup> Similarly, in *Med Center Cars, Inc. v.*

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percentage of what they perceive to be legitimate grievances). Even if the two attorneys in *Vernon* had filed their own claims, at most they would have secured individual rather than class relief. The company could have continued to pursue its arguably illegal course of action, and benefited substantially. The public interest in compensating victims, deterring wrongful conduct, and securing enforcement of the laws would be ill served.

29. No. 95-C-7567, 1996 WL 210073, at \*1 (N.D. Ill. Apr. 25, 1996).

30. *See id.*

31. *See id.*

32. Litigants who would choose to file such actions would have to be very wealthy and also quite driven by principle. For example, once credit card company First USA imposed binding arbitration, just four consumers chose to bring arbitration claims. *See Mayer, Win Some, Lose Rarely?*, *supra* note 11, at E1.

33. *See Lopez*, 1996 WL210073, at \*3.

34. *See id.* Even if one or two independently wealthy or fanatically committed persons chose to bring such actions, despite the economic costs, TILA would be severely under-enforced. A company will not be deterred from acting illegally when it knows that, at worst, a handful of customers may bring an arbitration action seeking a refund of improper fees. However, the *Lopez* court did refuse to enforce the arbitration clause on other grounds, specifically that it was unconscionable because it was nonmutual in that it preserved the company's right to litigate claims arising out of the debtor's alleged default. *See id.* at \*3-6. *Cf. Johnson v. Tele-Cash, Inc.*, 82 F. Supp. 2d 264, 266 (D. Del. 1999) (refusing to compel arbitration of claim brought under TILA on ground that doing so would violate the statute).

**EDITOR'S NOTE:** As this Article was going to press, the United States Court of Appeals for the Third Circuit reversed *Johnson v. Tele-cash, Inc.* in *Johnson v. West Suburban Bank*, No. 00-5047 (3d Cir. Aug. 29, 2000). The Third Circuit held that neither the TILA nor the EFTA are inherently inconsistent with a contract that eliminates plaintiffs' right to proceed in a class action. The court reasoned that plaintiffs' rights under the statutes were

*Smith*,<sup>35</sup> named plaintiff Gregory Tapscott alleged that defendant car dealers and insurance companies “had violated the Alabama Mini-Code and had committed common law fraud by financing the sale of automobile ‘extended service contracts’ as part of the purchase of their automobiles, without including the cost of the contracts in the ‘finance charge’ section of the sales documents.”<sup>36</sup> Plaintiffs sought classwide arbitration, observing that “actual damages recoverable by each individual are too small to justify the cost of commencing an arbitration proceeding.”<sup>37</sup> Plaintiffs hoped that if class arbitration were permitted, only the named plaintiffs, and not each class member, would be required to pay the minimum \$500 arbitral filing fee.<sup>38</sup> Nonetheless, while recognizing that plaintiffs’ contentions were “practically appealing,”<sup>39</sup> the Alabama Supreme Court reversed the lower court and ordered plaintiffs to proceed to arbitration on an individual basis.<sup>40</sup>

It is rather amazing that, despite its clear importance, the phenomenon of using arbitration to avoid class actions has received scant public attention. It has not been focused upon in Congress, in the popular press, or even among arbitration scholars.<sup>41</sup> For

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sufficiently protected by the right to proceed individually in arbitration, and by the administrative enforcement mechanisms available under those Acts. The court also observed, in dicta, that it “appears impossible” for class actions to be pursued in arbitration, but made no ruling on this issue. However, the court did state that a different result might have been reached if plaintiff had shown that the arbitral forum selected was inadequate to vindicate his statutory rights, and the court also found that arbitration clauses can be struck down as unconscionable. It is also important to note that the Third Circuit recognized that Congress has the power to prohibit use of arbitration agreements to eliminate class actions, even if it did not do so under TILA or EFTA. This decision will no doubt focus further attention on the issues raised in this Article.

35. 727 So. 2d 9 (Ala. 1998).

36. *Id.* at 11.

37. *Id.* at 19-20. While the court does not specify the amount of each plaintiff’s alleged injury, certainly it must have been quite small in dollar terms in that it represented only a portion of the finance charge on what would have been a several hundred dollar transaction.

38. *See id.* at 20.

39. *Id.*

40. The court held:

While we can understand and applaud the efforts of the trial court to seek a method that would allow those parties claiming small amounts of individual damages to obtain a remedy, we are persuaded by the federal authority on this issue and hold that class-wide arbitration should not be permitted in this case.

*Id.*

41. The few law review articles directly addressing this phenomenon are no longer entirely current. *See Note, Classwide Arbitration: Efficient Adjudication or Procedural Quagmire?*, 67 VA. L. REV. 787, 814 (1981) [hereinafter *Quagmire*] (suggesting that class

example, the relationship between class actions and binding arbitration has not been addressed in the Federal Arbitration Act ("FAA")<sup>42</sup> or in the Uniform Arbitration Act ("UAA").<sup>43</sup> Similarly, no state arbitration statute contains specific provisions dealing with the treatment of class actions.<sup>44</sup> Significantly, however, the Revised Uniform Arbitration Act, recently adopted by the National Conference of Commissioners on Uniform State Laws ("NCCUSL"),<sup>45</sup> indicates in its draft Reporter's notes that where arbitration provisions use the elimination of class actions to undermine consumer rights, it may be appropriate for courts to deny enforcement of the clause.<sup>46</sup>

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arbitration is feasible, and that allowing such claims is the best means of protecting all relevant policy interests); Daniel R. Waltcher, Note, *Classwide Arbitration & 10b-5 Claims in the Wake of Shearson/American Express, Inc. v. McMahon*, 74 CORNELL L. REV. 380, 403-05 (1989) (arguing that securities class actions should be allowed to proceed by way of arbitral class action, and advocating a model whereby the court would certify the class and then allow the arbitrator to manage the class action). For a brief but current analysis, see Georgene M. Vairo, *Classwide Arbitration: The Possibility of a Hybrid Procedure*, ADR CURRENTS, June 1999, at 19, 19-22 (concluding that contractual clause which either allows or disallows arbitral class action should be honored, summarizing conflicting cases regarding proper interpretation of silent clauses, and suggesting that those seeking to avoid class actions should draft a clause in order to accomplish that goal).

42. Ch. 213, 43 Stat. 883 (1925) (codified as amended at 9 U.S.C. §§ 1-208 (1994)).

43. 7 U.L.A. 1 (1997).

44. I base this statement on an analysis of all 50 states' arbitration statutes. See, e.g., CAL. CIV. PROC. CODE §§ 1280-1290 (West 1982 & Supp. 2000); FLA. STAT. ANN. §§ 682.01-682.22 (West 1990 & Supp. 2000); 710 ILL. COMP. STAT. ANN. 5/1-23 (West 1999 & Supp. 2000); N.Y.C.P.L.R. §§ 7501-7514 (Consol. 1988 & Supp. 1999); TEX. CIV. PRAC. & REM. CODE ANN. §§ 171.001-171.023 (West 1997 & Supp. 2000).

45. The Act was adopted at the NCCUSL Annual Conference, July 28-Aug. 4, 2000. See National Conference of Comm'rs on Unif. State Laws, *Uniform Arbitration Act (2000)* (visited Aug. 4, 2000), <<http://www.law.upenn.edu/blj/ulc/uarba/arb00ps.pdf>>.

46. The draft Reporter's notes to section 10, governing Consolidation, contains the following:

[C]ourts might closely scrutinize anti-consolidation provisions in adhesion contracts. There is evidence that a growing number of arbitration provisions in standardized consumer services agreements purport to prohibit class actions or consolidation. See Christopher R. Drahozal, *Unfair Arbitration Clauses* 2001 U. Ill. L. Rev. (manuscript at 41). In some cases, such provisions may effectively undermine consumers' rights by making the relative cost of arbitrating or of securing effective legal representation cost-prohibitive. In such cases, it may be appropriate for a court to refuse to enforce the term prohibiting class actions or consolidation under Section 4(a) and 6(a) of this Act. See, e.g., *Johnson v. Tele-Cash, Inc.*, 82 F.Supp2d 264 (D.De. 1999) (sic) (court refuses to require arbitration of claims because it would deprive plaintiffs of right to use class actions in contravention of congressional intent under Truth in Lending Act and Electronic Funds Transfer Act); *Ramirez v. Circuit City Stores*, 90 Cal.Rptr.2d

Moreover, few cases deal with the questions that arise when class actions must be reconciled with binding arbitration, although it is possible that the Supreme Court will address the issue this term in *Green Tree Financial Corp. v. Randolph*.<sup>47</sup> While the class action issue is not among the “questions presented” set out by the Court in *Green Tree*,<sup>48</sup> and while it was not addressed in the decision issued by the Eleventh Circuit,<sup>49</sup> the district court opinion did reject plaintiffs’ argument that their claim under TILA was exempt from arbitration because it was brought as a class action.<sup>50</sup> Further, the issue has been briefed already by the Petitioners—although they note that the Court need not reach the argument<sup>51</sup>—and by respondents and some amici.<sup>52</sup> Still, it is rather unlikely that the

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916 (Cal. App. 1999) (sic) (arbitration clause voided as unconscionable, in part, because it deprives arbitrator of authority to hear classwide claim); *Powertel v. Bexley*, 743 So.2d 570 (Fla.App.1999) (court refuses to enforce arbitration clause because of its retroactive application to claim and because it was unconscionable to deprive plaintiff of opportunity to proceed by way of class action); Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 William & Mary L. Rev., issue #1 (due out in October, 2000) (sic).

National Conference of Comm’rs on Unif. State Laws, *Proposed Revisions of the Uniform Arbitration Act*, Draft for Approval 36-37 (last visited Aug. 24, 2000) <<http://www.law.upenn.edu/bll/ulc/uarba/arb0500.pdf>>.

47. *Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235).

48. *See* 68 U.S.L.W. 3625 (U.S. Apr. 4, 2000) (No. 99-1235). The questions presented are: (1) Did court of appeals err in concluding that order compelling arbitration and dismissing lawsuit’s underlying claims is “final decision with respect [to] an arbitration” appealable under 9 U.S.C. § 16(a)(3)? (2) Did court of appeals err in concluding that arbitration provision that was “silent” on issue of costs and fees was unenforceable under Federal Arbitration Act because risk that plaintiff “might” be required to bear unknown costs and fees potentially undermined her ability to vindicate statutory rights?

*Id.*

49. *See Randolph*, 178 F.3d at 1157-59. The Eleventh Circuit reversed the district court’s grant of a motion to compel arbitration, concluding that because the arbitration clause failed to allocate fees among disputants, it failed to guarantee plaintiff could “vindicate her statutory rights” under the TILA and was unenforceable. *See id.*

50. *See* 991 F. Supp. 1410, 1418-19 (M.D. Ala. 1997).

51. *See* Brief of Petitioners, *Green Tree Fin. Corp. v. Randolph* (U.S. June 8, 2000) (No. 99-1235), *available in* 2000 WL 744132, at \*42-43.

52. *See* Brief of Respondent, *Green Tree Fin. Corp. v. Randolph* (U.S. July 24, 2000) (No. 99-1235), *available in* 2000 WL 1086800, at \*39-45; Brief of the Chamber of Commerce of the United States of America as Amicus Curiae in Support of Petitioners, *Green Tree Fin. Corp. v. Randolph* (U.S. June 8, 2000) (No. 99-1235), *available in* 2000 WL 744157, at \*6-29; Brief Amici Curiae of AARP and the National Consumer Law Center in Support of Respondent,

Court will reach out to decide this issue. First, one of the questions the Court is considering is whether it was appropriate for the Eleventh Circuit to consider an appeal from the district court's grant of the motion to compel arbitration.<sup>53</sup> If the Court decides the appeal was not appropriate, it presumably would not go on to consider whether the district court erred. Second, even if the Court determines that the appeal was permissible, it likely would not choose to decide a question that was not addressed by the appellate court and thus not adequately developed in the record.<sup>54</sup>

In previous decisions the U.S. Supreme Court has made no definitive rulings in the area, but *Gilmer v. Interstate/Johnson Lane Corp.*<sup>55</sup> contains some relevant dicta.<sup>56</sup> While confusing, this dicta seems to state that the Court would not necessarily be troubled by an arbitration clause that effectively required an age discrimination plaintiff to resolve a dispute on an individual basis,<sup>57</sup>

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*Green Tree Fin. Corp. v. Randolph* (U.S. June 24, 2000) (No. 99-1235), available in 2000 WL 1014563, at \*19-24.

53. See *supra* note 48.

54. In similar circumstances the Court has declined to address issues falling outside the questions presented. See, e.g., *Roberts v. Galen of Va., Inc.*, 525 U.S. 249, 253-54 (1999) (declining to address issues for which certiorari was not granted, and also noting that the claims were not "sufficiently developed" in the lower court); *National Collegiate Athletic Ass'n v. Smith*, 525 U.S. 459, 470 (1999) (refusing to "decide in the first instance issues not decided below").

55. 500 U.S. 20 (1991).

56. Plaintiff, who brought suit under the federal Age Discrimination in Employment Act, argued that the unavailability of class action procedures in arbitration was one reason the Court should not compel him to arbitrate. See *id.* at 32. The Court's rejection of the argument is dicta because the Court found that plaintiff was wrong on the facts, stating that the New York Stock Exchange Rules provide for "collective" proceedings. See *id.* The Court seemingly assumed that NYSE "collective proceedings" were equivalent to class actions. Although this premise may be false, in that collective or consolidated proceedings are quite different from the representative suit that allows a few named plaintiffs to carry the brunt of plaintiffs' burden, it apparently does form the basis for the Court's holding. See *id.* A second decision, *Southland Corp. v. Keating*, 465 U.S. 1 (1984), failed to address the issue of whether courts may allow class arbitrations to proceed, instead ruling that the Court lacked jurisdiction to address the issue given the context of the case. See *id.* at 7-9 (observing that because *Southland* did not argue in state court that federal law preempted state law class action arbitration procedures, and because the California Supreme Court did not pass on that issue, the Supreme Court "[was] without jurisdiction to resolve this question").

57. Specifically, the Court opined that "even if the arbitration could not go forward as a class action or class relief could not be granted by the arbitrator, the fact that the [ADEA] provides for the possibility of bringing a collective action does not mean that individual attempts at conciliation were intended to be barred." *Gilmer*, 500 U.S. at 32 (alteration in original) (quoting *Nicholson v. CPC Int'l Inc.*, 877 F.2d 221, 241 (3d Cir. 1989) (Becker, J., dissenting)). This language will be examined and critiqued later in the Article. See *infra*

at least where classwide relief would be available through the EEOC.<sup>58</sup>

Even those few lower court cases that address the issue directly provide mixed results. In several cases defendants have proved successful in using pre-dispute arbitration agreements to eliminate the class remedy.<sup>59</sup> While courts have not thus far allowed companies to impose arbitration *after* the filing of a class suit,<sup>60</sup> several have implicitly accepted the idea that consumers, employees, and others can be deprived entirely of the opportunity to proceed by way of class action.<sup>61</sup> On the other hand, two courts have recently found that the use of arbitration to eliminate the class action remedy can be unconscionable.<sup>62</sup> In addition, a third court has refused to apply an arbitration clause to claims brought under the Truth in Lending Act and the Electronic Funds Transfer Act, reasoning that because the clause would deprive plaintiffs of the opportunity to proceed by way of class action, it was inconsistent with those statutes.<sup>63</sup>

This Article offers a comprehensive analysis of how the confluence of arbitration and class actions has been and ought to be

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notes 414-17 and accompanying text. Interestingly, the language cited by the Supreme Court is itself dicta, in that Judge Becker concluded in his dissent that "arbitrations may in fact go forward as class actions." *Nicholson*, 877 F.2d at 240 (Becker, J., dissenting).

58. The Court noted "it should be remembered that arbitration agreements will not preclude the EEOC from bringing actions seeking class-wide and equitable relief." *Gilmer*, 500 U.S. at 32. Note, however, that subsequent to *Gilmer*, several appellate courts have issued decisions holding that, regarding an individual who has signed an agreement to arbitration, the EEOC may not pursue damages claims on that individual's behalf. *See* EEOC v. Waffle House, Inc., 193 F.3d 805, 812 (4th Cir. 1999) (barring the EEOC from seeking "make whole" relief); EEOC v. Kidder Peabody & Co., 156 F.3d 298, 301-03 (2d Cir. 1998) (holding that an arbitration agreement precludes the EEOC from seeking purely monetary relief). *But see* EEOC v. Frank's Nursery & Crafts, Inc., 177 F.3d 448, 459-68 (6th Cir. 1999) (holding that neither the FAA nor principles of preclusion limit the EEOC's right to pursue all remedies, even where employee agreed to arbitration).

59. *See infra* notes 211-25, 262-81 and accompanying text.

60. *See infra* notes 289-308 and accompanying text.

61. *See infra* notes 262-81 and accompanying text.

62. *See* *Ramirez v. Circuit City Stores*, 90 Cal. Rptr. 2d 916, 919-20 (Cal. Ct. App. 1999) (holding unconscionable a mandatory arbitration clause imposed on employees, in part because the clause deprived employees of the opportunity to bring class actions); *Powertel v. Bexley*, 743 So. 2d 570, 576-77 (Fla. Dist. Ct. App. 1999) (refusing to enforce arbitration clause imposed on consumer by phone company in part because elimination of class action remedy contributed to unconscionability). For further discussion of the unconscionability argument, see *infra* notes 420-27 and accompanying text.

63. *See* *Johnson v. Tele-Cash, Inc.*, 82 F. Supp. 2d 264, 266 (D. Del. 1999). For more discussion of this case, see *infra* notes 385-99 and accompanying text.



addressed. In doing so, it attempts to clarify and distinguish crucial legal and policy issues that too frequently have been blurred or ignored by the few courts and commentators that have begun to address these questions. Specifically, this Article considers the implications of contractual doctrines, federal statutory provisions, and the Due Process Clause of the Constitution for courts' handling of arbitrations and class actions.

The basic array of options facing courts is straightforward. Assuming that the traditional prerequisites for a class action have been met,<sup>64</sup> courts have four choices: (1) order the dispute to be resolved in an individualized arbitration, thereby denying plaintiffs either a litigation or arbitration venue for their class claims; (2) refuse to mandate arbitration, and instead allow plaintiffs to litigate their class claims; (3) order that the dispute be resolved through an arbitral class action, also known as classwide arbitration; or (4) order the dispute to arbitration but allow the arbitrators to make the determination as to whether the dispute should be resolved individually or on a class basis.

After exploring the relevant legal and policy arguments, this Article makes four major points. First, it concludes that federal statutes and contractual doctrines, particularly unconscionability, will sometimes, but not always, bar companies from entirely precluding plaintiffs from proceeding by way of class action. To determine whether the wholesale elimination of class actions is proscribed by statute or contractual doctrines, courts will need to examine the language of the arbitration agreement, the text of relevant statutes, the provisions of state contract law, and the feasibility of pursuing the suit on a nonclass basis. Second, this Article argues that while parties may elect to pursue their claims in classwide arbitration rather than through class action litigation, the Due Process Clause, federal statutes, and contractual doctrines will constrain this choice. Courts may not compel and should not permit classwide arbitration when the due process rights of class members would be jeopardized. Third, courts should interpret

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64. In federal court, one or more persons may sue or be sued as representatives of a larger group only if (1) the class is so numerous that joinder of all members is impracticable; (2) there are questions of law or fact common to the class; (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class; and (4) the representative parties will fairly and adequately protect the interests of the class. *See* FED. R. CIV. P. 23(a).

arbitration clauses that do not expressly deny the availability of class actions to permit classwide arbitrations. Fourth, to the extent that courts do not step in to prevent companies from using mandatory arbitration clauses to eliminate class actions, Congress should enact legislation to protect the use of this important procedural device.

This Article is organized as follows. Part I examines the law and policy underlying arbitration, class actions, and arbitral class actions. Part II then summarizes the decisions courts have issued in cases involving arbitration and class actions.<sup>65</sup> Next, Part III advises courts on how they *ought* to be analyzing these issues, focusing particularly on the policies underlying both class actions and arbitration. Finally, Part IV alerts Congress to the possible need for legislative action in order to protect the pivotal class action.

## I. EXPLORING THE RELEVANT POLICY UNDERLYING BINDING ARBITRATION AND CLASS ACTIONS

Because existing statutes offer no explicit guidance on how to reconcile class actions and arbitration, courts and legislators inevitably will turn to policy arguments as they attempt to resolve the clash between these competing procedural devices. Interestingly, binding arbitration and class actions share a few attributes: both are intended to be efficient; both are claimed by their supporters to be fair; and both have been attacked rather viciously for being unfair and not serving the public interest. This section will quickly explore the law and policy underlying each technique in order to examine whether and how it might be possible to protect the interests that are served by each device.

### A. Law and Policy Underlying Binding Arbitration

Supporters of binding arbitration have long praised the technique for purportedly being quicker and cheaper than litigation, for

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65. For purposes of completeness, Part II will briefly summarize the cases in which defendants have sought to impose arbitration *after* the filing of a class action. Parts I, III, and IV will not address these issues for two reasons. First, to date, courts have been united in rejecting defendants' attempt to impose arbitration after the fact. Second, these cases involve entirely different bodies of law than those discussed in the rest of this Article.

allowing disputants to select decisionmakers with special expertise, and for allowing parties to design a dispute resolution process that best serves their needs.<sup>66</sup> Recognizing these potential benefits, Congress passed the Federal Arbitration Act<sup>67</sup> ("FAA") in 1925 so that businesses would have the capability of entering into binding agreements to resolve future disputes through binding arbitration.<sup>68</sup> Where parties have contracted to arbitrate a dispute, this statute requires courts to compel arbitration and to stay litigation<sup>69</sup> unless the arbitration clause at issue is void according to standard contract law principles.<sup>70</sup>

The Supreme Court, while initially reluctant to mandate binding arbitration in contexts in which it felt the technique might be contrary to the public interest,<sup>71</sup> has now become an extremely

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66. See, e.g., STEPHEN B. GOLDBERG ET AL., DISPUTE RESOLUTION: NEGOTIATION, MEDIATION AND OTHER PROCESSES 234 (3d ed. 1999) (noting theoretical advantages of arbitration); Warren E. Burger, *Using Arbitration to Achieve Justice*, ARB. J., Dec. 1985, at 3, 6 ("[I]n terms of cost, time, and human wear and tear, arbitration is vastly better than conventional litigation for many kinds of cases."); Dwight Golann, *Developments in Consumer Financial Services Litigation*, 43 BUS. LAW. 1081, 1091 (1988) (arguing that arbitration is potentially faster, cheaper, and more private for all parties). See generally Edward Brunet, *Replacing Folklore Arbitration with a Contract Model of Arbitration*, 74 TUL. L. REV. 39 (1999) (arguing that the traditional, or "folklore," form of arbitration, characterized by informality, speed, and low cost, is being replaced by a form in which parties draft provisions often calling for complex and expensive procedures).

67. Ch. 213, 43 Stat. 883 (1925) (codified as amended at 9 U.S.C. §§ 1-208 (1994)).

68. For an excellent history of the circumstances leading to passage of the FAA, see IAN R. MACNEIL, AMERICAN ARBITRATION LAW: REFORMATION, NATIONALIZATION, INTERNATIONALIZATION 3-83 (1992). For an argument asserting that although Congress intended to help businesses enter into enforceable arbitration agreements, it never intended to allow a business to force its customers or employees to arbitrate, see Jean R. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 WASH. U. L.Q. 637, 644-49 (1996) [hereinafter Sternlight, *Panacea*].

69. Sections 3 and 4 of the statute provide the mechanisms for stays of litigation and for motions to compel arbitration. See 9 U.S.C. §§ 3-4 (1994).

70. Section 2 provides that arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." *Id.* § 2.

71. In *Wilko v. Swan*, 346 U.S. 427 (1953), a 7-2 majority of the Court interpreted the Securities Act of 1933 to preclude a brokerage firm from requiring its customers to arbitrate disputes, reflecting a concern that arbitration was desirable only if it was genuinely consented to and served the public interest. *Alexander v. Gardner-Denver Co.*, 415 U.S. 36 (1974), held that an employee whose union contract contained an arbitration clause could bring a statutory race discrimination claim in court, even if he had already lost that claim in arbitration. For a discussion of *Wilko*, *Gardner-Denver*, and subsequent cases limiting the use of the FAA in the civil rights context, see Sternlight, *Panacea*, *supra* note 68, at 652-55.

strong advocate of binding arbitration.<sup>72</sup> In decision after decision since 1983,<sup>73</sup> the Court has praised the technique, stated it is “favored,” and ensured that arbitration clauses will be enforced in a vast array of situations.<sup>74</sup>

At the same time, courts, arbitral organizations, and commentators<sup>75</sup> have increasingly recognized that companies can

72. For a discussion of the evolution of the Supreme Court's thought process regarding arbitration, see *id.* at 644-74. The growth in the Court's enthusiasm for binding arbitration paralleled Chief Justice Burger's statements that binding arbitration might be used to decrease the burdens on an overloaded judiciary. See Warren E. Burger, *Agenda for 2000 A.D.—A Need for Systematic Anticipation*, 70 F.R.D. 83, 93-96 (1976); Warren E. Burger, *Isn't There a Better Way?*, 68 A.B.A. J. 274, 277 (1982); Burger, *supra* note 66, at 4-6; see also William H. Rehnquist, *A Jurist's View of Arbitration*, 32 ARB. J. 1, 3-4 (concluding that arbitration is less costly than litigation).

73. In *Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp.*, 460 U.S. 1 (1983), the Court enunciated, for the first time, the concept that arbitration serves the public interest and should thus be favored:

[Q]uestions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration. . . . The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability.

*Id.* at 24-25.

74. See, e.g., *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 688-89 (1996) (reversing a Montana Supreme Court decision that refused to enforce an arbitration clause for failure to comply with Montana's statutory notice requirement, and further holding that the statute was preempted by the FAA); *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 281 (1995) (holding that the FAA applies to the full extent of Congress' permitted regulation under the Commerce Clause); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991) (citing federal policy favoring arbitration in holding that claims brought under the Age Discrimination in Employment Act may be required to be arbitrated); *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 481 (1989) (taking note of federal policy favoring arbitration in holding that federal securities fraud claims may be required to be arbitrated); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 227 (1987) (holding that securities fraud and RICO claims can be arbitrated, and stating that in light of federal favoritism toward arbitration, “[t]he burden is on the party opposing arbitration . . . to show that Congress intended to preclude a waiver of judicial remedies for the statutory rights at issue”); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985) (stating that while “the parties’ intentions control . . . those intentions are generously construed as to issues of arbitrability”); *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984) (holding that the FAA applies in state as well as federal court, and that it preempts conflicting state statutes).

75. See, e.g., Thomas E. Carbonneau, *Arbitral Justice: The Demise of Due Process in American Law*, 70 TUL. L. REV. 1945, 1955-67 (1996) (arguing that the institution of arbitration is being exploited in ways detrimental to justice); Paul D. Carrington & Paul H. Haagen, *Contract and Jurisdiction*, 1996 S. CT. REV. 331, 401 (1996) (concluding that Supreme Court's arbitral jurisprudence allows “birds of prey” to “sup on workers, consumers, shippers, passengers, and franchisees”); David S. Schwartz, *Enforcing Small Print to Protect*

sometimes use arbitration clauses abusively to achieve unfair advantages over consumers, employees, or others.<sup>76</sup> Courts have thus refused to enforce particularly egregious arbitration clauses on such grounds as unconscionability,<sup>77</sup> lack of considera-

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*Big Business: Employee and Consumer Right Claims in an Age of Compelled Arbitration*, 1997 WIS. L. REV. 33, 36 (stating that the "Supreme Court has created a monster"); Sternlight, *Panacea*, *supra* note 68, at 641-44 (arguing that as a matter of both legislative history and public policy, it is inappropriate for courts to apply a preference for arbitration over litigation when interpreting arbitral contracts of adhesion imposed on customers, employees, franchisees, or other "little guys"); Sternlight, *Rethinking*, *supra* note 4, at 10-14 (urging that courts' preference for arbitration over litigation at times violates constitutional rights to jury trial, to an Article III judge, and to due process).

76. See generally Sternlight, *Panacea*, *supra* note 68, at 680-86 (discussing the economic incentives which may lead companies to draft unfair arbitration clauses). Moreover, it is not at all clear that imposing binding arbitration makes it easier for consumers to state their claims against a company. See Mayer, *Win Some, Lose Rarely?*, *supra* note 11, at E1 (stating that in the period since credit card company First USA imposed binding arbitration, the process was used 51,622 times by the company to state claims against consumers, and only four times by consumers to state claims against the company).

77. See *Knepp v. Credit Acceptance Corp.*, 229 B.R. 821, 837-38 (Bankr. N.D. Ala. 1999) (refusing to enforce arbitration clause in which debtor/auto purchaser would be required to pay the costs of arbitration, partly on ground of unconscionability); *Hooters of Am., Inc. v. Phillips*, 39 F. Supp. 2d 582, 614 (D.S.C. 1998) (holding arbitration clause unconscionable in part because employee was "stripped of numerous substantive remedies under Title VII [in that] . . . compensatory damages, backpay relief, frontpay relief, punitive damages, and attorney's fees are either eliminated or substantially curtailed . . ." and also because procedural rules were biased against the employees and in favor of the company because the company had total control over the selection of arbitrators, employees had severely limited discovery, and witness disclosure and sequestration were one-sided), *aff'd on other grounds*, 173 F.3d 933 (4th Cir. 1999) (holding that employer had breached arbitration agreement by issuing biased rules); *Gonzalez v. Hughes Aircraft Employees Fed. Credit Union*, 83 Cal. Rptr. 2d 763, 766-67 (Cal. Ct. App. 1999) (voiding, as substantively unconscionable, clause which shortened statute of limitations, allowed employer to continue to seek judicial relief, and severely limited employee's discovery rights), *review granted and opinion superseded*, 978 P.2d 1 (Cal. 1999), *appeal dismissed per stipulation*, 990 P.2d 504 (Cal. 1999); *Armendariz v. Foundation Health Psychcare Servs., Inc.*, 80 Cal. Rptr. 2d 255, 266-68 (Cal. Ct. App. 1998) (holding unconscionable arbitration clause that limited plaintiffs' remedies to wages lost between date of discharge and date of arbitration, but severing that remedial restriction rather than voiding the entire arbitration clause), *review granted and opinion superseded*, 973 P.2d 51 (Cal. 1999); *Stirlen v. Supercuts, Inc.*, 60 Cal. Rptr. 2d 138, 150-52 (Cal. Ct. App. 1997) (holding unconscionable contract which, *inter alia*, precluded plaintiff from recovering damages other than actual damages for breach of contract); *Patterson v. ITT Consumer Fin. Corp.*, 18 Cal. Rptr. 2d 563, 565-66 (Cal. Ct. App. 1993) (refusing to enforce arbitration clause imposed by a financing organization upon California consumers which required arbitration to be heard in Minneapolis, Minnesota, and required plaintiffs to pay substantial filing fees, and further observing that procedures that might be fair as applied to business entities are not necessarily fair as applied to consumers); *Brower v. Gateway 2000, Inc.*, 246 A.D. 2d 246, 252 (N.Y. App. Div. 1998) (holding unconscionable, on ground of cost, clause which both required computer purchasers to arbitrate disputes in Chicago and also required arbitration according to the rules of the International Chamber of Commerce,

tion,<sup>78</sup> or on the ground that the clause is inconsistent with the particular statute under which the plaintiffs' claim is brought.<sup>79</sup> In making

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which impose high administrative costs).

78. *See, e.g., Gibson v. Neighborhood Health Clinics, Inc.*, 121 F.3d 1126, 1131 (7th Cir. 1997) (holding arbitration clause invalid in which current employee was required to sign clause providing for arbitration of future claims but was not given any compensation or other consideration in return and further holding that continued employment alone did not constitute adequate consideration); *cf. Michalski v. Circuit City Stores, Inc.*, 177 F.3d 634, 636-37 (7th Cir. 1999) (refusing to void arbitration agreement imposed upon existing employee for lack of consideration on the ground that company agreed to be bound by arbitration process, even though employee but not employer was required to arbitrate claims).

79. *See Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149, 1158 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235) (refusing to compel arbitration of claims brought under Truth in Lending Act because clause failed to specify allocation of costs, and court therefore feared that plaintiff's burden of costs might be so high as to render claim not feasible); *Shankle v. B-G Maintenance Management, Inc.*, 163 F.3d 1230, 1234-35 (10th Cir. 1999) (denying employer's motion to compel arbitration of claims under Title VII, the Americans with Disabilities Act, and the Age Discrimination in Employment Act where employee was required to pay half of arbitrator's fee, because that requirement denies employee an effective and accessible alternative forum to litigation); *Paladino v. Avnet Computer Techs. Inc.*, 134 F.3d 1054, 1059-60 (11th Cir. 1998) (refusing to compel arbitration of Title VII claims because clause did not clearly cover noncontractual claims and arbitrator was only permitted to award contract damages); *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1467-69 (D.C. Cir. 1997) (holding that a race discrimination claim brought under Title VII was arbitrable only if the employer paid the cost of the arbitration and a meaningful opportunity to appeal was afforded); *see also Floss v. Ryan's Family Steak Houses, Inc.*, 211 F.3d 306, 314-15 (6th Cir. 2000) (expressing doubts that the particular arbitral forum was sufficient to allow for enforcement of claims under FLSA, and holding clause unenforceable on contractual ground that provider's promise of arbitral forum was "fatally indefinite"). The above decisions, which void only particularly unfair arbitration clauses under a given statute, are distinct from other cases in which the Ninth Circuit has held that claims under certain statutes are never subject to mandatory arbitration, or that such arbitration is acceptable only if entered "knowingly." *See Duffield v. Robertson Stephens & Co.*, 144 F.3d 1182, 1189-90 (9th Cir. 1998), *cert. denied*, 119 S. Ct. 445 (1998) (holding that the Civil Rights Act of 1991 precluded employer from using pre-dispute arbitration agreements to compel employee to arbitrate Title VII claims because the employee was not given the choice of whether to accept arbitration); *Nelson v. Cyprus Bagdad Copper Corp.*, 119 F.3d 756, 758, 763 (9th Cir. 1997) (refusing to enforce agreement to arbitrate ADA claim because, although the employee signed an acknowledgment that he had received an Employee Handbook, and although the Handbook contained a provision describing the grievance process as "sole and exclusive procedures for the processing and resolution of any problem," the employee did not "knowingly waive his statutory rights to a judicial forum"). Other courts have refused to go this far, while remaining open to the case-by-case challenge. *See, e.g., Hooters*, 173 F.3d at 937 (holding that the Civil Rights Act of 1991 does not bar all mandatory arbitration but affirming the district court's refusal to compel arbitration because of the terms of clause); *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 170 F.3d 1, 11 (1st Cir. 1999) (stating that "neither the language of the statute nor the legislative history demonstrates an intent in the 1991 CRA to preclude pre-dispute arbitration agreements," but nonetheless holding the clause unenforceable due to lack of notice).

such fairness determinations courts have been particularly concerned with those aspects of arbitration clauses that would, as a practical matter, preclude plaintiffs from pursuing their claims or deprive them of remedies provided by statute. Such terms have included high filing fees and costs, distant locations, and explicit limitations on available relief.<sup>80</sup> As well, several of the key arbitration organizations have adopted "due process protocols,"<sup>81</sup> attempting to distinguish between fair and unfair arbitration agreements, and have stated that they will not assist in enforcing those agreements which fail to comply with the protocols.<sup>82</sup> These

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80. See *supra* notes 77-79.

81. Three Due Process Protocols have been drafted under the auspices of the American Arbitration Association: Due Process Protocol for Employment Disputes [hereinafter Employment Protocol]; Consumer Due Process Protocol [hereinafter Consumer Protocol]; and the Commission Health Care Dispute Resolution Draft Final Report [hereinafter Health Protocol]. These protocols, however, are in different stages of adoption. The Employment Protocol, dated May 9, 1995, has been adopted by many organizations including the AAA, the ABA Section on Labor and Employment, the National Academy of Arbitrators, and the National Employment Lawyers Association. See ABA LAB. & EMP. L. NEWSL. (Winter 1996). The Consumer Protocol, dated April 17, 1998, was drafted by persons designated by a variety of governmental, arbitral, and consumer organizations, but to this author's knowledge has not been adopted officially by such organizations. The Health Protocol, dated July 27, 1998, was drafted by representatives of the AAA, the ABA, and the AMA. This Protocol goes the furthest, in that its Recommendation 3 permits only *post*-dispute agreements to binding arbitration in disputes involving patients. It has been adopted by the ABA. See AMERICAN BAR ASSOCIATION, SECTION OF DISPUTE RESOLUTION, REPORT 114, at 4 (Feb. 8, 1999). All of the protocols are available online at <http://www.adr.org/protocol.html>. Several courts have looked to the protocols in attempting to rule on whether they should compel arbitration according to a particular agreement. See, e.g., *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1483-85 (D.C. Cir. 1997); *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 995 F. Supp. 190, 208 (D. Mass. 1998) (relying in part on Employment Protocol's requirement that parties have a role in selecting arbitral in refusing to compel arbitration where this requirement was not met), *aff'd on other grounds*, 170 F.3d 1 (1st Cir. 1999); *Hooters of Am., Inc. v. Phillips*, 39 F. Supp. 2d 582, 598-601 (citing extensively testimony alluding to Protocols to support conclusion that clause was void for unconscionability and other reasons), *aff'd on other grounds*, 173 F.3d 933, 937 (4th Cir. 1999). Organizations other than the AAA have also adopted special fairness protocols. For example, JAMS publishes a fairness protocol concerning financial services arbitration on its website. See *JAMS Minimum Standards of Procedural Fairness Policy on Financial Services Arbitrations* (visited Aug. 25, 2000) <[http://www.jamsadr.com/fin\\_minimum\\_stds.asp](http://www.jamsadr.com/fin_minimum_stds.asp)>. Similarly, the National Arbitration Forum (NAF) also makes available a fairness protocol. See *Arbitration Bill of Rights* (visited Aug. 25, 2000) <<http://www.arbforum.com/other/index.html>>. Nonetheless, the neutrality of the NAF has been challenged in litigation involving First USA. See *Mayer, Win Some, Lose Rarely?*, *supra* note 11, at E1 (recounting allegations that NAF procedures are biased in favor of First USA, which is NAF's largest client); cf. *Marsh v. First USA Bank, N.A.*, 103 F. Supp. 2d 909, 924-26 (N.D. Tex. 2000) (rejecting plaintiffs' argument that National Arbitration Forum is biased based on its ongoing financial relationship with defendant).

