INTRODUCTION

Prior to the United States Supreme Court’s decision in *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003) (“*Green Tree*”), arbitration clauses in consumer contracts were routinely utilized by defense counsel in order to defeat class certification. Where the contract permitted the corporation to demand arbitration unilaterally and without consent of the consumer, a corporate defendant’s first response to the filing of a putative class action was to prepare a letter to plaintiff’s counsel invoking its right to demand arbitration. The corporate defendant would then file a motion to dismiss the suit and compel arbitration of the dispute with the named class representative. In that motion, defense counsel customarily included the following argument: Because the corporation has the right to demand arbitration of each and every dispute with its customers, class treatment would not be appropriate in the case, as individual issues would predominate and separate arbitrations would render the litigation unmanageable. In short, defense counsel utilized arbitration clauses to demonstrate that the requirements of Rule 23 could not possibly be met by plaintiff, even assuming plaintiff could argue successfully that (s)he did not waive his or her right to a trial by jury in the contract with the corporation. Pre-*Green Tree*, arbitration clauses, in particular, those that could be invoked unilaterally by the defendant corporation, were viewed as a “blessing” by defense counsel and a “curse” by plaintiff counsel.

Post-*Green Tree*, however, the perspectives on arbitration clauses by defense and plaintiff counsel changed. The United States Supreme Court decided in the plurality of *Green Tree* that if an agreement to arbitrate is silent on the issue of the permissibility of class action arbitrations, the arbitrator and not the court should decide whether a class action can proceed in arbitration. Therefore, in response to defense counsel’s motion to dismiss and demand for arbitration, plaintiff’s counsel would simply demand a class-wide arbitration and make their case for class treatment before an arbitrator.

Adding insult to injury for the defense bar, one month after the Supreme Court’s decision, the American Arbitration Association (AAA) on July 11, 2003, stated that it would administer demands for class arbitration if (1) the underlying agreement specifies that disputes arising out of the parties’ agreement shall be resolved by arbitration in accordance with any of the American Arbitration Association’s rules and (2) the agreement is silent with respect to class claims, consolidation, or joinder of claims. The AAA further
stated that disputes over the availability of class relief and the arbitrator’s jurisdiction would be forwarded to the appointed arbitrator for determination.

All is not lost for the defense bar. Significantly, there are no clear winners and losers between plaintiffs and defendants on the issue of arbitration clauses and class actions. *Green Tree* raises more questions than it provides answers to practitioners. For example, the decision did not address:

- how an arbitration clause that is deemed to be “silent” on the issue of class actions should be interpreted by the arbitrator under the Federal Arbitration Act;
- the enforceability of provisions within arbitration agreements that either prohibit class or consolidated arbitration proceedings or expressly state that a court is to hear such claims rather than an arbitrator;
- the impact on defendant’s and absentee class member’s constitutional rights of class arbitrations.

This advisory (1) summarizes briefly the Supreme Court’s decision in *Green Tree*; (2) addresses how defense counsel can help their clients avoid class arbitrations; and (3) instructs defense counsel on how to prepare for class arbitrations if faced with one.

**BRIEF SUMMARY OF GREEN TREE V. BAZZLE**

The *Green Tree* case involved two related state court class actions by consumers alleging that Green Tree violated South Carolina’s consumer protection statute in financing the sale of manufactured homes. In *Bazzle v. Green Tree Financial Corp.*, No. 97-CP-18-258 (S.C. Ct. Com. Pl. 1997), the South Carolina trial court granted Green Tree’s motion to compel arbitration, but only after the court had granted the plaintiff’s motion for class certification. The trial court concluded that the arbitration provision in the contract between plaintiffs and Green Tree was sufficiently broad to infer that both parties intended to include class arbitration. Consequently, an arbitration was conducted on a class-wide basis. The arbitrator found Green Tree liable and entered a class-wide award of $14,598,252 in favor of 1900 class members. That award was confirmed by the trial court.

