

The Legal Intelligencer

3rd Circuit Deals Blow to Class-Arbitration Waivers

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Consumers and the lawyers who aim to represent them en masse scored a major victory Tuesday when a federal appeals court held that arbitration clauses may be struck down -- under state law -- as unconscionable if they prohibit the use of the class action vehicle in cases where a large number of consumers have claims that would individually yield only small sums.

In [*Homa v. American Express Co.*](#), the 3rd U.S. Circuit Court of Appeals revived a suit against American Express after finding that a lower court improperly dismissed the suit on the grounds that the consumers were barred from suing in court or as a class and instead were required to bring individual claims before arbitrators.

The unanimous three-judge panel concluded that state courts (as well as federal courts applying state law) are free to declare that such class-arbitration waivers are unconscionable -- even if the contract included a choice-of-law provision that called for applying the law of a state that is decidedly amenable to such pro-business provisions.

The ruling is a victory for attorney F. Paul Bland Jr. of Public Justice in Washington, D.C., and Gary S. Graifman of Kantrowitz Goldhamer & Graifman in Montvale, N.J.

Bland hailed the ruling as a major victory for consumers and said it clarified an important area of 3rd Circuit law by underscoring the power of state courts to reject arbitration and anti-class action provisions they deem unconscionable.

In the suit, a proposed class of New Jersey consumers claim that American Express cheated them by falsely promising rebates of up to 5 percent of purchases made with the Blue Cash Card, and that, in reality, the rebates proved to be much smaller than originally promised.

American Express won the first round of the litigation when U.S. District Judge Joel A. Pisano of the District of New Jersey enforced three provisions in the card members' agreements -- one that called for applying Utah law; a second that waived the right to pursue class actions; and a third that mandated individual and binding arbitration.

Utah has become an attractive home for credit-card issuing banks because a Utah statute expressly allows waivers of class rights in consumer credit arbitration agreements. American Express Centurion Bank, which issued the cards, is based in Utah.

In a May 2007 decision, Pisano rejected the argument that New Jersey law should apply, saying, "the parties' choice of Utah law controls because application of that law does not violate any fundamental public policy of New Jersey."

Applying Utah law, Pisano concluded that the plaintiffs had failed to show that the American Express arbitration clause suffered from any procedural or substantive unconscionability under Utah law.

"Although the boilerplate terms of the cardmember agreement, including the class-arbitration waiver, were presented in the context of a take-it-or-leave-it transaction, plaintiff was free to reject defendants' offer and open a credit account with one of any number of credit card issuers," Pisano wrote.

Pisano said consumers "had ample opportunity to read and understand the terms" of the cardmember agreement, including the class-arbitration waiver, "which appeared in large bold font."

As a result, Pisano said, "it cannot be said that plaintiff lacked a meaningful choice or was compelled to accept the terms of the agreement."

Pisano found that, while class arbitration "would likely be the most advantageous strategy for the purported class to pursue its claims," the class-arbitration waiver did not operate to completely preclude those claims or exculpate American Express in any way.

"Thus, the terms of the parties' contract is not 'so one-sided as to oppress' plaintiff," Pisano wrote. "Moreover, it cannot be said that the enforcement of the class-arbitration waiver would be so unconscionable that 'no decent, fairminded person would view the results without being possessed of a profound sense of injustice,' or that enforcement of the waiver would 'shock the conscience.'"

Instead, Pisano said, the class-arbitration waiver merely "creates an advantage for defendants and imposes a hardship on plaintiff."

Now the 3rd Circuit has ruled that Pisano erred in his choice-of-law analysis and should have recognized that New Jersey courts might refuse to apply a Utah law that so directly conflicts with New Jersey public policy.

"Given the contacts that New Jersey and Utah have with the parties and the litigation, and the policy reasons underlying the states' conflicting laws -- particularly New Jersey's interest in protecting its consumers' ability to enforce their rights under the Consumer Fraud Act -- we predict that the Supreme Court of New Jersey would determine that New Jersey has a materially greater interest than Utah in the enforceability of a class-arbitration waiver that could operate to preclude a New Jersey consumer from relief," U.S. Circuit Judge Franklin S. Van Antwerpen wrote.

Van Antwerpen, who was joined by Judges Thomas L. Ambro and Joseph F. Weis Jr., stopped short of ruling that the American Express class-arbitration waiver must be struck down under New Jersey law.

Instead, Van Antwerpen found that, on remand, Pisano must determine whether the New Jersey courts would deem such a provision unconscionable.

"We hold that, if the claims at issue are of such a low value as effectively to preclude relief if decided individually, then ... the application of Utah law to the class-arbitration waiver is invalid and the class-arbitration waiver is unconscionable," Van Antwerpen wrote.

Law professor Jean R. Sternlight of the University of Nevada-Las Vegas Boyd School of Law, whose writings were cited by the 3rd Circuit, said she believes the ruling is "important because it makes clear that the Federal Arbitration Act does not pre-empt unconscionability challenges to class action prohibitions, and because it finds that choice of law clauses are sometimes trumped by strong state public policy."

American Express' lawyer, Julia B. Strickland of Stroock & Stroock & Lavan in Los Angeles, could not be reached for comment.