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Catching the Waive: The Third Circuit Joins the Growing Trend of Circuit Courts in Voiding a Class-Arbitration Waiver in Homa v. American Express Co.

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CATCHING THE WAIVE: THE THIRD CIRCUIT JOINS THE GROWING TREND OF CIRCUIT COURTS IN VOIDING A CLASS-ARBITRATION WAIVER IN *HOMA v. AMERICAN EXPRESS CO.*

I. INTRODUCTION

The tiny print of a mandatory arbitration clause, often buried deep in a multi-page standard form contract, likely evades the average consumer.[1] While the inclusion of these provisions in the most common of consumer agreements is becoming more and more prevalent, few recognize the significant waiver of rights that accompanies acquiescence to such agreements.[2] Suddenly, without more than a pen stroke, the consumer agrees to settle all disputes arising out of the agreement with the corporation through binding arbitration and relinquishes all rights to traditional in-court litigation.[3] Now, with the proliferation of these mandatory arbitra-

1. *See* Press Release, Nat'l Consumer Law Ctr., Consumer and Media Alert: The Small Print That's Devastating Major Consumer Rights (July 28, 2003), *available at* http://www.consumerlaw.org/issues/model/arbitration.shtml (announcing that mandatory arbitration clauses found in everyday consumer agreements are "a giant trap door for consumers"). Blindly agreeing to contract provisions is a behavior routinely exhibited by the average consumer. *See* W. David Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529, 529 (1971) (recognizing that "an active consumer enters scores of contracts every week without in any real sense agreeing to the terms that are imposed upon him"). David Slawson laments what was once the common consumer culture where "both parties participate[d] in choosing the language of their entire agreement." *See* Slawson, *supra*, at 529 (acknowledging that standard form contracts "have come to dominate" consumer transactions); *see also* Emma Wilson, Douglas v. Talk America*: Making the Case for Proper Notice*, 45 IDAHO L. REV. 479, 479-80 (2009) (commenting on how proliferation of standard form contracts has "tremendously influenced consumer transactions").

2. *See* Press Release, Nat'l Consumer Law Ctr., *supra* note 1 (reporting that mandatory arbitration clauses are "popping up not only in [credit card agreements and health plans,] but also in mortgages and other loans, phone bills, home construction and repair contracts, stock brokerage agreements, pest-control contracts, bank depositors' agreements, college loans, mobile home purchases, employment agreements and many more" types of consumer contracts); *see also* Linda J. Demaine & Deborah R. Hensler, *"Volunteering" to Arbitrate Through Predispute Arbitration Clauses: The Average Consumer's Experience*, 67 L. & CONTEMP. PROBS. 55, 56, 62 n.30 (2004) (indicating that in recent years "the profile of arbitration has changed dramatically" to point where "55.1% of businesses that offer an ongoing product or service and use a written contract [include] an arbitration clause").

3. *See* Press Release, Nat'l Consumer Law Ctr., *supra* note 1 (illustrating rights waived by agreeing to mandatory arbitration); *see also* Bryon Allyn Rice, *Enforceable or Not?: Class Action Waivers in Mandatory Arbitration Clauses and the Need for a Judicial Standard*, 45 HOUS. L. REV. 215, 217 (2008) ("These contract clauses restrict consumers' rights to pursue any complaints against defendant companies via the court system by compelling plaintiffs to seek vindication through an arbitration process."). Below is an example of a typical mandatory arbitration provision:

tion clauses, the trend in consumer contracts is to include a ban on class mechanisms in the arbitral forum—meet the class-arbitration waiver.[4]

A class-arbitration waiver relinquishes "the right to participate in class-wide arbitration or to aggregate claims with others in any form of . . . arbitral proceeding."[5] As one might imagine, judicial recognition of the

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> You and we agree that any claim, dispute, or controversy between us . . . and any claim arising from or relating to this Note, no matter by whom or against whom . . . including the validity of this Note and of this agreement to arbitrate disputes as well as claims alleging fraud or misrepresentation shall be resolved by binding arbitration . . . NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION.

Johnson v. W. Suburban Bank, 225 F.3d 366, 369-70 (3d Cir. 2000) (providing text of arbitration clause at issue).

4. *See* Falon M. Wrigley, Kristian v. Comcast*: Another Drop in the Bucket, or the Achilles Heel of Arbitration Agreements Banning Class Mechanisms?*, 27 ST. LOUIS U. PUB. L. REV. 163, 163 (2007) (documenting increasing popularity of class-arbitration waivers); *see also* Leah Snyder Batchis, *Third Circuit Chimes in on Controversy Surrounding Enforcement of Mandatory Arbitration Clauses and Class Action Waivers, Holding that Certain Class Action Waivers May Be Unconscionable Under New Jersey Law*, SCHNADER ALERT (Sept. 27, 2009), http://www.schnader.com/files/Publication/c6fafd90-d4a7-481b-80b2-3fa95b0ce0e5/Presentation/PublicationAttachment/f40e6af1-19a0-4cfe-9255-44b3a0bda752/APG%20and%20FSL-Third%20Circuit%20Chimes%20in%20on%20Controversy%2003.2009.pdf (noting "growing trend among financial services providers to include mandatory arbitration clauses and class action waivers in consumer credit card contracts"). Until recently, "most courts refused to allow individuals to seek class certification within an arbitration except where the arbitration agreement expressly authorized individuals to maintain class actions." *See* Jeffrey S. Klein & Nicholas J. Pappas, *Enforceability of Class Arbitration Waiver Clauses*, 239 N.Y. L.J. 23 (2008) (explaining that Supreme Court's decision in *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003), reversed trend); *see also* AM. ARBITRATION ASS'N, 2005 PRESIDENT'S LETTER & FINANCIAL STATEMENTS 3 (2005), *available at* http://www.adr.org/annual_reports (follow "2005 ANNUAL REPORT" hyperlink) ("Implicit in the [*Bazzle*] decision is that class action proceedings could take place in an arbitration setting.").

5. *See* Myriam Gilles, *Opting Out of Liability: The Forthcoming, Near-Total Demise of the Modern Class Action*, 104 MICH. L. REV. 373, 376 n.15 (2005) (explaining effect of class-arbitration waivers); *see also* Paul Karlsgodt, *The Latest on Class Arbitration Waivers*, CLASSACTIONBLAWG.COM (Aug. 28, 2008), http://classactionblawg.com/2008/08/28/the-latest-on-class-arbitration-waivers/ (defining class-arbitration waivers as "contract clauses requiring arbitration but prohibiting class treatment of claims in the arbitration"). Below is an example of a typical class-arbitration waiver:

> THERE SHALL BE NO RIGHT OR AUTHORITY FOR ANY CLAIMS TO BE ARBITRATED ON A CLASS ACTION OR CONSOLIDATED BASIS OR ON BASES INVOLVING CLAIMS BROUGHT IN A PURPORTED REPRESENTATIVE CAPACITY ON BEHALF OF THE GENERAL PUBLIC (SUCH AS A PRIVATE ATTORNEY GENERAL), OTHER SUBSCRIBERS, OR OTHER PERSONS SIMILARLY SITUATED.