82. See Thomas J. Stipanowich, *Behind the Neutral: A Look at Provider Issues: Due*

protocols mandate that a fair process should provide that participants should be assured adequate choice of representative,<sup>83</sup> that fees and costs should not be excessive,<sup>84</sup> that some discovery is desirable,<sup>85</sup> and that neutrals should be skillful and impartial and apply relevant law.<sup>86</sup>

The Supreme Court itself has recognized that its "favoritism" or "preference" for arbitration must be tempered by other factors. It has stated that as arbitration is a creature of contract, parties should not be compelled to arbitrate disputes they have not agreed to arbitrate.<sup>87</sup> As well, the Court has recognized that agreements which are not sufficiently clear will not be enforceable,<sup>88</sup> and that, at least in the collective bargaining context, it may be inappropriate to apply a presumption in favor of arbitrability to statutory as opposed to contractual issues.<sup>89</sup>

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*Process Protocol Protects Consumer Rights*, 1102 PRACTISING L. INST. 813, 823 (1999) ("If the AAA determines that a particular consumer dispute resolution program substantially and materially deviates from the minimum standards of the protocol, it will decline to administer cases under the program.").

83. See Consumer Protocol, *supra* note 81, at Principle 9; Employment Protocol, *supra* note 81, at B1; Health Protocol, *supra* note 81, at Principle 6.

84. See Consumer Protocol, *supra* note 81, at Principles 6 & 7; Employment Protocol, *supra* note 81, at B2.

85. See Consumer Protocol, *supra* note 81, at Principle 13; Employment Protocol, *supra* note 81, at B3; Health Protocol, *supra* note 81, at Principle 7.

86. See Consumer Protocol, *supra* note 81, at Principles 3-4; Employment Protocol, *supra* note 81, at C1-6; Health Protocol, *supra* note 81, at Principles 4 & 5.

87. See *First Options, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995) (stating that "a party who has not agreed to arbitrate will normally have a right to a court's decision about the merits of its dispute" and holding that parties may choose whether a court or an arbitrator determines arbitrability); *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 57-64 (1995) (holding that because arbitration turns on parties' choices, it is up to them to determine whether punitive damages are available in arbitration); *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989) (stating that "[a]rbitration under the Act is a matter of consent, not coercion," and holding that parties could elect to be bound by state arbitration statute); see also *United Steelworkers v. Warrior & Gulf Navigation Co.*, 363 U.S. 574, 582 (1960) (stating that in the collective bargaining context, "arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit"). There is some tension between the principle of "favoring" arbitration over litigation, because it is supposedly better for society, and the principle of enforcing arbitration contracts only to the extent that they are agreed to by the parties. See Sternlight, *Panacea*, *supra* note 68, at 662-63.

88. See *Wright v. Universal Maritime Serv. Corp.*, 525 U.S. 70, 82 (1998) (holding that a union member could not be required to arbitrate his ADA claim against the employer because the CBA provision did not contain a "clear and unmistakable waiver of the covered employees' rights to a judicial forum for federal claims of employment discrimination").

89. See *id.* at 77-80 (interpreting contract governed by the Labor Management Relations



In sum, although binding arbitration is still popular and although courts are still enforcing many clauses, they are now beginning to distinguish between fair and unfair clauses and to refuse to enforce those clauses which are blatantly unfair.

## *B. Law and Policy Underlying Class Actions*

### *1. Nature and Benefit of Class Actions*

The class action is a procedural device which allows a small number of "named" persons to represent their fellow plaintiffs or defendants in litigation.<sup>90</sup> What the representatives win, the class wins; what the representatives lose, the class loses.<sup>91</sup> While the roots of the class action can be traced back to the Middle Ages,<sup>92</sup> modern Federal Rule of Civil Procedure 23 was adopted in 1966.<sup>93</sup>

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Act, but not necessarily by the FAA).

90. For a sample of some of the most useful sources on class actions, see HERBERT NEWBERG & ALBA CONTE, *NEWBERG ON CLASS ACTIONS* (3d ed. 1992); 7A CHARLES ALAN WRIGHT ET AL., *FEDERAL PRACTICE AND PROCEDURE* § 1751 (2d ed. 1986); STEPHEN C. YEAZELL, *FROM MEDIEVAL GROUP LITIGATION TO THE MODERN CLASS ACTION* (1987); John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343 (1995); Kenneth W. Dam, *Class Actions: Efficiency, Compensation, Deterrence, and Conflict of Interest*, 4 J. LEGAL STUD. 47 (1975); Eric D. Green, *Advancing Individual Rights Through Group Justice*, 30 U.C. DAVIS L. REV. 791 (1997); Harry Kalven, Jr. & Maurice Rosenfield, *The Contemporary Function of the Class Suit*, 8 U. CHI. L. REV. 684 (1941); Linda S. Mullenix, *The Constitutionality of the Proposed Rule 23 Class Action Amendments*, 39 ARIZ. L. REV. 615 (1997); Thomas D. Rowe Jr., *Beyond the Class Action Rule: An Inventory of Statutory Possibilities to Improve the Federal Class Action*, 71 N.Y.U. L. REV. 186 (1996); David L. Shapiro, *Class Actions: The Class as Party and Client*, 73 NOTRE DAME L. REV. 913 (1998); Symposium, *Mass Torts: Serving Up Just Desserts*, 80 CORNELL L. REV. 811 (1995) (including articles by Roger C. Cramton, William W. Schwarzer, Jack B. Weinstein, John C. Coffee, Jr., Richard L. Marcus, Jonathan R. Macey & Geoffrey P. Miller, Judith Resnik, Peter H. Schuck, John A. Siliciano, James H. Henderson, Jr., Francis E. McGovern, Robert L. Rabin, Susan P. Koniak, Carrie Menkel-Meadow, John Leubsdorf, and Charles W. Wolfram); Brian Wolfman & Alan B. Morrison, *Representing the Unrepresented in Class Actions Seeking Monetary Relief*, 71 N.Y.U. L. REV. 439 (1996); Arthur R. Miller, Comment, *Of Frankenstein Monsters and Shining Knights: Myth, Reality, and the "Class Action Problem,"* 92 HARV. L. REV. 664 (1979).

91. The preclusion of the absent class members' claims raises due process concerns. See *infra* notes 109-22 and accompanying text.

92. For discussions of the history of the class action, see generally YEAZELL, *supra* note 90; Geoffrey C. Hazard, Jr. et al., *An Historical Analysis of the Binding Effect of Class Suits*, 146 U. PA. L. REV. 1849 (1998).

93. See generally FED. R. CIV. P. 23 advisory committee's note (1966 amendment), 28 U.S.C. app. 695-99 (1994); Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356 (1967).

Its provisions are familiar.<sup>94</sup> Aspiring class representatives must demonstrate that they meet each of the Rule 23(a) requirements of numerosity, commonality, typicality, and fair and adequate representation.<sup>95</sup> In addition, they must establish that they meet the requirements of one of the three types of classes set out in Rule 23(b): that the class would avoid inconsistent or varying adjudications with respect to individual class members,<sup>96</sup> or the practical disposition of the interests of nonparties;<sup>97</sup> that the action seeks injunctive or declaratory relief with respect to the class as a whole;<sup>98</sup> or simply that questions of law or fact common to the class predominate over questions affecting only individual members, and that the class action is a superior method for obtaining fair and efficient adjudication of such issues.<sup>99</sup>

Class actions have been praised widely for a variety of attributes including efficiency,<sup>100</sup> improving access to the litigation system,<sup>101</sup>

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94. The Supreme Court recently sketched out the general requirements in *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 613-17 (1997); see also MANUAL FOR COMPLEX LITIGATION § 30 (3d ed. 1995) (providing detailed guidance for courts and attorneys on how to apply law of class actions).

95. See FED. R. CIV. P. 23(a)(1).

96. See *id.* 23(b)(1)(A); see also *Amchem*, 521 U.S. at 614 (explaining that 23(b)(1) class actions are designed for situations in which separate actions would risk “incompatible standards of conduct for the party opposing the class,” either because the class members must by law be treated alike or because a limited fund is available to satisfy class claims) (quoting FED. R. CIV. P. 23(b)(1)(A)).

97. See FED. R. CIV. P. 23(b)(1)(B); see also *Ortiz v. Fibreboard Corp.*, 119 S. Ct. 2295, 2308-12 (1999) (explicating history and purpose of 23(b)(1)(B) limited fund class actions).

98. See FED. R. CIV. P. 23(b)(2); see also *Amchem*, 521 U.S. at 614 (observing that civil rights cases are “prime examples” of appropriate 23(b)(2) classes).

99. See FED. R. CIV. P. 23(b)(3); see also *Amchem*, 521 U.S. at 614-15 (calling 23(b)(3) classes the “most adventuresome” in that they are designed for situations in which, although a class action is not clearly mandated, it may nonetheless be desirable) (citing Benjamin Kaplan, *A Prefatory Note*, 10 B.C. INDUS. & COM. L. REV. 497, 497 (1969) and 7A WRIGHT ET AL., *supra* note 90, § 1777, at 517). *Amchem* also observed that the primary purpose of Rule 23(b)(3) class actions was to allow persons to bring suit who otherwise would not be able to do so. See *Amchem*, 521 U.S. at 617.

100. See, e.g., *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 809 (1985) (“Modern plaintiff class actions . . . permit[] litigation of a suit involving common questions when there are too many plaintiffs for proper joinder.”); *Gulf Oil Co. v. Bernard*, 452 U.S. 89, 100 n.11 (1981) (“Rule 23 expresses ‘a policy in favor of having litigation in which common interests, or common questions of law or fact prevail, disposed of where feasible in a single lawsuit.’”) (citation omitted); see also *Developments, The Paths of Civil Litigation*, 113 HARV. L. REV. 1783, 1805, 1810 (2000) (discussing efficiency savings).

101. See, e.g., *Deposit Guar. Nat’l Bank v. Roper*, 445 U.S. 326, 338-39 (1980) (observing that class actions make it possible to bring claims that otherwise would not be economically possible); *Eisen v. Carlisle*, 417 U.S. 156, 161 (1974) (noting that without class action, “[n]o

and serving the public interest.<sup>102</sup> In terms of efficiency, it is claimed that they allow issues involving multiple persons or institutions to be resolved more cheaply and expeditiously.<sup>103</sup> As to access, numerous courts including the Supreme Court have emphasized that the class mechanism can make possible suits which otherwise would have been logistically or economically impossible. The Court famously stated in *Eisen*:

A critical fact in this litigation is that petitioner's individual stake in the damages award he seeks is only \$70. No competent attorney would undertake this complex antitrust action to recover so inconsequential an amount. Economic reality dictates that petitioner's suit proceed as a class action or not at all.<sup>104</sup>

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competent attorney would undertake [petitioner's] action to recover so inconsequential an amount"); see also Developments, *supra* note 100, at 1808-10 (discussing how class actions seem to "enhance procedural fairness by ensuring that people who have been wrongly harmed have access to the judicial system").

102. This public interest includes compensating injured plaintiffs and deterring wrongful conduct. See, e.g., Geoffrey P. Miller, *Overlapping Class Actions*, 71 N.Y.U. L. REV. 514, 514 (1996) ("The class action, because it can dispose of multiple claims in a single proceeding, represents a potentially effective mechanism for privately enforcing the law, deterring wrongful conduct, and compensating victims."); Wolfman & Morrison, *supra* note 90, at 441 (observing that while class actions serve these important purposes, they can also be problematic when applied in complex cases).

103. See, e.g., *Amchem*, 521 U.S. at 617-18 (noting that class actions allow parties with numerous claims to obtain a "just, speedy, and inexpensive determination" of rights) (quoting FED. R. CIV. P. 1).

104. *Eisen*, 417 U.S. at 161. Years later, the court opined about this policy in *Amchem*:

The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights. A class action solves this problem by aggregating the relatively paltry potential recoveries into something worth someone's (usually an attorney's) labor.

*Amchem*, 521 U.S. at 617 (quoting *Mace v. Van Ru Credit Corp.*, 109 F.3d 338, 344 (7th Cir. 1997); see also *Phillips*, 472 U.S. at 809 ("Class actions . . . may permit the plaintiffs to pool claims which would be uneconomical to litigate individually. For example, this lawsuit involves claims averaging about \$100 per plaintiff; most of the plaintiffs would have no realistic day in court if a class action were not available."). Significantly, and despite the recognition that the suit could only be brought as a class action, the *Eisen* Court mandated that the representative plaintiff would have to give individualized notice to each of the 2 million or so identifiable members of the Rule 23(b)(3) class. See *Eisen*, 417 U.S. at 173-79. The Court fully realized that imposing this requirement would prevent the class action from being brought. See *id.* at 179 (remanding action with instructions to dismiss).

Finally, the use of class actions to fight racial discrimination,<sup>105</sup> to achieve prison reform,<sup>106</sup> and to tackle consumer fraud,<sup>107</sup> illustrates that these suits can often be used to achieve public goals, both by compensating victims and deterring future wrongful conduct.<sup>108</sup>

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105. See, e.g., *Brown v. Board of Educ.*, 347 U.S. 483 (1954) (holding, in class action, that school segregation violates the Equal Protection Clause); *Roberts v. Texaco, Inc.*, 979 F. Supp. 185 (S.D.N.Y. 1997) (approving \$115 million settlement and attorneys fee award against Texaco in class action by employees alleging race discrimination); *Ridgeway v. Flagstar Corp.*, Nos. C 93-20202 JW, C 93-20208 JW, 1994 WL 525553, at \*1 (N.D. Cal. Sept. 22, 1994) (approving \$27 million consent decree in class action brought against Denny's for failing to serve African American customers); *Haynes v. Shoney's, Inc.*, No. 89-30093-RV, 1993 WL 19915, at \*1 (N.D. Fla. Jan. 25, 1993) (approving consent decree against chain of restaurants for failure to hire African Americans); cf. *Hansberry v. Lee*, 311 U.S. 32 (1940) (concluding that because prior challenge to racially restrictive covenant was not class or representative suit, *Hansberry* family was not precluded from bringing own challenge). For a discussion of the underlying story of *Hansberry*, which is also recounted in Lorraine Hansberry's play, "A Raisin in the Sun," see generally Allen R. Kamp, *The History Behind Hansberry v. Lee*, 20 U.C. DAVIS L. REV. 481 (1987).

106. See, e.g., *Martarella v. Kelley*, 349 F. Supp. 575 (S.D.N.Y. 1972) (holding, in class action, that detention facility for persons in need of supervision violated Eighth Amendment by failing to provide adequate rehabilitative programs).

107. See, e.g., *Nickel v. Bank of Am., Nat'l Trust & Sav. Ass'n*, No. 96-16497, 1997 WL 419113, at \*1 (9th Cir. July 25, 1997) (discussing class action brought against bank for \$24 million overcharge of trustee fees); *In re Prudential Ins. Co. of Am. Sales Practices Litig.*, 962 F. Supp. 450 (D.N.J. 1997), *aff'd in relevant part*, 148 F.3d 283 (3d Cir. 1998) (approving settlement of class action in which life insurance policy holders brought suit against Prudential for engaging in churning and fraud in sale of replacement policies); *Lynch v. Household Fin. Corp.*, 360 F. Supp. 720 (D. Conn. 1973) (holding, in class action by owners of savings and checking accounts, that permanent garnishment of accounts without hearing violated Due Process Clause); *Sampson v. Eastman Kodak Co.*, 552 N.E.2d 1194 (Ill. App. Ct. 1990) (approving settlement of \$150 million in class action brought by purchasers of instant cameras alleging injury as a result of injunction secured by Polaroid to prohibit use of Kodak camera); *Avery v. State Farm Mut. Auto. Ins. Co.*, No. 97-L-114, 1999 WL 955543, at \*1 (Ill. Cir. Ct. Oct. 8, 1999) (approving award of more than \$456 million to automobile policy holders who were provided with nonfactory authorized replacement parts). See generally JONATHAN SHELDON & DANIEL A. EDELMAN, NATIONAL CONSUMER LAW CENTER, CONSUMER CLASS ACTIONS (4th ed. 1999) (detailing procedures involved in consumer class actions); Robert C. Eckhardt, *Consumer Class Actions*, 45 NOTRE DAME L. REV. 663, 663-64 (1970) (urging the passage of legislation to allow consumers to join together in class actions, "because existing private legal remedies cannot meet the needs of a consumer having a litigable claim," and suggesting that companies may deliberately defraud individuals out of small rather than large amounts of money to avoid legal consequences); Steven B. Epstein, *Synthetic Stucco Suits Swarm Southeast—and Spread*, THE BRIEF, Winter 2000, at 10 (discussing class actions brought in multiple states on behalf of home owners who installed defective siding that caused damage to their homes); James E. Starrs, *The Consumer Class Action-Part II: Considerations of Procedure*, 49 B.U. L. REV. 407 (1969) (explaining that class actions, used successfully in a variety of civil rights and other contexts, would be a valuable tool for consumer claims, providing economic, strategic, and psychological benefits).

108. For a discussion of the public purposes of litigation, see Owen M. Fiss, *Against*

## 2. Due Process Concerns Raised by Class Actions

The Supreme Court has recognized that while class actions can serve many desirable goals, they also raise due process concerns because they are “representative” litigation.<sup>109</sup> In particular, because class actions are an exception to the general rule that one cannot be bound to a judgment unless one was a party to that suit,<sup>110</sup> special measures are necessary to protect the interests of the non-named class members.<sup>111</sup> Thus, in *Phillips Petroleum Co. v. Shutts*,<sup>112</sup> the Court explained that, at least in an action for money damages or similar relief, due process requires that “absent” class members be afforded notice of the suit,<sup>113</sup> an opportunity to be heard and participate in the litigation, and a chance to opt out,<sup>114</sup> and also requires that the named plaintiff “at all times adequately represent the interests of the absent class members.”<sup>115</sup>

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*Settlement*, 93 YALE L.J. 1073 (1984).

109. See *Phillips*, 472 U.S. at 811-12 (stating that if a jurisdiction seeks to bind an absent class member concerning a claim for money damages or similar relief at law, “it must provide minimal procedural due process protection”); *Eisen*, 417 U.S. at 173-74 (observing that the notice requirement of Rule 23(c)(2) fulfills the Due Process Clause’s requirement of notice and an opportunity to be heard); see also *Ortiz v. Fibreboard Corp.*, 119 S. Ct. 2295, 2314-15 (1999) (explaining that due process concerns generally implicated in damages class actions are magnified when class members are not given an opportunity to opt out); *Hansberry*, 311 U.S. at 42-43, 45 (holding that Due Process Clause requires that named plaintiff adequately represent the interests of absent class members). For an interesting discussion of the implications of *Phillips* for preclusion of absent class members’ claims, see Henry Paul Monaghan, *Antisuit Injunctions and Preclusion Against Absent Nonresident Class Members*, 98 COLUM. L. REV. 1148 (1998) (arguing that absent class members should not be precluded, by an antisuit injunction, from filing a subsequent action in a new jurisdiction, if the initial class action did not adequately protect their due process rights). See generally Linda S. Mullenix, *Class Actions, Personal Jurisdiction, and Plaintiffs’ Due Process: Implications for Mass Tort Litigation*, 28 U.C. DAVIS L. REV. 871 (recommending alternative due process protections for plaintiffs in mandatory class actions).

110. See *Hansberry*, 311 U.S. at 40-41; Mullenix, *supra* note 109, at 884.

111. See *infra* notes 112-22 and accompanying text.

112. 472 U.S. 797 (1985).

113. See *id.* (holding that notice of class action sent by first-class mail, and including notification of opt out right, satisfied due process); see also *Eisen*, 417 U.S. at 173-76 (holding that representative plaintiff must pay costs of providing adequate notice to class members, even when such costs are so high as to make litigation infeasible).

114. See *Phillips*, 472 U.S. at 798; see also *Ortiz*, 119 S. Ct. at 2314-15.

115. *Phillips*, 472 U.S. at 812. The *Phillips* decision does not clearly state whether the due process requirement applies to both in-state and out-of-state class members. Its holding seems limited to “absent” class members, a term the Court defines at one point as referring to out-of-state plaintiffs. See *Phillips*, 472 U.S. at 802. In some places, however, the Court

Thus, while the Court has not specified that Rule 23 is constitutionally required, certainly elements of that Rule appear to be mandated by the Due Process Clause.<sup>116</sup> Rule 23 builds protective measures directly into its provisions, not only by requiring the court to certify the class,<sup>117</sup> but also by allowing the court to divide a class into subclasses where appropriate,<sup>118</sup> to mandate notice to class members,<sup>119</sup> to require opportunities be afforded for directly participating in the action,<sup>120</sup> and to approve or disapprove any settlement that is reached in a class action.<sup>121</sup> In short, not only are court supervision of notice and opt out mandatory as to those actions for damages brought under Rule 23(b)(3), the Supreme Court also has made clear that court supervision of the class mechanism is crucial to its legitimacy under the Constitution.<sup>122</sup>

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apparently uses the term "absent" more broadly, to refer to non-named plaintiffs. *See id.* at 812 (observing that named plaintiffs must "adequately represent the interests of the absent class members"). The Court's more recent decision in *Ortiz* is also ambiguous on the question of whether in-state as well as out-of-state class members are entitled to notice and an opportunity to participate or remove themselves from the class. *See Ortiz*, 119 S. Ct. at 2315. *See generally* Arthur R. Miller and David Crump, *Jurisdiction and Choice of Law in Multistate Class Actions After Phillips Petroleum Co. v. Shutts*, 96 YALE L.J. 1, 52-55 (1986) (observing that *Shutts* can variously be interpreted as a case about "distant forum abuse," or "as a decision protecting the right to opt out for its own sake").

116. It is not clear, for example, where the Due Process Clause compels the contents of FED. R. CIV. P. 26(e), which provides that class actions may not be dismissed or settled without court approval, and also mandates that all class members be afforded notice of a proposed compromise.

117. *See* FED. R. CIV. P. 23(c)(1). This certification requires the court to find that the named plaintiffs are suitable representatives of the class and that the matter is appropriate for resolution by a class action. *See id.* 23(b).

118. *See id.* 23(c)(4).

119. *See id.* 23(d)(2); *see also id.* 23(c)(2) (mandating notice as to 23(b)(3) class actions); *id.* 23(c)(1) (mandating notice of proposed dismissal or settlement).

120. *See id.* 23(d)(2).

121. *See id.* 23(e). For a discussion of the steps courts should follow in determining whether to approve a proposed class settlement, see Mark C. Weber, *A Consent-Based Approach to Class Action Settlement: Improving Amchem Products, Inc. v. Windsor*, 59 OHIO ST. L.J. 1155, 1165-69 (1998).

122. *See Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 809-11 (explaining that because Rule 23 and its state law equivalents safeguard the interests of absent class members by requiring a court to inquire into commonality of claims and the adequacy of representation, mandating notice and opt out, and requiring court approval of settlements, absent class members are less burdened than defendants who are sued in foreign jurisdictions); *see also id.* at 809 ("[U]nlike a defendant in a civil suit, a class-action plaintiff is not required to fend for himself. . . . The court and named plaintiffs protect his interests."); Steven T. O. Cottreau, Note, *The Due Process Right to Opt Out of Class Actions*, 73 N.Y.U. L. REV. 480 (1998).

### 3. Criticisms of Class Actions

Although popular among many, class actions have been criticized widely, particularly of late. One frequent refrain is that class actions serve the interests of plaintiffs' attorneys more than those of plaintiffs themselves.<sup>123</sup> The "coupon" class actions have become symbolic of this concern, with class members receiving a few coupons toward the purchase of a new car, airline ticket, or dog food, while class attorneys reap large fees.<sup>124</sup> Some have highlighted the inherent conflicts of interest that exist between class attorneys and their clients, in that dollars paid in fees will not be available to the class.<sup>125</sup> Class action attorneys also have been accused of driving

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(arguing that due process requires that nonresidents, and in some instances even residents, should have the option to opt out of a class action).

123. See, e.g., John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter Is Not Working*, 42 MD. L. REV. 215, 245 n.72 (1983) (describing class settlement of antitrust suit in which plaintiffs received 5% discount on brokerage services connected with sale of next home, and plaintiffs' counsel received \$350,000); Jill E. Fisch, *Class Action Reform, Qui Tam, and the Role of the Plaintiff*, 60 LAW & CONTEMP. PROBS. 167, 168 (1997) (discussing situation wherein class members receive little or nothing but counsel are compensated handsomely); Susan P. Koniak, *Feasting While the Widow Weeps: Georgine v. Amchem Products, Inc.*, 80 CORNELL L. REV. 1045, 1138-51 (1995) (suggesting that settlement in asbestos class action ill-served the interests of class members, and that the attorneys may have breached their fiduciary duties or engaged in malpractice); Susan P. Koniak & George M. Cohen, *Under Cloak of Settlement*, 82 VA. L. REV. 1051, 1053-54 (1996) (discussing class action settlements in which class lawyers negotiated or requested multimillion dollar fees while class members received minimal in-kind compensation); Note, *In-Kind Class Action Settlements*, 109 HARV. L. REV. 810, 810 nn.3-8 (1996) (providing examples of in-kind class action settlements such as coupons for food processors, groceries, air travel, or bar review courses).

124. See Robert Mauk, *Lawsuit Abuse: Public's Welfare Hurt When Lawyers Help Themselves*, CHARLESTON GAZETTE & DAILY MAIL, Apr. 28, 1997, at A5, available in 1997 WL 7098327 (criticizing coupon settlements); Barry Meier, *Fistfuls of Coupons*, N.Y. TIMES, May 26, 1995, at D1 (observing that while class action plaintiffs who settle receive little, their attorneys walk away with millions); cf. Geoffrey P. Miller & Lori S. Singer, *Nonpecuniary Class Action Settlements*, 60 LAW & CONTEMP. PROBS. 97, 99 (1997) (arguing that not all nonpecuniary settlements are undesirable).

125. See, e.g., Samuel Issacharoff, *Class Action Conflicts*, 30 U.C. DAVIS L. REV. 805 (1997) (arguing that despite their risks, class actions must exist in order to counter problems such as transaction costs and barriers to entry); Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1 (1991) (analyzing consequences of divergent interests between plaintiffs and their attorneys); Sylvia R. Lazos, Note, *Abuse in Plaintiff Class Action Settlements: The Need for a Guardian During Pretrial Settlement Negotiations*, 84 MICH. L. REV. 308 (1985) (arguing that the conflict of interest between plaintiffs' attorneys and class members calls for the appointment of a guardian to protect class members' interests). The fear is that most class members lack a sufficient incentive to

their own litigation.<sup>126</sup>

Given these concerns, some suggest that the costs of class actions exceed their benefits. Professor Christopher Drahozal has argued that it could be rational for individuals to give up their right to proceed in a class action.<sup>127</sup> He suggests that, given the conflicts of interest inherent in class actions and given the high costs of class litigation, individuals might be better off giving up the possible deterrence or other benefits of a class action in return for reduced dispute resolution costs.<sup>128</sup> As well, these criticisms of class actions sometimes have been tied to calls for "tort reform." Corporate defendants and their attorneys claim that class actions are being used to effectively blackmail defendants into paying out unduly high settlements in weak cases, and that these settlements are raising costs for all consumers.<sup>129</sup>

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monitor whether the attorney is adequately representing their interests.

126. *See generally* Common Sense Legal Reforms Act of 1995, H.R. 10, 104th Cong. § 202 (regarding the prevention of lawyer-driven litigation); NEWT GINGRICH ET AL., *CONTRACT WITH AMERICA* 147-55 (1994) (critiquing attorneys' control of litigation). The charge is that plaintiffs' attorneys are not sought out by plaintiffs, but rather that the attorneys use a ready stable of named plaintiffs or advertisements to solicit plaintiffs to support lawsuits envisioned by the attorneys. *See, e.g.*, Fisch, *supra* note 123, at 171 (describing the phenomenon of plaintiffs' attorneys initiating class suits) (citing Stephen E. Frank, *First USA Settles Lawsuit Alleging It Switched Rates*, WALL ST. J., Sept. 4, 1997, at B8); Richard M. Phillips & Gilbert C. Miller, *The Private Securities Litigation Reform Act of 1995: Rebalancing Litigation Risks and Rewards for Class Action Plaintiffs, Defendants and Lawyers*, 51 BUS. LAW. 1009, 1011 (1996) (describing class action attorneys' use of "professional" plaintiffs).

127. *See* Drahozal, *supra* note 5, at 62-63.

128. *See id.*

129. *See, e.g.*, *Securities Litigation Reform: Hearings Before the Subcomm. on Telecomms. and Fin. of the House Comm. on Energy and Commerce*, 103rd Cong. 22 (1994) (statement of Sen. Dodd) ("[M]any cases are filed just to coerce a settlement."); Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 500 (1991) (arguing that most securities suits settle, and that such settlements are not based upon the merits); Peter M. Saporoff, *The Private Securities Litigation Reform Act of 1995: Illusion or Reality*, SA90 ALI-ABA 505 (1996) (contending that securities litigation has a "blackmail effect" that forces "innocent" companies to settle cases); Ralph K. Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers: Raising the Cost of Capital in America*, 42 DUKE L.J. 945, 976 (1993) (concluding that derivative suits and class actions benefit only lawyers and raise the cost of capital in America); *cf.* James Bohn & Stephen Choi, *Fraud in the New-Issues Market: Empirical Evidence on Securities Class Actions*, 144 U. PA. L. REV. 903, 905 (1996) (discussing the "phenomenon" of "frivolous" lawsuits whereby "[o]pportunistic plaintiffs' attorneys continuously monitor securities prices, probing for recent offerings that perform poorly in the aftermarket," then filing suit "[o]nce a security's price suffers a decline sufficient to generate a potential damages award large enough to cover the expected costs of litigation").



Perhaps responding to such criticisms, both courts and Congress have recently placed limitations on class actions. The Supreme Court, in two decisions, has made clear that the normal class action certification requirements may not be relaxed merely because a settlement has already been reached between the class and the defendants.<sup>130</sup> In the securities context, Congress passed the Private Securities Litigation Reform Act of 1995,<sup>131</sup> specifically seeking, *inter alia*, to "transfer control of litigation away from lawyers and back to clients."<sup>132</sup> Other statutory limitations to the class action are under consideration.<sup>133</sup>

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130. See *Ortiz v. Fibreboard Corp.*, 119 S. Ct. 2295, 2316-23 (1999) (overruling certification of settlement class action brought against asbestos manufacturers, because the applicants for certification failed to show adequately that the fund was limited by more than the agreement of the parties, or that conflicts of interest among class members had been addressed adequately in the allocation process); *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 628-29 (1997) (affirming appellate court's reversal of asbestos settlement class action, explaining that class "cannot satisfy the requirements of common issue predominance and adequacy of representation").

131. Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended at 15 U.S.C. § 77z-1 (Supp. IV 1998)). While the Reform Act limited only securities actions brought in federal court, Congress acted quickly to close the perceived loophole allowing plaintiffs to file their securities class actions in state court. See Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (codified at 15 U.S.C. § 77 (Supp. IV 1998)); Rachel Witmer, *Congress Focuses on Closing "Loophole" in 1995 Act Barring Vexatious Class Suits*, 66 U.S.L.W. 2131, 2131 (Sept. 9, 1997).

132. Jill E. Fisch, *Class Action Reform: Lessons from Securities Litigation*, 39 ARIZ. L. REV. 533, 533 (1997). See generally Joint Explanatory Statement of the Committee of Conference—The "Private Securities Litigation Reform Act of 1995," H.R. CONF. REP. NO. 104-369, at 31 (1995), reprinted in 141 CONG. REC. H13692, H13699 (daily ed. Nov. 28, 1995) (discussing "abusive practices committed in private securities litigation includ[ing] . . . manipulation by class action lawyers of the clients whom they purportedly represent"); Joel Seligman, *The Private Securities Reform Act of 1995*, 38 ARIZ. L. REV. 717 (1996) (discussing the enactment of the Reform Act, including the provisions to prevent complete control of the class action by the attorney). The Act took such steps as granting special "lead plaintiff" control to the largest investor in the class (provided she has not played such role too frequently), limiting damages under some circumstances, mandating disclosure of settlement terms to the class, restricting attorney's fees, and limiting the lead plaintiff's share of recovery. The Act also imposes conflict of interest provisions on attorneys and prescribes guidelines for imposition of sanctions for abusive litigation. See Private Securities Litigation Reform Act § 77z-1.

133. One measure, the Class Action Fairness Act of 1999, S. 353, 106th Cong. (1999), was introduced by legislators who suggested it was needed to contend with "unscrupulous lawyers" who settle class actions in a way that provides few benefits for class members and large benefits for themselves. See Susan J. McGolrick, *DOJ Official Tells Senate Subcommittee of Opposition to Class Action Reform Bill*, 67 U.S.L.W. 2694 (May 25, 1999). The Act would allow nearly any class action brought in state court to be transferred to federal court because supporters contend that class actions are being used in state court to abuse hapless defendants in meritless cases, that elected state court judges cannot be relied

In short, while class actions are still tremendously popular in many quarters, they also have their critics. Some see them as essential to secure fair and efficient justice, while, conversely, others see them as undercutting these very goals.

### *C. Pros and Cons of Classwide Arbitrations*

At first blush the hybrid variously known as a “classwide arbitration” or an “arbitral class action” may seem to be the ideal way to have one’s cake and eat it too—that is, to reconcile the policies favoring both arbitration and class action. As will be seen, however, participants, courts, and commentators differ sharply regarding the desirability and feasibility of such an amalgam.<sup>134</sup> If the hybrid proves unworkable or undesirable, then one must seriously consider the other two major alternatives: allowing companies to eliminate class actions altogether, or permitting class actions to be handled in court.

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upon to stop this phenomenon, and that federal courts should be empowered to remedy the situation. *See Congress, Judicial Conference Mull Changes to Class Action, Mass Tort Rules*, 67 U.S.L.W. 2723 (June 8, 1999). The Senate Bill also would attempt to limit recoverable attorney fees and would require very detailed notice to class members in the event of a proposed class settlement. The bill was reported by the Judiciary Committee to the Senate on July 27, 2000. *See* S. 353, 106th Cong. (1999), WL 1999 US S.B. 353 (SN). Another measure, the Interstate Class Action Jurisdiction Act of 1999, H.R. 1875, 106th Cong., is somewhat more limited in scope. It would essentially allow for expanded removal of class actions to federal court. This Act was passed by the House on September 23, 1999, and awaits consideration by the Senate. *See Civil Procedure—Class Actions: House Approves Class Action Measure Moving Many State Suits to Federal Court*, 68 U.S.L.W. 2168 (Sept. 28, 1999). By broadening federal courts’ jurisdiction to hear class actions, the Act potentially would prevent state courts from hearing class actions that did not meet the stricter federal standards. Also, serious revisions to Rule 23 itself were considered but ultimately rejected within the last few years. *See Proposed Amendments to the Federal Rules of Civil Procedure, Rule 23, Class Actions*, 167 F.R.D. 559 (1996) (proposing that the “practical ability of individual class members to pursue their claims without class certification” and the question of “whether the probable relief to individual class members justifies the costs and burdens of class litigation” be made elements considered in Rule 23(b)(3)). The changes proposed by the Advisory Committee on Civil Rules were published and considered at public hearings but ultimately withdrawn by the Committee, which concluded further study was needed. *See Committee on Rules of Practice and Procedure, Minutes of the Meeting of June 19-20, 1997*, 1997 WL 1056244, at \*12-14 (J.C.U.S.); *see also* Edward H. Cooper, *Rule 23: Challenges to the Rulemaking Process*, 71 N.Y.U. L. REV. 13 (1996) (cautioning against making substantial revisions to Rule 23 before learning more about how class actions are currently being handled); Fisch, *supra* note 123 at 176-83 (summarizing various proposed class action reforms).

134. *See infra* notes 138-95 and accompanying text.

This discussion of classwide arbitrations will draw upon a few real life experiences from California,<sup>135</sup> but also will address hypothetical uses of classwide arbitration. Only a few courts in California and Pennsylvania have, at least in reported decisions, ordered or allowed arbitrations to proceed on a classwide basis, and several of these cases settled before classwide arbitration could actually take place.<sup>136</sup> Moreover, this author has uncovered just one instance in which an arbitrator independently ordered a dispute to be resolved as a class action.<sup>137</sup>

### 1. *Purported Virtues of Classwide Arbitration*

The California Court of Appeals, in *Keating v. Superior Court*,<sup>138</sup> seems to have been the first court or commentator to consider seriously the desirability and feasibility of a classwide arbitration. Its conclusion, that there was “no insurmountable obstacle” to such

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135. I was able to gain this information only by doing some academic detective work, as it seems no prior articles have discussed the actual handling of arbitral class actions. Other commentators have had similar difficulty finding examples of classwide arbitrations. See C. Evan Stewart, *Are Class Actions Appropriate in Arbitrations?*, N.Y. L.J., June 13, 1991, at 5 (stating “in no case to date, where a court has embraced the ‘hybrid’ approach, has anything actually taken place or been done beyond the certification decision”). In fact, it is noteworthy that the two main law review articles advocating the use of the hybrid approach were written by law students, who presumably had no personal experience in litigation, much less in handling classwide arbitrations. See *Quagmire*, *supra* note 41; Waltcher, *supra* note 41. Nor do either of these notes discuss any claims that were actually handled as classwide arbitrations.

136. See *infra* notes 138-47 and accompanying text. It should be noted that several governments also have adopted arbitration for resolving certain local disputes, and that their rules occasionally allow for class actions. See *infra* note 288 and accompanying text.

137. A recent press report discussed a case in which an arbitrator purportedly awarded more than \$20 million to a class of customers who had borrowed money from Conseco Financial Inc. See Douglas J. Fisher, *Conseco Finance to Pay \$20M in S.C.*, AP ONLINE, July 26, 2000, available at 2000 WL 24550570. Apparently, the class action was ordered by the arbitrator. See Kaplinsky, *Arbitration and Class Actions*, *supra* note 10, at 632-33 (discussing ruling of “renegade” arbitrator who ordered class action). The company reportedly is contending that the arbitrator lacked jurisdiction to consider a class action. See Fisher, *supra*. Other than this case, I did not find any reports of such orders in any articles, and also uncovered none in the course of conversations with Professor Tom Stipanowich (co-author of a leading arbitration treatise), Dean Tim Heinsz (Reporter for the Revised Uniform Arbitration Act), Gene Truncellito of AAA, and Bill Baten of JAMS.