In a separate case, *Lackey v. Green Tree Financial Corp.*, No. 96-CP-06-073, (S.C. Ct. Com. Pl. 1996), Green Tree obtained a ruling from the South Carolina Court of Appeals that the dispute was subject to the arbitration clause in the finance contract, and the matter proceeded to arbitration. However, over Green Tree’s objection, the arbitrator determined that a class action could proceed in arbitration and he could certify a class. The arbitrator subsequently certified a class, found Green Tree liable, and awarded $12,284,919 in favor of 1840 class members. The award was confirmed by the trial court.
Green Tree appealed both decisions. Both cases were consolidated in the South Carolina Supreme Court, where the awards were affirmed. The South Carolina Supreme Court held that, even though the contract was silent on the issue of class action arbitration, the arbitrations were consistent with South Carolina law. Three reasons were given by the South Carolina Supreme Court in upholding the decisions of the trial courts: (i) the contract was ambiguous, and therefore should be construed against Green Tree, the drafter; (ii) South Carolina law favors arbitration and does not expressly prohibit class–wide arbitration; and (iii) Green Tree’s contracts with consumers were contracts of adhesion and should not be utilized to preclude class action arbitrations.

The United States Supreme Court granted certiorari to consider whether the South Carolina Supreme Court’s holding was consistent with the Federal Arbitration Act. In the Supreme Court, Green Tree argued that its contracts with its consumers were not silent, but rather forbid class arbitration. The arbitration provision in Green Tree’s contracts states as follows:

ARBITRATION—All disputes, claims, or controversies arising from or relating to this contract or the relationships which result from this contract … shall be resolved by binding arbitration by one arbitrator selected by us with consent of you. This arbitration contract is made pursuant to a transaction in interstate commerce, and shall be governed by the Federal Arbitration Act at 9 U.S.C. section 1… THE PARTIES VOLUNTARILY AND KNOWINGLY WAIVE ANY RIGHT THEY HAVE TO A JURY TRIAL, EITHER PURSUANT TO ARBITRATION UNDER THIS CLAUSE OR PURSUANT TO COURT ACTION BY U.S. [sic] (AS PROVIDED HEREIN)…. The parties agree and understand that the arbitrator shall have all powers provided by the law and the contract. These powers shall include all legal and equitable remedies, including, but not limited to, money damages, declaratory relief, and injunctive relief.

Green Tree, 539 U.S. at 448. Writing for the plurality, Justice Breyer’s opinion focuses on the following language: “[a]ll disputes, claims, or controversies arising from or relating to this contract or the relationships which result from this contract” are to be submitted to the arbitrator. The Court concluded that whether the arbitration contract forbids the use of class arbitration procedures is a dispute “relating to this contract” and the resulting “relationships.” Green Tree, 539 U.S. at 448. Following this rationale, the Court held that, pursuant to the express terms of the contract, the parties agreed that an arbitrator, not a judge, would answer the question of whether class arbitration is prohibited or not. In support of this analysis, the plurality relies upon First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 943, 115 S. Ct. 1920 (1995) (“Arbitration is simply a matter of contract….”) and Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626, 105 S. Ct. 3346 (1985) (stating that if there is any doubt about the “scope of arbitrable issues,” we should resolve that doubt “in favor of arbitration.”)
While the Supreme Court acknowledged in its opinion that parties frequently intend courts, and not arbitrators, to decide particular arbitration-related matters, the Court described such situations as involving “certain gateway matters, such as whether the parties have a valid arbitration agreement at all or whether a concededly binding arbitration clause applies to a certain type of controversy.” *Green Tree*, 539 U.S. at 452. The Supreme Court held as follows:

The question here – whether the contracts forbid arbitration – does not fall into this narrow exception. It concerns neither the validity of the arbitration clause nor its applicability to the underlying dispute between the parties. . . . Rather the relevant question here is what kind of arbitration proceeding the parties agreed to. That question does not concern a state statute or judicial procedures. . . . It concerns contract interpretation and arbitration procedures. Arbitrators are well situated to answer that question. Given these considerations, along with the arbitration contracts’ sweeping language concerning the scope of the questions committed to arbitration, this matter of contract interpretation should be for the arbitrator, not the courts, to decide.