Kristian v. Comcast Corp., 446 F.3d 25, 53 (1st Cir. 2006) (quoting terms provided in class-arbitration waiver at issue). For additional examples of class-arbitration waiver provisions, see Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 WM. & MARY L. REV. 1, 6 n.5 (2000).

validity of class-arbitration waivers has been controversial and varied.[6] Many courts that once "overwhelmingly embraced" mandatory arbitration clauses are now attempting to cope with the lack of a judicial standard for analyzing the enforceability of class-arbitration waivers.[7] Some commentators argue that bolstering standard form contracts with class-arbitration waivers is a "surreptitious" technique used by corporations as a means of avoiding liability altogether.[8] Conversely, corporate defendants, who often view the class action ban as the most valuable provision in an arbitration clause, contend that the class action remedy allows plaintiffs to extort inequitable settlements from innocent defendants.[9]

Federal circuit courts are currently split on the question of whether to enforce class action bans in the arbitral forum; however, what was once a staunch majority in favor of upholding class-arbitration waivers has developed into a distinct trend of courts refusing to enforce class-arbitration bans.[10] Specifically, while the overwhelming body of case law upholds the

6. For a discussion of the varying conclusions reached by courts regarding the validity of class-arbitration waivers, see *infra* notes 39-78 and accompanying text.

7. *See* Rice, *supra* note 3, at 218-19 (discussing how addition of class action waiver in otherwise enforceable mandatory arbitration clause has left question of whether ban on class actions in mandatory arbitration clauses is enforceable and commenting on lack of uniform judicial standard among federal and state courts confronted with issue of class-arbitration waivers).

8. *See* Sternlight, *supra* note 5, at 5 ("Today, such potential defendants . . . have found a surreptitious way to defeat the feared class action: mandatory binding arbitration."); *see also* Robert S. Safi, *Beyond Unconscionability: Preserving the Class Mechanism Under State Law in the Era of Consumer Arbitration*, 83 TEX. L. REV. 1715, 1716 (2005) (opining that arbitration is being exploited "as a means of completely avoiding liability").

9. *See* F. Paul Bland, Jr. & Claire Prestel, *Challenging Class Action Bans in Mandatory Arbitration Clauses*, 10 CARDOZO J. CONFLICT RESOL. 369, 370 (2009) (explaining how class action ban is often characterized as most valuable provision in arbitration clause from company's perspective); Sternlight, *supra* note 5, at 6 ("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."); *see also* Muhammad v. County Bank of Rehoboth Beach, Del., 912 A.2d 88, 101, 102 n.6 (N.J. 2006) (recognizing that courts and commentators have acknowledged pressure that potential class action places on corporate defendants to settle "arguably frivolous claims"). *But see* Sternlight, *supra* note 5, at 6-9 (examining possible ulterior motive potential defendants may have, which leads them to incorporate class action bans in arbitration clauses). "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." *Id.* at 9.

10. *See* Rice, *supra* note 3, at 226 (indicating that when article was published in 2008, "the Third, Fourth, Fifth, Sixth, Seventh, Eighth, and Eleventh Circuits [had] all upheld compulsory class arbitration waivers"). *But see* Karlsgodt, *supra* note 5 ("Although courts have upheld class arbitration waivers . . . under some circumstances, the trend seems to favor striking them down as unconscionable or void as against public policy, especially in consumer contracts where any individual dispute is likely to involve only small amounts of money."); Bland & Prestel, *supra* note 9, at 374 n.25 (noting "definite trend" of courts striking class-arbitration waivers as unconscionable (citing Pamela MacLean, *Class Action Waivers Hit a Wall*, 29

enforceability of such class-arbitration waiver provisions, a growing number of circuits have held that class-arbitration waivers are "unconscionable, void as against public policy, or otherwise unenforceable when they effectively exculpate corporate defendants from any meaningful liability for their alleged misconduct."[11] To date, the United States Court of Appeals for the Third Circuit has handed down rulings straddling both sides of the debate.[12]

The Third Circuit first encountered this issue in *Johnson v. West Suburban Bank*[13] and found that parties are free to contractually waive judicial remedies in favor of arbitration so long as legislative intent does not articulate otherwise.[14] As a result, the court enforced the arbitration clause in question even though it rendered the class action remedy unavailable.[15] Then, in *Gay v. CreditInform*,[16] the Third Circuit, along with enforcing the defendant's class-arbitration waiver, ostensibly held that the Federal Arbitration Act (FAA)[17] preempted consideration of state law contract defenses.[18] A mere two years later, however, as both a reaction to rampant misinterpretation of its *Gay* holding and a response to evolving case law,

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NAT'L L. J. 5 (2007))). For a discussion on the current status of the circuit split, see *infra* note 119 and accompanying text.

11. *See* Veronica D. Jackson, *The End of the Arbitration Clause?*, CONSUMER FIN. L. BLOG (Apr. 9, 2009), http://www.consumerfinancelawblog.com/2009/04/articles/class-action/the-end-of-the-arbitration-clause/ (acknowledging that majority of precedents uphold arbitration and class waiver provisions); *see also* Bland & Prestel, *supra* note 9, at 370 (discussing recent trend in case law).

12. *Compare* Gay v. CreditInform, 511 F.3d 369, 395 (3d Cir. 2007) (holding waiver of right to bring class action did not render arbitration clause unconscionable), *and* Johnson v. W. Suburban Bank, 225 F.3d 366, 369 (3d Cir. 2000) (enforcing class-arbitration waiver where plaintiff agreed to binding arbitration in loan agreement and there was no congressional intent to preclude enforcement of arbitration clauses in either Truth In Lending Act or Electronic Fund Transfer Act), *with* Homa v. Am. Express Co., 558 F.3d 225, 233 (3d Cir. 2009) (holding "if the claims at issue are of such a low value as effectively to preclude relief if decided individually, then . . . the class-arbitration waiver is unconscionable"). For further analysis of the Third Circuit's treatment of class-arbitration waivers, see *infra* notes 39-118 and accompanying text.