138. 167 Cal. Rptr. 481 (Cal. Ct. App. 1980) (concluding franchisees’ claims against franchisor were arbitrable, and that trial court erred in failing to consider class action issues before sending dispute to arbitration), *vacated*, 645 P.2d 1192 (Cal. 1982), *rev’d on other grounds*, *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1984).

a device,<sup>139</sup> is typical of the reaction of many to the technique. Without raving about the benefits of classwide arbitration, these courts and commentators in essence state that the hybrid can best preserve the benefits of both the class action and the arbitration;<sup>140</sup> that logistically the hybrid is workable,<sup>141</sup> particularly so long as the court determines the major class action issues;<sup>142</sup> and that while perhaps not ideal, the hybrid is superior to either barring arbitration or barring classwide relief.<sup>143</sup>

Significantly, all of the supportive court decisions call upon the court to play an extremely active role in resolving the class action issues relevant to the classwide arbitration. For example, the *Keating* court stated:

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139. See *Keating*, 167 Cal. Rptr. at 492 ("In an appropriate case, such a procedure undoubtedly would be the fairest and most efficient way of resolving the parties' dispute. The initial determinations regarding certification and notice will not unduly burden the arbitration because those matters must be resolved by the trial court before arbitration begins.").

140. For example, the California Supreme Court in *Keating* stated:

This court has repeatedly emphasized the importance of the class action device for vindicating rights asserted by large groups of persons. We have observed that the class suit "both eliminates the possibility of repetitious litigation and provides small claimants with a method of obtaining redress for claims which would otherwise be too small to warrant individual litigation."

*Keating*, 645 P.2d at 1206 (quoting *Richmond v. Dart Indus., Inc.*, 629 P.2d 23 (Cal. 1981)); see also *Quagmire*, *supra* note 41, at 787-96 (summarizing the benefits of both class actions and arbitration). In *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315 (Cal. Ct. App. 1986), the California Court of Appeals reiterated this praise for class actions and also praised arbitration, which it stated "is generally considered to be a mutually advantageous process, providing for resolution of disputes in a presumptively less costly, more expeditious, and more private manner by an impartial person or persons typically selected by the parties themselves." *Id.* at 320 (quoting *Keating*, 645 P.2d at 1198).

141. See *Keating*, 645 P.2d at 1209.

142. See *infra* notes 438-71 and accompanying text (discussing what steps would be necessary for classwide arbitration to comply with due process).

143. The *Izzi* court was particularly damning with its faint praise, recognizing that the argument that class actions and arbitration are incompatible has considerable support, entertaining some thought that the two techniques might possibly be irreconcilable, but ultimately concluding it was bound by the *Keating* precedent to accept the possibility of the hybrid. See *Izzi*, 231 Cal. Rptr. at 321; see also *Dickler v. Shearson Lehman Hutton, Inc.*, 596 A.2d 860, 867 (Pa. Super. 1991), in which the court stated:

Given the three paths down which this litigation can be directed—compelled individual arbitration, class action in a court of law, or compelled classwide arbitration—the last choice best serves the dual interest of respecting and advancing contractually agreed upon arbitration agreements while allowing individuals who believe they have been wronged to have an economically feasible route to get injunctive relief from large institutions employing adhesion contracts.

Without doubt a judicially ordered classwide arbitration would entail a greater degree of judicial involvement than is normally associated with arbitration, ideally "a complete proceeding, without resort to court facilities." . . . A good deal of care, and ingenuity, would be required to avoid judicial intrusion upon the merits of the dispute, or upon the conduct of the proceedings themselves and to minimize complexity, costs, or delay.<sup>144</sup>

The court went on to explain:

The court would have to make initial determinations regarding certification and notice to the class, and if classwide arbitration proceeds it may be called upon to exercise a measure of external supervision in order to safeguard the rights of absent class members to adequate representation and in the event of dismissal or settlement.<sup>145</sup>

In *Dickler v. Shearson Lehman Hutton, Inc.*,<sup>146</sup> the Pennsylvania Superior Court similarly stated that the trial court would not only need to certify the class, insure that proper notice is provided, and review any proposed settlement, but also deal with such eventualities as conflict among multiple class representatives as to selection of arbitrators.<sup>147</sup>

The attorneys who have participated in hybrid class action arbitrations report that courts have, in fact, retained the responsibility for resolving all of the major class action issues. In every class action arbitration as to which this author was able to obtain information,<sup>148</sup> it was the court that decided whether the matter could proceed as a class action, defined the class, and approved the

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144. *Keating*, 645 P.2d at 1209 (citations omitted) (citing *Quagmire*, *supra* note 41, at 789).

145. *Id.* at 1209.

146. 596 A.2d 860 (Pa. Super. 1991).

147. *See id.* at 866.

148. I made an extensive effort to locate and speak to attorneys who had been involved with arbitral class actions. I not only contacted attorneys who, according to published decisions, represented parties in class actions that were ordered to arbitration, but I also made calls to numerous arbitration experts and organizations in an attempt to identify participants in nonpublished cases. Still, after all this, I found just a handful of attorneys, which I believe is reflective of the fact that very few arbitrations have been handled as class actions.

notice to the class.<sup>149</sup> In the instances in which the suits settled, the court approved the settlement.<sup>150</sup> In several cases, the court

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149. Attorney Gordon Bosserman represented Blue Cross in *Blue Cross of California v. Superior Court*, 78 Cal. Rptr. 2d 779 (Cal. App. 1998), cert. denied, 119 S. Ct. 2338 (1999), and in an unpublished case, *Harder v. Blue Cross*. He reported that in the *Superior Court* case, the class action dispute was ordered to arbitration. The parties then conducted discovery under the supervision of the judge. Prior to either class certification or selection of arbitrators, the dispute was settled. In *Harder*, arbitrators were selected only after the court had handled class certification and notice issues. Telephone Interview with Gordon Bosserman (Oct. 11, 1999).

Attorney John F. Wells represented the plaintiff-franchisees in *Keating*, 645 P.2d 1192 (Cal. 1982). He reported that the judge decided all the class issues, including defining the class and determining the contents of the notice. The court also decided an important evidentiary issue, in connection with defining the class, and the arbitrators refused to revisit the ruling. Certain other motions were decided by the arbitrators, subject to appeal to the court. Telephone Interview with John F. Wells (Sept. 29, 1999).

Jon A. Shoenberger represented the plaintiffs in *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315 (Cal. Ct. App. 1986). He reported that the trial judge made all of the orders to define the class and to provide notice to class members, retained jurisdiction over all discovery matters, and handled all pleadings such as motions to dismiss and motions for summary judgment. Arbitrators were not selected until the point at which the dispute was ready to be tried. Once the arbitrators issued an award, the court retained jurisdiction to distribute the money and approve a final accounting. The court also ruled on plaintiffs' petition for attorney fees. Telephone Interview with Jon A. Shoenberger (Sept. 22, 1999).

Steven J. Nelson represented the plaintiffs in *Gainey v. Occidental Land Research*, 231 Cal. Rptr. 249 (Cal. Ct. App. 1986). Although the merits of the dispute were handled by the arbitrators, the judge decided the class certification and notice issues. Nelson also opined that if the plaintiffs had prevailed, it would have been the responsibility of the court, not the arbitrators, to divide up the winnings. Telephone Interview with Steven J. Nelson (Sept. 13, 1999).

Steven G. Zieff represented the plaintiffs in *Kerr v. Snap-On, Inc.*, No. CV758116 (Cal. Super. 1997), a wage and hour class action brought under California law. Although the court ordered that the dispute be resolved through class action arbitration, the court itself handled all issues relating to class certification, including relevant discovery, and also supervised and approved the class notice. The American Arbitration Association handled opt-outs from the class. Telephone Interview with Steven G. Zieff (Aug. 25, 1999). Zieff also supplied this author with an order from the court which authorized the classwide arbitration. The order stated that the court would retain jurisdiction over disputes concerning issues of class notice, final approval of class settlement, enforcement of the arbitrators' decision, and other issues that may be appropriate for resolution by the court. Letter from Steven G. Zieff to Jean R. Sternlight (Sept. 20, 1999) (on file with author).

150. Telephone Interview with John F. Wells (Sept. 29, 1999) (observing that the *Keating* case was eventually settled after the arbitrators had made factual findings, and that the settlement was approved by the court); Telephone Interview with Steven G. Zieff (Aug. 25, 1999) (stating that once the dispute settled, the court approved the process that would be used to assess its fairness, and that after the arbitrators held a substantive fairness hearing, the court itself held its own hearing as to which class members were provided notice); see also Letter from Steven G. Zieff to Jean R. Sternlight (Sept. 20, 1999) (on file with author) (stating that the settlement was approved "following a fairness hearing under procedures approved by the [court]").

assumed even more responsibilities, such as resolving all discovery issues and motions leading up to the point of trial.<sup>151</sup>

In accord with the decisions discussed above, student commentator Daniel Waltcher contends that courts would have to play a very active role in deciding "class" issues.<sup>152</sup> Without discussion, he assumes that the court, rather than the arbitrator, will make the initial certification decision.<sup>153</sup> He then asserts that due process also requires the court to play some kind of ongoing role in ensuring adequacy of representation. He concludes that the most permissible way to do so would be for the arbitrator to handle the post-certification class issues without allowing interlocutory appeals to the court, but then to allow challenges to adequacy of representation after the arbitrators issued their decision.<sup>154</sup>

Not all supporters of the hybrid advocate heightened judicial involvement. Another student note suggests that courts should play

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151. *E.g.*, Telephone Interview with Jon A. Shoenberger (Sept. 22, 1999) (discussing procedure used in *Izzi v. Mesquite Country Club*). In this action, the arbitrators were not even selected until all of the pretrial motions had been resolved, all of the discovery had been completed, and only the trial remained.

152. Waltcher suggests that this active role is necessary in order to protect due process interests. *See* Waltcher, *supra* note 41, at 401-02 (explaining that because the majority of class action participants are absent from the classwide arbitral proceedings, due process concerns are raised as to notice and adequacy of representation). Attorney James Sturdevant similarly suggests that courts need to play an active role in supervising the class in order to comport with due process:

Under the special rules and procedures established by the courts for cases that are filed as class actions and that are also subject to arbitration, the court may compel arbitration of the merits of the action, but must retain jurisdiction to allow class discovery, to rule on the plaintiffs' class certification motion, to order class notice, and to supervise the proceedings as otherwise necessary to protect the due process rights of absent class members.

James C. Sturdevant, *Current Issues in Arbitration, Recent Developments in Deposit/Retail Banking*, 1114 PRACTISING L. INST. 846, 848 (1999).

153. *See* Waltcher, *supra* note 41, at 403.

154. *See id.* at 403-05. Waltcher rejects the possibility of interlocutory appeals as too inefficient, and rejects the elimination of court review as violative of due process. He states:

[D]ue process issues connected with class action aspects of classwide arbitration are simply too important to be relegated to arbitrators. While the panelists in a 10b-5 arbitration may be experts in securities regulation, they are not experts in the constitutional concerns attached to class certification. As a result, they cannot ensure the fairness of the proceedings to all absent class members.

*Id.* at 404-05. Waltcher does not address specifically who would review the adequacy of a proposed class settlement, nor who would deal with issues such as propriety of communication with class members or division of a class into subclasses.

a far more limited role in classwide arbitration.<sup>155</sup> This commentator prefers that the certification determination be made by the arbitrator, with court review only following the termination of the arbitration.<sup>156</sup> This commentator further envisions that while class members would be afforded individual notice<sup>157</sup> and provided a right to appear in certain situations,<sup>158</sup> the matter would not differ too much from a typical arbitration. The arbitration would remain private,<sup>159</sup> and if too many class members disagreed on the choice of arbitrator or sought to participate directly, the matter would be denied certification<sup>160</sup> or those persons would have to opt out of the class.<sup>161</sup> The Note suggests that the arbitral model would be sufficient to protect any due process property interests,<sup>162</sup> and that "arbitrators can deal with potential abuses as effectively as can courts."<sup>163</sup>

In short, none see arbitral class actions as a panacea,<sup>164</sup> and

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155. See *Quagmire*, *supra* note 41, at 806-09.

156. See *id.* "If the arbitrator decides the class arbitration issue and if that decision is not immediately reviewable by the court, arbitral independence will not be compromised." *Id.* at 809. The author is, however, open to court determination of certification or more immediate review. See *id.* at 806.

157. See *id.* at 804.

158. See *id.*

159. See *id.*

160. See *id.* at 800.

161. See *id.* at 799.

162. See *id.* at 800-04. The author expresses uncertainty as to whether due process would attach to private arbitral proceedings, see *id.* at 800-01, but concludes that assuming due process were required, "the procedural flexibility inherent in the arbitration mechanism would prove to be an asset." *Id.* at 803.

163. *Id.* at 811. The Note's author does not, however, provide any detailed analysis regarding how the court or arbitrator would ensure ongoing adequacy of representation, nor who would rule on the adequacy of any settlement.

164. Blue Cross attorney Gordon Bosserman stated that the company decides whether to compel arbitration in a particular dispute on a case-by-case basis. Stating that he saw no real cost difference between class action litigation and arbitration, Bosserman explained that the company weighs its interest in avoiding a jury trial against its interest in preserving full appellate rights. Telephone Interview with Gordon Bosserman (Oct. 11, 1999). In a separate interview, Jon Schoenberger noted that the arbitral class action was little different from a litigated class action, except that arbitrators replaced a judge, and that the parties were provided with the convenience of certain dates for the trial. He further noted that class action issues are generally poorly suited for arbitration. Telephone Interview with Jon Schoenberger (Sept. 22, 1999). Several of the interviewed attorneys stated that the arbitral class action seemed to work reasonably efficiently in their particular cases, but did not suggest that the process in general was preferable to class action litigation. Telephone



opinions differ on precisely how arbitral class actions can or should be handled. Summing up its less than enthusiastic endorsement of classwide arbitration, the California Supreme Court stated:

Classwide arbitration, as Sir Winston Churchill said of democracy, must be evaluated, not in relation to some ideal but in relation to its alternatives. If the alternative in a case of this sort is to force hundreds of individual franchisees each to litigate its cause with Southland in a separate arbitral forum, then the prospect of classwide arbitration, for all its difficulties, may offer a better, more efficient, and fairer solution.<sup>165</sup>

## *2. Purported Failings of Classwide Arbitration*

The hybrid arbitral class action has been subjected to criticism on several fronts. In the securities industry, both self-regulated organizations ("SROs") and the SEC have concluded that the arbitral class action is not an acceptable means of dispute resolution.<sup>166</sup> Also, several academics and dissenting or concurring judges have concluded that the technique is inherently flawed, raising both logistical and due process concerns.<sup>167</sup> Finally, several

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Interview with Steven J. Nelson (Sept. 13, 1999); Telephone Interview with John F. Wells (July 29, 1999); Telephone Interview with Steven G. Zieff (Aug. 25, 1999).

165. *Keating v. Superior Court*, 645 P.2d 1192, 1209 (Cal. 1982). This quote is cited approvingly by one commentator. See Waltcher, *supra* note 41, at 403; see also Lewis v. Prudential Bache Sec., Inc., 225 Cal. Rptr. 69, 75 (Cal. Ct. App. 1986) ("[T]he alternative to class arbitration here is to force each Prudential customer to individually arbitrate claims, most of which probably cannot justify the time and money required to prove."); Dickler v. Shearson Lehman Hutton, Inc., 596 A.2d 860, 867 (Pa. Super 1991) ("The availability of class suits in arbitration proceedings precludes either party from forcing the other to litigate in a position less advantageous than that for which they contracted" by either defeating arbitration altogether or "forc[ing] individuals already straitjacket[ed] by an industry-wide practice of arbitration agreements to fight alleged improprieties at an exorbitant economic cost.").

166. See *infra* notes 169-78 and accompanying text.

167. See *Keating*, 645 P.2d at 1210 (Richardson, J., concurring and dissenting); *Harris v. Shearson Hayden Stone, Inc.*, 441 N.Y.S.2d 70, 98 (N.Y. App. Div. 1981) (Bloom, J., dissenting); Stephen H. Kupperman & George C. Freeman III, *Selected Topics in Securities Arbitration: Rule 15c2-2, Fraud, Duress, Unconscionability, Waiver, Class Arbitration, Punitive Damages, Rights of Review, and Attorneys' Fees and Costs*, 65 TUL. L. REV. 1547 (1991); Stewart, *supra* note 135, at 5; Elizabeth P. Allor, Note, *Keating v. Superior Court: Oppressive Arbitration Clauses in Adhesion Contracts*, 71 CAL. L. REV. 1239 (1983).

attorneys who have actually participated in classwide arbitrations have found that the procedure, at least as used to date, differs very little from litigation and thus offers few, if any, advantages.<sup>168</sup>

*a. The Securities Industry's Rejection of Classwide Arbitration*

Although the securities industry has long been a major proponent and advocate of binding arbitration in general,<sup>169</sup> its policies foreclose arbitration of class actions and instead allow investors to litigate such claims.<sup>170</sup> In adopting the exclusion, both the SROs and

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168. *E.g.*, Telephone Interview with Gordon Bosserman (Oct. 11, 1999) (reporting no real difference in terms of cost or speed between the two processes, but observing that arbitration can be desirable in order to avoid a jury trial); Telephone Interview with Steven J. Nelson (Sept. 13, 1999) (stating that while he saw no particular problems in his case, which was largely documentary, he could imagine that arbitral class actions would sometimes be problematic); Telephone Interview with Jon A. Shoenberger (Sept. 22, 1999) (reporting no significant efficiency differences between litigated and arbitrated class actions, and noting that the only difference was a final hearing before arbitrators instead of before a judge; also concluding that although arbitral class action worked fine in the *Izzi* case, the mechanism "doesn't make a lot of sense"); Telephone Interview with John F. Wells (Sept. 29, 1999) (stating that he was very pleased with the result of arbitral class action in which the judge first decided major class issues, and further observing that the hearing was probably more thorough before arbitrators than it would have been before a court, but failing to set out efficiency advantages); Telephone Interview with Steven G. Zieff (Aug. 25, 1999) (observing that he was pleased with the process and result, but failing to identify any major efficiency or other savings).

169. For over one hundred years, so-called self-regulatory organizations ("SROs") such as the New York Stock Exchange have established arbitration programs for resolution of consumer claims against brokerages. See PHILIP J. HOBLIN, *SECURITIES ARBITRATION: PROCEDURES, STRATEGIES, CASES 1-2* (2d ed. 1992); Constantine N. Katsoris, *SICA: The First Twenty Years*, 23 *FORDHAM URB. L.J.* 483, 485 (1996); Norman S. Poser, *When ADR Eclipses Litigation: The Brave New World of Securities Arbitration*, 59 *BROOK. L. REV.* 1095, 1103 (1993). Moreover, the Supreme Court has explicitly upheld the use of arbitration with respect to both customer and employee claims in the securities context. See *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (holding that employee who had agreed to be bound by arbitration rules of exchange could be required to arbitrate claim under Age Discrimination in Employment Act); *Rodriguez de Quijas v. Shearson/American Express*, 490 U.S. 477 (1989) (upholding use of pre-dispute arbitration agreements with respect to claims brought under the Securities Act of 1933); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987) (ruling that companies could compel arbitration of claims brought under the Securities Exchange Act of 1934). These decisions reflected a reversal of *Wilko v. Swan*, 346 U.S. 427 (1953), which had refused to enforce pre-dispute arbitration as to claims brought under the 1933 Act.

170. The history of excluding arbitration of class actions can be traced to 1988, when SEC Chair David S. Ruder asked all the SROs "to consider adopting procedures that would give investors access to the courts in appropriate cases, including class actions." Self-Regulatory

the SEC foreclosed the possibility that companies might be permitted to deprive customers of the class action device simultaneously in both litigation and arbitration forums.<sup>171</sup> The rule barring arbitral class actions was unanimously adopted in 1992 by the Securities Industry Conference on Arbitration ("SICA").<sup>172</sup>

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Organizations; Proposed Rule Change by National Association of Securities Dealers, Inc., Relating to Improvements in the NASD Code of Arbitration Procedure, 57 Fed. Reg. 30,519, 30,520 (1992).

171. While this alternative was not discussed in detail, both the SEC and NASD rejected it in responding to a letter submitted during the comment period. The SEC explained that although a letter from Stone, Pigman, Walther, Wittman & Hutchinson stated that it favored the NASD rule proposal, "in direct opposition to the rule, Stone, Pigman suggested that the NASD and Commission both should adopt a policy that would provide that any claim governed by an arbitration agreement should be arbitrated pursuant to the terms of the agreement, regardless of whether the claim is subject to the class action." Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. 52,659, 52,660 (1992). Rejecting this interpretation, "the NASD stated that the proposed rule change will ensure that class actions and the claims of individual class members are not eligible for arbitration at the NASD, regardless of any previously existing agreement to arbitrate." *Id.* The exception, as noted in the rule itself, is that an investor may individually arbitrate a claim once the court has refused to certify the class or once the investor has chosen not to participate in the class action. *See id.* The SEC similarly stated: "[t]he comments of Stone, Pigman misconstrue the intent of the NASD proposal. As approved, the rule will exclude all class actions from arbitration at the NASD." *Id.* at 52,661. Interestingly, the drafters of the Stone, Pigman letter were Stephen Kupperman and George C. Freeman III, who also wrote an article arguing that persons who agree to arbitration should be foreclosed from participating in class action litigation or arbitration. *See Kupperman & Freeman, supra* note 167, at 1583-84 ("In light of the Supreme Court's trend away from judicial activism and its embracement of literalism and the concept of sanctity of contracts, the arbitration process should prevail."). The authors suggest that "even without the class action device, arbitration provides a reasonable forum for persons with small claims." *Id.* at 1591. The authors would, however, permit arbitration tribunals to "fashion their own rules concerning classwide actions, although the ultimate wisdom of any rule permitting class arbitration is questionable." *Id.* at 1592.

172. Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions from Arbitration Proceedings, 57 Fed. Reg. at 52,660. The NASD's Rule 10301(d) and the NYSE's Rule 600(d) are virtually identical. The NASD Rule states:

(d) Class Action Claims.

...

(2) Any claim filed by a member or members of a putative or certified class action is also ineligible for arbitration at the Association if the claim is encompassed by a putative or certified class action filed in federal or state court, or is ordered by a court to an arbitral forum not sponsored by a self-regulatory organization for classwide arbitration. However, such claims shall be eligible for arbitration in accordance with paragraph (a) or pursuant to the parties' contractual agreement, if any, if a claimant demonstrates that it has elected not to participate in the putative or certified class action or, if applicable, has complied with any conditions for withdrawing from the class prescribed by the court.

...

One by one the various individual brokerages secured SEC approval for the same rule.<sup>173</sup>

The SEC opposed arbitration of class actions because whereas courts already had developed rules for handling class actions, arbitral organizations had not. It found that allowing arbitration of class actions would be wasteful and duplicative.<sup>174</sup> In approving

(3) No member or associated person shall seek to enforce any agreement to arbitrate against a customer, other member or person associated with a member who has initiated in court a putative class action or is a member of a putative or certified class with respect to any claims encompassed by the class action unless and until: (A) the class certification is denied; (B) the class is decertified; (C) the customer, other member or person associated with a member is excluded from the class by the court; or (D) the customer, other member or person associated with a member elects not to participate in the putative or certified class action or, if applicable, has complied with any conditions for withdrawing from the class prescribed by the court.

NASD MANUAL & NOTICES TO MEMBERS, CODE OF ARBITRATION PROCEDURE § 10301(d) (visited Apr. 4, 2000) <<http://www.nasd.com>>. The NYSE Rule similarly provides that “[a]ny claim filed by a member . . . of a putative or certified class action is also ineligible for arbitration at the New York Stock Exchange.” NYSE, *Constitution of the New York Stock Exchange, Inc., Article IX*, Rule 600(d) (visited Aug. 25, 2000) <<http://www.nyse.com/about/about/html>> [hereinafter NYSE Rule 600(d)]. For a discussion of the complex self-governance structure of the securities industry, see generally Katsoris, *supra* note 169.

173. Each exchange first published a proposed rule change for public comment and then secured SEC approval for the requisite changes to its internal rules and handbooks. See Order Granting Approval to Proposed Rule Change Relating to the Exchange’s Arbitration Rules, 61 Fed. Reg. 2849 (1996); Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Exclusion of Class Action Claims from Arbitration, 59 Fed. Reg. 4299 (1994) (clarifying that exclusion applies to actions brought by employees, as well as by customers); Order Approving Proposed Rule Change by American Stock Exchange, Inc. Relating to Arbitration, 58 Fed. Reg. 48,680 (1993); Order Granting Approval to Proposed Rule Change Relating to Amendments to Rule 12, Arbitration, of the Rules of the PSE, 58 Fed. Reg. 42,588 (1993); Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions from Arbitration Proceedings, 57 Fed. Reg. at 52,659; Proposed Rule Change by National Association of Securities Dealers, Inc., Relating to Improvements in the NASD Code of Arbitration Procedure, 57 Fed. Reg. 30,519 (1992); see also NASD MANUAL & NOTICES TO MEMBERS, CODE OF ARBITRATION PROCEDURE § 10301(d), *supra* note 172 (stating that a “claim submitted as a class action shall not be eligible for arbitration”); NASD, Rules of Fair Practice, Art. III, § 21(f)(6), (visited Jan. 27, 2000) <<http://www.nasd.com>>

(noting that all agreements shall include a statement that “No person shall bring a putative or certified class action to arbitration, nor seek to enforce any pre-dispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class who has not opted out of the class with respect to any claims encompassed by the putative class action [until certification is denied or customer opts out or is excluded]”).

NYSE Rule 600(d), *supra* note 172 (stating that a claim submitted as a class action is not eligible for arbitration at the NYSE).

174. It stated:

later versions of the exclusion of class actions from arbitration, the SEC frequently reiterated that it "is an important initiative to protect investors and the public interest."<sup>175</sup> Interestingly, the SEC chose not to opine on whether the exclusion was also mandated by the Due Process Clause of the Constitution, nor on whether arbitrators lack the experience and qualifications necessary to decide class action issues,<sup>176</sup> although both arguments had been offered during the notice and comment period.<sup>177</sup> Meanwhile, the

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NASD believes, and the Commission agrees, that the judicial system has already developed the procedures to manage class action claims. Entertaining such claims through arbitration at the NASD would be difficult, duplicative and wasteful. . . . The Commission agrees with the NASD's position that, in all cases, class actions are better handled by the courts and that investors should have access to the courts to resolve class actions efficiently. In the past, individuals who attempted to certify class actions in litigation were subject to the enforcement of their separate arbitration contracts by their broker-dealers. Without access of class actions in paragraph cases, both investors and broker-dealers have been put to the expense of wasteful, duplicative litigation. The new rule ends this practice.

....

Over the years of the evolution of class action litigation, the courts have developed the procedures and expertise for managing class actions. Duplication of the often complex procedural safeguards necessary for these hybrid lawsuits is unnecessary. The Commission believes that investor access to the courts should be preserved for class actions and that the rule change approved herein provides a sound procedure for the management of class actions arising out of securities industry disputes between NASD members and their customers.

Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. at 52,661.

175. Order Approving Proposed Rule Change by American Stock Exchange, Inc. Relating to Arbitration, 58 Fed. Reg. at 48,681; *see also* Self-Regulatory Organizations; Pacific Stock Exchange, Inc., Order Granting Approval to Proposed Rule Change Relating to Amendments to Rule 12, Arbitration, of the Rules of the PSE, 58 Fed. Reg. 42,588, 42,589-90 (1993) (observing that the measure "should increase customer confidence in the markets and promote the efficient resolution of disputes for both investors and broker-dealers").

176. The SEC simply set out both positions without choosing a side. *See* Arbitration Proceedings, 57 Fed. Reg. at 52,660-61.

177. The comments were offered by Nikko Securities Co. International, which stated that it favored the class action exclusion because

(i) The procedures mandated by rule 23 of the Federal Rules of Civil Procedure have due process implications and require extensive judicial involvement throughout the entire class action process; (ii) class actions in arbitration proceedings would be contrary to the arbitration policy goal of having a prompt resolution of disputes; and (iii) arbitrators do not have the background, training or expertise to address class actions.

Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. at 52,660. The author of the comment letter was Evan Stewart, who also penned an article criticizing classwide arbitration. *See* Stewart, *supra*

NASD rejected both the due process and the inexperience arguments, but nonetheless agreed that class actions would be better handled by the courts than by arbitrators.<sup>178</sup>

*b. Logistical Concerns*

Outside the securities context, critics of classwide arbitration have similarly focused on logistics.<sup>179</sup> One logistical difficulty deals with who chooses the arbitrator, and when this choice is made. Unlike with individual arbitrations, where a purported advantage is that all disputants can play a role in selecting the arbitrator, this advantage is not feasible in the class setting. Rather, the arbitrators would presumably be selected by the named plaintiffs or by class counsel, acting as agents for the plaintiff class, and by defendant or its counsel. In this event, one of the purported virtues of arbitration is lost, in that the individual disputants have not directly selected the decisionmaker. In addition, it would be inappropriate to allow the named plaintiffs or class counsel to make such a choice unless and until the class was certified.

More generally, critics of classwide arbitration have argued that the process necessarily will be awkward, inconvenient, and perhaps inefficient because of the need for extensive coordination between the judge and the arbitrators in a classwide arbitration.<sup>180</sup> This

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note 135.

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[T]he NASD does not agree that the arbitration process would provide less due process protection than the courts. Similarly, the NASD did not believe that arbitrators lack the training and expertise to deal with class action disputes. Finally, the NASD stated that it did not propose the ban on class actions in arbitration proceedings because they might be more time consuming, but rather because it believes that they are better handled by the judicial system.

Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. at 52,660.

179. As will be discussed, these logistical concerns are closely tied to due process concerns. See *infra* text accompanying notes 191-95.

180. Commentator Allor stated that "when conducted on a classwide basis, arbitration is unlikely to remain inexpensive and efficient. It will increase the burden on the judge and divide authority between the judge and the arbitrator. . . . [T]he division of authority over the proceedings between the judge and the arbitrator would entail many procedural complications." Allor, *supra* note 167, at 1253. Justice Richardson of the California Supreme Court stated: "class procedures would tend to make arbitration inefficient instead of efficient, lengthy instead of expeditious, and procedural instead of informal. . . . In my view, because

criticism is premised on the idea that the Due Process Clause, or perhaps other policy concerns, will require judges to play a far more active role in a classwide arbitration than they would play in an individual arbitration. Specifically, the critics suggest that because the court must be heavily involved in certification,<sup>181</sup> including relevant discovery,<sup>182</sup> supervision of notice,<sup>183</sup> ongoing monitoring of the adequacy of class representation,<sup>184</sup> providing notice of and

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of the complications resulting from continued judicial monitoring, the imposition of class action procedures on the arbitration process would be self-defeating." *Keating v. Superior Court*, 645 P.2d 1192, 1215-16 (Cal. 1982) (Richardson, J., concurring and dissenting). Similarly, Judge Bloom concluded:

Arbitration does not lend itself to the many subsidiary proceedings incident to an ongoing class action, e.g. determination of whether class action status should be granted, definition of the class, determination of the nature and kind of notice and by whom it should be sent, provision for opting out, etc.

*Harris v. Shearson Hayden Stone, Inc.*, 441 N.Y.S.2d 70, 79 (N.Y. App. Div. 1981) (Bloom, J., dissenting).

181. Attorney C. Evan Stewart explained that the court's determination of certification must be based on a "rigorous analysis" of whether the requirements of Rule 23 have been met. *See Stewart, supra* note 135, at 5 (quoting *General Telephone Co. v. Falcon*, 457 U.S. 147, 161 (1982)). Stewart cited a number of additional cases to support his point that parties seeking certification must satisfy a difficult legal burden: *Rosini v. Ogilvy & Mather Inc.*, 798 F.2d 590, 597 (2d Cir. 1986); *Roby v. St. Louis Southwestern Ry. Co.*, 775 F.2d 959, 962 (8th Cir. 1985); *Walker v. Jim Dandy*, 747 F.2d 1360, 1364-65 (11th Cir. 1985). *See Stewart, supra* note 124, at 6 n.7; *see also Keating*, 645 P.2d at 1215 (Richardson, J., concurring and dissenting) (citations omitted) (explaining that to determine whether class proceedings are appropriate "a court must carefully evaluate the nature of the proof that will be presented by the parties, and the parties are likely to devote extensive resources to developing the facts and arguments fully in regard to the usually complex certification issues").

182. In order to make its certification decision, the court must allow sufficient discovery to support the parties' arguments on certification, and parties often engage in lengthy, complex battles over the appropriate scope of discovery. *See Kupperman & Freeman, supra* note 167, at 1579. Moreover, depositions are often required. *See id.* at 1583. If standard arbitration procedures were followed this might be problematic, in that less discovery is typically available in arbitration. *See id.* at 1580. Instead, Commentators Kupperman and Freeman explain that "[c]areful court supervision and monitoring of a purported class action, even at the initial stage regarding certification, . . . is essential." *Id.* at 1579-80.

183. If the class is certified, the court in most cases must supervise the provision of notice to absent class members. This function, too, is complex, as parties may battle over who should receive notice, the form of notice (e.g. mail v. newspaper), the precise wording of the notice, and the availability of opt-in or opt-out mechanisms. *See id.*; *see also Harris*, 441 N.Y.S.2d at 79 (Bloom, J., dissenting) (arguing that a court must be involved in complex notice issues).

184. Critics believe that this ongoing monitoring will again result in confusion and inefficiency. *See Stewart, supra* note 135, at 5 ("[G]iven that judicial involvement would in fact be required beyond the certification stage, there would be obvious duplication of effort, as well as confusion for the parties over to whom they should focus their energies."). Justice Richardson stated that "substantial judicial involvement by the court will be required to

approving any settlement,<sup>185</sup> and postjudgment determinations of the scope of class relief,<sup>186</sup> it would be extremely confusing and inefficient to allow an arbitral class action.<sup>187</sup> Some critics further explain that judicial involvement is necessary because arbitrators lack the qualifications and experience to decide complicated class issues.<sup>188</sup>

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monitor the progress of the arbitration and potentially will undermine the arbitrator's discretion." *Keating*, 645 P.2d at 1215 (Richardson, J., concurring and dissenting). Justice Richardson goes on to explain that the Due Process Clause requires the court to examine the adequacy of representation on a continuing basis, and that this examination must be stringent. *See id.*

185. If, as in most cases, a settlement is reached, the court must hold a hearing to allow any objecting class members to voice their concerns with the settlement, and the court must ultimately rule on whether the settlement is acceptable. Stewart explained that the judge's role in approving or disapproving settlements is complex.

A judge must take into account: the distribution of monetary relief and its appropriateness; other class relief; the completeness of the settlement; the participation of class members in the settlement, or lack thereof, and the reasons therefore; the interests of each segment of the class, as well as the class as a whole; and, the appropriateness of counsel fees.

Stewart, *supra* note 135, at 5 (citing MANUAL FOR COMPLEX LITIGATION § 30.41 (2d ed. 1985)). He further observed "it is extremely difficult to envision arbitrators dealing with objecting class members." *Id.* at 6. Justice Richardson, similarly, explained that in ruling on the propriety of a settlement, "[t]he court must review the entire proceedings to determine if the settlement was fair, reasonable, and adequate in light of the strength of each party's case, and take evidence on any substantial objection to the proposed settlement brought by any class member." *Keating*, 645 P.2d at 1215 (citation omitted) (Richardson, J., concurring and dissenting). He emphasized that the traditional absence of a transcript or record in arbitral proceedings will be problematic, "because without a record . . . objection to settlements would be difficult to assess." *Id.*

186. In instances in which the case does not settle, Justice Richardson foresees that the absence of a transcript may pose logistical difficulties. "[A] court may have difficulty in applying an arbitrator's decision to all class members, since it could not determine whether the arbitrator's judgment was applicable to each member of the class, or based on equities applicable only to the individual claimant." *Keating*, 645 P.2d at 1215 (Richardson, J., concurring and dissenting).

187. "What sense . . . would it make to have a court, after it has made a 'rigorous analysis' of the case at the certification stage, bow out and hand over the case for a *de novo* 'merits' determination by a panel?" Stewart, *supra* note 135, at 6.

188. *See, e.g., Keating*, 645 P.2d at 1215 (Richardson, J., concurring and dissenting) ("[A]rbitrators, of course, are not necessarily either lawyers or judges. Requiring the administration of complex class procedures during arbitration may either make lay experts unavailable as arbitrators as a practical matter, or result in intrusive judicial participation and supervision."); Kupperman & Freeman, *supra* note 167, at 1591-92 (questioning whether arbitrators have experience and qualifications to decide not only class issues, but also substantive legal issues in complex cases); *cf.* Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. 52,659, 52,660 (1992) (summarizing the NASD's rejection of the argument that arbitrators lack requisite expertise to resolve class action issues); Stewart, *supra* note 135, at 5



Interestingly, interviews with several attorney participants in some of the few classwide arbitrations that have taken place to date did not tend to support these concerns. The attorneys uniformly reported that the hybrid process had worked relatively smoothly, and that they had not found the combination of judicial and arbitral decisionmaking to be inefficient as compared to class action litigation.<sup>189</sup> However, it should also be noted that none of the attorneys reported that the arbitral class action was particularly *more* efficient than class action litigation.<sup>190</sup>

*c. Due Process Concerns*

As discussed earlier, the Supreme Court has repeatedly held that class actions raise due process concerns.<sup>191</sup> Specifically, a class action cannot be held to be binding as to nonparticipating class members unless, because of the structure and supervision of the class action, their interests were adequately protected.<sup>192</sup> A number of critics of arbitral class actions have suggested that these due process concerns pose a major hurdle for arbitral class actions. Specifically, they contend that while substantial court supervision and involvement will purportedly pose major logistical problems, as discussed above, that such involvement is nonetheless mandated by the Due Process Clause.<sup>193</sup> Evan Stewart makes the point bluntly:

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(asserting that the argument that arbitrators lack sufficient expertise and training to decide class action issues is a "red herring," in that although the author believes arbitrators lack such experience, the Supreme Court has already ruled that they may decide statutory claims under RICO, ERISA, and the securities acts, which are equally complex).

189. *See supra* note 168.

190. *See id.*

191. *See supra* notes 109-22 and accompanying text.

192. *See supra* notes 109-16 and accompanying text.

193. Not everyone accepts the proposition that arbitral class actions raise due process concerns, or certainly that such concerns mandate intensive court involvement. *See* Order Approving Proposed Rule Change Relating to the Exclusion of Class Actions From Arbitration Proceedings, 57 Fed. Reg. at 52,660-61 (summarizing the NASD's view that arbitration process would not be less protective of due process than the courts); *Quagmire*, *supra* note 41, at 800-04 (expressing ambivalence as to whether constitutional concerns would apply to private classwide arbitration).