*Green Tree*, 539 U.S. at 452-53 (citations omitted).

The plurality, therefore, vacated the decision of the South Carolina Supreme Court and remanded the case to arbitration. Their rationale for vacating and remanding was their belief that the arbitrator’s prior decisions reflected a court’s interpretation of the contracts rather than an arbitrator’s interpretation. For practitioners, the oft-quoted holding of *Green Tree* is as follows: Whether a class action can be brought in arbitration is to be decided by an arbitrator rather than a court.

**HOW DEFENSE LAWYERS CAN AVOID CLASS ARBITRATIONS**

The *Green Tree* opinion does not directly address the question of whether an express class action waiver in an arbitration clause is enforceable under the Federal Arbitration Act even if it is determined to be unconscionable or invalid as a matter of state law. A comprehensive survey of the law on this issue can be found in the article, by Alan S. Kaplinsky and Mark J. Levin, *Arbitration Update: Green Tree Financial Corp. v. Bazzle—Dazzle for Green Tree, Fizzle for Practitioners*, 59 Bus. Law 1265 (2004). In their survey, Kaplinksy and Levin found that the majority of federal courts have “enforced such express no-class action clauses,¹ except for those in the Ninth Judicial

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¹ See, e.g., *Livingston v. Assocs. Fin., Inc.*, 339 F.3d 553, 559 (7th Cir. 2003) (“The Arbitration Agreement at issue here explicitly precludes the Livingsons from bringing class claims or pursuing ‘class action arbitration’, so we are therefore ‘obliged to enforce the type of arbitration to which these parties agreed, which does not include arbitration on a class basis.’”) (quoting *Champ v Siegel Trading Co.*, 55 F.3d 269, 277 (7th Cir. 1995)); *Thompson v. Ill. Title Loans, Inc.*, No. 99 C 3952, 2000 WL 45493, at *4 (N.D. Ill. Jan. 11, 2000) (“The class action is a procedural device that . . . claimants may waive by agreeing to arbitrate their claims.”); *Zawikowski v. Beneficial Nat’l Bank*, No. 98 C 2178, 1999 WL 35304, at *2 (N.D. Ill. Jan. 11, 1999) (rejecting the argument
that inclusion in a consumer loan agreement of a clause prohibiting class actions was void as a matter of public policy by holding that "[n]othing prevents the Plaintiffs from contracting away their right to a class action.";  *Lloyd v. MBNA Am. Bank, N. A.*, No. 01-1752, 2002 U.S. App. LEXIS 1027, at *4-*5 (3d Cir. Jan. 7, 2002) (stating that because right to a class action is "merely procedural, and 'may be waived,' an arbitration agreement barring classwide relief for claims brought under the TILA is not unconscionable.");  *Snowden v. CheckPoint Check Cashing*, 290 F.3d 631, 638-39 (4th Cir. 2002) (finding no-class action provision to be not unconscionable);  *Pick v. Discover Fin. Servs., Inc.*, No. CIVA.00-935-SLR, 2001 WL 1180278, at *5 (D. Del. Sept. 28, 2001) ("[I]t is generally accepted that arbitration clauses are not unconscionable because they preclude class actions.");  *Sagai v. First USA Bank, N. A.*, 69 F. Supp. 2d 627, 632 (D. Del. 1999) (compelling arbitration of plaintiffs TILA claims even though he was precluded from representing a class), aff’d, 254 F.3d 1078 (3d Cir. 2001);  *Lomax v. Woodmen of the World Life Ins. Soc’y*, 228 F. Supp. 2d 1360, 1365 (N.D. Ga. 2002) ("Generally, prohibiting class-wide arbitration does not render an otherwise valid arbitration clause unconscionable.");  *Vigil v. Sears Nat’l Bank*, 205 F. Supp. 2d 566, 573 (E.D. La. 2002) (rejecting argument that arbitration clause was unconscionable because it prohibited class actions);  *Lewis Tree Serv., Inc. v. Lucent Techs., Inc.*, 239 F. Supp. 2d 332, 338 (S.D.N.Y. 2002) ("Federal courts have . . . consistently enforced arbitration provisions in the context of class action lawsuits when federal statutory claims have been at issue.");  *Mattix v. Decision One Mortgage Co.*, No. CIVA. 01-10657-GAO, 2002 WL 31121087 (D. Mass. Sept. 26, 2002) (finding an arbitration clause enforceable even in absence of class action);  *McIntyre v. Household Bank*, 216 F. Supp. 2d 719, 724 (ND. Ill. 2002) (stating that the right to class action may be “waived in order to enforce arbitration.”);  *Shales v. Discover Card Servs., Inc.*, Nos. CIVA.02-80, 2002 WL 2022596, at *2 (E.D. La. Aug. 30, 2002) ("Shales raised the issue of the validity of the class action restriction contained in the agreement. . . Such restrictions are routinely enforced in this jurisdiction");  *Christopher A. Taravella, et al., An Annotated Arbitration Clause*, 56 Consumer Fin. L.Q. Rep. 263, 265-67 (2002).  *Id.* at n.43.