13. 225 F.3d 366 (3d Cir. 2000).

14. *See id.* at 369 (stating holding of case).

15. *See id.* (detailing court's holding). For further discussion of *Johnson*'s place in Third Circuit class-arbitration waiver jurisprudence, see *infra* notes 39-47 and accompanying text.

16. 511 F.3d 269 (3d Cir. 2007).

17. 9 U.S.C. §§ 1-16 (2006).

18. *See* Jessie Kokrda Kamens, *Third Circuit Limits Holding in* Gay, *Finds Class Arbitration Waiver Unconscionable*, 10 CLASS ACTION LITIG. REP. (BNA) 184 (2009) (explaining that initial understanding of *Gay*'s holding was that Federal Arbitration Act (FAA) "preempted consideration of state law contract defenses"). The application of the preemption holding in *Gay* was substantially limited by the Third Circuit in its subsequent decision in *Homa*. *See id.* (discussing *Homa*'s impact on *Gay*). For further discussion of *Homa*'s limiting effect on *Gay*, see *infra* notes 95-100 and accompanying text.

the court, in the precedential decision *Homa v. American Express Co.*,[19] reversed a district court order upholding the enforcement of a class-arbitration waiver.[20] Joining the growing trend among circuit courts, the Third Circuit concluded in *Homa* that class-arbitration waivers in credit card holder agreements are likely unenforceable.[21]

This Casebrief identifies the Third Circuit's current treatment of class-arbitration waivers and serves as a guide to practitioners bringing or defending claims that a particular contractual class-arbitration waiver is unenforceable.[22] Part II reviews the arguments for and against class-arbitration waivers in mandatory arbitration clauses and provides a chronology of the Third Circuit's treatment of class-arbitration waivers.[23] Part III details the factual background and holding in *Homa*, as well as explains the Third Circuit's rationale in determining that contractual class-arbitration waivers can be challenged as unconscionable under state law.[24] Part IV examines *Homa*'s effect on class-arbitration waiver jurisprudence within the Third Circuit and discusses the growing trend among circuit courts of refusing to uphold class-arbitration waivers.[25] It also highlights the drafting adjustments that companies should make to consumer contracts post-*Homa*.[26] Finally, Part V concludes that the Third Circuit's *Homa* decision provides an effective blueprint from which to develop a viable judicial standard for judging the validity of class-arbitration waivers.[27]

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19. 558 F.3d 225 (3d Cir. 2009).

20. *See* Kamens, *supra* note 18 (declaring *Homa* decision to be "incredibly important," as "Third Circuit clarified that the preemption ruling in the *Gay* decision is narrow and only applies to the idiosyncratic law in Pennsylvania"); *see also Third Circuit Rejects Enforcement of Class-Arbitration Waiver*, BLANK ROME CORP. LITIG. ALERT (Mar. 2009), http://www.blankrome.com/index.cfm?contentID=37&itemID=1896 ("Adding to a developing trend, the Third Circuit reversed [the district court order], and determined instead that if the claims at issue are of such low value that a consumer likely would not pursue an individual claim, enforcement of the waiver provision would be unconscionable under New Jersey law.").

21. *Homa*, 558 F.3d at 233 (stating Third Circuit's holding).

22. For a discussion of the enforceability of class-arbitration waivers within the Third Circuit, see *infra* notes 95-118 and accompanying text.

23. For a discussion of the historical development and treatment of class-arbitration waivers within the Third Circuit and, more generally, within federal jurisprudence, see *infra* notes 36-78 and accompanying text.

24. For a discussion of the facts and the Third Circuit's holding in *Homa*, see *infra* notes 79-118 and accompanying text.

25. For a complete discussion of *Homa*'s wide-reaching impact on class-arbitration waiver jurisprudence within the Third Circuit and beyond, see *infra* notes 123-41 and accompanying text.

26. For a discussion of the changes companies should make in their consumer contracts post-*Homa*, see *infra* notes 128-36 and accompanying text.

27. For a discussion of the possibility and the benefits of adopting a judicial standard for judging the validity of class-arbitration waivers, see *infra* notes 142-48 and accompanying text.

II. BACKGROUND

A. *The Class-Arbitration Waiver: "Efficient Business Practice or Unconscionable Abuse?"*[28]

The class-arbitration waiver is a relatively new phenomenon.[29] Prior to *Green Tree Financial Corp. v. Bazzle*,[30] most courts did not permit class-wide arbitration except where expressly authorized by an arbitration agreement.[31] Although the United States Supreme Court has yet to directly rule on the enforceability of class-arbitration waivers, it intimated in *Bazzle* that class actions can be pursued in the arbitral setting.[32] With *Baz-*

28. The heading of this section was inspired by the title of an article coauthored by Jean R. Sternlight and Elizabeth J. Jenson. *See* Jean R. Sternlight & Elizabeth J. Jenson, *Using Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse?*, 67 LAW & CONTEMP. PROB. 75 (2004) (analyzing both sides of debate over validity of class-arbitration waivers).

29. For a complete discussion of the proliferation of the class-arbitration waiver, see *supra* notes 4-9 and accompanying text.

30. 539 U.S. 444 (2003).

31. *See* Klein & Pappas, *supra* note 4 (recounting history of class actions in arbitral setting). For a comprehensive examination of *Bazzle*'s effect on class-arbitration waiver jurisprudence, see P. Christine Deruele & Robert Clayton Roesch, *Gaming the Rigged Class Arbitration Game: How We Got Here and Where We Go Now – Part I*, METRO. CORP. COUNSEL., Aug. 2007, at 9, *available at* http://www.metrocorpcounsel.com/current.php?artType=view&artMonth=August&artYear=2007&EntryNo=6992.

