



Consumer Financial Services Litigation Bulletin



COURTS INCREASINGLY HOSTILE TO CLASS ACTION WAIVERS IN ARBITRATION CONTRACTS

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Following what seems to be a trend of courts refusing to uphold class action waivers in arbitration provisions, both the 2nd and 3rd Circuits recently held as unenforceable class action waiver provisions in American Express (AMEX) customer and merchant agreements. In *Homa v. American Express Company*, No. 07-2921, 2009 U.S. App. LEXIS 3688 (3d Cir. Feb. 24, 2009), the 3rd Circuit ruled that AMEX's class action waiver in its arbitration agreement was unenforceable because it violated New Jersey's public policy. In *In re: American Express Merchants' Litigation*, 554 F.3d 300 (2d Cir. 2009), the 2nd Circuit refused to enforce a class action waiver because doing so "would grant Amex de facto immunity from antitrust liability by removing the plaintiffs' only reasonably feasible means of recovery."

This bulletin provides a summary of the *Homa* and *AMEX Merchants* decisions and some key take-aways on how courts may treat class action waiver arbitration provisions going forward.

In *Homa*, the 3rd Circuit considered a class action arbitration waiver in the context of a consumer credit card claim. *Homa* had filed a class action in the U.S. District Court for the District of New Jersey against AMEX for violations of the New Jersey Consumer Fraud Act. Although AMEX's cardholder agreement was governed by Utah law, which permits class action waiver provisions in arbitration clauses, the choice-of-law rules of the forum state, New Jersey, required the court to consider whether the waiver would violate New Jersey's public policy. If so, the waiver would be unenforceable.

Finding no New Jersey precedent directly on point, the 3rd Circuit predicted how the New Jersey Supreme Court would hold. Citing *Muhammad v. County Bank of Rehoboth Beach, Del.*, 912 A.2d 88 (N.J. 2006), the 3rd Circuit concluded that the New Jersey Supreme Court "would find that the class-arbitration waiver at issue violates the fundamental public policy of

New Jersey." The court found persuasive the holding in *Muhammad* that "the public interest at stake in . . . consumers' ability to effectively pursue their statutory rights under [New Jersey's] consumer protection laws' constituted the 'most important' reason for holding a similar class-arbitration waiver unconscionable." The 3rd Circuit noted that the contract at issue in *Homa*, as in *Muhammad*, appeared to be a contract of adhesion. Moreover, given the procedural posture of a motion to dismiss, the court had to assume as true plaintiffs' allegation that the "claims at issue are of low monetary value" and "because of the nature of the individual class members' claims in this litigation, few, if any, could . . . afford to seek legal redress' if the case could not be resolved on a class basis." Accordingly, the 3rd Circuit held that, based on the pleading, the class arbitration waiver provision was unconscionable.

While the *Homa* decision facially seems to prevent the enforcement of any class action arbitration waiver clause in New Jersey, a concurring opinion emphasizes the limited holding of this case. The concurrence emphasizes that the majority based its ruling on a motion to dismiss standard and therefore was "constrained" by plaintiffs' allegations that only a class action could afford relief. Next, the concurrence notes that class action waivers are not per se unenforceable in New Jersey. Instead, courts should examine several factors, including (1) whether the contract is one of adhesion; (2) the consumer's ability to obtain representation; (3) complexity of the lawsuit; (4) amount of damages; and (5) availability of attorneys' fees and statutory multipliers. Indeed, based on these factors, the holding in *Muhammad* was limited to "low-value" cases, although the New Jersey Supreme Court did not define that term. The concurrence reviews a number of factors that would be pertinent for the parties in *Homa* to address on remand and opens the door for a dispute over whether the class action waiver at issue is unconscionable under New Jersey law in light of the claims at issue.



In *AMEX Merchants*, the 2nd Circuit considered the enforceability of a class action arbitration waiver provision in AMEX's "Card Acceptance Agreements" in the context of an antitrust claim against AMEX by its merchants. The court framed the issue as whether enforcement of the class action waiver was improper because the costs of litigating the antitrust issues alleged were prohibitively high for any individual plaintiff to bear.

The 2nd Circuit reversed the district court's holding that the waiver provision was enforceable. The court relied on plaintiffs' evidence establishing that the recovery for any individual plaintiff "would be too small to justify the expenditure of bringing an individual action." Plaintiffs had hired an expert who opined that the average recovery for an individual plaintiff would be about \$40,000 (after trebling damages), while expert fees alone would exceed \$1 million. Simply stated, in this case, enforcing the class action waiver amounted to granting AMEX "de facto immunity from antitrust liability." The 2nd Circuit acknowledged that the relevant federal antitrust statutes permitted recovery of attorneys' fees for a prevailing plaintiff, but found this fact unpersuasive because "the plaintiffs must include the risk of losing, and thereby not recovering any fees, in their evaluation of their suit's potential costs."

The 2nd Circuit carefully noted that its holding was limited to the facts of the instant case and did not render class action waivers per se unenforceable, either generally or in the arbitration context.

Key take-aways from the *Homa* and *AMEX Merchants* cases are:

- Courts increasingly seem willing to invalidate class action waivers in arbitration agreements.
- The key issue in challenges to class arbitration waivers is whether litigants would effectively have a legal remedy, in light of the types of claims and potential recovery at issue, if forced to litigate on an individual rather than a class basis.
- As a general rule, the more complex a case is the more courts will be inclined to invalidate a class arbitration waiver clause, on the presumption that cost is directly correlated to complexity.
- That said, high damages, statutory attorneys' fees, damages multipliers, and other factors increasing the "value" of a lawsuit could offset the complexity of a case and swing the analysis in favor of upholding the class action waiver.
- Plaintiffs alleging violations of TILA, FDCPA, FCRA, and other similar consumer protection laws will likely argue that these types of cases are of "low value" on an individual basis, as plaintiffs seldom have actual damages and the statutory damages are relatively nominal. Of course, attorneys' fees generally are available to a prevailing plaintiff under these laws, and the litigation costs in these cases typically should be lower than in antitrust and other complex cases.