3  *Leonard v. Terminix Int’l Co.*, 854 So. 2d 529 (Ala. 2002) (per curiam). Practically all of the cases in which courts have invalidated class action waivers involved arbitration clauses that contained other alleged unfair features, such as excessive arbitration costs, a lack of mutuality or a limitation on remedies.  *Id.* at n.45.


5  *Lytle v. CitiFinancial Servs., Inc.*, 810 A.2d 643 (Pa. Super. Ct. 2002) (vacating order dismissing complaint and remanding to the trial court to conduct a hearing upon the issue of unconscionability after finding compelling evidence of a one-sided arbitration clause).  *Id.* at n.47.

6  *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862 (Cal. Ct. App. 2002). In  *Discover Bank v. Superior Court of Los Angeles County*, however, a different panel of the California Court of Appeals enforced a no-class action clause in an arbitration agreement and held that  *Szetela* was “wrongly decided.” 129 Cal. Rptr. 2d 393, 406 (Ct. App. 2003). Subsequently, the California Supreme Court granted review. 132 Cal. Rptr. 2d 526 (2003).  *Id.* at n.48.

In order to avoid class arbitrations, defense counsel should counsel their clients to draft arbitration agreements in such a manner as to avoid being struck as a contract of adhesion or unconscionable under state law. Defense counsel should expect arguments from plaintiffs that arbitration clauses which prohibit class, mass, or consolidated actions are unenforceable. For example, in Szetela v. Discover Bank, 118 Cal. Rptr. 2d 862 (Cal. Ct. App. 2002), the court held as follows:

“If the right to a class-wide proceeding could be automatically eliminated in relationships governed by adhesion contracts through the inclusion of a provision for arbitration, the potential for undercutting [the principles that favor class actions], and for chilling the effective protection of interests common to a group, would be substantial,” and denial of a class action in cases where it is appropriate “may have the effect of allowing an unscrupulous wrongdoer” to retain the benefits of its wrongful conduct.

Garcia v. DIRECTTV, Inc., 9 Cal. Rptr. 3d 190, 196 n.4 (2004) (quoting Szetela). These are the types of arguments one would expect from plaintiff counsel.