32. *See Bazzle*, 539 U.S. at 450-51 (recognizing possibility of arbitral class actions); *see also* Safi, *supra* note 8, at 1716 (noting that *Bazzle* "signals the Court's acceptance of class arbitration"); AM. ARBITRATION ASS'N, 2005 PRESIDENT'S LETTER & FINANCIAL STATEMENTS, *supra* note 4, at 3 ("Implicit in [*Bazzle*] is that class action proceedings could take place in an arbitration setting."). In *Bazzle*, the Court declined to expressly determine whether arbitration could proceed on a class-wide basis. *See* Wrigley, *supra* note 4, at 181 (discussing *Bazzle*'s holding); *cf.* Green Tree Fin. Corp.-Ala. v. Randolph, 531 U.S. 79, 92 (2000) (examining previous instance of Court expressly declining to decide class-arbitration waiver issue when confronted with it and instead choosing to decide case on other grounds). The Court, however, implicitly recognized the legitimacy of arbitral class actions when it noted that an arbitration clause's silence on the matter of class actions indicated the absence of the contracting parties' intent to waive the class mechanism. *See* Rice, *supra* note 3, at 249 (analyzing *Bazzle*'s holding); *see also* Klein & Pappas, *supra* note 4 ("In *Bazzle*, the Supreme Court recognized that even where an arbitration agreement makes no mention of class actions or the possibility that nonparties to the arbitration agreement might be permitted to assert claims for relief, an individual claim could be transformed into a class action."). *But see* Nina Yadava, *Can You Hear Me Now? The Courts Send a Stronger Signal Regarding Arbitration Class Action Waivers in Consumer Telecommunications Contracts*, 41 COLUM. J.L. & SOC. PROBS. 547, 570 (2008) (explaining that "Court did not deem class actions and arbitrations compatible, thereby allowing the theory of incompatibility to persist if the arbitrator supports it"). *Bazzle* further indicates that when an arbitration clause is silent on the matter of class arbitration, it is up to the arbitrator, not a court, to determine whether the matter should be able to proceed on a class-wide basis. *See Bazzle*, 539 U.S. at 452-53 (ruling that arbitrators, not courts, should interpret these contracts); *see also* Sternlight & Jenson, *supra* note 28, at 76 n.4 (stating that "the Court remanded to the arbitrator the question whether, given the terms of the particular arbitration clause, an arbitral class action was permitted").

zle marking the Court's unofficial acceptance of class-wide arbitration, many companies responded by including class action waivers in arbitration agreements.[33] Corporate defendants contend that this practice is necessary to protect against "the unexpected expense, risk, and lack of procedural safeguards, including full appellate rights, inherent in class arbitration."[34] On the other hand, plaintiffs argue that such clauses are inserted to completely immunize corporations from liability, and that the class action remedy is the most effective way to redress exploitation of consumers and, therefore, must be preserved.[35]

B. *The Federal Arbitration Act*

Originally enacted in 1925, the FAA was intended to "place arbitration agreements upon the same footing as other contracts."[36] Under the

33. *See* Klein & Pappas, *supra* note 4 ("Many [companies] have responded to *Bazzle* by crafting arbitration agreements that expressly prohibit class arbitration.").

34. *See id.* (illustrating corporate response to *Bazzle*); *cf.* Rice, *supra* note 3, at 224 ("Corporate defense attorneys tout the use of the class-action arbitration bans as a legitimate contract tool used to defend benevolent companies from the ever-increasing onslaught of frivolous 'multimillion-dollar class action lawsuits.'").

35. *See* Cari K. Dawson, *Arbitration Agreements: No Longer Defendants' Silver Bullet to Defeat Class Actions*, 22 ANDREWS CORP. OFFICERS AND DIR. LIAB. LITIG. REP. 13 (2007) (summarizing arguments of plaintiffs involved in disputes over class-arbitration waivers); *see generally* Sternlight & Jenson, *supra* note 28, at 85-92 (documenting arguments that influence courts to find particular class action prohibitions unconscionable). Other arguments submitted by plaintiffs in favor of the class action mechanism include, but are not limited to, the fact that class actions are: (1) necessary to support modest claims; (2) serve a deterrent purpose; and (3) facilitate the discovery of claims among absent class members. *See* Bland & Prestel, *supra* note 9, at 376-80 (listing arguments proffered by plaintiffs).

36. *See* Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 24 (1991) (discussing history and purpose of FAA). The FAA recognizes the validity and enforceability of arbitration agreements. *See* 9 U.S.C. § 2 (2006) (declaring "[v]alidity, irrevocability, and enforcement of agreements to arbitrate"). FAA Section 2 provides:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, *shall be valid, irrevocable, and enforceable,* save upon such grounds as exist at law or in equity for the revocation of any contract.

Id. (emphasis added). Although the FAA legitimized agreements to arbitrate as early as 1925, arbitration has not always been fully accepted as a valid course of dispute resolution. *Compare Gilmer*, 500 U.S. at 24 (stating purpose of FAA "was to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts"), *with* Wrigley, *supra* note 4, at 167 (discussing how courts and legislatures were still "skeptical of arbitration," even after codification of FAA, but have since accepted arbitration). Since the 1980s, however, arbitration agreements between companies and consumers have actually been "favored" by the U.S. Supreme Court. *See* Joshua S. Lipshutz, *The Court's Implicit Roadmap: Charting the Prudent Course at the Juncture of Mandatory Arbitration Agreements and Class Action Lawsuits*, 57 STAN. L.

FAA's primary substantive provision, Section 2, "an agreement in writing to submit to arbitration an existing controversy arising out of [a transaction involving commerce] shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[37] While agreements to arbitrate are now generally enforced, a fissure arises among the courts when a class action waiver is incorporated into a mandatory arbitration provision.[38]

C. *The Third Circuit's Treatment of Class-Arbitration Waivers*

Because the Supreme Court has not yet ruled on the enforceability of class-arbitration waivers in consumer contracts, "a kaleidoscope of conflicting decisions" has emerged among federal and state courts considering the issue—the Third Circuit is no exception.[39] The Third Circuit's first major decision on class-arbitration waivers had a considerable impact on several other circuit courts.[40] In *Johnson*, the Third Circuit considered whether claims under the Truth in Lending Act (TILA) could be heard in the arbitral setting when the plaintiff sought to bring a class action against the defendant lenders.[41] The plaintiff argued that the mandatory arbitration clause, which compelled arbitration to the exclusion of any potential class action, clashed with the legislative intent of TILA.[42] The Third Circuit disagreed, however, noting that nothing in the statutory language or legislative history of TILA indicates that "parties cannot [voluntarily] waive judicial remedies in favor of arbitration," even if the opportunity to bring a class action is lost.[43] Absent such contrary legislative intent, the court

REV. 1677, 1678 n.1 (2005) (recognizing that Court first documented its policy of "favoring" arbitration in *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1 (1983)).

37. 9 U.S.C. § 2. For the full text of FAA Section 2, see *supra* note 36.

38. *See* Lipshutz, *supra* note 36, at 1680-81 ("It is generally settled law that mandatory pre-dispute arbitration agreements will be enforced by courts despite being contained in contracts of adhesion, subject only to being voided on traditional contract grounds."); *see also* Michael C. Duffy, *Making Waives: Reining in Class Action Waivers in Consumer Contracts of Adhesion*, 80 TEMP. L. REV. 847, 858 (2007) (discussing inconsistent stance on class action waiver issue among state courts); Rice, *supra* note 3, at 226 (acknowledging circuit split on issue of whether to uphold class-arbitration waivers).