The fundamental problem is more basic: the procedures mandated by Rule 23 have due process implications and require extensive judicial involvement throughout the entire class action process. The court's role at the certification stage can not suddenly be stopped; it must carry on to such stages as notice, settlement, protection of class members, etc. It is inconceivable to believe that non-Article III arbitrators could properly oversee, for example, the notice procedures mandated by the Supreme Court. Moreover, it is extremely difficult to envision arbitrators dealing with objecting class members. Other and equally obvious problems (e.g., fairness of settlement, protection of absent class members, etc.) are no less daunting.<sup>194</sup>

Similarly, Justice Richardson stated:

Because of the due process safeguards required to keep class members apprised of the course of the litigation, substantial judicial involvement by the court will be required to monitor the progress of the arbitration and potentially will undermine the arbitrator's discretion. In fact, the court's due process responsibilities include the duty to "undertake a stringent and continuing examination of the adequacy of representation by the named class representative at all stages of the litigation."<sup>195</sup>

I argue within that these due process concerns must be carefully considered in determining how courts should handle the confluence of class actions with binding arbitration.

## II. THE CURRENT LAW: WHEN ARBITRATION MEETS THE CLASS ACTION

Courts that have considered questions relating to arbitration and class actions have not typically focused on the "big picture" issue of whether companies should be permitted to use binding arbitration

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194. Stewart, *supra* note 135, at 6.

195. Keating v. Superior Court, 645 P.2d 1192, 1215 (Cal. 1982) (Richardson, J., concurring and dissenting) (quoting National Ass'n of Reg'l Med. Programs, Inc. v. Mathews, 551 F.2d 340, 344 (D.C. Cir. 1976), *cert. denied*, 431 U.S. 954 (1977)).

to eliminate the class action remedy. Instead, likely because of the litigation approaches of the attorneys, most courts have addressed these cases on a piecemeal basis, taking on only one issue at a time, as discussed below. That is, courts have not typically addressed the fact that if class actions are referred to arbitration, and if arbitral class actions are prohibited, plaintiffs will not be permitted to proceed by way of class action in any venue.<sup>196</sup>

### *A. Effects of Pre-Dispute Arbitration Agreements Upon Class Actions*

When companies have sought to use arbitration agreements to prevent consumers or others from bringing class actions, plaintiffs have typically offered three responses: (1) the arbitration agreement, virtually always imposed as a contract of adhesion,<sup>197</sup> is invalid; (2) arbitration is not appropriate for their class claims; and (3) if arbitration is appropriate, the court ought to order that class arbitration is permissible.<sup>198</sup> To date, none of these arguments has proved particularly successful, although each has prevailed on occasion.

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196. There are a few exceptions. *See infra* notes 231-45 and accompanying text (discussing three courts' decision to void, on unconscionability or federal statutory grounds, arbitration agreements that would have prevented plaintiffs from proceeding by way of class action); *see also infra* notes 213-20 and accompanying text (discussing opinions stating that class actions should not be required to be arbitrated because this would deprive plaintiffs of the ability to obtain effective relief); *cf.* *Thompson v. Illinois Title Loans, Inc.*, No. 99 C 3952, 2000 WL 45493, at \*3-4 (N.D. Ill. Jan. 11, 2000) (rejecting plaintiff's argument that mandating arbitration of Truth in Lending Act claim would violate that statute by depriving plaintiff of the right to proceed by way of class action); *Sagal v. First USA Bank, N.A.*, 69 F. Supp. 2d 627, 631-32 (D. Del. 1999) (same); *Lopez v. Plaza Fin. Co.*, No. 95-C-7567, 1996 WL 210073, at \*3 (N.D. Ill. Apr. 25, 1996) (same).

197. By contract of adhesion I mean nothing more than a term that is imposed, typically in a form in small print, on a take-it-or-leave-it basis. *See supra* note 3.

198. Note that it may be difficult for a plaintiff to attempt to argue both that arbitration should not be permitted, because class litigation is essential, and that if arbitration is ordered the court should order classwide arbitration. To prevail on the first argument, plaintiff will try to convince the court that arbitration is not an effective remedy. But, to prevail on the second, plaintiff will try to convince the court that classwide arbitration is workable and desirable. In short, there is some tension between the two arguments, which may explain why most plaintiffs choose only one.

### 1. *Mandatory Binding Arbitration may be Imposed by Contracts of Adhesion*

Despite the arguments of this author<sup>199</sup> and many others,<sup>200</sup> most courts are currently willing to enforce arbitration agreements that are imposed as contracts of adhesion, absent other problems with the clause. Inspired by the Supreme Court's heightened enthusiasm for arbitration,<sup>201</sup> in case after case, most federal and state courts have found that arbitration may be compelled based on clauses contained in small writing and inconspicuous locations in form contracts,<sup>202</sup> in employee handbooks

199. See Sternlight, *Panacea*, *supra* note 68, at 637-74 (1996) (arguing that, as a matter of legislative history and policy, courts should not enforce arbitration clauses imposed by companies on consumers, employees, franchisees, or other "little guys" through contracts of adhesion); Sternlight, *Rethinking*, *supra* note 4, at 47-48 (arguing that courts have been too willing to reject constitutional challenges to mandatory binding arbitration, and suggesting that some clauses may be subject to challenge); see also Jean R. Sternlight, *Compelling Arbitration of Claims Under the Civil Rights Act of 1866: What Congress Could Not Have Intended*, 47 U. KAN. L. REV. 273 (1999) (using historical arguments to contend that claims brought under the Civil Rights Act of 1866, 42 U.S.C. § 1981, should not be subject to mandatory arbitration).

200. See, e.g., Carrington & Haagen, *supra* note 75, at 333 (critiquing Supreme Court's arbitration jurisprudence as hostile to consumers and employees); Schwartz, *supra* note 75, at 60-61 (arguing that big business is using arbitral contracts of adhesion to gain unfair advantages); Jeffrey W. Stempel, *Bootstrapping and Slouching Toward Gomorrah: Arbitral Infatuation and the Decline of Consent*, 62 BROOK. L. REV. 1381 (1996) (arguing for a reinvigoration of consent concepts that would invalidate some arbitration clauses).

201. As discussed above, see *supra* notes 72-74 and accompanying text, the Supreme Court has repeatedly interpreted the Federal Arbitration Act to favor arbitration, not only where it is entered into knowingly by two businesses, but also where it is imposed by a company through a contract of adhesion on its customers or employees.

202. See, e.g., *Harris v. Green Tree Fin. Corp.*, 183 F.3d 173, 182-83 (3d Cir. 1999) (explaining that the fact that the arbitration clause imposed on borrowers was contained in fine print on the back of a form contract does not render that term unconscionable); *Adams v. Merrill Lynch Pierce Fenner & Smith*, 888 F.2d 696, 700-01 (10th Cir. 1989) (holding that the arbitration clause imposed by brokerage on customers is not unenforceable merely because it is "form boilerplate"); *Cohen v. Wedbush, Noble, Cooke, Inc.*, 841 F.2d 282, 287-88 (9th Cir. 1988) ("We know of no case holding that parties dealing at arm's length have a duty to explain to each other the terms of a written contract . . . . We see no unfairness in expecting parties to read contracts before they sign them . . . . We are unable to understand how any person possessing a basic education and fluent in the English language could fail to grasp the meaning of that provision."); *McCarthy v. Providential Corp.*, No. C94-0627 FMS, 1994 WL 387852, at \*8-9 (N.D. Cal. July 19, 1994) (compelling arbitration based on clause contained in forms used for "reverse mortgage loans," though plaintiffs were a group of senior citizen homeowners who claimed they had no idea that they were waiving important rights); *Green Tree Fin. Corp. v. Vinton*, No. 1972191, 1999 WL 778496, at \*1 (Ala. Oct. 1, 1999) (holding enforceable arbitration clause contained in paragraph 14 of financing

or related documents,<sup>203</sup> in flyers contained in mailings with bills or other statements,<sup>204</sup> in packaging that arrives with a computer,<sup>205</sup> or in medical consent or HMO forms or contracts.<sup>206</sup> Courts and commentators have defended such clauses on the ground that form contracts of adhesion are common, efficient, and generally accepted in today's economy.<sup>207</sup>

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documents accompanying purchase of mobile home).

203. *See, e.g.,* *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 170 F.3d 1, 17 (1st Cir. 1999) ("Absent a showing of fraud or oppressive conduct," Form U-4 was not unenforceable on grounds that it was a contract of adhesion); *Koveleskie v. SBC Capital Mkts., Inc.*, 167 F.3d 361, 366-67 (7th Cir. 1999), *cert. denied*, 120 S. Ct. 44 (1999) (holding that pursuant to Illinois law, brokerage employee could not avoid arbitral provision merely by arguing that it was imposed on a "take-it-or-leave-it" basis); *Patterson v. Tenet Healthcare, Inc.*, 113 F.3d 832, 835 (8th Cir. 1997) (concluding that arbitration clause contained in handbook was an enforceable contract, where employee signed acknowledgment form including arbitration provision—even though the handbook contained a clause stating that it was not a contract); *see also* *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (holding that securities industry employee who had been required to sign Form U-4 calling for arbitration would have to arbitrate rather than litigate ADEA claims, but failing to address adhesion argument).

204. *See, e.g.,* *Herrington v. Union Planters Bank, N.A.*, No. CIV A. 2:98CV231GR, 2000 WL 424232, at \*1 (S.D. Miss. Jan. 21, 2000) (compelling arbitration where bank imposed arbitration by enclosing clause as part of change of terms notice, although account did not originally require arbitration and customer signed nothing calling for arbitration); *Perry v. Beneficial Nat'l Bank USA*, No. Civ. A. CV97-218, 1998 WL 279174, at \*1 (Ala. Cir. Ct. May 15, 1998) (stating that although the credit card agreement did not contain an arbitration provision when initially obtained, when the new Bank purchased the accounts receivable and amended the terms of the credit card to require arbitration, customer was bound by such). *But see* *Long v. Fidelity Water Sys., Inc.*, No. C-97-20118 RMW (N.D. Cal. May 26, 2000) (finding plaintiffs had failed to "agree" to arbitration where defendants imposed arbitration by mailing clause as part of change of terms notice) (on file with author).

205. *See, e.g.,* *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147 (7th Cir. 1997) (mandating arbitration which was imposed by the company via a clause included as part of the "terms and conditions" clause contained in the box with the computer ordered by mail, when consumer failed to reject arbitration by returning computer within 30 days). *See generally* Jean R. Sternlight, *Gateway Widens Doorway to Imposing Unfair Binding Arbitration on Consumers*, FLA. B. J., Nov. 1997, at 8 (critiquing *Gateway* on statutory, contractual, and constitutional grounds).

206. *See, e.g.,* *Sosa v. Paulos*, 924 P.2d 357, 361-62 (Utah 1996) (refusing to void an arbitration agreement that required a medical malpractice claim to be heard by a panel of board-certified orthopedic surgeons, in that patient had two-week period to reject clause); *cf.* *Engalla v. Permanente Med. Group, Inc.*, 938 P.2d 903, 917-21 (Cal. 1997) (holding that arbitration clause imposed by HMO potentially could be voided for fraud because company gave false assurances as to speed of arbitration).

207. *See, e.g.,* *Drahozal*, *supra* note 5, at 51-81; Stephen J. Ware, *Consumer Arbitration as Exceptional Consumer Law (With a Contractualist Reply to Carrington & Haagen)*, 29 MCGEORGE L. REV. 195, 196, 210-13 (1998) (arguing that law governing arbitration ought to be "an island of contract in a sea of anti-contract" law often governing consumer transactions, and urging that providing consumers with the ability to contract away the right to litigate

There are some rare exceptions. In a few highly-publicized cases, several courts have recently relied on a combination of statutory, policy, and constitutional analyses to refuse to enforce at least certain arbitration clauses imposed through contracts of adhesion.<sup>208</sup> Even these cases, however, have not voided the clauses simply because they were imposed as contracts of adhesion, but rather relied on other factors and arguments.<sup>209</sup> Thus, while a company would be well advised to give its customers or employees the clearest notice possible, and to explain the scope of the arbitration clause with particularity, companies in most jurisdictions in this country can feel comfortable that if they use a form contract to impose arbitration on their customers or patients, a court will not refuse to enforce the clause on that ground alone.<sup>210</sup>

## 2. No General Class Action Exemption from Arbitration

Some plaintiffs have attempted to argue that even though it may be permissible for companies to impose binding arbitration

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will enhance their freedom and autonomy and add value to their transactions); *see also* *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 593-95 (1991) (noting that form contracts often provide benefits for all concerned, and upholding the validity of a forum selection clause contained in small print on a boat ticket).

208. *See, e.g., Rosenberg*, 170 F.3d at 20-21 (holding that “where appropriate” language of Civil Rights Act of 1991 should be interpreted to preclude mandatory arbitration of employment claims by a securities employee who, although she signed a Form U-4 calling for arbitration of claims required to be arbitrated by stock exchange rules, was never provided with a copy of those rules); *Duffield v. Robertson Stephens & Co.*, 144 F.3d 1182, 1189-90 (9th Cir. 1998), *cert. dismissed*, 525 U.S. 982 (1998), and *cert. denied*, 525 U.S. 996 (1998) (holding that the Civil Rights Act of 1991 precluded employer from using pre-dispute arbitration agreements to compel employee to arbitrate Title VII claims, where employee was not given the choice of whether to accept arbitration); *Badie v. Bank of Am.*, 79 Cal. Rptr. 2d 273, 277 (1998) (finding that bank customers had not consented to arbitration merely by agreeing that the bank could unilaterally change any “term, condition, service or feature” of the account); *see also Seifert v. United States Home Corp.*, 1999 WL 1044175, at \*1 (Fla. Nov. 18, 1999) (taking notice of policy arguments opposing deprivation of jury trial rights in holding that agreement to arbitrate contained in purchase and sales agreement did not mandate arbitration of subsequent tort action based on common law duties).

209. *See, e.g., Rosenberg*, 170 F.3d at 16-17 (rejecting the argument that arbitration clause imposed on employee was void on unconscionability grounds because it was a contract of adhesion); *Badie*, 79 Cal. Rptr. 2d at 288 (implying that it might have been permissible for the bank to include a mandatory ADR provision in the account agreement, had it done so in the first instance).

210. *Cf. In re Turner Bros. Trucking Co.*, 1999 WL 1054787, at \*1 (Tex. App. Nov. 23, 1999) (refusing to compel arbitration that was mandatorily imposed on functionally illiterate employee).

through contracts of adhesion, arbitration cannot ever be required when it would deprive plaintiffs of their right to proceed by way of class action in court.<sup>211</sup> Generally, as will be discussed, this broad argument has not proved successful.<sup>212</sup> Nonetheless, the argument that class actions are never arbitrable has been accepted by a few lower courts, although two of these three decisions have been reversed on appeal.<sup>213</sup> For example, in *In re Knepp*,<sup>214</sup> the one decision which was not reversed, plaintiff brought a consumer class action in the bankruptcy context<sup>215</sup> and opposed binding arbitration in part because it “interferes with class action relief and consequently eliminates any reasonable opportunity for

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211. In the cases discussed here, the arbitration clause and accompanying rules did not expressly allow or disallow class actions. Where the rules explicitly prohibit class actions or state that class actions may not be arbitrated, a plaintiff can make a separate and stronger argument that it would be inappropriate to mandate arbitration. *See infra* text accompanying notes 357-59.

212. *See infra* notes 221-25 and accompanying text. However, other more narrow arguments have worked, based on the language of the clause, a particular statute, or unconscionability. *See infra* notes 226-45 and accompanying text.

213. In *Vernon v. Drexel Burnham & Co.*, 125 Cal. Rptr. 147 (Cal. Ct. App. 1975), plaintiffs brought a class action against 25 stock brokerages, alleging overcharges on margin accounts. Although the named plaintiff who maintained an account with Drexel Burnham had signed an arbitration agreement, the trial court refused to compel arbitration, in part on the ground that

[w]hile the policy of the law is in favor of arbitration, it is also the policy of the law that class actions shall not be subverted by depriving the class of its representative, and in a case such as this the two policies clash. The policy which should prevail is the one against subversion of class actions.

*Id.* at 150 (alteration in original). The appellate court reversed, finding that “in the instant case, the policy of law favoring arbitration prevails over the policy of law pertaining to class actions.” *Id.* at 152. The court expounded on this policy at some length, stating, “[t]he sanctity of valid contractual agreements in a free society, such as ours, is of paramount importance and is rooted in both the United States and California Constitutions, which predate and outweigh the body of law on class actions as presently evolving.” *Id.* at 153. Similarly, in *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315 (Cal. Ct. App. 1986), a suit in which a class of condominium purchasers sued vendors for failing to disclose that various fees would be assessed in the future, the lower court refused to compel arbitration based on a clause found in the escrow agreement, observing that “the Court is unable to find any cases in which a class action lawsuit was ordered into arbitration.” *Id.* at 316. On appeal, the Superior Court rejected this analysis, remanding the dispute so that the trial court could consider whether it would be appropriate to resolve the dispute through class arbitration. *See id.* at 320-22.

214. 229 B.R. 821 (Bankr. N.D. Ala. 1999).

215. The case was a Chapter 13 bankruptcy proceeding in which debtors filed an adversary complaint against the creditor that had financed the purchase of their car, alleging fraud, civil conspiracy, and violations of the Alabama Mini-Code. *See id.* at 827.

effective redress.”<sup>216</sup> The bankruptcy judge accepted the argument, explaining:

If [courts continue to preclude the use of class actions in arbitration] the pervasive use of arbitration agreements in consumer contracts could have the effect of eliminating class actions as an option available to aggrieved consumers. If class actions are no longer an option, the vast majority of consumer claims involving relatively small sums of money on an individual basis will be left without a remedy.<sup>217</sup>

Similarly, while several individual judges have accepted the argument, all either wrote in concurrence or in dissent.<sup>218</sup> For

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216. *Id.* at 841.

217. *Id.* at 842. The court further stated: “This Court concludes that the Plaintiff would be prejudiced in prosecuting this action as a class action if arbitration were enforced.” *Id.*

218. Two judges, dissenting in *Harris v. Shearson Hayden Stone, Inc.*, 441 N.Y.S.2d 70 (N.Y. App. Div. 1981), reasoned that it would be inappropriate to compel arbitration of plaintiffs’ consumer class action. Judge Sandler stated:

As the majority opinion acknowledges, absent the arbitration agreement, “plaintiffs might have a strong case for class action certification since the institution of an individual lawsuit for the paltry sum at issue would be self-defeating.”

....  
[T]he sum in question is likely to discourage most if not all of the allegedly aggrieved persons from incurring the expense of prosecuting even an arbitration proceeding. The nature of arbitration proceedings makes it unlikely that a successful determination in favor of one person would result in restitution to the others. Indeed there is no assurance that a successful determination in favor of a single complainant would alter the practices here challenged.

In short, not only does a class action appear to be the most suitable means for addressing the issues presented, but there are compelling reasons to believe that individual arbitration proceedings would be wholly ineffective to redress whatever wrongs may be found to have occurred.

*Id.* at 76-77 (Sandler, J., dissenting). Judge Sandler also expressed concern with the fact that the practice of mandating arbitration was industrywide, stating that this fact bolstered the public policy argument for favoring the class action over an arbitration. *See id.* Judge Bloom similarly reasoned that the class action should prevail over arbitration to ensure that the wrongdoer was not favored. *See id.* at 77-79 (Bloom, J., dissenting). He stated:

While the loss to the class by reason of Shearson’s actions may aggregate millions of dollars, the loss to each member of the class may well be so miniscule as to make it scarcely practical to resort to arbitration with the expense incident thereto. Indeed, were it not for the class action the practicality of litigation would be substantially non-existent.

*Id.* at 79. Judge Bloom also rejected the feasibility of “class arbitration.” *See id.*



example, California Supreme Court Justice Richardson, concurring and dissenting in *Keating v. Superior Court*,<sup>219</sup> suggested that even though it might generally be appropriate to mandate individualized arbitration of claims brought as class actions, it would not be appropriate “where an arbitration clause in an adhesion contract would allow the stronger party to evade responsibility for its acts.”<sup>220</sup>

Far more courts have explicitly held that the mere fact that a suit is captioned as a class action does not render it exempt from being sent to arbitration. For example, although the California Supreme Court in *Keating* considered the possibility of ruling that “arbitration agreements contained in contracts of adhesion may not operate to stay properly maintainable class actions,”<sup>221</sup> it ultimately concluded: “The statutes and public policy supportive of arbitration require . . . that [litigation] be avoided if means are available to give expression to the basic arbitration commitment of the parties.”<sup>222</sup>

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219. 645 P.2d 1192 (Cal. 1982).

220. *Id.* at 1217. Justice Richardson was concerned about “a case where class proceedings provide the only economical method of presenting a claim.” *Id.* In such a situation, he opined that the clause should “be found oppressive and . . . invalidated. In instances where an arbitration clause would effectively deny relief to the weaker party in an adhesion contract, relief under settled principles of law would potentially be available.” *Id.* Rejecting the broader suggestion made by some, that “arbitration agreements contained in contracts of adhesion may not operate to stay properly maintainable class actions,” *id.*, Richardson instead proposed using a “reasonable expectations” analysis to void those clauses which were particularly oppressive. *See id.* In the instant case, a group of franchisees had failed to allege, much less prove, that they would be unable to pursue their claim against the franchisor without the class action procedure. *See id.*

221. *Id.* at 1207.

222. *Id.* The court went on to remand the dispute to the trial court so that it could rule on whether plaintiffs should be permitted to proceed with an arbitral class action. *See id.* at 1209-10; *see also* Nielsen v. Greenwood, No. 91C6537, 1993 WL 144857, at \*6 (N.D. Ill. Feb. 26, 1993) (holding that “[t]he strong federal policy in favor of arbitration is not outweighed by Plaintiffs’ desire for class treatment of their claims against PJH”), *vacated*, 873 F. Supp. 138 (N.D. Ill. 1995) (ruling that subsequent adoption by the NASD of rule prohibiting arbitration of class actions should be applied to allow plaintiffs to pursue their claims in court), *and aff’d sub nom.* Nielsen v. Piper, 66 F.3d 145 (7th Cir. 1995); Erickson v. PaineWebber Inc., No. 87C10592, 1990 WL 104152, at \*1-2 (N.D. Ill. July 13, 1990) (holding that class action brought on behalf of purchasers of allegedly fraudulent investment and tax shelter program could not evade arbitration required by Client Commodity agreement, even though plaintiffs asserted that arbitration would deprive them of an appropriate forum to hear their class claims); Perry v. Beneficial Nat’l Bank USA, No. CIV.A.CV97-218, 1998 WL 279174, at \*1 (Ala. Cir. Ct. May 15, 1998) (stating class action allegations do not defeat arbitration clause because any person who agreed to arbitrate cannot be part of class);

Several other courts similarly have emphasized that where the arbitration agreement is silent, it cannot be assumed that the parties meant to exclude a class action from arbitration.<sup>223</sup> A number of courts have expressed a concern that making class actions nonarbitrable would make it too easy for persons to evade arbitration, simply by constructing their claim as a class action.<sup>224</sup> Some of the courts that ordered class claims to be arbitrated did so

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*Steinberg v. Prudential-Bache Sec., Inc.*, 1986 WL 5024, at \*1 (Del. Ch. Apr. 30, 1986) (compelling arbitration of class claims because arbitration is favored); *Harris v. Shearson Hayden Stone, Inc.*, 441 N.Y.S.2d 70, 74-76 (N.Y. Sup. Ct. 1981) (mandating arbitration of class claim brought by customers against brokerage because state law does not justify avoiding arbitration on such a basis, and because policy arguments favor arbitration).

223. *See, e.g.*, *Howard v. Klynveld Peat Marwick Goerdeler*, 977 F. Supp. 654, 665 n.7 (S.D.N.Y. 1997) (observing that a plaintiff "who has agreed to arbitrate all claims arising out of her employment may not avoid arbitration by pursuing class claims"); *Doctor's Assocs., Inc. v. Hollingsworth*, 949 F. Supp. 77, 84 (D. Conn. 1996) (concluding that class actions are not excluded from arbitration by terms of arbitration clause between franchisor and franchisees); *Coleman v. National Movie-Dine Inc.*, 449 F. Supp. 945, 948 (E.D. Pa. 1978) (concluding that class action brought on behalf of movie distributors must be arbitrated, given the broad arbitration clause, which lacked an express provision excluding class actions).

224. *See, e.g.*, *Meyers v. Univest Home Loan, Inc.*, No. C-93-1873, 1993 WL 307747, at \*1 (N.D. Cal. Aug. 4, 1993). The court compelled arbitration of a consumer class action and stated:

To rule otherwise would be to carve a gaping exception into the Arbitration Act: any California consumer could circumvent an agreement to arbitrate by bringing her claim "on behalf of the general public" and praying for injunctive relief. Such an exception would plainly undermine Congress's policy to promote the enforceability of such agreements.

*Id.* at \*5 n.8; *Vernon v. Drexel Burnham & Co.*, 125 Cal. Rptr. 147, 153 (Cal. Ct. App. 1975) ("A class action cannot be used to subvert an otherwise enforceable agreement to arbitrate contained in a valid contract merely because other individuals, who might qualify as members of a class, were subject to the same provision."); *Frame v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 97 Cal. Rptr. 811, 814 (Cal. Ct. App. 1971) (requiring that employee arbitrate claim for unfair business practices and observing that class members should not be allowed "to evade the terms of the [arbitration] agreement simply by bringing their action together as a 'class' rather than as individuals"); *Leason v. Merrill Lynch, Pierce, Fenner & Smith*, No. 6914, 1984 WL 8232, at \*3 (Del. Ch. Aug. 23, 1984) (compelling arbitration of class claim on ground that "responsibility to arbitrate cannot be evaded by asserting claims through a class," even while recognizing that "the arbitration defense might prove a potent, and decisive economic barrier to obtaining complete legal relief"); *see also Coleman*, 449 F. Supp. at 948 ("Arbitration should not be foreclosed simply by adding persons to a civil action who are not parties to the arbitration agreement because such an inclusion would thwart the federal policy in favor of arbitration."). *But see Harris*, 441 N.Y.S.2d at 77 (Sandler, J., dissenting) (recognizing that there is a risk that rule of excluding class actions from arbitration would be abused, but doubting that risk is "substantial" in that "[t]he common run of arbitration litigation involves commercial disputes between business entities of a kind clearly unsuited to class action").

based on the reasoning that the two techniques are not inconsistent, and that a class action could be conducted in the arbitration context.<sup>225</sup>

### 3. *Specific Wording of Arbitration Clauses and Relevant Rules*

Most of the arbitration clauses that have been litigated to date do not expressly address the availability of class action relief, but the precise wording of those that do may prove critical to courts' decisions. In the securities industry, arbitration rules since 1992 have stated that class action claims are not arbitrable.<sup>226</sup> Numerous courts have interpreted these rules to mean that plaintiffs may *litigate* class action claims, and need only arbitrate *individual* claims.<sup>227</sup> By contrast, in a recent case in which the arbitration clause expressly prohibited class action, except with all parties' consent, the court compelled individual arbitration.<sup>228</sup> It rejected plaintiffs' argument that the prohibition was void based on public

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225. See, e.g., *Keating*, 645 P.2d at 1206-10 (ordering arbitration but remanding to trial court the question of whether arbitration should proceed by way of class action); *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315, 320-23 (Cal. App. 1986) (ordering arbitration of class claims brought by condominium purchasers, and remanding to trial court the question of whether arbitration itself should proceed by way of class action).

226. See *supra* notes 169-78 and accompanying text for a detailed discussion of these rules.

227. See, e.g., *Nielsen v. Piper, Jaffray & Hopwood, Inc.*, 66 F.3d 145, 148 (7th Cir. 1995) (concluding that contract prohibited compelled arbitration); *Olde Discount Corp. v. Hubbard*, 4 F. Supp. 2d 1268, 1271 (D. Kan. 1998) (concluding that because "[t]he plain language of the arbitration agreements and incorporated rules dictates that Mr. Hubbard's [class action race discrimination] claim is ineligible for arbitration at this time," it would be inappropriate for court to compel arbitration of such claim), *aff'd*, 172 F.3d 879 (10th Cir. 1999); *Martens v. Smith Barney, Inc.*, 181 F.R.D. 243, 252 (S.D.N.Y. 1998) (concluding class action claim not arbitrable because U-4 forms signed by plaintiffs stated that class actions suits are not subject to NASD arbitration); *In re Regal Communications Corp. Sec. Litig.*, No. 94-179, 1995 WL 550454, at \*11 (E.D. Pa. Sept. 14, 1995) (holding plaintiffs class action claim was not subject to mandatory arbitration because "[b]oth the NYSE and NASD have promulgated rules which make any claim filed as a class action ineligible for arbitration"); *Scher v. Equitable Life Assurance Soc'y*, 866 F. Supp. 776, 777 (S.D.N.Y. 1994) (observing that class actions are not subject to compulsory arbitration under NASD rules); *Berger v. E\*Trade Group, Inc.*, No. 600721/99, 2000 WL 360092, at \*1 (N.Y. Sup. Mar. 28, 2000) (holding class action securities claims could not be arbitrated until class certification was denied).

228. See *Zawikowski v. Beneficial Nat'l Bank*, No. 98C2178, 1999 WL 35304, at \*1 (N.D. Ill. 1999) (involving a consumer class action brought against H&R Block).

policy grounds,<sup>229</sup> instead stating “[n]othing prevents the Plaintiffs from contracting away their right to a class action.”<sup>230</sup>

#### *4. Recent Decisions Voiding Arbitration Agreements that Prohibited Class Actions*

Two cases have applied unconscionability concepts to void arbitration clauses in part because they would have denied plaintiffs the chance to litigate as a class.<sup>231</sup> *Powertel, Inc. v. Bexley*,<sup>232</sup> a Florida decision, involved a plaintiff who filed a class action claiming that her cellular phone service had improperly charged her \$4.50 for long distance calls when in fact the calls were made within the local area.<sup>233</sup> The day after plaintiff filed a complaint, she received her bill and a new mandatory arbitration provision.<sup>234</sup> The court refused to enforce this provision not only because it was retroactive, but also because it was unconscionable—in part because it deprived plaintiff of the opportunity to proceed by way of class action.<sup>235</sup> The court explained:

The arbitration clause also effectively removes Powertel's exposure to any remedy that could be pursued on behalf of a class of consumers. . . . Class litigation provides the most economically feasible remedy for the kind of claim that has been

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229. *See id.* at \*2.

230. *Id.*; *see also* *Doctor's Assocs., Inc. v. Hollingsworth*, 949 F. Supp. 77, 80 (D. Conn. 1996) (stating that dispute was arbitrable because arbitration agreement required individual arbitration and precluded consolidation, emphasizing that defendant had demanded separate arbitrations and had not sought to consolidate them, and implying that classwide arbitration would not be available).

231. A third decision held that plaintiff, a putative class member, had not “agreed” to arbitration imposed through a change in terms notice, in part because the company did not adequately inform him of the pending class action. *See Long v. Fidelity Water Sys., Inc.*, No. C-97-20118 RMW (N.D. Cal. May 26, 2000) (on file with author). Not all courts have found the use of arbitration clauses to eliminate class actions unconscionable. *See In re RealNetworks, Inc.*, No. 00 C 1366, 2000 WL 631341, at \*7 (N.D. Ill. May 8, 2000) (rejecting argument that arbitration clause was unconscionable because it would preclude bringing claims on a class basis).

232. 743 So. 2d 570 (Fla. Dist. Ct. App. 1999).

233. *See id.* at 572.

234. *See id.*

235. *See id.* at 574.

asserted here. The potential claims are too small to litigate individually, but collectively they might amount to a large sum of money. The prospect of class litigation ordinarily has some deterrent effect on a manufacturer or service provider, but that is absent here. By requiring arbitration of all claims, Powertel has precluded the possibility that a group of its customers might join together to seek relief that would be impractical for any of them to obtain alone. Again, this is an advantage that inures only to Powertel. The arbitration clause precludes class litigation by either party, but it is difficult to envision a scenario in which that would work to Powertel's detriment.<sup>236</sup>

Similarly, in *Ramirez v. Circuit City Stores, Inc.*<sup>237</sup> a California court of appeal voided as unconscionable an arbitration clause imposed by an employer on its employees, relying in part on the fact that the clause expressly deprived the arbitrator of the power to hear class actions.<sup>238</sup>

Another decision, *Johnson v. Tele-Cash, Inc.*,<sup>239</sup> relies on two federal statutes, rather than unconscionability doctrine, to void an arbitration clause as applied to a putative class action. Plaintiff Terry Johnson had filed suit under both the Truth in Lending Act (TILA)<sup>240</sup> and the Electronic Funds Transfer Act (EFTA)<sup>241</sup> alleging that defendants violated the rights of class members "by failing to properly disclose the excessively high rates of interest which they charge for their short-term loans and by requiring borrowers to consent to a complicated electronic fund transfer scheme in order

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236. *Id.* at 576. The court also noted that the clause limited defendant's liability to actual damages, and forced plaintiffs to waive statutory remedies of injunctive and declaratory relief. *See id.*

237. 90 Cal. Rptr. 2d 916 (Cal. Ct. App. 1999), *review granted*, 94 Cal. Rptr. 2d 1 (Cal. 2000).

238. *See id.* at 918-19. The court also found other aspects of the clause unfair, in that it limited discovery, shortened the statute of limitations, and limited available damages. *See id.*

The limitations imposed by the arbitration agreement on class actions and on the rights and remedies available to its employees and prospective employees are relevant to the question of the agreement's unconscionability. We need not and do not here determine if, in and of themselves, they provide alternative bases for upholding the trial court's ruling.

*Id.*

239. 82 F. Supp. 2d 264 (D. Del. 1999) [*See* EDITOR'S NOTE, *supra* note 34].

240. 15 U.S.C. §§ 1601-67 (1994).

241. 15 U.S.C. § 1693 (1994).

to obtain these loans.”<sup>242</sup> The court held that because a ruling compelling arbitration of claims brought under these statutes “would contravene the express congressional intent to ‘encourage the use of class actions as an important tool for enforcing Truth in Lending’”<sup>243</sup> and also the Electronic Funds Transfer Act,<sup>244</sup> it would not enforce the arbitration clause as applied to claims brought under those statutes.<sup>245</sup>

### 5. Class Actions Frequently are Ordered to Arbitration

In sum, with certain important exceptions noted above, most courts have been willing to order cases styled as class actions to arbitration. Thus, the next question becomes whether the arbitration itself will be handled as a class action, or as an individual claim. This seemingly straightforward issue has many aspects, as will be discussed below. It should also be noted that many courts have compelled arbitration of putative class actions without addressing the question of whether the arbitration will potentially proceed as a class action or only as an individual suit.<sup>246</sup>

242. *Johnson*, 82 F. Supp. 2d at 266.

243. *Id.* at 267 (quoting *Bantolina v. Aloha Motors, Inc.*, 419 F. Supp. 1116, 1120 (D. Haw. 1976)). Note that several other courts, most in the Northern District of Illinois, have rejected the argument that courts cannot compel arbitration of class actions brought under TILA. *See Brown v. Surety Fin. Serv., Inc.*, No. 99 C 2405, 2000 WL 528631, at \*3 (N.D. Ill. Apr. 24, 2000); *Thompson v. Illinois Title Loans, Inc.*, No. 99 C 3952, 2000 WL 45493, at \*3 (N.D. Ill. Jan. 11, 2000); *Sagal v. First USA Bank, N.A.*, 69 F. Supp. 2d 627, 632 (D. Del. 1999); *Randolph v. Green Tree Fin. Corp.*, 991 F. Supp. 1410, 1418 (M.D. Ala. 1997), *rev'd on other grounds*, 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235); *Lopez v. Plaza Fin. Co.*, No. 95-C-7567, 1996 WL 210073, at \*3 (N.D. Ill. Apr. 25, 1996); *see also Herrington v. Union Planters Bank, N.A.*, No. CIV. A. 2:98CV231GR, 2000 WL 424232, at \*6-7 (S.D. Miss. Jan. 21, 2000) (rejecting argument that imposition of arbitration would violate the Truth in Savings Act by eliminating the opportunity to proceed by class action).

244. The court found that although EFTA itself had no legislative history explicitly spelling out the importance of class actions, the fact that Congress had chosen to use the same language as in TILA allowed the court to presume that Congress was similarly trying to encourage class actions. *See Johnson*, 82 F. Supp. 2d at 272.

245. *See id.* at 272. This Article will discuss the court's reasoning in more detail. *See infra* text accompanying notes 385-99.

246. *See, e.g., Zawikowski v. Beneficial Nat'l Bank*, No. 98 C 2178, 1999 WL 35304, at \*2 n.2 (N.D. Ill. Jan. 11, 1999) (noting that because agreement precluded class actions, court ordered arbitration but stating that “[t]he parties have not briefed, and I do not reach, whether the class's claims may be consolidated in arbitration”); *Erickson v. PaineWebber Inc.*, No. 87C 10592, 1990 WL 104152, at \*1 (N.D. Ill. July 13, 1990) (holding that class action claims must be arbitrated given wording of clause, but failing to address whether arbitration would be handled individually or as class action); *Coleman v. National Movie-Dine, Inc.*, 449

## 6. *Class Actions in Arbitration*

The U.S. Supreme Court has not ruled on whether arbitrations may be handled as class actions, but has suggested, in dicta, that such a proceeding might be possible.<sup>247</sup> In *Gilmer*, the plaintiff in an ADEA suit opposed arbitration partly on the ground that he would be deprived of the opportunity to proceed by way of class action.<sup>248</sup> The Court rejected plaintiff's argument without issuing a holding on the subject of arbitral class actions. It implied, first, that arbitrators *might* have the authority to allow for a class action under the NYSE rules.<sup>249</sup> In so stating, the Court suggested that class actions and arbitration are not entirely incompatible. Second, the Court explained that even if plaintiff were deprived of the opportunity to proceed by class action, this deprivation would not necessarily violate the ADEA.<sup>250</sup> Third, the Court emphasized that the arbitration agreement would not, in any event, prohibit the EEOC from bringing an action seeking classwide relief.<sup>251</sup> Thus, while *Gilmer* leaves unanswered many questions regarding the availability of classwide arbitration, it hints that the resolution may depend upon the wording of the arbitration clause and upon the language of the relevant statute under which plaintiff's claim is brought.

In determining whether an arbitration may be handled as a class action, one would expect courts to have addressed the subsidiary but seemingly crucial question of whether this decision should be made by a court or by the arbitrators. That is, does the court

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F. Supp. 945, 948 (E.D. Pa. 1978) (same); *Vernon v. Drexel Burnham & Co.*, 125 Cal. Rptr. 147, 152 nn.4, 5 (Cal. Ct. App. 1975) (same); *Frame v. Merrill Lynch, Pierce, Fenner & Smith Inc.*, 97 Cal. Rptr. 811, 815 (Cal. Ct. App. 1971) (same); *Harris v. Shearson Hayden Stone, Inc.*, 441 N.Y.S.2d 70, 76 (N.Y. App. Div. 1981) (same).