The basic rules of drafting apply to arbitration clauses which include class action, mass action, and/or consolidation waivers. Companies should make certain that the language in the arbitration clause is prominent, clear, conspicuous, and understandable. The provision should indicate whether the Federal Arbitration Act or state arbitration statutes will govern the arbitration. The arbitration clause should contain language that limits the arbitrator’s scope of authority to resolving individual disputes involving just one consumer (or employee) and the company, and that expressly prohibits the arbitrator from determining as an initial matter whether class, mass or consolidated relief is permitted in arbitration. In addition to language limiting the arbitrator’s authority, companies increase their chances of fending off challenges based upon unconscionability by bearing the cost of the arbitration of individual disputes and offering to conduct the arbitration within 30 miles of the residence of the consumer. Finally, in those instances where the arbitration clause expressly prohibits class, mass or consolidated arbitrations, companies may consider giving the consumer the choice of rejecting the arbitration provision in their contract with the company when they choose to purchase the product or elect to work for a company. By giving consumers a choice of whether or not to be bound by the arbitration clause, defendant corporations gain a distinct advantage in refuting arguments by plaintiff’s counsel that the clause is part of an adhesion contract, and is therefore unenforceable. In short, defendant corporations must take consider-

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9 AutoNation USA Corp. v. Leroy, 105 S. W.3d 190 (Tex. App. 2003). Id. at n.51.


able time and effort to draft arbitration clauses that address some of the unanswered questions from Green Tree.

**HOW TO PREPARE FOR AND FEND OFF A CLASS ARBITRATION**

As an initial matter, it should be noted that, in some instances, a company may in fact wish to resolve a dispute through class arbitration. If a company wishes to resolve multiple claims together, a class arbitration is a faster and sometimes less expensive alternative to traditional judicial proceedings in state or federal court. If this is the case, then the American Arbitration Association provides rules that may assist in conducting a class wide arbitration.  

However, whether due process rights can be adequately protected through class-wide arbitration is an open issue, and one which defense counsel can exploit if forced to arbitrate consumer claims on a class-wide basis. Interestingly, these due process concerns are not limited to protections for corporate defendants, as many due process issues involve members of the class. For example, absentee class members have no say in the selection of the arbitrator, yet in their contracts with corporate defendants, they are each entitled to select their own arbitrator. There are questions regarding the sufficiency of notice, such that absentee class members can affirmatively consent to proceed in class arbitration. In the judicial system, the judge, in addition to class counsel, has a duty to protect the interests of the absent class members. It is questionable whether or not arbitrators are equally capable of protecting adequately the interests of absentee class members. And, from the defendant’s perspective, it is questionable whether or not the judicial review afforded class determinations by arbitrators is commensurate with the judicial review afforded class determinations in court.

Given the potential class-wide arbitration has for violating parties’ due process rights, the American Arbitration Association has attempted to incorporate certain safeguards into its rules. One such rule permits any party to move to confirm or vacate the “clause construction award” in court. The “clause construction award” is the arbitrator’s threshold determination of whether an arbitration can proceed on behalf of or against a class. After the “clause construction award” is issued, the arbitrator must stay the proceedings for at least 30 days to permit any party to seek judicial review. Federal Rule of Civil Procedure 23 requirements are incorporated into the AAA rules, and specific rules regarding notice and settlement have been incorporated as well. But given the standard of review applied to arbitrators’ decisions, the sufficiency of those safeguards is questionable. The issue of whether or not the AAA’s class arbitration rules satisfy

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due process requirements has yet to be examined meaningfully by trial and appellate courts. As such, we practitioners are in many respects on the verge of the unknown.

**CONCLUSION**

Arbitration clauses appear to be both a blessing and a curse in the context of class action litigation. Without guidance from the United States Supreme Court, there will continue to be conflicting opinions and rulings both at the state and federal level. In addition, with the advent of the AAA rules for class-wide arbitration, the landscape will become all the more complex, as “decisions/opinions” of arbitrators may be cited by parties in judicial proceedings, not as binding, but as instructive. It is more important than ever for companies to examine carefully their contracts with consumers and employees and to be prepared to proceed if a class action is referred to arbitration.

— by Cari Katrice Dawson

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