39. *See* Dawson, *supra* note 35 (discussing circuit split).

40. *See* Johnson v. W. Suburban Bank, 225 F.3d 366, 369 (3d Cir. 2000) (ruling for first time on class-arbitration waiver issue); Duffy, *supra* note 38, at 851-53 (documenting widespread reliance on *Johnson*, including in the Fourth, Seventh, and Eleventh Circuits).

41. *See Johnson*, 225 F.3d at 368 (reciting issue facing court). The question before the court was an issue of first impression in the Third Circuit. *See id.* (discussing historical treatment of class-arbitrations waivers).

42. *See id.* at 368-69 (describing facts of case). The arbitration clause was included in an adhesion contract adopted by the plaintiff in connection with a loan. *See id.* at 368 (describing facts of case).

43. *See id.* at 369 ("[B]ecause we can discern no congressional intent to preclude the enforcement of arbitration clauses in either statute's text, legislative history, or purpose, we hold that such clauses are effective even though they may

concluded that the arbitral class action bar was enforceable based on three assertions: (1) class actions do not automatically provide plaintiffs with healthier incentives to bring individual suits;[44] (2) plaintiffs can still acquire representation without the class action mechanism because attorney's fees are recoverable under TILA;[45] and (3) TILA's administrative enforcement provisions can still deter violators of TILA even if plaintiffs are discouraged from bringing private suits.[46] After *Johnson*, a number of other circuit courts heard similar cases and reached the same result as the Third Circuit.[47]

Most of these circuit cases upholding class-arbitration waivers shared two primary commonalities that, when absent in subsequent cases, seemed to shift the trend of enforcement.[48] In *Kristian v. Comcast Corp.*,[49] the First Circuit noted that, unlike prior decisions by the Third, Fourth, Seventh,

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render class actions to pursue statutory claims under the TILA . . . unavailable."). The court also noted the Supreme Court's position that the FAA created a powerful presumption in favor of arbitration. *See id.* at 369 (relying on Supreme Court precedent). The court held that, under TILA, the right to a class action was "merely a procedural one, arising under FED. R. CIV. P. 23, which may be waived by agreeing to an arbitration clause." *See id.* (stating court's holding). The court further acknowledged that, even though fewer plaintiffs would seek to enforce TILA against offending creditors due to the unavailability of the class remedy, the waiver of class remedies was permissible absent an express congressional pronouncement. *See id.* at 374.

44. *See id.* ("[S]ums available . . . to individual plaintiffs are not automatically increased by use of the class forum . . . . [I]ndividual plaintiff recoveries available in a class action may be lower than those possible in individual suits because the recovery available under TILA's statutory cap on class recoveries is spread over the entire class.").

45. *See id.* at 374-75 ("Nor will arbitration necessarily choke off the supply of lawyers willing to pursue claims on behalf of debtors. Attorneys' fees are recoverable under the TILA . . . and would therefore appear to be recoverable in arbitration, as arbitrators possess the power to fashion the same relief as courts.").

46. *See id.* at 375 ("[TILA's administrative enforcement] provisions offer meaningful deterrents to violators of the TILA if private enforcement actions should fail to fulfill that role.").

47. *See* Duffy, *supra* note 38, at 852 (noting that, as of 2007, Fourth, Seventh, and Eleventh Circuits followed suit); *see, e.g.*, Livingston v. Assocs. Fin., Inc., 339 F.3d 553, 559 (7th Cir. 2003) ("Having found the Arbitration Agreement enforceable we must give full force to its terms . . . . The Arbitration Agreement at issue here explicitly precludes . . . class claims or pursuing 'class action arbitration.'"); Snowden v. Checkpoint Check Cashing, 290 F.3d 631, 638 (4th Cir. 2002) ("We also reject [the plaintiff's] argument that the Arbitration Agreement is unenforceable as unconscionable because without the class action vehicle, she will be unable to maintain her legal representation given the small amount of her individual damages."); Randolph v. Green Tree Fin. Corp., 244 F.3d 814, 819 (11th Cir. 2001) ("We hold that a contractual provision to arbitrate TILA claims is enforceable even if it precludes a plaintiff from utilizing class action procedures in vindicating statutory rights under TILA.").

48. *See* Kristian v. Comcast Corp., 446 F.3d 25, 56 (1st Cir. 2006) (noting that *Johnson*, *Livingston*, *Snowden*, and *Randolph* had two important commonalities that were absent in case at bar). For a discussion of the two commonalities, see *infra* note 50 and accompanying text.

49. 446 F.3d 25 (1st Cir. 2006).

and Eleventh Circuits that upheld class-arbitration waivers, here: (1) attorney's fees and costs were not recoverable by plaintiffs; and (2) the claim did not arise under TILA.[50] Instead, the claim in *Kristian* was brought under state and federal antitrust laws after Comcast Corporation allegedly inflated the costs of their cable services through "anticompetitive practices."[51] Comcast sought to compel the plaintiff to arbitrate the claim on an individual basis under a class-arbitration waiver provision, but the First Circuit disagreed.[52]

In distinguishing *Kristian* from *Johnson*, the First Circuit highlighted the inherently complex nature of an antitrust case as compared to a TILA violation.[53] Namely, while a TILA violation typically arises out of one particular transaction, an antitrust violation "is usually a complicated question of fact" requiring the services of numerous expert witnesses.[54] Consequently, expert witness fees and attorney's fees could cost several million dollars, with individual recovery ranging from "a few hundred dollars to a few thousand dollars at most."[55] In the First Circuit's view, such exorbitant costs and complex legal issues undermined the *Johnson* court's rationales for supporting the class-arbitration ban.[56] In essence, the First Circuit determined that the *Johnson* court's three assertions were contradicted by the "completely unrealistic and impractical" notion of spending millions of dollars to prosecute a case where recovery for an individual claim was so small.[57]

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50. *See id.* at 56 (identifying that *Johnson, Livingston, Snowden,* and *Randolph* had commonalities absent in *Kristian*: "First, attorney's fees and costs were either recoverable by the plaintiffs who contested the arbitral forum on the basis of the class arbitration ban, or the fees and costs issue was moot . . . [and second] the plaintiffs raised claims against banks or other financial lenders primarily under the TILA.").

51. *See id.* at 30 (stating case's factual and procedural history).