247. See *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 32 (1991).

248. See *id.* Plaintiff contended that if he were denied the right to proceed by class action, he would be deprived of his rights under the ADEA. See *id.*

249. See *id.* (stating that the NYSE rules "provide for collective proceedings").

250. See *id.* ("[e]ven if the arbitration could not go forward as a class action or class relief could not be granted by the arbitrator, the fact that the [ADEA] provides for the possibility of bringing a collective action does not mean that individual attempts at conciliation were intended to be barred.") (quoting *Nicholson v. CPC Int'l Inc.*, 877 F.2d 221, 241 (3d Cir. 1989) (Becker, J., dissenting)). Interestingly, Judge Becker's dissent itself stated that "arbitrations may in fact go forward as class actions." *Nicholson*, 877 F.2d at 240 (Becker, J., dissenting).

251. See *Gilmer*, 500 U.S. at 32.

have the authority to order that a dispute either shall or shall not be handled as a class action by the arbitrators? Or, is this an issue that should be resolved by the arbitrators themselves? Unfortunately, courts typically have not focused on this distinction, instead generally making the ruling themselves without even addressing the question of leaving it to the arbitrators.<sup>252</sup>

Addressing the availability of an arbitral class action, lower courts have often stated that the answer varies depending upon the language of the arbitration agreement as well as any rules that are adopted by that agreement. The following section will therefore first summarize extant law regarding when the clause is silent, and then when the clause explicitly addresses the availability of classwide relief.

*a. Interpreting Silence in Agreements*

*i. Classwide Arbitration Permitted*

Several courts—almost all state courts in California—have held that a court may order an arbitration to be handled as a class action, even though the arbitration clause is silent on the issue.<sup>253</sup>

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252. The few courts that have addressed the question have reached disparate conclusions. Compare *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315, 321 (Cal. Ct. App. 1986) (observing that while in theory court could allow arbitrator to make class determinations, it would seem preferable to have court do so, in order to be less disruptive to arbitral proceeding), with *McCarthy v. Providential Corp.*, No. C 94-0627 FMS, 1994 WL 387852, at \*8-9 (N.D. Cal. July 19, 1994) (stating that while court lacks authority, absent explicit language, to order arbitration to proceed on class basis, arbitrators themselves are free to decide whether arbitration rules permit class actions). Cf. *Sterling Truck Corp. v. Allegheny Ford Truck Sales*, No. 1:00-CV-565 (N.D. Ohio May 23, 2000) (holding that only the arbitrator may decide whether 21 disputes should be consolidated or handled individually) (on file with author).

253. The question of whether the FAA might preempt this California interpretation was flagged but not resolved by the U.S. Supreme Court in *Southland Corp. v. Keating*, 465 U.S. 1, 8-9 (1984), in which the Court found that it lacked jurisdiction to address the question. The California appellate court later reasoned that the FAA did not preempt California's decisional law allowing classwide arbitration where the agreement is silent, because California's approach "neither contradicts the contractual terms nor contravenes the policy behind the act." *Blue Cross v. Superior Court*, 78 Cal. Rptr. 2d 779, 790 (Cal. Ct. App. 1998), cert. denied, 119 S. Ct. 2338 (1999). While recognizing that one federal circuit and several federal district courts had ruled that classwide arbitration was impermissible, absent an express agreement to arbitrate class claims, see *id.* at 788-89, the California court emphasized that it was not bound by those decisions and that the U.S. Supreme Court had not ruled on the question. See *id.* at 788. *Keating* was reversed on other grounds in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), in which the Supreme Court held that the California Supreme Court had erred in



The leading case is *Keating v. Superior Court*,<sup>254</sup> in which the California Supreme Court developed a balancing test that trial courts should apply in deciding whether to permit an arbitration to proceed as a class action.<sup>255</sup> In so doing, the court drew on policy arguments supporting class actions<sup>256</sup> and favoring the protection of weaker parties against unfair treatment.<sup>257</sup> *Keating* also cited the policies favoring arbitration in refusing to eliminate arbitration of class claims.<sup>258</sup> *Keating* recognized that classwide arbitration would

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holding that claims brought under the California Franchise Investment Law were nonarbitrable.

254. *Keating* was reversed on other grounds in *Southland Corp. v. Keating*, 465 U.S. 1 (1984). See *supra* note 253.

255. The *Keating* court envisioned that the trial court would exercise its discretion to decide whether classwide arbitration would be appropriate, weighing the administrative costs of necessary court involvement in the arbitral process against the likely costs and unfairness which would ensue if all of the claimants were required to arbitrate their claims individually. See *id.* at 1209-10. "If the alternative in a case of this sort is to force hundreds of individual franchisees each to litigate its cause with Southland in a separate arbitral forum, then the prospect of classwide arbitration, for all its difficulties, may offer a better, more efficient, and fairer solution." *Id.* at 1209. *Keating* also asserted that the trial court should consider whether any other options, such as consolidation of individual claims, might be superior. See *id.* at 1209-10. Thus, having laid out this balancing test the California Supreme Court remanded the dispute to the trial court to make a determination on classwide arbitration. See *id.* at 1210. Earlier in its opinion, the court suggested that if the lower court decided that classwide arbitration were appropriate, it should condition the order to arbitrate on Southland's acceptance of arbitration. See *id.* at 1195. The court never explained why such "acceptance" should be required.

256. The court emphasized the importance of the class action for allowing large groups to vindicate rights that otherwise might not feasibly be asserted: "We have observed that the class suit both eliminates the possibility of repetitious litigation and provides small claimants with a method of obtaining redress for claims which would otherwise be too small to warrant individual litigation." *Id.* at 1206 (quoting *Richmond v. Dart Indus., Inc.*, 629 P.2d 23, 27 (Cal. 1981)).

257. The court expressed considerable concern that companies might impose arbitration through contracts of adhesion in order to block an otherwise appropriate class action: "If the right to a classwide proceeding could be automatically eliminated in relationships governed by adhesion contracts through the inclusion of a provision for arbitration, the potential for undercutting these class action principles, and for chilling the effective protection of interests common to a group, would be substantial." *Id.* at 1207. The court went on to state, "[i]f . . . 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.* The court also explained that an "unscrupulous wrongdoer" should be proscribed from benefiting from its own wrongdoing. See *id.*

258. The court seriously considered but ultimately rejected the argument that companies should be barred from using arbitral contracts of adhesion to eliminate litigated class actions. See *id.* The court found that such a result should be avoided, if possible, in order to support public policies favoring arbitration. See *id.*

require courts to play an active role in such issues as class certification, notice, adequacy of representation, and fairness of any class settlement.<sup>259</sup> Subsequent to *Keating*, several other courts, all but one in California,<sup>260</sup> also published decisions recognizing the propriety of arbitral class actions.<sup>261</sup>

## ii. Classwide Arbitration Prohibited

Several federal and state courts have reached precisely the opposite conclusion, holding that when an arbitration agreement is silent, it is impermissible for a court to order, or perhaps even to allow, the arbitration to be handled as a class action. The leading

259. *See id.* at 1209.

260. The one non-California decision to the same effect is *Dickler v. Shearson Lehman Hutton, Inc.*, 596 A.2d 860, 866-67 (Pa. Super. Ct. 1991), in which the Pennsylvania Superior Court ordered the trial court to mandate classwide arbitration if it found the prerequisites for a class action had been established. It concluded that the arbitral class action "best serves the dual interest of respecting and advancing contractually agreed upon arbitration agreements while allowing individuals who believe they have been wronged to have an economically feasible route to get injunctive relief from large institutions employing adhesion contracts." *Id.* at 867.

261. *See* *Blue Cross v. Superior Court*, 78 Cal. Rptr. 2d 779, 790 (Cal. Ct. App. 1998) (holding California decisional law permitting classwide arbitrations not preempted by FAA); *Izzi v. Mesquite Country Club*, 231 Cal. Rptr. 315, 322 (Cal. Ct. App. 1986) (remanding determination of classwide arbitration to trial court); *Gainey v. Occidental Land Research*, 231 Cal. Rptr. 249, 253 (Cal. Ct. App. 1986) (resolving various issues as to class notice which arose after court certified class in arbitration matter); *Lewis v. Prudential Bache Sec., Inc.*, 225 Cal. Rptr. 69, 75-76 (Cal. Ct. App. 1986); *Dickler*, 596 A.2d at 867 (stating that "there is no policy reason so paramount in this state which would preclude class action proceedings from being imposed on an arbitration agreement"). The *Lewis* court ordered the trial court to take steps to certify the class, and rejected defendant's arguments that the matter was too complex:

The alternative to class arbitration here is to force each Prudential customer to individually arbitrate claims, most of which probably cannot justify the time and money required to prove. This case appears to offer no great difficulty in adapting arbitration to fit the class action mold, with adequate judicial supervision over the class aspects.

*Id.* at 75. Likewise, in *Nicholson v. CPC Int'l Inc.*, Judge Becker opined in dissent that arbitrations "may in fact go forward as class actions," where such procedure is not specifically barred by the arbitration clause. 877 F.2d 221, 241 (3d Cir. 1989) (Becker, J., dissenting).

While *Nicholson* has agreed to *arbitrate* his claims pursuant to the rules of the American Arbitration Association, he has not agreed to go forward alone and has not agreed not to proceed on the basis of a class action arbitration. In fact, the agreement does not speak to the form his arbitration may take.

*Id.* at 240-41 n.12.

case is *Champ v. Siegel Trading Co.*,<sup>262</sup> a consumer class action<sup>263</sup> in which the Seventh Circuit affirmed the district court's decision ordering plaintiff to arbitration and refusing to certify an arbitral class action.<sup>264</sup> The Seventh Circuit supported its decision by citing federal appellate cases holding that a trial court lacks the power to *consolidate* arbitral proceedings when the parties' arbitral agreement does not allow for consolidation, even when consolidation would be expeditious.<sup>265</sup> Finding "no meaningful basis to distinguish between the failure to provide for consolidated arbitration and class arbitration,"<sup>266</sup> the Seventh Circuit reasoned that the FAA's concern "to enforce the parties' arbitration as they wrote it"<sup>267</sup> should be given priority even over efficiency concerns.<sup>268</sup> *Champ* has been followed by another Seventh Circuit panel,<sup>269</sup> by several federal district courts both within<sup>270</sup> and

262. 55 F.3d 269 (7th. Cir. 1995).

263. The plaintiff class alleged violations of the Commodity Exchange Act, RICO, and several state laws. *See id.* at 271.

264. *See id.* at 271-72.

265. *See id.* at 274-75 (citing *Government of United Kingdom v. Boeing Co.*, 998 F.2d 68, 74 (2d Cir. 1993)); *American Centennial Ins. v. National Cas. Co.*, 951 F.2d 107, 108 (6th Cir. 1991); *Baessler v. Continental Grain Co.*, 900 F.2d 1193, 1195 (8th Cir. 1990); *Protective Life Ins. Corp. v. Lincoln Nat'l Life Ins. Corp.*, 873 F.2d 281, 282 (11th Cir. 1989) (per curiam); *Del E. Webb Constr. v. Richardson Hosp. Auth.*, 823 F.2d 145, 150 (5th Cir. 1987); *Weyerhaeuser Co. v. Western Seas Shipping Co.*, 743 F.2d 635, 637 (9th Cir. 1984).

266. *Champ*, 55 F.3d at 275. This reasoning will be critiqued in Part III. *See infra* text accompanying notes 328-40.

267. *Champ*, 55 F.3d at 275.

268. While recognizing the possibility that "various inefficiencies and inequities" might result from the refusal to certify an arbitral class, *id.* at 277, the Seventh Circuit nonetheless concluded that even if that were the case it was bound to enforce the parties' agreement. *See id.* at 275. The court stated: "For a federal court to read such a term into the parties' agreement would 'disrupt[ ] the negotiated risk/benefit allocation and direct[ ] [the parties] to proceed with a different sort of arbitration.'" *Id.* (quoting *New England Energy, Inc. v. Keystone Shipping Co.*, 855 F.2d 1, 10 (1st Cir. 1988) (Selya, J., dissenting)). The Seventh Circuit also rejected the argument that Federal Rule of Civil Procedure 81(a)(3) justifies a district court in certifying an arbitral class action. The court found 81(a)(3) inapplicable in that, whereas the Rule is only intended to fill gaps, the parties purportedly left no gap but rather chose to prohibit class arbitration. *See Champ*, 55 F.3d at 276. The court insisted that by failing to expressly provide for class arbitration the parties elected nonclass arbitration. *See id.* Further, the court found Rule 81(a)(3) entirely inapplicable, in that it applies only to judicial and not arbitral proceedings under the FAA. *See id.* The court also rejected the idea that the district court could certify an arbitral class using its "inherent equitable powers." *Id.* at 277 n.4.

269. *See Iowa Grain Co. v. Brown*, 171 F.3d 504, 509 (7th. Cir. 1999).

270. *See, e.g., Lopez v. Plaza Fin. Co.*, No. 95-C-7567, 1996 WL 210073, at \*2-3 (N.D. Ill.

without<sup>271</sup> the Seventh Circuit, as well as by a few state courts.<sup>272</sup> However, even assuming that the consolidation cases are relevant to the class action issue,<sup>273</sup> it may prove significant that the Seventh Circuit has recently limited the holding of *Champ*. In *Connecticut General Life Insurance Co. v. Sun Life Assurance Co.*,<sup>274</sup> the court held that a silent and ambiguous contract could be interpreted to allow consolidation.<sup>275</sup>

Apr. 25, 1996).

271. See *Herrington v. Union Planters Bank, N.A.*, No. CIV. A. 2:98CV231GR, 2000 WL 424232, at \*7 (S.D. Miss. Jan. 21, 2000); *Howard v. Klynveld Peat Marwick Goerdeler*, 977 F. Supp. 654, 665 n.7 (S.D.N.Y. 1997), *aff'd*, 173 F.3d 844 (2d Cir. 1999); *McCarthy v. Providential Corp.*, No. C 94-0627 FMS, 1994 WL 387852, at \*8-9 (N.D. Cal. July 19, 1994); *Gammara v. Thorp Consumer Discount Co.*, 828 F. Supp. 673, 674 (D. Minn. 1993), *appeal dismissed*, 15 F.3d 93 (8th Cir. 1994); see also *Collins v. International Dairy Queen, Inc.*, 169 F.R.D. 690 (M.D. Ga. 1997) (stating that the franchisees who were subject to mandatory binding arbitration would not receive notice of class action); *Sanders v. Robinson Humphrey/American Express, Inc.*, 1990 WL 105894, at \*2 (N.D. Ga. 1990) (certifying suit as class action, for settlement purposes only, but observing that absent agreement, "those purchasers who signed arbitration agreements likely would be required to adjudicate their claims individually in separate proceedings").

272. See *Med Ctr. Cars, Inc. v. Smith*, 727 So. 2d 9, 20 (Ala. 1998); *Ex parte Green Tree Fin. Corp.*, 723 So. 2d 6, 10 n.3 (Ala. 1998); *Steinberg v. Prudential-Bache Sec., Inc.*, 1986 WL 5024, at \*4-5 (Del. Ch. Apr. 30, 1986). Most of the courts that have adopted the *Champ* holding have emphasized that by ordering a dispute to classwide arbitration, a court would impermissibly alter the agreement entered into by the parties. See, e.g., *Iowa Grain*, 171 F.3d at 510 (observing that "[b]ecause arbitration is based fundamentally on an agreement between the parties, the kind of class action contemplated by Fed.R.Civ.P. 23(b) is normally unavailable in arbitration"); *Howard*, 977 F. Supp. at 665 n.7 (observing that a plaintiff "who has agreed to arbitrate all claims arising out of her employment may not avoid arbitration by pursuing class claims"); *McCarthy*, 1994 WL 387852, at \*8 (stating that the court lacks authority, absent specific language, to order arbitration to proceed on class basis); *Gammara*, 828 F. Supp. at 674-75 (holding that the court may not order class arbitration and dismissing plaintiff's class allegations because agreement did not provide for class arbitration); *Med Ctr. Cars*, 727 So. 2d at 20 ("Although the plaintiffs' contentions are practically appealing, after reviewing the authorities we conclude that to require classwide arbitration would alter the agreements of the parties, whose arbitration agreements do not provide for classwide arbitration."); *Ex parte Green Tree*, 723 So. 2d at 10 n.3 (stating, in dicta, that "[a]rbitration agreements cannot be forced into the mold of class action treatment without defeating the parties' contractual rights"); *Steinberg*, 1986 WL 5024, at \*5 (holding that to order classwide arbitration "would amount to rewriting the contract between the plaintiff and Prudential-Bache. That contract provides for arbitration under specific and well-established rules that, insofar as this record shows, do not provide for class arbitration."). It is not clear to this author, however, why a *silent* agreement should be interpreted as foreclosing an arbitral class action. See *infra* text accompanying notes 328-54.

273. The relevance is questioned *infra* notes 334-40 and accompanying text.

274. 210 F.3d 771 (7th Cir. 2000).

275. See *id.* at 774-76.

*b. Agreements Addressing Class Actions*

*i. Agreements Precluding Arbitral Class Actions*

Companies seeking to avoid being sued in a class action may draft an arbitration clause or incorporate arbitral rules<sup>276</sup> that explicitly exclude arbitration of class actions.<sup>277</sup> Indeed, one arbitration provider, the National Arbitration Forum (NAF), has marketed its rules to corporations in part with the assurance that its rules do not allow for class actions.<sup>278</sup> Some commentators have assumed that such a clause is valid and must be respected by the courts;<sup>279</sup> however, companies that employ such a clause may be unpleasantly surprised. Depending upon the specific wording, some courts may interpret such a clause to allow *litigation* of class claims.<sup>280</sup> On the one hand, several courts have stated or implied that a company may use explicit language in the arbitration clause

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276. This Article assumes that when an arbitration clause explicitly adopts particular arbitral rules, those rules are effectively part of the contract. Conceivably, a contrary argument might be made under the contract law of certain jurisdictions.

277. Companies typically have not sought to use a form contract other than an arbitration clause to eliminate class action. In fact, this author found no cases discussing such a practice. At least one company, however, now has issued an envelope "stuffer" seeking to eliminate customers' opportunity to sue in a class action, without agreeing to arbitration. *See Sprint PCS Terms and Conditions of Service* effective Apr. 1, 2000 (on file with author).

278. NAF Rule 19.A provides that "consolidations" are permitted only with the consent of all parties. The NAF has relied on this Rule in assuring potential company clients that NAF rules will prevent signatories from being sued in class actions. *See* Letter from Edward C. Anderson, Attorney, NAF (Oct. 20, 1997) (enclosing memorandum of law assuring that courts will not order class treatment pursuant to NAF rules) (on file with author); Letter from Curtis D. Brown, V.P. and General Counsel, NAF, to Robert S. Banks, Jr., (Jan. 14, 1999) (noting that numerous courts have held that arbitration clauses can be used to eliminate class actions and including attachment designed to show NAF rules are more likely than competitor rules to preclude class actions) (on file with author); Letter from Roger S. Haydock, Director of Arbitration, NAF, to Alan Kaplinsky, Attorney, Ballard, Spahr, Andrews & Ingersoll (Apr. 16, 1998) ("[T]he *only* thing which will prevent 'Year 2000' class actions is an arbitration clause in every contract, note, and security agreement.") (on file with the author).

279. *See Vairo, supra* note 41, at 19.

280. This Article urges such an interpretation where the clause does not clearly bar class actions in both litigation and arbitration. *See infra* text accompanying notes 357-59. Moreover, as will be discussed, even a clause which clearly is intended to deprive plaintiffs of *all* class remedies conceivably may be voided on statutory or contractual grounds. *See infra* notes 360-432 and accompanying text.

to deny plaintiffs the opportunity to proceed by class action.<sup>281</sup> By contrast, the Seventh Circuit, in *Nielsen v. Piper, Jaffray & Hopwood, Inc.*,<sup>282</sup> interpreted the securities industry's rules prohibiting arbitral class actions<sup>283</sup> to allow the plaintiff class to pursue its claims of securities fraud through litigation rather than arbitration.<sup>284</sup> Other courts have similarly held that clauses prohibiting classwide arbitration should be interpreted to permit class action litigation of the claim, both in the securities<sup>285</sup> and

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281. For example, *Zawikowski v. Beneficial Nat'l Bank*, No. 98 C2178, 1999 WL 35304, at \*2 (N.D. Ill. Jan. 11, 1999), ordered a consumer class action to be arbitrated, even though the arbitration clause expressly prohibited class actions absent the parties' consent. The court stated "[n]othing prevents the Plaintiffs from contracting away their right to a class action." *Id.* In *Doctor's Assocs., Inc. v. Hollingsworth*, 949 F. Supp. 77, 80 (D. Conn. 1996), involving a class action brought by Subway sandwich shop franchisees against the franchisor, the franchise agreements provided: "[e]ach claim or controversy will be arbitrated by the Franchisee on an individual basis and shall not be consolidated in any arbitration action with the claim of any other franchisee." *Id.* The court compelled arbitration even though the clause excluded class arbitration, implying but not holding that the arbitration would have to be conducted individually. The franchisee attempted to argue that given this clause, the class action claims that had been filed in court fell outside the scope of the arbitration clause and could not be litigated. *See id.* The district court rejected this argument, however, stating that because the franchisor had demanded 18 separate arbitrations and had not sought to consolidate them, the arbitration was permitted by the arbitration clause. *See id.*

282. 66 F.3d 145 (7th Cir. 1995). The district court's prior decision in the same case is reported at *Nielsen v. Greenwood*, 873 F. Supp. 138 (N.D. Ill. 1995) (adopting magistrate's report and holding that where SEC had approved new NASD rule excluding class actions from arbitration, plaintiff class would not be required to arbitrate their class claim against brokerage).

283. *See supra* notes 169-78 and accompanying text.

284. Rejecting the brokerage's argument that plaintiffs should be compelled to resolve their claim through individualized arbitration, the court stated that the contrary result was compelled by straightforward contract interpretation. *See Nielsen*, 66 F.3d at 148 ("This case does not present us with difficult interpretive questions."). Explaining that the brokerage had agreed to be bound by the NASD Code of Arbitration, and that this Code prohibited arbitration of class claims, the court summarized that "the contract expressly prohibited PJH from compelling arbitration of this claim." *Id.* The *Nielsen* case was more complex than most in that it involved a transitional situation. The parties had originally agreed to arbitrate their disputes prior to when the NASD and the NYSE adopted the prohibition on arbitrating class actions. *See id.* at 146-49. Nonetheless, the court found that the new rule was applicable in that the original arbitration agreement had provided that disputes would be governed by rules "then in effect," *id.* at 146, and in that the new rule applied to "all open arbitrations." *Id.* at 149.

285. *See, e.g., Olde Discount Corp. v. Hubbard*, 4 F. Supp. 2d 1268, 1271 (D. Kan. 1998) (concluding that because "[t]he plain language of the arbitration agreements and incorporated rules dictate that Mr. Hubbard's [class action race discrimination] claim is ineligible for arbitration at this time," it would be inappropriate for the court to compel arbitration of such claim), *aff'd*, 172 F.3d 879 (10th Cir. 1999); *Martens v. Smith Barney, Inc.*, 181 F.R.D. 243, 252 (S.D.N.Y. 1998) (concluding class action claim not arbitrable because U-4

nonsecurities context.<sup>286</sup>

## *ii. Agreements Allowing Class Arbitration*

It is highly unlikely that companies that use contracts of adhesion to impose binding arbitration on their customers would draft a contract explicitly allowing for class arbitration.<sup>287</sup> Several governments have adopted arbitration programs for resolving taxation or other disputes, however, and their rules at times allow for class arbitration. Where they do, courts have allowed arbitrations to proceed on a class basis.<sup>288</sup>

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forms signed by plaintiffs stated that class actions suits are not subject to NASD arbitration); *In re Regal Communications Corp. Sec. Litig.*, No. 94-179, 1995 WL 550454, at \*11 (E.D. Pa. Sept. 14, 1995) (holding plaintiffs class action claim was not subject to mandatory arbitration because “[b]oth the NYSE and NASD have promulgated rules which make any claim filed as a class action ineligible for arbitration”); *Scher v. Equitable Life Assurance Soc’y*, 866 F. Supp. 776, 777 (S.D.N.Y. 1994) (observing that class actions are not subject to compulsory arbitration under the NASD rules). This author did not locate any decisions reaching the contrary result, of requiring plaintiffs asserting class claims in the securities context to arbitrate such claims on an individual basis. It should be noted, however, that a person who is a member of a class action will not be *required* to arbitrate her claim. Putative class members still have the option to arbitrate their claim if they choose to pursue an individual claim through arbitration, rather than participating in a class action. *See* NYSE Rule 600 (d); NASD Rule 12 (d)(3); *see also In re Piper Funds Inc. v. Piper Capital Management, Inc.*, 71 F.3d 298, 299 (8th Cir. 1995) (holding that investor who elected not to participate in class action and instead preferred to arbitrate claim could not be enjoined from arbitrating its claim, pending the finalization of the class action settlement).

286. *See, e.g., Minge v. Cohen*, No. Civ.A. 98-2352, 1999 WL 1021836, at \*1 (E.D. La. Nov. 9, 1999) (denying motion to compel arbitration where plaintiff brought a putative class action and where customer agreement stated “[n]o person shall bring a putative or class action to arbitration”); *Ramirez v. Circuit City Stores, Inc.*, 90 Cal. Rptr. 2d 916, 918-19 (Cal. Ct. App. 1999) (observing that mandatory arbitration clause imposed on employees—which deprived arbitrator of power to hear class actions—had been interpreted by trial court to allow litigation of such claims, and concluding that the clause was, in any event, unconscionable), *review granted*, 94 Cal. Rptr. 2d 1 (Cal. 2000).

287. *See supra* text accompanying notes 1-10 (discussing companies’ opposition to class litigation); *supra* note 278 (discussing National Arbitration Forum’s use of marketing boasting of the unavailability of class actions under their rules); *see also Vairo, supra* note 41, at 19 (observing that “[i]t is rare for drafters of arbitration agreements to include a provision that explicitly allows for classwide arbitration” since “business entities are not inclined to provide for the aggregation of claims because of the potential for greater exposure”). Indeed, I have located no examples of such a clause.

288. *See, e.g., Callaway v. Carswell*, 242 S.E.2d 103, 106-07 (Ga. 1978) (stating that class arbitration would not be permitted in the future with respect to the purely legal question of whether county could assess property piecemeal, but implying that class arbitrations might still be permitted as to valuation issues); *Boynton v. Carswell*, 233 S.E.2d 185, 186-87 (Ga. 1977) (approving use of arbitral class actions to resolve taxpayer claims of overassessment);

*B. Imposition of Binding Arbitration Subsequent to Filing of Class Action*

An entirely different set of legal issues is raised when a putative class action has already been filed, and a company attempts to apply a binding arbitration provision to the putative class members and then use this provision to prevent such persons from participating in the class action.<sup>289</sup> Thus far, courts have not looked favorably on this strategy. In *Carnegie v. H&R Block, Inc.*,<sup>290</sup> customers of the H&R Block "Rapid Refund" program filed a class action claiming that they were lured to take out loans and pay finance charges.<sup>291</sup> Prior to certification of the class, the company imposed an arbitration clause and sought to apply it to the putative class members.<sup>292</sup> A New York court ruled that the clause adopted by H&R Block could not be used by the company to prevent customers' participation in the class action, unless those customers were provided a separate form advising them of their rights and then chose arbitration over the class action by signing the form.<sup>293</sup>

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*Stevenson v. Commonwealth*, 413 A.2d 667, 668 (Pa. 1980) (permitting maintenance of arbitral class action against state because the rules adopted pursuant to statute governing Board of Arbitration Claims provided that proceedings should be handled, "as nearly as possible, in accordance with the Pennsylvania Rules of Civil Procedure relating to the action of Assumpsit").

289. Companies' *deliberate* imposition of arbitration, after the filing of a class action must be distinguished from a situation in which a defendant may inadvertently, or as a matter of administrative simplicity, impose binding arbitration on putative class members, but does not actually seek to use the arbitration clause to defeat the class action. In other words, a defendant may occasionally decide to impose binding arbitration on all current customers, a group which inadvertently includes putative class members. One author found that at the time Bank of America imposed its binding arbitration clause on its customers, the bank had seven class actions pending against it. *See Davis, supra* note 12, at B3. The author noted, however, that the bank had not yet attempted to arbitrate any of the pending actions nor to use the clause to eliminate the class actions. *See id.*

290. 687 N.Y.S.2d 528 (N.Y. Sup. Ct. 1999).

291. *See id.* at 530.

292. *See id.* Specifically, the loan application form used in connection with these transactions was revised to include a clause requiring arbitration of past as well as future claims, and to explicitly prohibit class actions absent H&R Block's consent. *See id.* H&R Block's attorney drafted a letter stating that "the claims of that portion of the putative class who were recipients of RALs in 1997 . . . shall be arbitrated individually . . . and cannot proceed in this putative class action." *Id.*

293. *See id.* at 533. The court explained that while class actions "serve an important function in our system of civil justice," they also present "opportunities for abuse," and that "[b]ecause of the potential for abuse, a district court has both the duty and the broad



Relying on cases restricting communication between defendants and putative class members, in which those communications are found to interfere impermissibly with the class or to violate relevant attorney disciplinary rules,<sup>294</sup> the court concluded that “the enforceability of the arbitration clause in the revised RAL form must be conditioned on steps to protect the fairness of the class action process in this case.”<sup>295</sup> The notification and opt-out<sup>296</sup> process imposed by the court was designed to reconcile these concerns for fairness with the court’s recognition of the general support for arbitration,<sup>297</sup> and the fact that some customers might prefer arbitration to the class action.<sup>298</sup>

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authority to exercise control over a class action and to enter appropriate orders governing the conduct of counsel and the parties.” *Id.* at 531 (citing *Gulf Oil Co. v. Bernard*, 452 U.S. 89, 99-100, 101 (1981)).

294. *See, e.g., In re School Asbestos Litig.*, 842 F.2d 671, 681-83 (3d Cir. 1988); *Erhardt v. Prudential Group, Inc.*, 629 F.2d 843, 846 (2d Cir. 1980); *Hampton Hardware, Inc. v. Cotter & Co.*, 156 F.R.D. 630, 634 (N.D. Tex. 1994); *Haffer v. Temple Univ. of Commonwealth Sys. of Higher Educ.*, 115 F.R.D. 506, 510 (E.D. Pa. 1987); *In re Federal Skywalk Cases*, 97 F.R.D. 370, 377 (W.D. Mo. 1983). The *Carnegie* court explained that “[t]he test for whether a party, with or without aid of its counsel, has had impermissible contact with potential members of the plaintiff class, is whether the contact is coercive, misleading, or an attempt to affect a class member’s decision to participate in the litigation.” *Carnegie*, 687 N.Y.S.2d at 531 (citing *Kleiner v. First Nat’l Bank of Atlanta*, 751 F.2d 1193, 1203 (11th Cir. 1985)).

295. *Id.* at 532. The court explained that “those who signed the RAL application containing the arbitration clause were completely unaware of this litigation and that by signing the RAL form, they were waiving their right to participate in this class action.” *Id.* It further opined that H&R Block’s tactic of requiring customers to sign the form, without informing them about the existence of the class action and the company’s refusal to consent to class certification, was “patently deceptive.” *Id.*

296. It is significant that as the procedure devised by the court was an “opt out,” those putative class members who ignored the supplemental notice or chose to take no action would remain members of the class, and would not be precluded from participation by the new arbitration clause. *See id.* Had the court instead required such persons to “opt in” to the class, or “opt out” of the arbitration, it is likely that many more customers would have ended up arbitrating rather than litigating their claims. *See generally HENSLER ET AL., supra* note 1, at 26 (observing that “[t]he social science research on active versus passive assent suggests that minority and low-income individuals might be disproportionately affected by an opt-in requirement”); Eric D. Green, *What Will We Do When Adjudication Ends? We’ll Settle in Bunches: Bringing Rule 23 Into the Twenty-First Century*, 44 UCLAL. REV. 1773, 1782 (1997) (stating that while theoretically there may be no difference between opt-in and opt-out class actions, testimony before the Advisory Committee in 1997 showed that in fact there is an enormous difference); Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356, 397-98 (1967) (arguing for opt-out rather than opt-in class actions, to better serve the interests of class members).

297. *See Carnegie*, 687 N.Y.S.2d at 532.

298. *See id.* at 533; *see also H&R Block, Inc. v. Haese*, No. 13-97-673-CV, 2000 WL

Similarly, in *Navarro-Rice v. First USA Bank*,<sup>299</sup> First USA Bank attempted to use a new binding arbitration agreement to defend against a putative class action alleging it had illegally increased the interest rate charge for its credit card.<sup>300</sup> Although the clause exempted class action claims to the extent they “have been finally certified as class actions and . . . notice of class membership has been given as directed by the court” prior to January 1, 1998,<sup>301</sup> timing was such that the *Navarro-Rice* suit could not possibly meet this schedule, so that only those customers who closed their accounts would be able to avoid arbitration.<sup>302</sup> The Oregon trial court refused to allow First USA to require the putative class members to arbitrate their claims, instead granting a temporary restraining order which later functioned as a preliminary injunction restraining defendant “from attempting to enforce any requirement to arbitrate, against any plaintiff or putative class member in this action, as to any claim asserted in Plaintiffs’ First Amended Complaint or any substantially similar claim until further order of this Court.”<sup>303</sup>

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924805, at \*3-4 (Tex. App. June 29, 2000) (affirming in relevant part trial court’s order precluding defendant from imposing arbitration regarding existing claims of members of certified class).

299. Memorandum In Support of Plaintiff’s Motion for Preliminary Injunction at 2, *Navarro-Rice v. First USA Bank* (Oregon Cir. Ct., Multnomah County Dec. 1, 1997) (Civ. No. 97-09-06901) (on file with author).

300. Specifically, First USA sent a substantial number of its customers a notice stating that unless they closed their account by December 30, 1997, they would be covered by a new card agreement requiring that all disputes, including “claims now in existence,” be arbitrated rather than litigated. *Id.* at 2.

301. *Id.*

302. *See id.* at 2-3.

303. Temporary Restraining Order at 2, *Navarro-Rice v. First USA Bank* (Oregon Cir. Ct., Multnomah County July 25, 1998) (No. 9709-06901) (on file with author). While the court issued no published decision and provided no reasoning in its written order, the transcript of the hearing on plaintiff’s motion for a temporary restraining order reflects the court’s concerns that defendants were seeking to interfere with the proper definition of the class and that persons were being provided with inadequate information to make an informed decision, particularly at a time when the court should have been supervising their participation in the class action. The court repeatedly expressed its concern that although the plaintiffs’ rights to participate in the class action were “fixed on the date the action was commenced,” Transcript Hearing on Temporary Restraining Order at 64 (on file with author), the defendant was claiming a right to “change the status quo” while the court was still considering whether to certify the class. *See id.*; *see also id.* at 65 (“How is it that the defendant can say unilaterally we are just going to prohibit the court from addressing the issues that are properly before it by soliciting all of these people out under a general

Finally, in *Powertel, Inc. v. Bexley*,<sup>304</sup> the court addressed a situation in which the day after plaintiff filed a putative class action against Powertel, she received with her bill a pamphlet describing the terms of Powertel's service and also requiring arbitration of all disputes.<sup>305</sup> The court refused to enforce the clause in part because it purported to apply retroactively.<sup>306</sup> Emphasizing that by filing the class action Ms. Bexley had already "elected a remedy that was inconsistent with arbitration,"<sup>307</sup> the court stated:

It is one thing to say that the failure to object to the arbitration clause is an implied consent to arbitration, but it is quite another to conclude that the failure to object is the equivalent of a voluntary decision to dismiss a pending lawsuit. Nothing in the record suggests that the plaintiff agreed to dismiss her suit, and we cannot draw such a conclusion on the basis of her failure to object to [a] new condition sent to her along with her phone bill.<sup>308</sup>

### III. HOW COURTS SHOULD BE HANDLING THE MEETING OF CLASS ACTIONS WITH BINDING ARBITRATION

Section III(A) will first address the question of whether companies ought to be permitted to use arbitration agreements to eliminate persons' rights to proceed by way of class action in either litigation or arbitration. It concludes that existing federal statutes and traditional contract doctrines should sometimes, but not always, prohibit companies from entirely precluding consumers or others from bringing class actions. Second, Section III(B) concludes that while parties should generally be allowed to choose to handle their

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arbitration policy?"); *id.* at 72 ("How can your client unilaterally, without notice to this potential group, effect a contract modification that works a limitation on the court's ability to adjudicate the litigation if the matter develops that far?"); *id.* at 66 (expressing concerns about lack of access to counsel and absence of court supervision). The judge noted that "people . . . may be members of this class without even knowing that the class exists or that there is an opportunity to consider those very kinds of issues within the context of this pending proceeding." *Id.* at 67.

304. 743 So. 2d 570 (Fla. Dist. Ct. App. 1999).

305. *See id.* at 572.

306. *See id.* at 574.

307. *Id.* at 577.

308. *Id.* The court also found the clause unconscionable, for reasons discussed elsewhere in this Article. *See supra* notes 232-36 and accompanying text.

class actions through arbitration, rather than through litigation, their agreements on these issues may be constrained by statutory, contractual, and constitutional doctrines. Finally, Section III(C) approaches the same issues from a different perspective, providing courts with a guide on how they should resolve these tough questions.

*A. Using Existing Law to Preserve Plaintiffs' Right to Class Actions*

The most critical question underlying this entire debate is whether companies do or should have the power to eliminate entirely the class action remedy; however, defense attorneys, courts, and even commentators often fail to focus on this issue.<sup>309</sup> Perhaps, not long ago, the question was not addressed because it was *assumed* that companies could not entirely eliminate the class action in all forums.<sup>310</sup> Today, however, the issue must be addressed directly, because it is evident that at least some defense attorneys are seeking to use binding arbitration to accomplish the total elimination of class actions.<sup>311</sup> This section suggests that while the language of the arbitration clause is one important factor courts should consider in determining how to handle arbitration and class actions, it should not always be determinative.

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309. Instead, they may address the question of whether a class action claim may be sent to arbitration without determining whether arbitral class actions are permitted. *See supra* notes 211-25 and accompanying text. Or, they may address the question of whether class action arbitration may be ordered without considering whether it should be left to the arbitrators to decide if a class action is permitted. *See supra* note 252 and accompanying text.

310. As discussed earlier, it seems that the securities industry did not contemplate seriously the possibility that it might use arbitration clauses to entirely eliminate class actions, and instead merely tried to choose between the litigated class action and the arbitrated class action. *See supra* notes 169-78 and accompanying text. Similarly, the early commentators on class actions and arbitration did not address whether arbitration agreements could be used to eliminate entirely class actions. *See generally Quagmire, supra* note 41 (arguing, similarly, that class actions and arbitrations should be joined); Waltcher, *supra* note 41 (exploring the advantages of combining class actions with arbitration).

311. *See supra* notes 4-17 and accompanying text. At least one company is also trying to eliminate class actions without imposing arbitration. *See Sprint PCS Terms, supra* note 277.

### 1. *Many Claims can be Brought Only as Class Actions*

As the Supreme Court and numerous commentators have recognized, many claims can be brought only if pursued as a class action and not on an individual basis.<sup>312</sup> Certainly this is true not only in general, but also of the arbitration matters with which this Article is concerned. It also seems clear that denial of the class action remedy will potentially be detrimental not only to the affected putative class plaintiffs, but also to society at large, in that absent a class action, wrongful conduct may go unpunished and undeterred and laws may go unenforced.<sup>313</sup> The examples of actual arbitration cases, discussed in the introduction to this Article, show that this concern is not hypothetical.<sup>314</sup> Some courts have explicitly recognized that requiring disputes to be pursued on an individual basis, in arbitration, would as a practical matter preclude plaintiffs from pursuing their claims under federal or state consumer protection statutes.<sup>315</sup>

While many praise arbitration as relatively inexpensive, and geared to help persons with small claims to achieve justice, no one has seriously suggested that arbitration ensures an economically viable forum for persons with claims of five dollars, ten dollars, or even two hundred dollars. Rather, in many arbitration venues the minimum filing fee will exceed the size of a small claim, even before one begins to take account of arbitrators' salaries, hearing fees, room fees, or lawyers' fees.<sup>316</sup> It is therefore not surprising that after

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312. See *supra* note 104 and accompanying text.

313. See generally Fiss, *supra* note 108 (contending that settlements may not serve the public interest); Geraldine Szott Moohr, *Arbitration and the Goals of Employment Discrimination Law*, 56 WASH. & LEE L. REV. 395, 396 (1999) (arguing that "arbitration is not an effective forum in which to satisfy the public policy goals of the employment discrimination statutes, even when employees are accorded a fair hearing").

314. See *supra* notes 28-40 and accompanying text.

315. See, e.g., *Med Ctr. Cars, Inc. v. Smith*, 727 So. 2d 9, 20 (Ala. 1998) (recognizing the practical appeal of plaintiffs' argument that requiring each individual to pay over \$500 as a filing fee would preclude plaintiffs from pursuing small claims in arbitration).

316. See Victoria Nugent, *Arbitration Clauses That Require Individuals to Pay Excessive Fees Are Unconscionable*, 5 THE CONSUMER ADVOCATE, Sept. 1999, at 8 (on file with author) (taking note of initial filing fees, daily hearing fees, room rental fees, and arbitrators' hourly rates); Cliff Palefsky, *The Civil Rights Struggle of the '90s: From "Separate But Equal" to "Just Another Forum,"* THE RECORDER (San Francisco), May 1999, at 35, available in WL

credit card company First USA imposed its binding arbitration program in early 1998, just four consumers filed arbitration claims against the company.<sup>317</sup>

One can imagine the responses that may be offered by those seeking to eliminate class actions, but each can easily be answered.<sup>318</sup> The availability of a small statutory damages award, even perhaps a few hundred dollars, is unlikely to affect the viability of most claims. Further, most persons with small claims cannot afford to file or certainly would not choose to file, based only on the hope that a portion of the fees and costs would be reimbursed in the event of victory.<sup>319</sup> Most consumer claims require sufficient legal and factual analysis so that persons could not successfully expect to represent themselves, and few lawyers would be willing to take a very small case based only on the possible recovery of some attorney's fees and costs.<sup>320</sup> Although some arbitral venues now

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5/1999 RECORDER-SF 535 ("The costs for employment arbitrations are frequently in excess of \$40,000. Even at the theoretically not-for-profit American Arbitration Association, the filing fee alone for a discrimination case can be as high as \$7,000, and that's before the arbitrators charge at least \$350 per hour, per arbitrator, in addition to other administrative charges."); see also Plaintiffs' Response to Defendant First USA's Motion To Dismiss and/or Stay Proceedings and To Compel Arbitration at 44, *Marsh v. First USA Bank, N.A.* (N.D. Tex. 1999) (No. 3-99CV0783-T) ("Without the availability of the class action tool, most lawyers experienced in consumer law cannot justify handling [small consumer claims], particularly where the claims are relegated to mandatory arbitration. Consumers cannot afford to hire and pay on an hourly basis an attorney to pursue TILA claims for less than \$1,000. Even though the Act permits recover of fees, neither the client nor the attorney is willing to assume the cost of presenting a TILA claim when the underlying damage is so small. A contingent fee arrangement is similarly inadequate because of the size of the consumer claim.").

317. See Mayer, *Win Some, Lose Rarely?*, *supra* note 11, at E1. By contrast, in the same period, First USA filed 51,622 arbitration claims against consumers. See *id.*; see also Plaintiffs' Response at 25, *Marsh* (No. 3-99CV0783-T) (stating that fewer than 10 cardholders had attempted to arbitrate disputes with First USA since it imposed mandatory arbitration in early 1998) (on file with author). The brief also argues that the fees imposed by the National Arbitration Forum under the program are both "excessive and indeterminate." *Id.* at 30-35.

318. Many of these arguments have been made by Petitioner and by some of the amici supporting their position in *Green Tree Financial Corp. v. Randolph*, and have been opposed by Respondent and some of its amici. See *supra* notes 51-52.

319. See *Shankle v. B-G Maintenance Management, Inc.*, 163 F.3d 1230, 1234 n.4 (10th Cir. 1999) (stating that "it is unlikely that an employee in [the plaintiffs'] position, faced with the mere possibility of being reimbursed for arbitrator fees in the future, would risk advancing those fees in order to access the arbitral forum").

320. Quite possibly the inability to obtain counsel has deterred many potential plaintiffs from filing arbitration claims against First USA. See Mayer, *Win Some, Lose Rarely?*, *supra*

claim to make available fee waivers or lower cost systems for persons who are indigent or bringing small claims,<sup>321</sup> these systems do not clearly provide all persons with an adequate forum within which to bring small claims.<sup>322</sup> Moreover, money aside, most people simply will not expend the time or emotional energy to pursue a small claim.

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note 11, at E1 (stating that only four consumers had filed claims since early 1998).

321. The NAF, in its rules effective December 1, 1999, spells out in Rule 45 the possibility that an "indigent Party, who is an individual and not a business or other entity, may request a waiver of the Small Claim filing and administrative fees" by filing a request with the Director. National Arbitration Forum, *Rule 45. Waiver of Fees* (visited Apr. 8, 2000) <<http://www.arb-forum.com/library/code/part7.html>> [hereinafter NAF, *Rule 45*].

The AAA, in its *Arbitration Rules for the Resolution of Consumer-Related Disputes*, provides that consumers who bring claims for less than \$10,000 can obtain an arbitration for just \$125, including the arbitrator's fee. See AMERICAN ARBITRATION ASSOCIATION, *ARBITRATION RULES FOR THE RESOLUTION OF CONSUMER-RELATED DISPUTES* (1999) (on file with author). See generally *Dobbins v. Hawk's Enters.*, 198 F.3d 715, 717 (8th Cir. 1999) (holding that plaintiffs should not have been permitted to challenge arbitration clause calling for AAA arbitration as unconscionable until they first attempted to explore fully AAA's fee waiver procedures).

322. As to the waiver provided by the NAF, the factual predicates to obtain a waiver are not detailed. That is, the NAF rules set out no specific guidelines for determining indigency. See generally NAF, *Rule 45*, *supra* note 321 (providing no definition of "indigent"). Although the consumer is directed to provide evidence of family size, income, assets, and liabilities, the criteria are left to the discretion of the director of the NAF. See *id.* In *Baron v. Best Buy Co.*, 75 F. Supp. 2d 1368 (S.D. Fla. 1999), the court emphasized this arbitrariness in refusing to grant a defendant's motion to compel arbitration before the NAF. Finding the clause unenforceable, the court stated:

The Defendants have failed to demonstrate in this record that the National Arbitration Forum is a neutral, inexpensive and efficient forum to determine these claims as required by law. Further, it is unclear what procedures the NAF would apply to this dispute, given the changing nature of the rules they adopt and the almost total discretion of the director to issue or modify any award or rule.

*Id.* at 1370. Note that the decision has been appealed, and that the matter has been stayed pending the appeal. See *Baron v. Best Buy Co.*, 79 F. Supp. 2d 1350 (S.D. Fla. 1999). Moreover, the NAF waiver is only temporary. NAF provision 45(D) states that if a waiver is granted, and if the indigent ultimately recovers money, the fees must be paid out of the settlement or award. Finally, it is not clear whether the waiver would cover arbitrator salaries, and it certainly does not cover attorney fees. See NAF, *Rule 45*, *supra* note 321; see also Plaintiff's Response at 28-30, *Marsh* (No. 3-99CV0783-T) (arguing that because the NAF changes rules frequently, it is impossible to know what rules would be applied to the dispute).

The inexpensive AAA procedure applies only where the consumer is willing to forego all personal appearances, and instead allow the arbitrator to decide the claim exclusively on a paper record. See AAA Consumer Rule 5 (on file with author). If the consumer wants to have a telephonic hearing she must pay an additional \$100, and if she wants an in-person hearing she must "pay all the administrative fees, expenses, and compensation costs in the Commercial Arbitration Rules." *Id.* Rule 6 (on file with author).

Yet, the mere fact that claims are not viable on an individual basis does not mean that they are not worth pursuing from a group or societal standpoint. Foreclosing such claims may allow companies to obtain large and illegal benefits.<sup>323</sup> Although an individual plaintiff may have been deprived of only ten dollars, a company may stand to profit by one million dollars if 100,000 plaintiffs are involved. Thus, even commentators Stephen Kupperman and George Freeman, who argue that "arbitration provides a reasonable forum for persons with small claims,"<sup>324</sup> do not go so far as to argue that arbitration can fully substitute for class action relief.<sup>325</sup>

Nor is it fair to assume that federal or state administrative agencies can enforce the laws when persons with small claims cannot afford to do so. Not all statutes provide for such administrative enforcement. Moreover, even when administrative enforcement is available, agency resources are typically too small to afford a remedy to most claimants.

In short, courts should consider the fact that some cases are feasible only if pursued as a class action.<sup>326</sup> It must be recognized, however, that some claims filed as class actions may also be feasible on an individual basis.

## *2. The Importance of Agreement Language*

Traditionally, because arbitration is said to be primarily a matter of contract, courts focus closely on the wording of the arbitration clause to determine whether arbitration is required, and on what terms. In the past, very few arbitration agreements have expressly discussed the treatment of class actions. This subsection will first discuss how courts ought to interpret those arbitration clauses that are silent on the subject of class actions. It will next discuss how

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323. Cf. Moohr, *supra* note 313, at 427-32 (discussing the importance of litigation to deter companies from behaving illegally).

324. Kupperman & Freeman, *supra* note 167, at 1591.

325. See *id.* ("Even if arbitration does not satisfy all the policies underlying the class action device, the question arises whether arbitration provides an appropriate forum for resolution of class actions.").

326. The question of whether the arguable benefits of class actions are outweighed by their costs is considered later in this Article as part of the discussion of possible legislative reform. See *infra* notes 489-93 and accompanying text.



courts ought to interpret clauses that expressly preclude class actions. As companies are increasingly perceiving arbitration as a way to avoid class actions, clauses are becoming more common.<sup>327</sup>

*a. Courts Should Not Interpret Silent Agreements as Barring Class Arbitration*

As a matter of pure contract interpretation it is striking, and rather odd, that so many courts have interpreted silence in arbitration agreements to foreclose rather than to permit arbitral class actions. Numerous courts have held that because they must be true to the parties' contractual choice, they may not compel, and perhaps may not even permit, arbitral class actions.<sup>328</sup> Rather than engaging in adequate analysis, however, most courts have simply *assumed* that a silent arbitration agreement should be interpreted to foreclose arbitral class actions without fully considering the ramifications of the interpretation.

To the extent courts have focused at all on the meaning of a silent arbitration agreement for class actions, they have done so, as discussed above, by drawing an analogy to the question of whether courts may order consolidation of two or more arbitration matters absent an express contractual provision.<sup>329</sup> In the consolidation area, although a leading commentator,<sup>330</sup> one federal appeals court,<sup>331</sup> and

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327. See *supra* note 5.

328. See *supra* notes 262-75 and accompanying text.

329. See *id.* The leading case is *Champ v. Siegel Trading Co.*, 55 F.3d 269, 274-75 (7th Cir. 1995). Other courts, in following *Champ*, have also relied on the "consolidation" cases. See, e.g., *McCarthy v. Providential Corp.*, No. C 94-0627 FMS, 1994 WL 387852, at \*8-9 (N.D. Cal. July 19, 1994); *Gammaro v. Thorp Consumer Discount Co.*, 828 F. Supp. 673, 674 (D. Minn. 1993); *Med Ctr. Cars, Inc. v. Smith*, 727 So. 2d 9, 20 (Ala. 1998). Interestingly, in *Keating v. Superior Court*, 645 P.2d 1192 (Cal. 1982), the California Supreme Court used the consolidation analogy to support a classwide arbitration order, stating that courts have frequently ordered consolidation of arbitral matters in the interests of justice. See *id.* at 1208-09.

330. See Thomas J. Stipanowich, *Arbitration and the Multiparty Dispute: The Search for Workable Solutions*, 72 IOWA L. REV. 473, 475-76 (1987) [hereinafter Stipanowich, *Arbitration and the Multiparty Dispute*] (arguing that consolidation can be essential to achieve efficient dispute resolution, and that even absent explicit contractual authorization, courts should be permitted to order consolidation of arbitration disputes).

331. See *New England Energy, Inc. v. Keystone Shipping Co.*, 855 F.2d 1, 5 (1st Cir. 1988).

multiple state courts<sup>332</sup> have concluded that courts should be permitted to order consolidation where the agreement is silent, most federal appellate courts considering the question have reached the opposite conclusion.<sup>333</sup>

The consolidation analogy, however, is highly problematic. To the extent that the anticonsolidation cases are wrongly decided, their holdings should not be expanded.<sup>334</sup> Significantly, the Proposed Revised Uniform Arbitration Act would *allow* courts to order consolidation, unless the parties' arbitration agreement expressly excludes consolidation.<sup>335</sup> Admittedly, however, absent statutory

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332. See *Litton Bionetics, Inc. v. Glen Constr. Co.*, 437 A.2d 208, 209 (Md. 1981); *Grover-Diamond Assocs. v. American Arbitration Ass'n*, 211 N.W.2d 787, 788 (Minn. 1973); *Exber, Inc. v. Sletten Constr. Co.*, 558 P.2d 517, 523-24 (Nev. 1976); *James Stewart Polshek & Assocs. v. Bergen County Iron Works*, 362 A.2d 63, 70 (N.J. Super. Ct. Ch. Div. 1976); *County of Sullivan v. Edward L. Nezelek, Inc.*, 366 N.E.2d 72, 73 (N.Y. 1977).

333. See cases cited *supra* notes 269-72. See generally 3 IAN R. MACNEIL ET AL., *FEDERAL ARBITRATION LAW: AGREEMENTS, AWARDS AND REMEDIES UNDER THE FEDERAL ARBITRATION ACT* § 33.3.2 (1994) (discussing basic standards for ordering consolidation). A recent Seventh Circuit decision reins in this doctrine somewhat. In *Connecticut General Life Insurance Co. v. Sun Life Assurance Co.*, 210 F.3d 771 (7th Cir. 2000), the court rejected the argument that consolidation is only permitted where it is clearly or expressly allowed by the arbitration clause, instead holding that the court could use normal contract interpretation tools to discern whether the parties intended to allow consolidation. See *id.* at 773-75.

334. This author believes that the cases prohibiting consolidation, absent explicit language, are wrong for the reasons set out by Professor Stipanowich. Professor Stipanowich argues that, as a matter of policy, consolidation is often desirable for all concerned. See Stipanowich, *Arbitration and the Multiparty Dispute*, *supra* note 330, at 480-82. Yet, arbitrators frequently lack the knowledge or ability to order consolidation. See *id.* at 513-14. Further, "[p]ractically speaking, the absence of a provision specifically addressing multiparty arbitration probably signifies only that the parties did not consider the matter." *Id.* at 496. Professor Stipanowich calls for law reform, if necessary, to allow courts to order consolidation when it would be appropriate. See *id.* at 523-28.

335. The Draft for Approval of the Proposed Revised Uniform Arbitration Act § 10 states:

(a) Except as provided in subsection (c), upon motion of a party to an agreement to arbitrate or to an arbitration proceeding, the court may order consolidation of separate arbitration proceedings as to all or some of the claims if:

- (1) there are separate agreements to arbitrate or separate arbitration proceedings between the same persons or one of them is a party to a separate agreement to arbitrate or a separate arbitration proceeding with a third person;
- (2) the claims subject to the agreements to arbitrate arise in substantial part from the same transaction or series of related transactions;
- (3) the existence of a common issue of law or fact creates the possibility of conflicting decisions in the separate arbitration proceedings; and
- (4) the prejudice resulting from a failure to consolidate is not outweighed by the risk of undue delay or prejudice to the rights of or hardship to

revision, this argument will have little weight in those jurisdictions in which the highest court has already ruled that courts may not order consolidation where the contract is silent.

Most important, therefore, is the fact that the analogy between class actions and consolidations is inapt. First, the consequences of a court's refusal to order consolidation of two or more arbitral matters are far different than the consequences of a court's refusal to allow an arbitral matter to proceed as a class action. A court will only be faced with the consolidation issue after two or more arbitrations have been filed. Without consolidation, the disputes can still be aired, albeit at greater expense. By contrast, many small claims simply cannot be heard unless the claims are allowed to proceed by way of class action.<sup>336</sup>

Second, whereas a consolidation order may well cause conflict in interpreting multiple contracts, an order for class arbitration need not. As the court in *Keating* explained,

Consolidated arbitration often involves a tripartite relationship in which the parties in dispute each have a contract with a third party, but not with each other. Each contract may provide a different procedure for arbitration, or a different method of selecting the arbitrator. Federal courts have held that a court "can mold the method of selection and the number of arbitrators to implement the consolidated proceedings." . . . Thus, a party may be forced into a coordinated arbitration proceeding in a dispute with a party with whom he has no agreement, before an arbitrator he had no voice in selecting and by a procedure he did not agree to.

In these respects, an order for classwide arbitration in an adhesion context would call for considerably less intrusion upon

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parties opposing consolidation.

(b) The court may order consolidation of separate arbitration proceedings as to certain claims and allow other claims to be resolved in separate arbitration proceedings.

(c) The court may not order consolidation of the claims of a party to an arbitration agreement which prohibits consolidation.

*Proposed Revisions of the Uniform Arbitration Act*, *supra* note 46, § 10. The Reporter's Notes explain that the provision is designed to effectuate efficiency in conflict resolution and avoid conflicting results. *See id.* at Reporter's Note 3.

336. *See supra* note 104.

the contractual aspects of the relationship. The members of a class subject to classwide arbitration would all be parties to an agreement with the party against whom their claim is asserted; each of those agreements would contain substantially the same arbitration provision; and if any of the members of the class were dissatisfied with the class representative, or with the choice of arbitrator, or for any other reason would prefer to arbitrate on their own, they would be free to opt out and do so.<sup>337</sup>

Third, where an arbitrator might have the power to order consolidation on his or her own, it is not at all clear that arbitrators could properly handle class actions without assistance from the courts. As has been noted,<sup>338</sup> and as will be discussed in further detail below,<sup>339</sup> class actions raise important due process issues. Therefore, if an arbitrator, on her own, were to attempt to handle certification, notice and other class issues, it is not clear that her decision would be binding on absent class members. In other words, while a court's refusal to order consolidation potentially still leaves arbitrators the flexibility to consolidate matters on their own,<sup>340</sup> a

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337. *Keating v. Superior Court*, 645 P.2d 1192, 1208-09 (Cal. 1982) (quoting *In re Czarnikow-Rionda Co.*, 512 F. Supp. 1308, 1309 (S.D.N.Y. 1981)). The court's point would be undermined in cases in which a class action was deemed to be a mandatory or non-opt-out class action. While the Federal Rules of Civil Procedure mandate that persons be allowed to opt out of class actions brought under Rule 23(b)(3), opt out is not always permitted for class actions brought for joint claims or injunctive relief under Rule 23(b)(1) or Rule 23(b)(2). See FED. R. CIV. P. 23(b). See generally NEWBERG & CONTE, *supra* note 90, §§ 1.22, 16.17 (discussing the standards and policy rationale for opting out).

338. See *supra* notes 109-22 and accompanying text.

339. See *infra* notes 438-71 and accompanying text.

340. Interestingly, very few of the consolidation cases discuss whether the arbitrators, as opposed to the court, might have the power to consolidate. Those few decisions that have, vary in their approach. In *Del E. Webb Construction v. Richardson Hospital Authority*, 823 F.2d 145 (5th Cir. 1987), the court acknowledged that the issue was not clear, but concluded that consolidation could be resolved only by the court. See *id.* at 149-50. *Connecticut General Life Insurance Co. v. Sun Life Assurance Co.*, 210 F.3d 771 (7th Cir. 2000), observed that neither party had argued that arbitrators, rather than the court, should decide the consolidation question. See *id.* at 773. In *CRS Serrine Engineers, Inc. v. Aetna Casualty and Surety Co.*, No. 96-11749-GAO, 1997 WL 136335, at \*1 (D. Mass. Feb. 24, 1997), the court raised the possibility that arbitrators might have the power to order consolidation on their own, but concluded that the question was moot because the particular consolidation sought would violate the arbitration agreement. See *id.* at \*3. As the *Del E. Webb* and *Connecticut General* courts observed, arbitral consolidation orders clearly raise logistical concerns such as which panel would make the determination and how a transfer might be effected. See *Del E. Webb*, 823 F.2d at 150; *Connecticut Gen.*, 210 F.3d at 773. Also, unless the two sets of arbitrators are identical, a panel that ordered consolidation would deprive either themselves

refusal to order classwide arbitration effectively deprives plaintiffs of the opportunity to proceed as a class. In short, for all of these reasons, even where courts are required to interpret a silent contract as preventing them from ordering consolidation, they should not feel compelled to apply the same "logic" to foreclose arbitral class actions.

Once courts take a fresh look at the question of whether silent arbitration clauses should be interpreted to foreclose class actions, there are many reasons to conclude that they should not. First, as the Supreme Court explained in *Mastrobuono v. Shearson Lehman Hutton, Inc.*,<sup>341</sup> the federal policy favoring arbitration requires that ambiguous contracts be read to favor arbitration.<sup>342</sup> *Mastrobuono* interpreted this to mean that arbitrators should be *permitted* to award punitive damages where the agreement was ambiguous on the subject;<sup>343</sup> this preference should similarly be interpreted to permit class actions to be handled in arbitration. Second, *Mastrobuono* also relied on the "common-law rule of contract interpretation that a court should construe ambiguous language against the interest of the party that drafted it."<sup>344</sup> Companies should not be permitted to rely on a silent arbitration clause, which they drafted, to prevent persons on whom the clause was imposed from proceeding by way of class action. Third, as a matter of policy, there is no clear reason why courts should disfavor rather than favor class actions. Class actions are permitted by the Federal Rules of Civil Procedure, and despite criticisms levied against them of late, Congress has not seen fit to eliminate them. Rather, Congress apparently remains convinced that the benefits of class actions, including efficiency and practicality, outweigh their downsides.<sup>345</sup> Fourth, even if courts were to interpret a silent clause

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or their fellow arbitrators of employment. These concerns alone, however, do not justify precluding arbitrators from making such an order when it is feasible.

341. 514 U.S. 52 (1995) (refusing to vacate arbitrator's award of punitive damages).

342. *See id.* at 62.

343. *See id.*

344. *See id.*

345. The Seventh Circuit, in *Connecticut General Life Insurance Co. v. Sun Life Assurance Co.*, 210 F.3d 771 (7th Cir. 2000), made a similar point when it held that "silent" arbitration clauses do not necessarily preclude consolidation:

[W]e cannot see any reason why, in interpreting the arbitration clause for

to prohibit a *court* from ordering an arbitral class action, they should not foreclose *arbitrators* from choosing to proceed by way of class action.<sup>346</sup> The court in *McCarthy v. Providential Corp.*<sup>347</sup> drew this distinction when it refused to compel arbitration but stated that the arbitrators might have the power to order class treatment.<sup>348</sup> While such arbitral decisions may require assistance from the courts, there seems to be no good reason why they should not be permitted.<sup>349</sup>

Finally, and extremely importantly, even if courts were to interpret a silent arbitration clause to preclude arbitral class actions, they would not be justified in also interpreting that same clause to preclude class action *litigation*. That is, if a court reads a silent clause to mean that certain class action claims are not covered, then plaintiffs should be permitted to pursue those claims through class action litigation. As discussed earlier, several courts,

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purposes of deciding whether to order consolidation, the court should . . . place its thumb on the scale, insisting that it be "clear," rather than merely more likely than not, that the parties intended consolidation. It is not as if consolidation of arbitration proceedings were somehow disfavored; quite the contrary—the same considerations of adjudicative economy that argue in favor of consolidating closely related court cases argue for consolidating closely related arbitrations.

*Id.* at 774.

346. Several courts have adopted a contrary position. *See, e.g., Iowa Grain Co. v. Brown*, 171 F.3d 504, 510 (7th Cir. 1999) (noting that "the kind of class action contemplated by Fed.R.Civ.P. 23(b) is normally unavailable in arbitration"); *Howard v. Klynveld Peat Marwick Goerdeler*, 977 F.Supp. 654, 665 n.7 (S.D.N.Y. 1997) ("[A] plaintiff such as Howard, who has agreed to arbitrate all claims arising out of her employment may not avoid arbitration by pursuing class claims. Such claims must be pursued in non-class arbitration."); *Med Ctr. Cars, Inc. v. Smith*, 727 So. 2d 9, 20 (Ala. 1998) (holding that "class-wide arbitration should not be permitted in this case"); *see also Champ v. Siegel Trading Co.*, 55 F.3d 269, 277 (7th Cir. 1995) (implying that arbitrators would not have the power to order class arbitration by stating "[w]e are thus obliged to enforce the type of arbitration to which these parties agreed, which does not include arbitration on a class basis"); *Gammara v. Thorp Consumer Discount Co.*, 15 F.3d 93, 96 (8th Cir. 1994) (implying that court's denial of class certification would require plaintiff to proceed through arbitration on individual basis); *cf. Sterling Truck Corp. v. Allegheny Ford Truck Sales*, No. 1:00-CV-565 (N.D. Ohio May 23, 2000) (stating that it is up to arbitrator, not judge, to determine propriety of consolidation) (on file with author).

347. No. C 94-0627 FMS, 1994 WL 387852, at \*1 (N.D. Cal. July 19, 1994).

348. *See id.* at \*9 ("The Commercial Arbitration Rules of the American Arbitration Association may provide for class treatment of plaintiffs [sic] claims; but, that question is for the arbitrator to consider, not the court.").

349. Presumably, jurisdiction to assist with class action issues would not be an issue, as the court would have needed jurisdiction in order to compel arbitration in the first place.

including the Seventh Circuit Court of Appeals, have taken precisely this approach in interpreting securities industry arbitration clauses that explicitly exclude class action arbitrations.<sup>350</sup> Those decisions have held that because the arbitral class action is prohibited, plaintiffs must be permitted to pursue the class action in litigation.<sup>351</sup> Several other courts have reached the same conclusion outside the securities context.<sup>352</sup> The conclusion is correct. Courts have properly held that a clause that explicitly excludes arbitration of class actions should be interpreted to permit litigation of those claims, just as they would allow litigation of antitrust claims if those were not covered by the arbitration clause. When a silent clause is interpreted, as a default rule, to bar arbitration of class actions, it should be treated no differently than a clause that explicitly bars arbitration of class actions.<sup>353</sup> No principle of contract interpretation should permit a company, through a silent clause, to eliminate completely a person's pre-existing right to litigate certain claims through a class action.<sup>354</sup>

*b. The Growing Trend of Agreements Expressly Prohibiting Class Actions in any Venue*

Although the above arguments are powerful, they will likely have limited relevance in many future disputes. Practical reality dictates that interpretation of arbitration agreements that are "silent" as to class actions may soon become rare.<sup>355</sup> If a company's goal is to

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350. See *supra* note 227.

351. See *id.*

352. See *supra* note 286.

353. Some courts' default rule of interpreting silent clauses to proscribe consolidations in arbitration does not have the same impact. Where consolidation is prohibited, the unconsolidated arbitrations are likely to proceed. But, where a class action is excluded from arbitration, it is likely that many if not most of the claimants will not be able to arbitrate their claims. Thus, interpreting a silent clause to exclude arbitration of class actions should be treated comparably to interpreting a clause to include certain substantive claims.

354. Professor Stipanowich has made a similar point with respect to punitive damages. Where a company writes an arbitration clause that precludes arbitrators from awarding punitive damages, that clause should not entirely foreclose plaintiffs from seeking punitive damages. Rather, the clause will simply require plaintiffs to seek nonpunitive damages through arbitration, and punitive damages in litigation. See Thomas J. Stipanowich, *Punitive Damages and the Consumerization of Arbitration*, 92 N.W. U. L. REV. 1, 34-35 (1997).

355. See Vairo, *supra* note 41, at 19-22 (observing that most companies will prefer not to

entirely eliminate class actions, and if courts begin to announce that companies can achieve this goal only through more explicit drafting, companies will, in very short order, revise their form arbitration agreements to provide that customers and employees agree to waive their right to proceed by way of class action in arbitration, or more likely in both arbitration and litigation. Some companies have already gone this route.<sup>356</sup> Thus, the most significant and interesting question becomes whether companies should be permitted to employ such a waiver.

### *3. Interpretation of Arbitration Agreements Precluding Class Actions to Allow Litigation of Class Action Claims*

Companies that seek to use arbitration to eliminate class actions may draft a clause that precludes the use of class actions in arbitration, although this might well be unwise from the company's perspective. As has already been discussed, while some courts have interpreted such clauses to require plaintiffs to pursue their claims as individual arbitrations, if at all, other courts have interpreted similar clauses to provide plaintiffs with a class action exemption from arbitration, allowing plaintiffs to litigate their claims.<sup>357</sup> This latter interpretation is more defensible. When an arbitration clause does not cover a particular category of dispute, plaintiffs retain their right to litigate such claims.<sup>358</sup> To the extent a court believes there is ambiguity as to whether a provision prohibiting class actions in arbitration was intended to foreclose class action litigation as well, the ambiguity should be read in favor of the plaintiff and against the drafter to allow for class litigation.<sup>359</sup> Courts should not laxly assume plaintiffs intended to waive their right to proceed as a class.

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be sued in class actions and concluding that companies seeking to avoid class actions should draft arbitration clauses to expressly prohibit class claims or consolidation).

356. See *supra* note 5 and accompanying text.

357. See *supra* notes 226-30 and accompanying text.

358. See, e.g., *Seifert v. U.S. Home Corp.*, 750 So. 2d 633, 641 (Fla. 1999) (holding that agreement to arbitrate claims arising out of construction contract did not mandate arbitration of common law claim for negligence).

359. See generally *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 62 (1995) (relying in part on presumption favoring nondrafting party to conclude that arbitration clause was not intended to preclude recovery of punitive damages).



#### 4. *Unenforceability of Arbitration Agreements Foreclosing Class Actions in both Litigation and Arbitration*

The question of whether creative drafters may eliminate class actions altogether by directly precluding their use in any forum is more complex. Assume that a company drafts a contractual clause that provides in part as follows: "All parties to this contract agree that any dispute arising out of or relating to this agreement will not be resolved in a class action, either in litigation or in arbitration; rather, all such disputes shall be resolved through individual binding arbitration."<sup>360</sup> The drafters of such a clause undoubtedly would argue that it must be enforced, according to its terms, because courts are required to honor parties' contracts.<sup>361</sup>

There should, however, be some limit. This can easily be seen if one imagines companies attempting to draft a similar contract outside the arbitration context. Suppose a company, without requiring arbitration, simply insisted that all consumers or all employees be bound by a contract stating that they waived any right they might have had to litigate claims using class actions.<sup>362</sup> As discussed below, courts should find that at least some of these clauses are impermissible,<sup>363</sup> on one of two possible

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360. Some companies have already begun to draft clauses to this effect, although not necessarily using this precise wording. *See supra* note 5 and accompanying text.

361. Some commentators have assumed such a clause would be valid. *See, e.g.,* Vairo, *supra* note 41, at 19.

362. At least one company has already done so. Sprint PCS issued a document entitled "Terms and Conditions of Service" that states, in part,

Waiver of class actions. You agree that all claims between you and Sprint PCS related to this agreement will be litigated individually and that you will not consolidate or seek class treatment for any claim, unless previously agreed to in writing by both of us. This waiver applies to this agreement as amended or modified. This section survives termination of this agreement.

Sprint PCS Terms, *supra* note 277; cf. Edward Wood Dunham, *Enforcing Contract Terms Designed to Manage Franchisor Risk*, 19 FRANCHISE L.J. 91, 98-99 (2000) (noting that there is no sound theoretical reason why companies should be permitted to impose certain terms like jury trial waivers and forum selection clauses by including them in arbitration clauses, but be prohibited from imposing such terms outside the arbitration context).

363. After a court finds that an arbitration clause's mandated waiver of class actions is impermissible, it has two choices. In some cases the court may find it appropriate to "reform" the clause, in other words, to mandate arbitration but allow plaintiffs to bring a class action either in litigation or in arbitration. *Cf. Armendariz v. Foundation Health Psychcare Servs., Inc.*, 80 Cal. Rptr. 2d 255, 266-67 (Cal. Ct. App. 1998) (holding unconscionable an arbitration clause which limited plaintiffs' remedies to wages lost between date of discharge and date of arbitration, but severing that remedial restriction rather than voiding entire arbitration

grounds.<sup>364</sup> In some situations a federal statute may preclude a company from mandating waiver of one of the statute's provisions. In other situations, a mandatory waiver of class actions may be void as a matter of standard contract law based on unconscionability or other contract principles. The strength of each of these arguments will, however, depend on the specific facts. Thus, under some particular circumstances, it may be acceptable for parties to enter into an agreement promising not to sue each other in a class action.

*a. Federal Statutory Arguments for Unenforceability*

A plaintiff who seeks to bring a claim under a particular federal statute may be able to show that a purported waiver of class actions is unenforceable, given the specific terms, legislative history, or purpose of the statute.<sup>365</sup> It is well recognized that Congress has the

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clause), *review granted and opinion superseded*, 83 Cal. Rptr. 2d 274 (Cal. 1999). In other cases the court may find that it must void the entire arbitration clause. *See* *Graham Oil Co. v. ARCO Prods. Co.*, 43 F.3d 1244, 1247-48 (9th Cir. 1994) (holding that arbitration agreement which precluded plaintiff from recovering exemplary damages or attorneys fees conflicted with terms of federal Petroleum Marketing Practices Act and must be voided in its entirety). As both conclusions would result in the voiding of the anti-class-action provision, the choice between these two approaches exceeds the scope of this Article.

364. A third argument suggests that eliminating the class action procedure violates a constitutional right, such as the right to due process, by depriving plaintiffs of access to court. It would seem difficult, however, to argue that there is a constitutional right to proceed by way of class action, and such an argument would hinge on the showing that state action was implicated and that the disputant had not waived any relevant constitutional right. *Cf.* *Sternlight, Rethinking*, *supra* note 4, at 83-95 (arguing that certain arbitration clauses that, for example, deprive disputants of a neutral decisionmaker, may be violative of due process); *see also* Richard C. Reuben, *Constitutional Gravity: A Unitary Theory of Alternate Dispute Resolution and Public Civil Justice*, 47 UCLA L. REV. 949, 963-64 [hereinafter Reuben, *Constitutional Gravity*] (arguing that many ADR processes, including contractual arbitration, raise due process concerns).

365. It is more difficult, but not impossible, to argue that *state* statutes can also be used to void purported waivers of the right to proceed by way of class action. Pursuing this line of inquiry would exceed the scope of this Article; therefore, I will primarily address only the federal statutes. I cannot resist, however, spelling out the beginning of an argument. While some might contend that any such state statute is necessarily preempted by the FAA, I suggest this is incorrect. Rather, I suggest a company cannot use an arbitration clause to achieve waivers of state consumer law that it could not achieve in other ways. The FAA's pro-arbitration stance does not give companies leave to entirely gut state laws. That is, companies are only permitted to require consumers to arbitrate their claims where such arbitration would not fundamentally compromise the consumers' substantive rights. Several state courts have relied on state law to void an arbitration provision, while holding that the state statute was not preempted. *See, e.g., Avedon Eng., Inc. v. Seatex*, 126 F.3d 1279, 1286-88 (10th Cir. 1997) (holding FAA does not preempt a New York law treating arbitration

power to bar waivers of both substantive and procedural rights that are provided by statute. Thus, many statutes provide that involuntary waivers of their substantive provisions are invalid,<sup>366</sup> or are invalid if not made knowingly and voluntarily,<sup>367</sup> and courts

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clause as "substantial modification" to contract that was not enforceable without express agreement); *Strawn v. AFC Enters.*, 70 F. Supp. 2d 717 (S.D. Tex. 1999) (holding that mandatory arbitration clause was unenforceable in that it would have denied employee's rights available under the Texas Workers' Compensation Act); *Broughton v. Cigna Healthplans of Cal.*, 90 Cal. Rptr. 2d 334, 343-47 (Cal. 1999) (interpreting California's Consumer Legal Remedies Act to prohibit arbitration of claims for public injunctive relief under that Act, and concluding that such prohibition was not preempted by FAA); *see also* *Keystone, Inc. v. Triad Sys. Corp.*, 971 P.2d 1240, 1244-46 (Mont. 1998) (holding general provision protecting Montana citizens from mandatory out-of-state forums was applicable to arbitration clause and was not preempted by FAA, but permitting arbitration to occur within state). Several other decisions have also used state statutes or constitutional provisions to void arbitration clauses, while failing to explain adequately why the provisions were not preempted. *See* *Bill Butler Assocs. v. New England Sav. Bank*, 611 A.2d 463, 465 (Conn. Super. 1991) (holding plaintiff's claim under Connecticut Unfair Trade Practices Act was not arbitrable, in that Connecticut legislature intended statute's provisions be enforceable only in civil actions); *Heurtebise v. Reliable Bus. Computers, Inc.*, 550 N.W.2d 243, 257 (Mich. 1996) (Cavanagh, J., concurring) (concluding that the Michigan Constitution should be interpreted to preclude persons from waiving right to bring substantive civil rights claims in court).