52. *See id.* at 31 (stating factual and procedural history of case). It should be noted that, even though the arbitration agreement was added to Comcast's policies after the plaintiffs began receiving service from Comcast, the court found that the arbitration policies applied retroactively. *See id.* at 64 (holding in favor of Comcast on issue of whether policies applied retroactively, but stating it still needed to determine whether class-arbitration waiver was enforceable).

53. *See id.* at 58 (discussing difference between current case brought under antitrust law and prior courts of appeals cases brought under TILA). The complexity described by the court involved both the "complexity of an antitrust case generally, and the complexity and cost required to prosecute a case against Comcast." *See id.* (discussing inherent complexity of antitrust cases).

54. *See id.* (discussing complex nature of antitrust cases).

55. *See id.* (noting that expert witness fees would cost between $300,000 and $600,000, attorneys fees would cost several million dollars, and individual recovery would amount to few thousand dollars at most).

56. *See id.* (stating court's analysis).

57. *See id.* at 58-59 (discussing why complexity and cost associated with prosecuting antitrust claim against Comcast undermines Third Circuit's rationale in *Johnson*). The First Circuit noted:

> *Johnson* first asserts that a class action does not necessarily provide greater incentives for private enforcement actions in the TILA context. Yet,

A few months later, the Supreme Court of New Jersey implemented a scheme comparable to that used by the *Kristian* court and issued two decisions with wide-ranging implications.[58] In companion cases decided the same day, the court voided a class-arbitration waiver in *Muhammad v. County Bank of Rehoboth Beach, Delaware*,[59] but, in *Delta Funding Corp. v. Harris*,[60] enforced a similar clause.[61] The primary difference between the two cases was the vast disparity in potential recovery if the claims were brought on an individual basis.[62]

In *Muhammad*, the court invalidated the class-arbitration waiver in a consumer loan contract because it effectively prevented the plaintiff from bringing her claim on an individual basis due to the low value of her claim (the court found that the maximum individual recovery was less than $600).[63] Due to the complexity and low value of the claim involved, the

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> Plaintiffs have provided uncontested and unopposed expert affidavits demonstrating that without some form of class mechanism—be it class action or class arbitration—a consumer antitrust plaintiff will not sue at all. . . . *Johnson*'s second assertion—that the availability of attorney's fees provides the necessary incentive for private enforcement actions—similarly finds little to no purchase in the antitrust context. A plaintiff's attorney in the consumer antitrust context would be required to invest a large initial outlay in time and money, including "opportunity costs"—estimated in the hundreds of thousands of dollars—for only a portion of an individual plaintiff's recovery, which at most is a few thousand dollars. Then, factoring in the uncertainty of success, the appeal for an attorney to take on an individual plaintiff's antitrust claim shrinks even further. . . . [T]he *Johnson* court's third assertion—that any decrease in private enforcement actions will be redressed by administrative enforcement—becomes even more suspect. When Congress enacts a statute that provides for both private and administrative enforcement actions, Congress envisions a role for both types of enforcement. Otherwise, Congress would not have provided for both. Weakening one of those enforcement mechanisms seems inconsistent with the Congressional scheme. Eliminating one of them entirely is surely incompatible with Congress's choice.

Id. (articulating court's rationale). The *Kristian* decision was not the first circuit court decision to invalidate a contractual class-arbitration waiver. *See* Yadava, *supra* note 32, at 549 n.12 (noting that Ninth Circuit was first circuit court to invalidate class-arbitration waiver in *Ting v. AT&T*, 319 F.3d 1126 (9th Cir. 2003)).

58. For a discussion of the two cases decided by the Supreme Court of New Jersey that share a similar rationale with *Kristian*, see *infra* notes 59-68 and accompanying text. It should be noted that while the *Kristian* court used a federal "vindication of statutory rights" theory to invalidate the class-arbitration waiver at issue, the Supreme Court of New Jersey considered the doctrine of unconscionability in its decision on whether to uphold similar clauses. *See* Duffy, *supra* note 38, at 868 (discussing contrasting mechanisms implemented by First Circuit and Supreme Court of New Jersey).

59. 912 A.2d 88 (N.J. 2006), *cert. denied*, 127 S. Ct. 2032 (2007).

60. 912 A.2d 104 (N.J. 2006).

61. For a discussion of the differences between the companion cases, see *infra* notes 62-68 and accompanying text.

62. *See* Duffy, *supra* note 38, at 858 n.95 (discussing difference between *Muhammad* and *Delta Funding*).

63. *See Muhammad*, 912 A.2d at 99 ("The difference lies in the fact that [the plaintiff's] individual consumer fraud case involves a small amount of damages,

court held that the contract precluded the plaintiff from pursuing her statutory rights—and the rights of any potential class of consumers—and, therefore, violated New Jersey's public policy.[64] Because the plaintiff's inability to vindicate her statutory rights superseded the defendant's entitlement to seek enforcement of the class-arbitration waiver, the court held that the clause was unconscionable.[65]

In *Delta Funding*, however, the court noted that the plaintiff's claim was "not the type of low-value suit that would not be litigated absent the availability of a class proceeding."[66] There, the plaintiff claimed over $100,000 in damages, and the court determined that such a figure was an "adequate incentive" to bring the claim as an individual action.[67] Thus, the court found the class-arbitration waiver enforceable.[68]

D. Gay v. CreditInform: *A Rogue Waive*

While *Muhammad*'s rationale gained national momentum in the year following the decision, the Third Circuit's decision in *Gay* showed that it

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rendering individual enforcement of her rights, and the rights of her fellow consumers, difficult if not impossible."); *id.* at 100 (detailing extent of damages that could be recovered if prosecuted on individual basis). The New Jersey Supreme Court, which was considering the validity of class-arbitration waivers for the first time, noted that "[o]ther courts have referred to such small damage cases as 'negative value' suits recognizing that they 'would be uneconomical to litigate individually.'" *Id.* at 97 (citing *In re* Monumental Life Ins. Co., 365 F.3d 408, 411 n.1 (5th Cir. 2004)) (commenting on effect small damage claim has on viability of individual suit).

64. *See id.* at 98-99 (finding that New Jersey contract law principles would not permit enforcement of class-arbitration waiver). To determine whether such an adhesion contract should be deemed unenforceable based on policy considerations, the court looked to: "(1) the subject matter of the contract, (2) the parties' relative bargaining positions, (3) the degree of economic compulsion motivating the 'adhering' party, and (4) the public interests affected by the contract." *See id.* at 97 (applying controlling test for determining unconscionability of adhesion contracts (quoting Rudbart v. N.J. Dist. Water Supply Comm'n, 605 A.2d 681, 687 (N.J. 1992), *cert. denied*, 506 U.S. 871 (1992))). The court concentrated its analysis on the fourth factor and found that, although not an exculpatory waiver, the small amount of damages involved rendered individual enforcement of the plaintiff's rights virtually impossible. *See id.* at 99 (declaring class-arbitration waiver at issue unconscionable).