366. For example, the Equal Credit Opportunity Act (ECOA), 15 U.S.C. § 1691(a)(3) (1994), prohibits the conditioning of the extension of credit upon a consumer's waiver of rights. Also, in *Alexander v. Gardner-Denver*, 415 U.S. 36 (1994), the Supreme Court stated: "there can be no prospective waiver of an employee's rights under Title VII." *Id.* at 51. Another example is Section 14 of the Securities Act of 1933 § 14, 15 U.S.C. § 77n (1994), which provides that "[a]ny condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void." Similarly, Section 29(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(a) (1994), states: "Any condition, stipulation, or provision binding any person to waive compliance with any provision of this chapter or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void." At one point the Supreme Court read the 1933 Act's exclusion to bar mandatory arbitration of such claims. *See Wilko v. Swan*, 346 U.S. 427 (1953). However, in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), the Court held that the 1934 Act provision applied only to waivers of substantive rights, and did not preclude mandatory arbitration. *See id.* at 226-28. The Court later applied similar reasoning to reverse *Wilko* and held that mandatory arbitration could be valid under the 1933 Act as well. *See Rodriguez de Quijas v. Shearson/American Express Inc.*, 490 U.S. 477, 478 (1989).

367. *Gilmer* observed that in "the recently enacted Older Workers Benefits Protection Act, Pub. L. 101-443, 104 Stat. 978, Congress amended the ADEA to provide that 'an individual may not waive any right or claim under this Act unless the waiver is knowing and voluntary.'" *See Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 n.3; *cf. Thiele v. Merrill Lynch, Pierce, Fenner & Smith*, 59 F. Supp. 2d 1060, 1063-66 (S.D. Cal. 1999) (holding that it would be inappropriate to compel arbitration of age discrimination claim because the clause did not meet requirement that waiver of jury trial right be knowing and voluntary).

have recognized the validity of such provisions.<sup>368</sup> As to arbitration in particular, despite the Supreme Court's general pro-arbitration stance,<sup>369</sup> the Court has frequently enunciated that Congress has the power to declare that certain claims are nonarbitrable or at least cannot be the subject of mandatory arbitration.<sup>370</sup> For a variety of policy reasons stated earlier—specifically efficiency, the value of the bringing of small claims, and the public interest in enforcement of statutes<sup>371</sup>—it is certainly conceivable that Congress might choose to ensure that the class action device be made available to plaintiffs bringing claims under particular statutes.<sup>372</sup>

Thus, the question of whether Congress has stated that plaintiffs bringing specific statutory claims must be allowed to proceed by way of class action is a matter of statutory interpretation.<sup>373</sup> At least three arguments are possible. First, plaintiff might be able to show that Congress, in a particular statute, explicitly provided that mandatory waivers of class actions would be unenforceable.<sup>374</sup> Second, plaintiff might be able to show that even though the statute does not expressly preserve the right to bring class actions, its language and legislative history demonstrate that Congress intended to allow class actions and viewed them as critical to enforcement of the statute. Third, plaintiff might be able to show that although the language and legislative history make no particular mention of class actions, they are nonetheless necessary to support the enforcement of the statute's provisions.

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368. See, e.g., *Alexander*, 415 U.S. at 51-52.

369. See *supra* notes 72-74 and accompanying text.

370. This declaration may, but need not, be explicit. See *infra* notes 383-400 and accompanying text.

371. See *supra* notes 90-108 and accompanying text.

372. While Congress cannot mandate the availability of class actions in state court, it can at least allow interested plaintiffs to file a class action in federal court.

373. It seems clear that Congress may regulate the availability of class action relief, just as it regulates the availability of a jury trial, subject to Constitutional limits, and certain kinds of damages. Indeed, as discussed earlier, Congress has recently passed legislation regarding the availability of class actions in federal securities cases, and has been considering broader legislation regarding class actions. See *supra* notes 130-33 and accompanying text.

374. In *Randolph v. Green Tree Fin. Corp.*, 991 F. Supp. 1410, 1418 (M.D. Ala. 1997), *rev'd*, 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235), the court recognized the possibility of such a statute, while concluding Truth in Lending Act did not bar waiver of class actions.

*i. Express Statutory Preclusion of Class Action Waiver*

Clearly Congress could, if it desired, draft language barring waiver of class actions through arbitration or otherwise. The question of whether any existing statutes already contain such language remains. Plaintiffs have attempted to make this argument most frequently with respect to TILA,<sup>375</sup> highlighting that Section 1640 of that statute speaks explicitly to class actions when it caps the damages available in such suits.<sup>376</sup> Indeed, the pending case of *Green Tree Financial Corp. v. Randolph*,<sup>377</sup> in which the Supreme Court may conceivably address some of the issues surrounding class actions and arbitration,<sup>378</sup> is brought under TILA.

Several courts, including the district court in *Green Tree*,<sup>379</sup> have rejected the argument that Section 1640 explicitly guarantees a right to proceed by class action, stating that the mere mention of class actions and imposition of a damages cap does not imply a right to proceed by class action.<sup>380</sup> Although one court has held that TILA

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375. 15 U.S.C. §§ 1601-1693 (1994 & Supp. IV 1998).

376. 15 U.S.C. § 1640(a) (1994 & Supp. IV 1998). The damages cap contained in § 1640(a) states:

[I]n the case of a class action, . . . the total recovery under this subparagraph in any class action or series of class actions arising out of the same failure to comply by the same creditor shall not be more than the lesser of \$500,000 or 1 per centum of the net worth of the creditor.

377. *Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235).

378. *See supra* notes 47-54 and accompanying text.

379. *See Randolph*, 991 F. Supp. at 1418 (refusing to deny motion to compel arbitration on ground that plaintiffs would be deprived of class action, because whereas Congress may preclude waiver of class claims, the mere inclusion of provisions governing class action litigation alone does not provide plaintiff with a right to proceed through class action).

380. *See Brown v. Surety Fin. Serv., Inc.*, No. 99 C 2405, 2000 WL 528631, at \*1 (N.D. Ill. Apr. 24, 2000) (rejecting argument that TILA class action cannot be arbitrated); *Thompson v. Illinois Title Loans, Inc.*, No. 99-C-3952, 2000 WL 45493, at \*4 (N.D. Ill. Jan. 11, 2000) (compelling consumers in putative class action to arbitrate claims under TILA on ground that while class action may possibly be "optimal" method for enforcing TILA, statute "neither requires class actions nor grants a substantive right to them"); *Sagal v. First USA Bank, N.A.*, 69 F. Supp. 2d 627, 632 (D. Del. 1999) ("Because Congress has not provided for a statutory right to pursue class actions under the TILA, and because there are alternative means to bring suit thereunder, this court does not find that the TILA amounts to a 'congressional command' to preserve class action suits at the expense of the FAA."); *Lopez v. Plaza Fin. Co.*, No. 95-C-7567, 1996 WL 210073, at \*3 (N.D. Ill. Apr. 25, 1996) ("It is true that compelling arbitration in light of *Champ* will eliminate plaintiff's ability to arbitrate his claims on behalf of a class. Nonetheless, this result is required because Congress has not created a statutory right to bring class actions under TILA, plaintiff's contrary assertions

precludes mandatory waiver of class actions, it bases its conclusion more on the overall intent and legislative history of Section 1640 than on its explicit words.<sup>381</sup> Yet, while the explicit language argument has not yet succeeded, it may in the future—particularly if Congress realizes the need to protect claimants' ability to pursue relief under particular statutes by way of class action.<sup>382</sup>

*ii. Legislative Intent and History as Precluding Class Action Waiver*

The Supreme Court has enunciated repeatedly that statutory prohibitions to arbitration may be found not only in explicit statutory provisions, but also in the legislation's history or purpose. Most recently, in *Gilmer v. Johnson/Interstate Lane Corp.*,<sup>383</sup> the Court explained that individual agreements to arbitrate are void where "Congress itself has evinced an intention," which is discoverable in a statute's text, legislative history or through an inherent conflict between arbitration and the purpose of the statute, "to preclude a waiver of judicial remedies for the statutory rights at issue."<sup>384</sup>

One recent Delaware district court decision has applied this powerful analysis to conclude that the language, legislative history, and overall intent of TILA preclude a court from compelling arbitration of a putative class action brought under that statute. *Johnson v. Tele-Cash, Inc.*<sup>385</sup> focused on the legislative history of TILA and its Section 1640s damages cap in detail,<sup>386</sup> and concluded

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notwithstanding. Section 1640 . . . does not establish a right per se; it only sets forth a limit on liability under class actions."); see also *Herrington v. Union Planters Bank, N.A.*, No. CIV. A. 2:98CV231GR, 2000 WL 424232, at \*6 (S.D. Miss. Jan. 21, 2000) (rejecting argument that the Truth in Savings Act contained language barring arbitration of claims brought under that statute).

381. See *Johnson v. Tele-Cash, Inc.*, 82 F. Supp. 2d 264 (D. Del. 1999). See *infra* notes 385-97 and accompanying text for a detailed discussion of this case and its reasoning.

382. See discussion *infra* text accompanying notes 489-503.

383. 500 U.S. 20 (1991).

384. *Id.* at 24-26; see also *Mitsubishi Motors Corp. v. Soler Chrysler Plymouth*, 473 U.S. 614, 628 (1985) ("We must assume that if Congress intended the substantive protection afforded by a given statute to include protection against waiver of the right to a judicial forum, that intention will be deducible from text or legislative history.").

385. 82 F. Supp. 2d 264 (D. Del. 1999).

386. See *supra* note 376 for the language of § 1640(a).

that "[t]he intended purpose of the TILA was 'to encourage class actions in the truth-in-lending context because of the apparent inadequacy of the Federal Trade Commission's enforcement resources and because of a continuing problem of minimum [sic] compliance with the Act on the part of creditors.'"<sup>387</sup> Specifically, the court explained that when Congress adopted the damages cap on liability for TILA class actions in 1974, it "was trying to encourage the use of class actions as a means for enforcing the TILA."<sup>388</sup> Prior to the imposition of the cap, successful large class actions would have resulted in huge damages awards because "each individual plaintiff was entitled to a minimum award of \$100."<sup>389</sup> Thus, "numerous federal courts refused to certify class actions under the TILA since the 'allowance of thousands of minimum recoveries . . . would carry to an absurd and stultifying extreme the specific and essentially inconsistent remedy Congress prescribed as the means of private enforcement.'"<sup>390</sup> *Johnson* found that the cap was adopted to counter this trend and "to encourage the federal courts to begin

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387. *Id.* at 266 (quoting *Watkins v. Simmons & Clark, Inc.*, 618 F.2d 398, 400 (6th Cir. 1980) (citing S. REP. NO. 93-278, at 14-15 (1973)). Another district court similarly explained: [T]here is not much incentive in the Act for individuals to pursue alleged Truth-in-Lending violations. The costs of litigation against a financial institution can be enormous, actual damages are difficult to prove and the statutory recovery is low. It is in most individuals' interests, however, and in the public interest that lending institutions comply with the Act and be found responsible to consumer borrowers if they do not comply. Were it not for the class action, many borrowers likely would not pursue their rights in court.

*Hughes v. Cardinal Fed. Sav. & Loan Ass'n*, 97 F.R.D. 653, 655-56 (S.D. Ohio 1983); *see also* *Goldman v. First Nat'l Bank*, 532 F.2d 10, 15 (7th Cir. 1976) (observing that class actions are important in TILA litigation "to prevent violators of the Act from limiting recovery to a few individuals where actual, wide-spread [sic] noncompliance is found to exist") (quoting *Haynes v. Logan Furniture Mart, Inc.*, 503 F.2d 1161, 1164 (7th Cir. 1974)); *Rivera v. Fair Chevrolet Geo Partnership*, 165 F.R.D. 361, 363 (D. Conn. 1996) ("TILA specifically provides for the maintenance of a class action."); *Chandler v. Southwest Jeep-Eagle, Inc.*, 162 F.R.D. 302, 310 (N.D. Ill. 1995) (noting propriety of class action to enforce TILA claims where most proposed class members "are probably unaware of their rights" and where such "[c]lass members, even if aware of their rights, likely would lack the initiative to bring suit individually"); *Sarafin v. Sears, Roebuck & Co.*, 73 F.R.D. 585, 588 (N.D. Ill. 1977) ("For [large] creditors the threat of a class action has a potent deterrent effect. Eliminating that deterrent for all large cases would emasculate the enforcement provisions of the Act.").

388. *Johnson*, 82 F. Supp. 2d at 269; *see also* *Guarte v. Furniture Fair, Inc.*, 75 F.R.D. 525, 528 (D. Md. 1977) (stating that in imposing the damages cap, Congress "indicated its intent that the class action vehicle be available in this area").

389. *Johnson*, 82 F. Supp. 2d at 269 (citing 15 U.S.C. § 1640 (1970)).

390. *Id.* (quoting *Ratner v. Chemical Bank N.Y. Trust Co.*, 54 F.R.D. 412, 414 (S.D.N.Y. 1972)).

certifying class actions in Truth in Lending lawsuits.<sup>391</sup> The court further cited legislative history, showing that class actions are critical to the enforcement of TILA.<sup>392</sup> Thus, based on the language and legislative history of TILA, *Johnson* found that compelling arbitration inherently would conflict with the underlying purposes of TILA and therefore refused to do so.<sup>393</sup> Furthermore, the court found that because the Electronic Funds Transfer Act<sup>394</sup> contained a virtually identical cap,<sup>395</sup> and “presum[ing] that Congress was trying to encourage courts to certify class actions under this statute as well,”<sup>396</sup> it would also deny defendants’ motion to compel arbitration of that claim.<sup>397</sup> To be sure, not all courts have concurred with the *Johnson* analysis,<sup>398</sup> and indeed this question may possibly

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391. *Id.* (citing *Watkins v. Simmons & Clark, Inc.*, 618 F.2d 398, 400 n.6 (6th Cir. 1980) (citing S. REP. NO. 93-278, at 14-15)). *Johnson* also cited *Bantolina v. Aloha Motors, Inc.*, 419 F. Supp. 1116, 1119-20 & n.11 (D. Haw. 1976) (citing S. REP. NO. 93-278, at 14-15)).

392. *See Johnson*, 82 F. Supp. 2d at 269-70. *Johnson* explained that the Senate Report issued in connection with the damages cap

concluded with an earlier conclusion by the Federal Reserve Board that “potential class action liability [wa]s an important encouragement to the voluntary compliance which [wa]s so necessary to [e]nsure nation-wide [sic] adherence to uniform disclosure” since “[m]ost Truth in Lending violations do not involve actual damages and . . . some meaningful penalty provisions are therefore needed to [e]nsure compliance.”

*Id.* (quoting S. REP. NO. 93-278, at 15). *Johnson* favorably quoted language from *Bantolina*, another district court decision: “The possibility of class-action exposure is essential to the prophylactic intent of the Act [ ] and is necessary to elevate truth-in-lending lawsuits ‘from the ineffective “nuisance” category to the type of suit which has enough sting to insure that management will strive with diligence to achieve compliance.’” *Id.* at 270 (quoting *Bantolina*, 419 F. Supp. at 1120 (citing S. REP. NO. 93-278, at 36-37)).

393. *See Johnson*, 82 F. Supp. 2d at 270.

394. 15 U.S.C. §§ 1693-1693r (1994 & Supp. IV 1998).

395. *See id.* § 1693m (“[I]n the case of a class action, . . . the total recovery under this subparagraph in any class action or series of class actions arising out of the same failure to comply by the same person shall not be more than the lesser of \$500,000 or 1 per centum of the net worth of the defendant.”).

396. *Johnson*, 82 F. Supp. 2d at 272. The court admitted that there was no legislative history explaining why Congress adopted the cap. *See id.*

397. *See id.*

398. *See Thompson v. Illinois Title Loans, Inc.*, No. 99 C 3952, 2000 WL 45493, at \*3 (N.D. Ill. Jan. 11, 2000) (rejecting plaintiffs’ argument that class action liability under TILA was necessary to ensure voluntary compliance with that Act); *Sagal v. First USA Bank, N.A.*, 69 F. Supp. 2d 627, 632 (D. Del. 1999) (observing that TILA does not “rely exclusively on class actions as an enforcement mechanism” and concluding that mandatory arbitration of TILA class action was permissible); *Randolph v. Green Tree Fin. Corp.*, 991 F. Supp. 1410, 1418-20 (M.D. Ala. 1997) (concluding plaintiff failed to present “compelling evidence” to support her position that class actions are essential to purposes of TILA), *rev’d on other grounds*, 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235).



be addressed by the Supreme Court in the pending case of *Green Tree Financial Corp. v. Randolph*.<sup>399</sup>

Plaintiffs asserting class action claims under other federal statutes will need to explore whether the language, legislative history, or inherent purposes of those statutes should similarly be interpreted to preclude mandatory arbitration of class actions brought under the statute in question.<sup>400</sup> Where they do, courts should deny motions to compel arbitration of such claims.

### *iii. Class Actions as Integral to Enforcement of Statute*

Finally, plaintiffs may also be able to show that class actions are critical to the enforcement of a particular statute without focusing

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399. 178 F.3d 1149 (11th Cir. 1999), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235). In discussing the importance of class actions to TILA, some may focus on the limited "class action moratorium" imposed by Congress as to certain claims for a period of roughly five months in 1995. *See* 15 U.S.C. § 1640(i) (Supp. IV 1998) (eliminating class actions for a narrow category of claims from May 18, 1995 to October 1, 1995). The respondents in *Green Tree* have argued that this partial and short term moratorium defeats the argument that class actions are essential to the enforcement of rights under TILA. *See* Brief for Petitioner, *Green Tree Fin. Corp. v. Randolph* (U.S. June 8, 2000) (No. 99-1235), *available in* 2000 WL 744132, at \*48-49. However, this brief and partial moratorium can also be used to make the opposite point. Surely if Congress had not felt class actions were critical it would have eliminated them on a broader and more permanent basis.

400. The Fair Labor Standards Act, 29 U.S.C. §§ 201-219 (1994 & Supp. IV 1998) is another statute which explicitly references the right to proceed in a representative or class action, and thus might form the basis for a claim that denial of the right to proceed in a class action is impermissible. Section 216(b) states:

An action to recover the liability prescribed in either of the preceding sentences may be maintained against any employer (including a public agency) in any Federal or State court of competent jurisdiction by any one or more employees for and in behalf of himself or themselves and other employees similarly situated. No employee shall be a party plaintiff to any such action unless he gives his consent in writing to become such a party and such consent is filed in the court in which such action is brought.

One district court initially seemed to recognize such an argument, holding unenforceable under the FLSA an arbitration clause which "denies plaintiffs' their statutorily-granted rights, under both the FLSA and Oregon law, to obtain attorney's fees and to participate collectively and without undue financial burden in the adjudication proceedings." *Horenstein v. Mortgage Mkt., Inc.*, Civ. No. 98-1104-AA, 1999 U.S. Dist. LEXIS 21463, at \*10 (D. Or. Jan. 11, 1999). In a subsequent decision in the same suit, however, the district court upheld use of a different and less onerous arbitration clause, which permitted recovery of attorney fees and did not impose substantial upfront fees, even though that clause would have prevented plaintiffs from proceeding collectively. *See Horenstein v. Mortgage Mkt., Inc.*, Civ. No. 98-1104-AA, at 7-8 (D. Or. Jul 23, 1999) (on file with author) ("Under the provisions of Employment Agreements, the absence of a the [sic] right to proceed collectively does not render the arbitration provisions unenforceable.").

on specific statutory language or legislative history. The Supreme Court has explained repeatedly that it will compel arbitration of federal statutory claims only "so long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum, [such that] the statute will continue to serve both its remedial and deterrent function."<sup>401</sup> In so ruling, the Court has recognized that not all forums are necessarily adequate, and that procedural provisions can be critical to enforcement of substantive rights.<sup>402</sup> Thus, in *Gilmer* the Court held the arbitration clause enforceable only after considering and rejecting plaintiff's claims that the arbitral forum would be biased and unworkable in various ways.<sup>403</sup> Similarly, in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,<sup>404</sup> the Court explained that where it could be shown that aspects of a particular arbitration clause operated to deprive a claimant of substantive rights, it "would have little hesitation in condemning the agreement as against public policy."<sup>405</sup> The Delaware district court in *Johnson* relied in part on this passage from *Mitsubishi* when it refused to compel arbitration of claims brought under TILA.<sup>406</sup>

Several federal appellate courts have already found arbitration clauses unenforceable on the ground that the particular form of arbitration required would not allow adequate enforcement of the

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401. *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 (1991) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985)).

402. This sharply undercuts the conclusion of one district court, which opined that class actions are mere procedural devices rather than substantive rights, and that procedural devices may never supersede arbitration, which the court found to be substantive. See *Randolph*, 991 F. Supp. at 1418.

403. See *Gilmer*, 500 U.S. at 30-32 (finding plaintiff had failed to make adequate factual showings that arbitral panels would be biased, that discovery would be insufficient, that arbitrators would not write adequate opinions, or that equitable relief or class relief would not be available).

404. 473 U.S. 614 (1985) (holding that Puerto Rican car dealer could be compelled to arbitrate dispute with foreign manufacturer).

405. *Id.* at 637 n.19. Plaintiff was objecting to the fact that the arbitration clause called for the arbitration to occur in Japan. The opinion states that "in the event the choice-of-forum and choice-of-law clauses operated in tandem as a prospective waiver of [the plaintiff's] right to pursue statutory remedies for antitrust violations, we would have little hesitation in condemning the agreement as against public policy." *Id.*

406. See *Johnson*, 82 F. Supp. 2d at 271 ("Thus, after considering the facts of this case in light of the teachings of the *Mitsubishi* decision, this court finds that there is 'inherent conflict' between compelling arbitration and the underlying purposes of the TILA. The court will, therefore, deny the defendants' motion to compel the arbitration of Johnson's TILA claims."). As discussed earlier, the *Johnson* court also relied on the explicit language and legislative history of the statute. See *supra* notes 385-93 and accompanying text.

relevant federal statute. As the Eleventh Circuit explained: "When an arbitration clause has provisions that defeat the remedial purpose of [a] statute, . . . the arbitration clause is not enforceable."<sup>407</sup> Moreover, the Eleventh Circuit favorably noted the Tenth Circuit's announcement that:

As *Gilmer* emphasized, arbitration of statutory claims works because potential litigants have an adequate forum in which to resolve their statutory claims and because the broader social purposes behind the statute are adhered to. This supposition[] falls apart, however, if the terms of an arbitration agreement actually prevent an individual from effectively vindicating his or her statutory rights. Accordingly, an arbitration agreement that prohibits use of the judicial forum as a means of resolving statutory claims must also provide for an effective and accessible alternative forum.<sup>408</sup>

These decisions have refused to enforce arbitration clauses that imposed excessively high fees on consumers or employees, thereby denying them access to any forum.<sup>409</sup>

The same argument can easily be applied to clauses that expressly prohibit claimants from bringing a class action, even when neither the language nor the legislative history of the relevant

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407. *Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149, 1157 (11th Cir. 1999) (quoting *Paladino v. Avnet Computer Techs., Inc.*, 134 F.3d 1054, 1062 (11th Cir. 1998)), *cert. granted*, 120 S. Ct. 1552 (2000) (No. 99-1235).

408. *Id.* (citations omitted) (quoting *Shankle v. B-G Maintenance Management, Inc.*, 163 F.3d 1230, 1234 (10th Cir. 1999)).

409. *See id.* (holding unenforceable, under TILA, an arbitration clause that did not set out explicitly the extent to which consumer would be held responsible for filing fees and arbitral salaries); *Shankle*, 163 F.3d at 1234-35 (refusing to enforce clause that required employees to split arbitral fees); *Paladino*, 134 F.3d at 1062 (holding unenforceable, under Title VII, arbitration clause that would have required plaintiff to pay filing fee of \$2,000 to arbitrate claim of gender discrimination, and might have required her to pay at least half of substantial costs of arbitration); *see also* *Floss v. Ryan's Family Steak Houses, Inc.*, 211 F.3d 306, 313 (6th Cir. 2000) ("[E]ven if arbitration is generally a suitable forum for resolving a particular statutory claim, the specific arbitral forum provided under an arbitration agreement must nevertheless allow for the effective indication of that claim. Otherwise, arbitration of the claim conflicts with the statute's purpose . . ."); *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1485-86 (D.C. Cir. 1997) (agreeing to mandate arbitration of a claim brought under a federal civil rights statute, only on condition that the employer bear the sole costs of the arbitrator's fee); *Strawn v. AFC Enters., Inc.*, 70 F. Supp. 2d 717, 722-26 (S.D. Tex. 1999) (holding arbitration cannot be substituted for litigation given policy underlying Texas workers' compensation statute).

federal statute discusses class actions. Many claims can be feasibly presented only by a class rather than on an individual basis,<sup>410</sup> despite the fact that some courts continue to enforce arbitration and deny class actions in such impractical situations. Where plaintiffs can establish that the prohibition on class actions would deprive them of any forum in which to present their federal statutory claim by making that lawsuit economically unfeasible, courts should refuse to enforce such a provision—either by voiding the arbitration clause altogether, by holding the arbitration clause inapplicable as to class claims, or by permitting plaintiffs to present their claims in an arbitral class action.<sup>411</sup> Some might suggest that class actions cannot be critical to enforcement of any federal statute that grants concurrent jurisdiction to state as well as federal courts, in that the federal class action is available only in federal court;<sup>412</sup> however, this ignores the fact that plaintiffs would have the option to proceed in federal court if they thought the class action procedure was critical, and that virtually all states also allow class actions.<sup>413</sup>

It is important, however, to recognize the limits of this statutory argument. The argument should succeed only where plaintiffs can present facts showing that the class prohibition would truly deprive them of an adequate forum in which to present their claims. Where, for example, each class member has a relatively large claim that could be feasibly presented individually, the above argument should fail. Also, where the clause permits arbitral class actions, and only disallows litigated class actions, it would be difficult to show that class prohibition violated claimants' rights to enforce the statute unless they could demonstrate some particular statutory or constitutional problem with the particular class action arbitration procedures. Finally, where the statutory scheme provides plaintiffs

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410. *See supra* notes 28-40, 100-04 and accompanying text. One court recently considered but ultimately rejected the argument that plaintiffs could not feasibly present their particular claim under the Fair Labor Standards Act unless they were permitted to proceed by way of class action. *See supra* note 400.

411. The interesting question of how a court should decide whether to bar arbitration altogether, or whether to reform an arbitration agreement to comport with relevant statutory or contractual requirements, exceeds the scope of this Article.

412. *See, e.g.*, Brief for Petitioner, *Green Tree Fin. Corp. v. Randolph* (U.S. June 8, 2000) (No. 99-1235), available in 2000 WL 744132, at \*45-46.

413. *See* HERBERT NEWBERG & ALBA CONTE, *NEWBERG ON CLASS ACTIONS* § 13.04 (3d ed. 1992) (noting that 36 states have adopted Federal Rule 23 in some form, and that additional states permit class actions at common law or under Field Code-based rules).

with an alternative administrative means by which to enforce their rights, courts should examine the available enforcement mechanisms to determine whether the prohibition on class actions has truly deprived plaintiffs of their statutory relief.

The Supreme Court's decision in *Gilmer*, although admittedly only dicta, supports the analysis suggested here with respect to class actions. In *Gilmer*, plaintiff sought to avoid mandatory arbitration of his claim under the ADEA based partly on an argument that deprivation of the opportunity to proceed by way of class action would preclude him from adequately enforcing his statutory rights.<sup>414</sup> The Court seemed to accept the possible viability of such an argument, but found plaintiff had failed to make an adequate factual showing supporting his claim.<sup>415</sup> The Court emphasized that the New York Stock Exchange rules at the time allowed for collective proceedings,<sup>416</sup> and that "arbitration agreements will not preclude the EEOC from bringing actions seeking class-wide and equitable relief."<sup>417</sup>

It is true that the Court also made a statement that some have interpreted as supporting the use of arbitration to disallow class actions. Specifically, the Court stated that "even if the arbitration could not go forward as a class action or class relief could not be granted by the arbitrator, the fact that the [ADEA] provides for the possibility of bringing a collective action does not mean that individual attempts at conciliation were intended to be barred."<sup>418</sup> In context, however, the statement should not be interpreted to preclude plaintiffs from arguing that class actions are necessary to

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414. See *Gilmer*, 500 U.S. at 32.

415. See *id.* at 35.

416. See *id.* at 32.

417. *Id.* It seems that the Court too easily assumes both that an individual's arbitration clause would not be interpreted to preclude the EEOC from pursuing relief on the individual's behalf and that a claim brought by the EEOC is an adequate replacement for an individual claim. Neither assumption is necessarily warranted. In several post-*Gilmer* decisions, courts have held that individual arbitration clauses may, at least in part, limit the EEOC's power to proceed on behalf of that individual. See cases cited *supra* note 58. Moreover, even when an EEOC enforcement action is brought, the EEOC may not choose to pursue all of the relief that an individual or class might have sought. For example, the EEOC might elect to seek injunctive relief, but not compensatory or punitive damages. In such an instance, it might well be argued that the limitation on individual class actions deprives persons of their opportunity to enforce their statutory rights.

418. *Gilmer*, 500 U.S. at 32 (quoting *Nicholson v. CPC Int'l Inc.*, 877 F.2d 221, 241 (3d Cir. 1989) (Becker, J., dissenting)).

allow enforcement of specific statutes in certain circumstances. It is important to recall that *Gilmer* was filed as an individual suit, and not as a purported class action. Thus, the Court seems to be saying only that it may sometimes be permissible for plaintiffs to waive any right they may have had to proceed by class action. This author does not disagree. An individual who, post dispute, decides she would prefer to arbitrate than to participate in a class action, should have this option.

Thus, according to extant decisions by the Supreme Court and by federal courts of appeal, when plaintiffs can show that an arbitral prohibition on class actions would deprive them of the opportunity to adequately enforce their statutory rights, courts should not enforce such a prohibition.<sup>419</sup>

### *b. Unenforceability as a Matter of Contract Law*

In addition to the above federal statutory arguments, plaintiffs may also contend that an arbitration clause that precludes class actions is void as a matter of traditional contract law. Citing the FAA's Section 2,<sup>420</sup> the Supreme Court has stated frequently that the Act preserves persons' rights to challenge arbitration on standard contract grounds such as lack of agreement to arbitrate, fraud, duress, violation of public policy, or unconscionability.<sup>421</sup>

### *i. Unconscionability*

Of these potential contractual arguments, unconscionability is the most promising. Particularly of late, courts have become increasingly willing to use this defense to void arbitration clauses they believe are particularly unfair,<sup>422</sup> and two courts have relied in

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419. The same analysis would apply if a company sought to exclude class actions without using an arbitration clause.

420. Section 2 provides arbitration clauses may be voided "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2 (1994).

421. See *Doctor's Assocs. v. Casarotto*, 517 U.S. 681, 686 (1996); *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 281 (1995); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc.*, 473 U.S. 614, 627 (1985); *Southland Corp v. Keating*, 465 U.S. 1, 16 n.11 (1984).

422. Plaintiffs could make the same argument as to a contractual provision which, without offering or requiring arbitration, prohibited plaintiffs from bringing a class action. Of course, the argument that the bar on class actions is unconscionable assumes that class actions are generally available, according to the prevailing rules of civil procedure. If

part on an arbitration clause's elimination of plaintiffs' class action opportunities in holding that clause unconscionable.<sup>423</sup>

The conclusion reached by these two courts is consistent with courts' overall handling of unconscionability in the arbitration context. In general, clauses which deprive claimants of adequate access to a forum,<sup>424</sup> or which deny claimants relief to which they would ordinarily be entitled<sup>425</sup> are among those provisions courts are most likely to strike down as unconscionable. Applying a similar analysis, courts should find unconscionable those arbitration clauses which, by precluding plaintiffs from joining together in a class action, effectively deny plaintiffs the opportunity to present their claims in any judicial or arbitral forum. As discussed above, many small claims can be economically pursued *only* if a group of plaintiffs can join together in a class action. Otherwise, plaintiffs may not be

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Congress chose generally to eliminate the class action, contracts which did not allow for class actions would not be unconscionable.

423. See *supra* notes 231-38 and accompanying text.

424. See, e.g., *Knepp v. Credit Acceptance Corp.* 229 B.R. 821, 838 (N.D. Ala. 1999) (refusing to enforce clause in part on ground of unconscionability where debtor would be required to pay for arbitration); *Patterson v. ITT Consumer Fin. Corp.*, 18 Cal. Rptr. 2d 563, 565-66 (Cal. Ct. App. 1993) (refusing to enforce arbitration clause imposed by financing organization on California consumers that apparently required arbitration to be heard in Minneapolis, Minnesota, and required plaintiffs to pay substantial filing fees, observing that procedures that might be fair as applied to business entities are not necessarily fair as applied to consumers); *Brower v. Gateway 2000, Inc.*, 676 N.Y.S.2d 569, 573 (N.Y. App. Div. 1998) (holding unconscionable on ground of cost, clause which both required computer purchasers to arbitrate disputes in Chicago and also required arbitration according to the rules of the ICC, which impose high administrative costs).

425. See, e.g., *Hooters of Am. Inc. v. Phillips*, 39 F. Supp. 2d 582, 614 (D.S.C. 1998) (holding arbitration unconscionable in part because employee was "stripped of numerous substantive remedies under Title VII [in that] . . . compensatory damages, backpay relief, frontpay relief, punitive damages, and attorney's fees are either eliminated or substantially curtailed," and because procedural rules were biased against employee in favor of company, where company had total control over selection of arbitrators, employee had severely limited discovery, and witness disclosure and sequestration were one sided), *aff'd on more limited grounds*, 173 F.3d 933, 940 (4th Cir. 1999); *Gonzalez v. Hughes Aircraft Employees Fed. Credit Union*, 83 Cal. Rptr. 2d 763 (Cal. Ct. App. 1999) (voiding, as substantively unconscionable, clause which shortened statute of limitations, allowed employer to continue to seek judicial relief, and severely limited employee's discovery rights), *review granted and opinion superseded*, 978 P.2d 1 (Cal. 1999), *appeal dismissed per stipulation*, 990 P.2d 504 (Cal. 1999); *Armendariz v. Foundation Health Psychcare Servs., Inc.*, 80 Cal. Rptr. 2d 255 (Cal. Ct. App. 1998) (holding unconscionable an arbitration clause that limited plaintiffs' remedies to wages lost between date of discharge and date of arbitration, but severing that remedial restriction rather than voiding entire arbitration clause), *review granted and opinion superseded*, 973 P.2d 51 (Cal. 1999); *Stirlen v. Supercuts, Inc.*, 60 Cal. Rptr. 2d 138, 150 (Cal. Ct. App. 1997) (holding unconscionable contract which, *inter alia*, precluded plaintiff from recovering damages other than "actual damages for breach of contract").

able to secure representation, to pay filing fees, or to make the commitment of time or emotion that litigation or arbitration requires.<sup>426</sup> When a company deprives plaintiffs of the class action opportunity in such circumstances, it entirely forecloses plaintiffs from enforcing their legal rights. Thus, the class action prohibition can easily be analogized both to those arbitral provisions that deny access by imposing high costs or distant locations, or to those provisions that deny remedies. As noted above, both of these types of arbitration clauses have been voided for unconscionability, and clauses which eliminate class actions should be evaluated similarly.<sup>427</sup>

As discussed above with respect to statutory remedies, however, the limitations of the unconscionability argument must also be recognized. When an arbitration clause eliminates the use of class actions but does not thereby prevent plaintiffs from presenting their claims, it is not at all clear if the clause would be unconscionable. Thus, the showing of unconscionability will turn on the specific facts of each case, as well as on the local jurisdiction's law of unconscionability. Plaintiffs who have large claims or who are independently wealthy might be less successful in using the unconscionability argument than would be poorer plaintiffs with smaller claims.

## *ii. Other Contractual Claims and Defenses*

While scholars have argued that courts should also use other contractual arguments, such as lack of consent,<sup>428</sup> fraud, duress, and

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426. See *supra* notes 28-40, 100-08 and accompanying text. The draft Reporter's Notes to the Revised Uniform Arbitration Act also support the use of an unconscionability argument to void an arbitration agreement that precludes class actions, when that prohibition may undermine consumers' rights by heightening the cost of arbitration or making it too difficult for claimants to procure legal counsel. See *supra* note 46.

427. Because the law of unconscionability varies somewhat from state to state, unconscionability determinations will depend upon state law. For example, some states require a showing of both substantive and procedural unconscionability. See, e.g., *Maciejewski v. Alpha Sys. Lab Inc.*, 87 Cal. Rptr. 2d 390, 393 (Cal. Ct. App. 1999) ("The concept includes both procedural and substantive elements . . ."). Nonetheless, it seems likely that a prohibition on class actions that has the effect of entirely foreclosing plaintiffs from pursuing relief that could have been sought in class action litigation may well qualify as unconscionable in many jurisdictions.

428. See, e.g., Jeffrey W. Stempel, *A Better Approach to Arbitrability*, 65 TUL. L. REV. 1377, 1434-47 (1991) [hereinafter Stempel, *A Better Approach*] (arguing that resisting parties should be able to revoke arbitration clauses by demonstrating "blameless ignorance," "dirty



violation of public policy to invalidate certain arbitration agreements, courts have often rejected such claims.<sup>429</sup> Nonetheless, some of these contractual defenses may be used to defend against clauses that require waiver of class action procedures. For example, when the deprivation of class action procedures is imposed to prevent plaintiff from proceeding with a claim in any forum, the clause should be voided for violation of public policy.<sup>430</sup> As well, unless such a waiver is very clear, a court should rule that the plaintiff did not actually consent to be deprived of class action procedures.<sup>431</sup> Also, when a company uses trickery or deception to impose such a clause, it should be voided for fraud.<sup>432</sup> As with unconscionability, the success of any of these defenses as a means of voiding the elimination of class actions will turn on the specific facts surrounding the imposition of the clause and its impact, as well as on the law of the particular jurisdiction.