65. *See id.* at 100-01 (stating court's holding).

66. *See* Delta Funding Corp. v. Harris, 912 A.2d 104, 115 (N.J. 2006) (distinguishing case from *Muhammad*).

67. *See id.* (stating court's holding).

68. *See id.* (stating court's holding). The court also used *Delta Funding* to clarify the *Muhammad* holding. *See* Dennis Casale, Stephen G. Harvey & Angelo A. Stio, III, *NJ Supreme Court Condemns Class Action Waiver in Consumer Loan Contract Dispute Involving Low Value Claim*, PEPPER HAMILTON ALERT (Aug. 10, 2006), http://www.pepperlaw.com/publications_update.aspx?ArticleKey=733 (discussing holding of *Delta Funding*). The court stated that under New Jersey law, class-arbitration waivers are not unconscionable per se. *See Delta Funding*, 912 A.2d at 115 (clarifying *Muhammad* holding).

was not yet on board with other jurisdictions.[69] In *Gay*, the plaintiff brought an action alleging that the defendant violated the Credit Repair Organizations Act (CROA)[70] and the Pennsylvania Credit Services Act (CSA);[71] the defendant filed a motion to compel arbitration.[72] The plaintiff, in response to this motion, argued that the CROA and the CSA created a right to litigate claims in a judicial forum and, further, that the CROA conferred to consumers the right to proceed in a class action.[73]

69. Gay v. CreditInform, 511 F.3d 369, 3395 (3d Cir. 2007) (stating court's holding).

70. 15 U.S.C. § 1679 (2006).

71. 73 PA. CON. STAT. ANN. § 2181 (2010).

72. *See Gay*, 511 F.3d at 375 (stating facts and procedural history of case). The defendant moved to compel arbitration on an individual basis pursuant to the parties' arbitration agreement: "Any claim arising out of or relating to the Product shall be settled by binding arbitration in accordance with the commercial arbitration rules of the American Arbitration Association on an individual basis not consolidated with any other claim." *Id.* (stating facts of case).

73. *See id.* at 377 (discussing plaintiff's arguments). The statute cited by the plaintiff, which allegedly granted consumers the right to litigate such claims in a judicial forum, states:

> Any buyer or borrower injured by a violation of this act or by the credit services organization's or loan broker's breach of a contract subject to this act may bring an action for recovery of damages. *Judgment* shall be entered for actual damages, but in no case less than the amount paid by the buyer or borrower to the credit services organization or loan broker, plus reasonable attorney fees and costs. An award, if the trial *court* deems it proper, may be entered for punitive damages.

Id. (emphasis added) (quoting 73 PA. CONS. STAT. ANN. § 2191). The plaintiff made note of the words "judgment" and "court" to support this contention. *See id.* (describing plaintiff's argument that statute granted consumers right to litigate claims in judicial forum). The CROA provision the plaintiff cited to support her contention that she could proceed in a class action provides:

> (a) Consumer waivers invalid
> Any waiver by any consumer of any protection provided by or any right of the consumer under this subchapter—
> (1) shall be treated as void; and
> (2) may not be enforced by any Federal or State *court* or any other person.
> (b) Attempt to obtain waiver
> Any attempt by any person to obtain a waiver from any consumer of any protection provided by or any right of the consumer under this subchapter shall be treated as a violation of this subchapter.
> (c) Contracts not in compliance
> Any contract for services which does not comply with the applicable provisions of this subchapter—
> (1) shall be treated as void; and
> (2) may not be enforced by any Federal or State *court* or any other person.

Id. at 377-78 (emphasis added) (quoting 15 U.S.C. § 1679f (2006)). The plaintiff further referred to the CSA's anti-waiver provision, which deemed any potential waiver of the provisions of the CSA to be contrary to public policy and thus unenforceable. *See id.* at 378 ("Any waiver by a buyer or borrower of the provisions of this act shall be deemed contrary to public policy and shall be void and unenforceable." (quoting 73 PA. CONS. STAT. ANN. § 2189(a))).

Citing the rationale from *Johnson*, the Third Circuit stated that "a party seeking to avoid arbitration for a statutory claim has the burden of establishing that Congress intended to preclude arbitration of the claims."[74] The court then compared the CROA and the CSA to the TILA at issue in *Johnson* and determined that no such congressional intent existed.[75]

Finally, the Third Circuit rejected the plaintiff's final contention that the class-arbitration waiver was unconscionable.[76] An unconvinced Third Circuit upheld the class-arbitration waiver and, notably, suggested in dicta that the FAA preempts state law decisions that invalidate class-arbitration waivers on unconscionability grounds.[77] *Gay* attracted a great deal of criticism in the years following the decision, but appeared—at least for a time—to be an unexpected victory for corporate defendants.[78]

III. THE *HOMA* DECISION: RIGHTING THE SHIP

A. *Factual and Procedural Background*

In September 2003, the American Express Company (AEC) initiated a promotional rewards program in which users of its "Blue Cash" credit card could earn up to five percent cash back on purchases.[79] On June 29, 2006, G.R. Homa, a Blue Cash cardholder for over two years, filed a complaint in the United States District Court for the District of New Jersey, purporting to represent a class of New Jersey Blue Cash cardholders.[80] Homa alleged that AEC and its wholly owned subsidiary American Express Centurion Bank (AECB) "misrepresented the actual terms of the rewards program and failed to award him the promised amount of cash back in violation of the New Jersey Consumer Fraud Act (NJCFA)."[81]

74. *Id.* at 379 (citing *Johnson* court's rationale).

75. *See id.* at 379-80 (finding that CROA and CSA do not confer right to bring judicial action and that CROA does not confer right to proceed as class).

76. *See id.* at 392 (stating that plaintiff's final claim is that "the arbitration provision is unconscionable because it requires cases to proceed 'on an individual basis not consolidated with any other claim'").

77. *See id.* at 395 (discussing FAA preemption in dicta).

78. *See* Bland & Prestel, *supra* note 9, at 389-90 (recognizing *Gay* as "surprise victory" for corporate defendants). *But see* Homa v. Am. Express Co., 558 F.3d 225, 229-30 (3d Cir. 2009) (limiting *Gay*'s holding). For a discussion of *Homa*'s limiting effect on *Gay*, see *infra* notes 137-41 and accompanying text.