### *B. Parties' Ability to Elect Classwide Arbitration Over Classwide Litigation*

Given the argument set out above—that at least in some situations plaintiffs cannot be deprived of their right to proceed by way of class action—should parties be permitted to choose to resolve their disputes through an arbitral class action rather than a litigated class action? In general, the policies supporting arbitration and parties' right to contract support such a choice. There may, however, be some constitutional, statutory, or contractual limits. Moreover, even assuming the election of classwide arbitration over class action litigation is permissible, it is unclear whether it would be desirable for many parties. The answers to both questions will

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dealing," "inescapable adhesion," "substantive unconscionability," or "defective agency").

429. See, e.g., Sternlight, *Rethinking*, *supra* note 4, at 25-39 (asserting that courts' favoritism toward arbitration leads them to reject valid common law defenses).

430. See, e.g., Stirlen v. Supercuts, Inc., 60 Cal. Rptr. 2d 138 (1997) (holding void, as a matter of public policy, an arbitration agreement that restricted arbitral remedies).

431. See Long v. Fidelity Water Sys., Inc., No. C-97-20118 RMW (N.D. Cal. May 26, 2000) (holding plaintiff never "agreed" to arbitration imposed by credit card company in change of terms notice) (on file with author); see also Stempel, *A Better Approach*, *supra* note 428, at 1426 (arguing that courts should use "consent" concept to void unfair arbitration clauses).

432. See, e.g., Engalla v. Permanente Med. Group, Inc., 938 P.2d 903, 917-22 (1997) (holding that arbitration clause could be voided for fraud because company gave false assurances as to speed of arbitration).

ultimately depend upon the nature and feasibility of the classwide arbitration.

It seems clear that under existing law parties should, in at least some circumstances, be permitted to resolve their class action disputes through arbitration rather than through litigation. The policy arguments favoring class actions do not necessarily dictate that the class action must be litigated rather than arbitrated.<sup>433</sup> In theory, at least, and assuming its basic feasibility, an arbitral class action might provide the same efficiencies as would class action litigation, thus serving the interests of plaintiffs with small cases and of the public at large. Moreover, the law and policy favoring arbitration would seem to support parties' election of an arbitral class action over a litigated class action.<sup>434</sup>

### *1. Possible Limitations on Parties' Choice of Classwide Arbitration*

#### *a. Statutory Limits*

As discussed above, Congress has the power to explicitly or implicitly legislate that certain disputes are not subject to arbitration.<sup>435</sup> If Congress so chose, it might specify that claims under particular statutes or even claims in general could not be resolved through arbitral class actions. It does not appear, however, that Congress has enacted such legislation to date.

#### *b. Contractual Limits*

Alternatively, it can be argued that courts need not and should not enforce arbitration clauses that they find to be unconscionable.<sup>436</sup> If the nature of an arbitral class action were such that plaintiff could show that an agreement contemplating such a mechanism was grossly unfair, then the court should refuse to

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433. See *supra* text accompanying notes 90-108 for a discussion of the policy arguments favoring class actions.

434. See *supra* text accompanying notes 66-74 for a discussion of the law and policy favoring arbitration.

435. See *supra* text and accompanying notes 365-419.

436. See *supra* text and accompanying notes 420-27.

compel such arbitration. To make such a showing plaintiff might demonstrate, for example, that the arbitral class action would be biased or excessively expensive or inconvenient, compared to class action litigation or that essential discovery would not be available. Thus far, while experiences with class action arbitration are scant, participants in the few classwide arbitrations that have been held have not voiced sharp criticism of the inefficiency of such arbitrations.<sup>437</sup>

### *c. Constitutional Limits*

#### *i. Due Process*

The most interesting question is whether the Due Process Clause limits parties' election of class action arbitration over litigation. As discussed, the Supreme Court has repeatedly held that because class actions, as "representative" litigation, raise special due process concerns,<sup>438</sup> certain elements of Rule 23 appear to be mandated by the Due Process Clause. In order for a litigated class action to be binding on absent class members, the court must have helped properly define the class, provided for adequate notification of absent class members, ensured the adequacy of the class representative and attorneys, and perhaps provided notice of and approved any settlement.<sup>439</sup>

But how are these due process concerns relevant to parties' decision to resolve their disputes through class action arbitration? The most straightforward implication of the existing body of law for arbitral class actions is that, if a named plaintiff and defendant agree to resolve a dispute through an arbitral class action, and if that class action does not provide adequate protection for absent

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437. See *supra* note 168. Significantly, however, the courts played an extensive role in each of these classwide arbitrations.

438. See generally Monaghan, *supra* note 109 (examining due process challenges to antisuit injunctions and preclusive judgments in class action suits); Mullenix, *supra* note 109 (focusing on plaintiffs' due process rights); Cottreau, *supra* note 122 (arguing that due process requires that nonresidents, and in some instances even residents, should have the option to opt out of a class action).

439. See *supra* notes 109-22 and accompanying text. As noted earlier, a question exists as to whether some of the due process protections are available only to out-of-state class members. See *supra* note 115. At minimum, therefore, such protections must be offered in all class actions involving out-of-state plaintiffs.

class members, those absent class members would not be bound by the result. It is inconceivable that courts would allow absent class members to be bound by an inadequate arbitral proceeding, where they would not have been bound by an inadequate judicial proceeding.<sup>440</sup> Thus, if the named plaintiff lost the class action, the absent class members would be free to bring their own suit if they could show that the notice they received was inadequate, that the named plaintiffs failed adequately to represent their interests, or that a settlement which was reached did not adequately represent their interests.

*ii. Court Protection of Due Process Rights*

Some may argue that arbitrators are just as capable of protecting due process interests as judges.<sup>441</sup> They may suggest that arbitrators do not need courts' assistance to protect due process interests. Or, they may argue that arbitrators should be permitted to function as magistrates or special masters, making the important class action determination subject to ceremonial approval by the court.

Without questioning the dedication or competence of many arbitrators,<sup>442</sup> this Article nonetheless suggests that some judicial participation in an arbitral class action is necessary to protect the due process rights of absent class members. Allowing arbitrators on their own to decide such issues simply will not comport with the Due Process Clause. One can best see the need for substantial judicial participation in arbitral class actions by considering some of the various stages of a class action and the due process interests that may be implicated. From the outset, the arbitral class action poses an interesting question: who chooses the arbitrators? In a nonclass arbitration, the arbitration clause typically will allow plaintiff and

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440. *See id.*

441. This seems to be the position of at least one commentator, who argued that, once the class is certified, arbitration would be sufficient to protect any due process interests and that no substantial court involvement would be necessary during the actual proceedings. *See* Waltcher, *supra* note 41, at 403-05.

442. In many instances, the attorneys or former judges who serve as arbitrators may be as familiar with class action issues as judges. Several of the attorneys interviewed in connection with this Article emphasized that the expertise of the arbitrators regarding class actions was a selling point for the process. *See supra* notes 148-49.

defendant jointly to select the arbitrator. Yet, in a class action, presumably the named plaintiff, or more likely the class attorney, will choose an arbitrator or arbitrators on behalf of the absent class plaintiffs. Without court supervision of the formation and treatment of the arbitral class action, this means that the absent class members will ultimately be bound by the ruling of an arbitrator they had absolutely no role in selecting.

The process and legitimacy of class certification is critical to the question of whether absent plaintiffs may be bound to the outcome of the class action. As the *Manual for Complex Litigation* states: "Whether a class is certified and how its membership is defined can often have a decisive effect not only on the outcome of the litigation[,] but also on its management."<sup>443</sup> Certification is key because it determines not only whether a representative suit may be brought, but also how it must be structured to ensure that all class members' interests are adequately represented. Discovery and an evidentiary hearing may be required in order to explore certification issues fully.<sup>444</sup> At times subclasses must be created to protect adequately the interests of class members with interests that conflict to some degree.<sup>445</sup>

Once the certification determination has been made, adequate notice must be afforded to class members—at least in damages actions—so that they can opt out. The notice issues are again complex, turning on not only the precise wording of the notice, but also on the means by which the notice will be communicated to class members.<sup>446</sup> Sometimes courts employ their subpoena powers to

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443. MANUAL FOR COMPLEX LITIGATION, *supra* note 94, § 30.1. The *Manual* goes on to explain:

[Class certification] determines the stakes, the structure of trial and methods of proof, the scope and timing of discovery and motion practice, and the length and cost of the litigation. The decision on whether or not to certify a class, therefore, can be as important as decisions on the merits of the action and should be made only after consideration of all relevant evidence and arguments presented by the parties.

*Id.*

444. *See id.* §§ 30.12-13.

445. *See id.* § 30.15.

446. *See id.* § 30.211.

obtain information necessary to provide adequate notice.<sup>447</sup> Then, if a tentative settlement is reached, the absent class members must be notified and afforded an opportunity to attack the validity of the settlement. To review the fairness and adequacy of a settlement a court will need to consider the likely results had the case litigated, and may well need to hear evidence.<sup>448</sup>

An arbitrator could play each of these roles, but it seems questionable whether a case in which each of these functions was performed by an arbitrator rather than a court would comport with due process. Put simply, judges are substantially burdened by the responsibility of protecting the interests of absent class members, and many commentators have questioned the practice, particularly with respect to mandatory as opposed to opt-out class actions.<sup>449</sup> It seems even more inappropriate to bind absent class members to class action determinations in a case supervised only by an arbitrator. First, the arbitrator will have been selected at least in part by the named plaintiff or their attorneys, not by the absent class members. Thus, it is difficult to see how such an arbitrator would play the role of the court in checking possible self-dealing.<sup>450</sup> Second, although the Supreme Court has expressed great enthusiasm for private arbitrators and their capabilities,<sup>451</sup> we may not yet have reached the point at which they are deemed equally

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447. *See id.*

448. *See id.* §§ 30.41-42.

449. *See Weber, supra* note 121, at 1215-17 (arguing that all class members should be given the choice, after they learn of the specific contents of a settlement agreement, of whether to accept the agreement or instead opt out of the class, thereby retaining their right to file an independent action). *See generally* Monaghan, *supra* note 109 (arguing that a court should not use antisuit injunctions to prevent nonparty, nonresident class members from making due process challenges in a second court); Mullenix, *supra* note 109 (discussing due process concerns that arise in class actions and suggesting possible reforms).

450. *Cf. MANUAL FOR COMPLEX LITIGATION, supra* note 94, § 30 (explaining that class litigation imposes unique responsibilities on the court to protect interests of class members); *see also supra* note 125 (collecting articles discussing possible conflicts of interest between class counsel or named plaintiffs and absent class members, and emphasizing concomitant duty of court to protect against unfairness).

451. For examples of the Court's acknowledgement of deference to legitimate arbitration agreements, *see Wright v. Universal Maritime Serv. Corp.*, 525 U.S. 70, 77-78 (1999); *First Options, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995); *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 55-56 (1995).

capable of protecting individuals' critical due process interests. Third, if arbitrators alone were to decide these crucial class action issues, it is unclear how a record could be made for possible appeal. How could a court review an arbitrator's decision without a transcript or other documents? Yet, at a minimum, due process would seem to require that a class member not be bound by an arbitrator's decision on class issues without at least having the opportunity to seek review by a higher court.<sup>452</sup>

In short, it is telling that in all of the arbitral class actions that attorneys have discussed with this author, the judge rather than the arbitrators decided all the critical class action issues.<sup>453</sup> The judge in each case defined the class, approved the wording of the notice to class members, approved any opt-out provision, and approved any proposed settlement.<sup>454</sup> In fact, in one of the arbitral class actions the judge decided all motions and supervised all discovery, and the parties did not even select an arbitration panel until they were ready to make their factual presentations.<sup>455</sup> Thus, real-world experience, as well as theory, supports the point that judges must play a substantial role in deciding class action issues in order to protect the due process interests of absent class members.<sup>456</sup>

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452. Some courts may reject the analysis proposed here, choosing instead to examine each arbitral class action on a case-by-case basis and to conclude that absent class members are bound by those class actions in which, even without court participation, the arbitrators adequately protected their rights. In order to permit such a review, it will at minimum be necessary for class arbitrations to keep a transcript and record that is more substantial than that kept in a typical arbitration. When transcripts are kept, such as in labor arbitrations, they will likely be sufficient. In most commercial arbitrations, however, no transcripts are currently maintained. *See Keating v. Superior Court*, 245 P.2d 1192, 1210, 1215 (Cal. 1982) (Richardson, J., concurring and dissenting).

453. *See supra* note 149.

454. *See id.*

455. *See supra* note 151.

456. As noted above, one commentator has suggested an alternative to active judicial participation in the early stages of the arbitration whereby the arbitrator makes preliminary decisions on class issues, subject to ultimate review and approval by the court. Such a scheme might be deemed acceptable on due process grounds in that the court would maintain final decision-making power. However, such an approach would seem unworkable, and I have uncovered no evidence that it has ever been attempted. If one reads through materials such as the *Manual for Complex Litigation*, one is immediately struck by the great complexity of class actions. The decisions are never simple or discrete. Rather, even the wording of a notice can require intensive arguments and hearings. A rule requiring courts to review arbitrators' decisions on all such matters would either call for a great deal of redundant analysis on the part of the litigants and the court, or otherwise result in the court simply rubber stamping the arbitral decisions. Either result is undesirable and the latter may be unconstitutional.

*iii. Raising Due Process Concerns in the Instant Case*

It is important to consider whether due process concerns regarding arbitral class actions can only be raised in a *subsequent* case, in which absent class members seek to assert their rights,<sup>457</sup> or whether such concerns can be raised at the time the arbitral class action is being heard. From a practical standpoint this question is critical. If due process concerns can only be raised in a subsequent proceeding, they may never be raised. As with other claims, many due process claims may feasibly be made only if brought on a class basis. Thus, once the initial class action is resolved, it may not be feasible for absent class members to bring individual claims.

Several Supreme Court decisions provide that due process concerns may be raised at the time of the initial proceeding. First, in *Eisen v. Carlisle & Jacquelin*,<sup>458</sup> the Court allowed defendant to secure dismissal of a class action because the named plaintiff could not afford to provide adequate notice to the absent class members.<sup>459</sup> Second, in *Phillips* the Court explicitly held that the defendant had standing to assert the due process concerns of the absent plaintiffs,<sup>460</sup> although it ultimately refused to dismiss the action for lack of personal jurisdiction over the absent class members.<sup>461</sup> Third, *Amchem* and *Ortiz* both took note of due process concerns in voiding settlements of class actions<sup>462</sup> without insisting that challengers wait to raise such concerns in a subsequent case.<sup>463</sup> Thus, it seems

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457. According to conventional terminology, this is the question of whether a due process challenge may be asserted only in the "F2." case, or whether it may be raised in the "F1." action. See Monaghan, *supra* note 109, at 1149-50.

458. 417 U.S. 156 (1974).

459. See *id.* at 161. *Eisen* did not explicitly address the question of whether a defendant should have standing to raise this due process concern, but did permit the claim.

460. See *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 805 (1985) ("Whether it wins or loses on the merits, petitioner has a distinct and personal interest in seeing the entire plaintiff class bound by res judicata just as petitioner is bound.").

461. See *id.* at 803-14.

462. *Amchem* recognized that constitutional concerns existed, but chose not to reach them, ruling instead only on statutory grounds. See *Amchem Prods. Inc. v. Windsor*, 521 U.S. 591, 628-29 (1997). *Ortiz* emphasized that mandatory class actions implicate the Due Process Clause by purporting to bind those who do not directly participate in the suit and in fact have no opportunity to opt out. See *Ortiz v. Fibreboard Corp.*, 119 S. Ct. 2295, 2314-15 (1999).

463. Rather, in *Ortiz* the Court approvingly cited *Phillips* for the proposition that "before an absent class member's right of action [is extinguished] Due Process require[s] that the member 'receive notice plus an opportunity to be heard and participate in the litigation.'"



clear that in the context of a class action arbitration, either defendants or objecting plaintiffs should be permitted to raise the claim that the procedures do not adequately protect the due process interests of absent class members. Moreover, courts should permit objectors to raise such challenges in court on an interlocutory basis, rather than requiring them to wait until the completion of the entire arbitral class action. Requiring challengers to wait until the completion of the entire class action would potentially cause challengers, participants, and the court to incur substantial delay and to waste time and resources. Purported class action arbitration should not be permitted to proceed unless it adequately protects the interests of the class members.<sup>464</sup>

*iv. Agreeing to Arbitration Should Not Waive Due Process Rights*

Finally, some may suggest that, simply by agreeing to arbitration, absent class members waive any due process right they may have had in court. The argument fails at several levels. First, and most importantly, waivers of constitutional rights may not be inferred lightly,<sup>465</sup> and at the very least must be clear.<sup>466</sup> Thus,

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*Ortiz*, 119 S. Ct. at 2315 (quoting *Phillips*, 472 U.S. at 812). In both suits, the challenges to the settlement were raised in the initial case by objecting class members. *See Ortiz*, 119 S. Ct. at 2305-06 (noting that district court allowed objectors to intervene in the suit); *Amchem*, 521 U.S. at 605.

464. In all of the arbitral class actions about which I could obtain information, the court preserved for itself the responsibility to make important decisions that would implicate due process. *See supra* note 149.

465. *See Aetna Ins. Co. v. Kennedy*, 301 U.S. 389, 393 (1937) (stating "courts indulge every reasonable presumption against waiver," and holding that party's request for directed verdict did not waive party's right to have jury resolve factual issues); *see generally Sternlight, Rethinking, supra* note 4, at 49-55 (discussing Supreme Court decisions that address waiver of constitutional rights).

466. *See Fuentes v. Shevin*, 407 U.S. 67 (1972) (holding that contract for sale of stove which permitted seller to repossess for nonpayment did not waive purchaser's due process right to notice and hearing because it did not specify that retrieval would be without notice and hearing); *see also Reuben, Constitutional Gravity, supra* note 364, at 1022 (arguing that the knowledge and voluntariness of a waiver of due process rights "should be structured according to the following three factors: (1) the visibility and clarity of the waiver agreement on its face, (2) the general contractual environment in which the waiver was secured, and (3) the specific facts and circumstances of the actual bargaining over the waiver"); *Sternlight, Rethinking, supra* note 4, at 49 (arguing that waiver must be clear).

unless an arbitration clause expressly provided that persons who agreed to its terms were waiving their due process rights to be protected by a court in the event of a class action, the arbitration clause should not be interpreted to have such an effect. Certainly few, if any, people would understand that their agreement to arbitrate also served as a waiver of their constitutional rights connected to the filing of a class action. Second, as I have argued elsewhere, the Supreme Court's waiver cases involving other issues use a more complex fact specific analysis to determine whether waiver of a constitutional right should be found.<sup>467</sup> Specifically, in *Fuentes v. Shevin*<sup>468</sup> and *D.H. Overmyer Co. v. Frick Co.*<sup>469</sup> the court has implicitly adopted a four-factor balancing test for waiver calling upon courts "to examine the visibility and clarity of the waiver itself, the relative knowledge and economic power possessed by the parties, the degree of voluntariness of the purported agreement, and the substantive fairness of the purported agreement."<sup>470</sup> Applying this test, courts should find that when companies use contracts of adhesion to impose binding arbitration on consumers and employees, those consumers and employees have not waived their due process rights to be treated fairly in the event a class action is filed on their behalf. Third, an argument can be made that the right to proceed in court, rather than through arbitration, is nonwaivable.<sup>471</sup> In short, the due process interests of absent class members cannot be ignored.

## 2. Likely Unpopularity of Classwide Arbitration

For the reasons set forth above, it is appropriate to allow parties to choose classwide arbitration over class action litigation, subject to statutory, contractual, and constitutional limitations. It is not at all clear, however, that classwide arbitration will be a popular

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467. See Sternlight, *Rethinking*, *supra* note 4, at 56-69.

468. 407 U.S. 67 (1972) (refusing to find waiver).

469. 405 U.S. 174 (1972) (upholding a clear confession-of-judgment clause which was the subject of lengthy negotiations by attorneys on behalf of two knowledgeable parties, and which was provided in return for consideration).

470. Sternlight, *Rethinking*, *supra* note 4, at 57-58.

471. See Reuben, *Constitutional Gravity*, *supra* note 364, at 1038-40 (suggesting that persons might not be able to waive their rights to certain kinds of fair procedures).

choice. First, if many companies have chosen arbitration over litigation in order to avoid class actions altogether,<sup>472</sup> those companies may have little interest in a classwide arbitration process. Second, given the due process protections that must be employed in order for arbitral class actions to pass constitutional muster, some companies may conclude that classwide arbitration would be as undesirable as or perhaps even more undesirable than classwide litigation.<sup>473</sup> If a body of practice or law were to develop that required substantial back-and-forth between judge and arbitrators in working out the details of certification, notice, adequacy of representation, and settlement approval, it might well be that classwide arbitration would prove more burdensome and time consuming than class action litigation.<sup>474</sup> That is, the concerns expressed by several courts and commentators as to the logistical difficulties of the hybrid process<sup>475</sup> may cause the technique to be unpopular. Third, because the technique of classwide arbitration is relatively new and untried, it is inevitably somewhat unpredictable. Companies and their attorneys may prefer to resolve their disputes through the known quantity of class action litigation, rather than risk a bad experience with the relatively unknown. As the SEC pointed out, whereas courts have already developed a substantial body of caselaw dealing with class actions, arbitrators would either have to follow the court rules or create their own set of rules.<sup>476</sup> Yet, if the arbitrators choose to follow courts' rules, there seems to be little reason to prefer classwide arbitration to class action litigation.

Attorneys' experiences with classwide arbitration, to date, support the idea that classwide arbitration is not likely to be popular. As might be expected, given the extensive role played by the judge in each case, none of the attorneys interviewed found that classwide arbitration held significant efficiency advantages over classwide litigation.<sup>477</sup> Instead, while the attorneys interviewed were generally

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472. *See supra* notes 1-17 and accompanying text.

473. I focus on the popularity of the technique among companies, rather than consumers, because, as a practical matter, companies are the ones drafting arbitration clauses.

474. It is not clear whether this increased burden would be worse for companies or class plaintiffs. Although in some types of litigation, defendants may use expense and slowness to weaken the plaintiffs, plaintiffs' class action attorneys may be able to withstand and even take advantage of such a lengthy process.

475. *See supra* notes 179-90 and accompanying text.

476. *See supra* note 174 and accompanying text.

477. *See supra* note 168.

pleased with a version of the process in which judges maintained control over the class action determinations, and arbitrators ultimately decided the merits of the dispute, they typically viewed the two processes as quite similar.<sup>478</sup> Thus, while some companies may draft arbitration clauses specifying that class actions must be arbitrated, others may follow the lead of the securities industry and opt for litigation of class action claims.<sup>479</sup>

### *C. How Courts Should Interpret Various Arbitration Clauses*

Some clauses purport to eliminate both litigated and arbitral class actions. Courts should refuse to enforce such a clause when the elimination of the class action remedy would explicitly violate a relevant federal statute, would prevent plaintiff from obtaining adequate relief under the statute, or would put plaintiff in an unfair situation such that the contract should be held unconscionable or violative of other contractual doctrines. However, absent any of these circumstances, and absent viable arguments that others may develop, courts should permit parties to opt not to proceed with class actions.

Other clauses specify that class actions will be handled in litigation, and that individual disputes will be handled through arbitration. Courts should enforce both aspects of such a clause.<sup>480</sup> There is no reason why parties should not be able to elect to resolve some disputes through litigation, and others through arbitration. Agreements along these lines have been used in the securities industry for several years, and courts have been interpreting them appropriately.

Finally, some clauses specify that class actions, as well as individual claims, will be handled through arbitration. Such a clause

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478. Although one defense attorney believed that it was sometimes advantageous to his client to be able to pick an arbitral factfinder, rather than to depend on a judge or jury, he did not suggest that this choice resulted in a substantial savings in time or money. Rather, he hoped that the arbitrators might be more sympathetic to his client's position. He also observed that in other circumstances he would find the in-depth appellate review of litigation more attractive. *See* Telephone Interview with Gordon Bosserman, attorney for defendant in *Blue Cross* cases (Oct. 11, 1999).

479. One attorney reported that franchisor Southland had ceased to require arbitration of class actions in its franchise agreements. *See* Telephone Interview with John F. Wells, attorney for plaintiff in *Keating* (Sept. 29, 1999).

480. This assumes, of course, that no independent reasons exist for voiding the agreement.

will often be enforceable. In some situations, however, it may be impermissible for the parties to resolve disputes through class arbitration. Specifically, when, due to the inadequacies of the particular classwide arbitration, the clause denies absent parties their due process rights, violates a relevant statute, or is so unfair as to be considered unconscionable, courts should refuse to mandate class arbitration.

Currently, however, most arbitration agreements remain silent on the issue: they require arbitration of a broad category of claims but do not explicitly state whether disputes may be resolved in an arbitral class action. While companies will likely soon begin to state explicitly that disputes may not be resolved through class actions, in the immediate future courts will be required to deal with the silent clause. This Article has argued that when a clause is silent, it is inappropriate for a court to assume that the parties meant to eliminate the right to proceed by way of class action.<sup>481</sup> Courts should not, as some have done, simply apply the consolidation cases to this new context without considering the distinctions between consolidation and class action.<sup>482</sup> Thus, a court has only three conceivably legitimate choices in interpreting a silent clause: (1) hold the class issue to be nonarbitrable, therefore allowing it to be litigated; (2) order the dispute to be handled through classwide arbitration (assuming the prerequisites for certification are met); or (3) order the dispute to be arbitrated, and let the arbitrators determine whether classwide arbitration should be allowed. The choice is not easy, but the second option best protects all of the relevant contractual and policy interests,<sup>483</sup> at least when no federal statute or contractual doctrine prohibits classwide arbitration in the particular setting.<sup>484</sup> When the parties have agreed to a broad arbitration clause, it is not appropriate to exclude an entire class of disputes from arbitration, unless permitting class arbitration would violate constitutional, statutory, or contractual interests.<sup>485</sup> As

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481. *See supra* text accompanying notes 328-54.

482. *See supra* text accompanying notes 328-40.

483. This is the approach taken by the California courts, and by one Pennsylvania court. *See supra* notes 253-61 and accompanying text.

484. *See supra* notes 360-419 and accompanying text. As noted earlier, it might be argued that state statutes or additional constitutional arguments also bar classwide arbitration or the entire elimination of class actions. *See supra* note 365.

485. For a discussion of the arguments supporting classwide arbitration even when agreements are silent on the issue, *see supra* notes 253-61 and accompanying text.

between the second and third options, it is preferable on due process and policy grounds for the court, rather than the arbitrator, to determine the permissibility of class actions.<sup>486</sup>

When courts, notwithstanding the arguments presented here, interpret a silent contract to proscribe them from ordering a dispute to be handled through classwide arbitration, they should at minimum refrain from impermissibly interfering with arbitrators' own determination to allow a classwide arbitration.<sup>487</sup> Even if a silent contract may be read to deny courts the authority to order classwide arbitration, certainly such a contract should not be read to allow a court to prohibit arbitrators from ordering classwide arbitration. Then if, as is admittedly unlikely,<sup>488</sup> the arbitrators were to order classwide arbitration, the court should assist in at least supervising certification, notice, and approval of any settlement to ensure that the interests of absent class plaintiffs are adequately protected.

#### IV. A CALL FOR LEGISLATIVE REFORM

As set out above, courts can adequately protect the policies underlying both class actions and arbitration using existing case law. Nonetheless, to the extent courts fail adequately to protect consumers, employees, and others from companies' unfair attempts to eliminate class actions, Congress should enact protective legislation.

##### *A. Legislation Precluding the Use of Arbitration Clauses to Eliminate Class Actions*

Legislation will be needed to prevent companies from using binding arbitration clauses to eliminate class actions entirely, to the extent we decide it would be undesirable to allow companies to insulate themselves from class actions, and to the extent that courts fail to accept the statutory and contractual arguments set out in this

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486. See *supra* notes 441-56 and accompanying text.

487. A few courts have not only refused to certify a classwide arbitration, but have also ordered arbitration to proceed on an individual basis. See *supra* note 346.

488. Few arbitrators are likely to order classwide arbitration on their own volition. See *supra* note 137 (noting no record of such cases); *supra* note 340 (discussing why arbitrators are not likely to order consolidated arbitration).

Article or elsewhere. By allowing suits to be brought by small claimants who otherwise could not afford to sue, the class action not only protects the rights of those persons, but also facilitates enforcement of laws passed by our legislatures. Potential defendants should not be permitted to insulate themselves from liability in such small cases simply by imposing an arbitration clause in a contract of adhesion. While such defendants might seek to cloak themselves in the rubric of freedom of contract, what they really are seeking is freedom from statutory regulation.

Nor can such insulation from class action liability be justified by the fact that class actions are controversial and have been under attack recently. Some of these attacks, such as that class actions may at times benefit the attorneys more than the class members, may well be justified.<sup>489</sup> The solution to such problems, however, is not to allow companies to entirely insulate themselves from liability in small cases, but rather to attack any specific problems with class actions more directly—through court disapproval of proposed settlements,<sup>490</sup> or perhaps even through rule changes or legislation.<sup>491</sup> One plaintiff-side organization, the National Association of Consumer Advocates, has taken the need for reform seriously and published *Standards and Guidelines for Litigating and Settling Consumer Class Actions*.<sup>492</sup>

Even if Congress and state legislatures were to determine that class actions are an undesirable device, and should be entirely

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489. See *supra* notes 123-26 and accompanying text.

490. See, e.g., *Crawford v. Equifax Payment Servs., Inc.*, 201 F.3d 877, 880-82 (7th Cir. 2000) (disapproving proposed class settlement in consumer suit on ground that settlement, while providing benefits to named plaintiffs and class counsel, was not fair to absent class members).

491. If class attorneys are not adequately representing the interests of class members, the solution would seem to be improved court supervision of class settlements, rather than total elimination of the class action. See, e.g., Issacharoff, *supra* note 125, at 805-06 (arguing that despite their risks, class actions must exist to counter problems such as transaction costs and barriers to entry); Macey & Miller, *supra* note 125, at 3-118 (analyzing consequences of divergent interests between plaintiffs and their class action attorneys); Lazos, *supra* note 125, at 308-32 (arguing that conflicts of interest between plaintiffs' attorneys and class members calls for appointment of guardian to protect class members' interests); HENSLER ET AL., *supra* note 1, at 31-35 (arguing that increasing judicial regulation of damages class actions is the key to improving the balance between the good and the ill consequences of such class actions, and urging judges to scrutinize proposed settlements more closely, and to reward attorneys only for their actual services).

492. See Brian Wolfman, *Forward: The National Association of Consumer Advocates' Standards and Guidelines for Litigating and Settling Class Actions*, 176 F.R.D. 370, 370-74 (1998).

eliminated, they should have the courage to make such a determination explicit by, for example, eliminating the provision for class actions in the Federal Rules of Civil Procedure or comparable state rules. Such a measure, while opposed by this author, would at least put the real issue before the public, rather than allowing putative defendants to achieve the result clandestinely through arbitration clauses.<sup>493</sup>

If Congress does decide to act to prevent companies from using arbitration to abolish the class action, it would need to think carefully about how to structure such legislation. For example, it might not be desirable to entirely eliminate parties' right to freely waive their right to proceed by way of class action. At the extreme, if two sophisticated companies, represented by counsel, knowingly contract that they will never sue each other in a class action<sup>494</sup> absent other special circumstances, it should not be voided on statutory<sup>495</sup> or contractual grounds. A workable but less extreme statute might bar companies from using contracts of adhesion to prevent persons from suing in a class action. Such a rule would protect consumers and employees from unknowingly waiving their right to sue in a class action, without preventing larger, more sophisticated parties from knowingly reaching a similar agreement. The California Supreme Court in *Keating* laid the foundation for such an approach, by focusing on the defendant's troubling use of adhesion contracts to require arbitration and to eliminate the class action.<sup>496</sup> Of course, approaching the issue in this manner would

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493. Professor Christopher Drahozal has argued that because rational consumers or others might well waive their rights to class actions, concluding that their costs outweigh their benefits, courts should not void such seemingly unfair clauses. *See Drahozal, supra* note 5, at 62-64. However, he fails to present any empirical data supporting this claim, but instead merely asserts a theoretical possibility. Moreover, the argument fails to account adequately for significant economic and psychological phenomena including lack of information, lack of perfect competition, overoptimism, and disparate treatment of potential losses and potential gains. *See Sternlight, Panacea, supra* note 68, at 686-93. Further, because no one can plausibly assert that consumers are actually making an informed decision as to whether to waive their opportunity to proceed by class action, it would be more honest to handle these concerns legislatively than to pretend that consumers are voluntarily giving up the class action.

494. Although sophisticated companies typically do not sue one another in class actions, such a scenario is not entirely impossible to imagine. For example, a class of distributorships might choose to sue a manufacturer or a dealer in a class action.

495. The exception would be if a relevant substantive statute explicitly barred such a waiver.

496. *See Keating v. Superior Court*, 645 P.2d 1192 (Cal. 1982) (observing that allowing



require the drafters to define "contracts of adhesion," but this does not seem to be an insurmountable obstacle.<sup>497</sup>

Alternatively, Congress might attempt to bar the elimination of class actions in those cases where plaintiffs have no feasible alternative by which to present their claim. Such a statute would more narrowly address the particular situation that seems most troubling: elimination of plaintiffs' only viable way of preventing their claims. The drafting and enforcement of such a provision, however, might prove unworkable. It is hard to imagine how a statute could define clearly those situations in which class actions are logistically necessary to permit enforcement of a claim.

### *B. Legislation Precluding the Use of Classwide Arbitration*

Existing law permits parties to select classwide arbitration over class action litigation, subject to statutory, contractual, and constitutional constraints. Given the inherent problems with classwide arbitration, however, Congress may conclude it would be desirable to prohibit use of the technique.

As discussed earlier, the various self-regulated securities organizations and the Securities and Exchange Commission have rejected the use of classwide arbitration in the securities context, concluding that the technique was undesirable for logistical reasons.<sup>498</sup> Therefore, class action claims against brokerages are litigated, and individual claims are arbitrated.<sup>499</sup> This dual system, which has been in place since 1992, appears to be working

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companies to use adhesion contracts to eliminate class actions would chill effective protection of common interests, foreclose many individual claims, and protect the drafter against liability; and noting that such a practice "may well be oppressive and may defeat the expectations of the nondrafting party").

497. One piece of pending legislation, the Consumer Fairness Act of 1999, H.R. 2258 106th Cong., takes on a broader but related definitional task. Its goal is "[t]o treat arbitration clauses which are unilaterally imposed on consumers as an unfair and deceptive trade practice and prohibit their use in consumer transactions, and for other purposes." *Id.* To achieve this end the bill defines "consumer transaction" as "the sale or rental of goods, services, or real property, including an extension of credit or the provision of any other financial product or service, to an individual in a transaction entered into primarily for personal, family, or household purposes." *Id.* § 1002.

498. *See supra* text accompanying notes 169-78. Some also urged that classwide arbitration was undesirable because arbitrators could not adequately protect the due process interests of absent class members or that arbitrators lacked the requisite expertise to decide class action issues. *See supra* text accompanying notes 176-78.

499. *See supra* text accompanying notes 169-78.

smoothly.<sup>500</sup> Despite the fear that a rule prohibiting arbitration of class action claims creates a major loophole in the general requirement of arbitration of individual claims,<sup>501</sup> this apparently has not occurred.<sup>502</sup>

Thus, Congress might also determine that class action arbitration is simply an unworkable idea, and might choose to prohibit parties from electing that dispute resolution process in lieu of class action litigation. Congress might conclude that such legislation is desirable to protect the interests of absent class members and to decrease the workload of the courts. Supervision of class action arbitrations may well prove even more burdensome for the courts than handling class action litigation. However, while this author is skeptical as to the merits of arbitral class actions, Congress should not hurry to pass such legislation. Rather, Congress should allow further experience with the technique and refrain from outlawing classwide arbitration until more information is available as to its realistic workability. Thus far, while none of the participants in classwide arbitration has raved about its advantages over litigation, neither have they harshly criticized the technique.<sup>503</sup>

## CONCLUSION

As arbitration meets the class action, one thing seems clear: companies should not be permitted to use arbitration clauses as a stealth weapon or Trojan horse<sup>504</sup> to preclude plaintiff class actions in both the litigation and arbitration arenas. If companies believe the class action device is being abused and ought to be eliminated, they are free to seek such legislative reform. They should not, however, be permitted to use contracts of adhesion to eliminate class

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500. *See supra* note 189 and accompanying text. Indeed, while the system has not been modified, there does not appear to be a widespread call for change.

501. *See supra* note 224 and accompanying text.

502. It is quite likely that the great expense and logistical complexities of class action litigation deter plaintiffs and their attorneys from filing class suits solely to evade an arbitration clause.

503. Instead, participants seem to agree that the technique works fairly well, at least so long as the court continues to do all the major tasks associated with class actions. *See supra* notes 164-65 and accompanying text.

504. I credit Professor Katsoris for the Trojan horse metaphor. *See* Constantine N. Katsoris, *Riding the Trojan Horse Back to Wilko?* SEC. ARB. COMMENTATOR, July 1999, at 1, 3 (arguing that securities brokerages should not be permitted to use arbitration clauses to prevent customers from recovering punitive damages).

actions on a wholesale basis. When companies attempt to do so, they should be stopped, at least to the extent that the elimination of the class action deprives plaintiffs of statutory rights or results in a contract that is unconscionable or otherwise unenforceable. If courts do not begin to step in to prevent companies from eliminating the class action, Congress should legislate to defend this important procedural device which has helped to achieve so many important and just results.

Some of the other legal and policy issues raised by the clash between mandatory binding arbitration and class action are more complex. This Article concludes that the hybrid arbitral class action should be permitted, but only so long as courts maintain sufficient involvement to protect the due process rights of absent class members. Given the rarity with which classwide arbitrations have been employed, it is somewhat difficult to conceptualize precisely how the interplay between courts and arbitrators should work, and what protections must be utilized to comply with due process. To date, however, it seems that courts have chosen to retain all of their usual class action responsibilities, including definition of the class, notification of absent class members, and approval of settlements. This seems to be the wisest way to proceed in order to ensure that the due process rights of absent class members are protected.

Some questions regarding how arbitral class actions ought to be handled may soon become moot. If courts begin to conclude that statutory and contractual doctrines often prevent companies from entirely evading the class action, it may become clear that the disputes over the permissibility of classwide arbitration were just a decoy. That is, it may become obvious that the fight over the permissibility of classwide arbitration has distracted observers from the companies' true goal: total evisceration of consumer and employment class actions. This author predicts that, as courts begin to reject defendants' attempts to eliminate class actions altogether, it will become evident that the hybrid of classwide arbitration has few advocates. Rather, defendants, plaintiffs, and society as a whole, likely will adopt the securities industry's conclusion that class actions are most efficiently and justly handled through litigation.