79. *See Homa* 558 F.3d at 226 (describing facts of case). American Express Company (AEC), a New York corporation, is the ultimate parent of American Express Centurion Bank (AECB), "a Utah industrial bank engaged in the business of, among other things, issuing American Express credit cards." *See id.* (stating factual background).

80. *See id.* at 226-27 (describing facts of case). Homa, who was issued a Blue Cash card on February 8, 2004, brought the class action suit on behalf of "New Jersey consumers who obtained a Blue Cash card on or after September 30, 2003, as well as a subclass of New Jersey cardholders who carried a monthly balance on their cards." *See id.* (describing class of which Homa was lead plaintiff).

81. *See id.* at 227 (presenting facts of case).

AEC and AECB responded by citing two specific provisions from the cardholder agreement.[82] The provisions on which the companies relied contained the controlling terms and conditions of each cardholder's account.[83] The first provision, a class-arbitration waiver, required "arbitration of all claims upon election of either party and . . . specifically required all claims to 'be arbitrated on an individual basis . . . with no right or authority for any [c]laims to be arbitrated as a class action.'"[84] The second clause cited by AEC and AECB, a choice-of-law provision, indicated "that any disputes arising out of the Agreement would be governed by Utah state law."[85] The defendants argued that these two provisions would require Homa to arbitrate his claims on an individual basis because class-arbitration waivers in consumer credit card agreements are expressly valid and enforceable under Utah law.[86]

Conversely, Homa argued that New Jersey law should apply.[87] Homa contented that the implementation of Utah law would violate New Jersey's public policy against particular class-arbitration waivers and, therefore, that the choice of Utah law would be invalid under New Jersey choice-of-law principles.[88] The district court agreed with AEC and AECB and dis-

82. *See id.* (describing facts of case). The cardholder agreement was a document sent to Homa upon issuance of the Blue Cash card. *See id.*

83. *See id.* (detailing facts of case). AEC and AECB filed a motion to compel arbitration based upon the cardholder agreement between the parties. *See id.* at 226 (describing procedural posture of case). The cardholder agreement, which was mailed to Homa upon issuance of the Blue Cash card, was entitled "Agreement Between American Express Credit Cardmember and American Express Centurion Bank." *See id.* at 227 (describing facts of case).

84. *Id.* (stating terms of class-arbitration waiver); *see also* Homa v. Am. Express Co., 496 F. Supp. 2d 440, 443 (D.N.J. 2007) (documenting cardholder agreement's class-arbitration waiver in its entirety), *rev'd*, 558 F.3d 225 (3d Cir. 2009). This provision, in its entirety, states:

> If either party elects to resolve a Claim by arbitration, that Claim shall be arbitrated on an individual basis. There shall be no right or authority for any Claims to be arbitrated on a class action or on bases involving Claims brought in a purported representative capacity on behalf of the general public, other Cardmembers or other persons similarly situated.

Homa, 496 F. Supp. 2d at 443 (providing cardholder agreement's class-arbitration waiver). For an in-depth explanation of class-arbitration waivers, see *supra* notes 1-7 and accompanying text.

85. *Homa*, 558 F.3d at 227 (describing facts of case); *see also Homa*, 496 F. Supp. 2d at 443-44 (quoting cardholder agreement's choice-of-law provision). This provision, in its entirety, states:

> This Agreement and your Account, and all questions about their legality, enforceability and interpretation, are governed by the laws of the state of Utah (without regard to internal principles of conflicts of law), and by applicable federal law. We are located in Utah, hold your Account in Utah, and entered into this Agreement with you in Utah.

Homa, 496 F. Supp. 2d at 443-44 (quoting cardholder agreement's choice-of-law provision).

86. *See Homa*, 558 F.3d at 227 (stating defendants' argument in favor of motion to compel arbitration).

87. *See id.* (stating plaintiff's argument).

88. *See id.* (stating plaintiff's argument).

missed Homa's complaint with prejudice.[89] As such, the court ordered Homa to arbitrate his claim on an individual basis.[90] Homa refused and filed an appeal with the United States Court of Appeals for the Third Circuit.[91]

B. *The Third Circuit's Analysis*

In *Homa*, the Third Circuit engaged in a two-part analysis to ascertain whether the class-arbitration waiver was valid.[92] First, the court sought to determine whether the FAA precluded the application of state law unconscionability principles to void a class-arbitration waiver.[93] Second, the court set out to resolve whether the parties' choice of Utah law could be enforced under New Jersey's choice-of-law rules.[94]

1. *Third Circuit Declares the FAA Does Not Preclude Application of State Law Unconscionability Principles*

Before considering whether to enforce the choice-of-law provision in the cardholder agreement, the Third Circuit first had to decide if the FAA precluded it from applying state law contract defenses.[95] In answering this question, the court, following the Supreme Court's interpretation of FAA Section 2, stated that an agreement to submit to arbitration is enforceable unless the contract would be invalidated under generally applicable state law contract defenses, "such as fraud, duress, or unconscionability."[96] Despite the Supreme Court's instruction on this issue, AEC and AECB contended that the Third Circuit's recent decision in *Gay* precluded it from applying New Jersey unconscionability principles to a class-arbitration waiver.[97] The Third Circuit disagreed and asserted that *Gay* only compels

89. *See id.* at 226-27 (outlining procedural history of case and discussing how district court dismissed complaint after treating credit card companies' motion to compel as motion to dismiss under FED. R. CIV. P. 12(b)(6)).

90. *See id.* at 227 (outlining procedural history of case).

91. *See id.* at 226 (outlining procedural history of case).

92. *See id.* (summarizing issues presented).

93. *See id.* at 228-30 (discussing implications of FAA on application of state law unconscionability principles). For a discussion of the court's analysis of whether the FAA precludes application of state law unconscionability principles to void a class-arbitration waiver, see *infra* notes 95-100 and accompanying text.

94. *See Homa*, 558 F.3d at 227-28, 230-34 (discussing enforceability of choice-of-law provision contained in cardholder agreement). For a discussion of the court's analysis of the choice-of-law issue, see *infra* notes 101-20 and accompanying text.

95. *See Homa*, 558 F.3d at 226 (outlining analytical framework of decision).

96. *See id.* at 229-30 ("[S]tate law may be applied if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. Thus, generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening § 2 [of the FAA]." (quoting Doctor's Assocs. v. Casarotto, 517 U.S. 681, 686-87 (1996))).

97. *See id.* at 230 (stating "appellees argue that, even if the choice-of-law provision were invalidated and New Jersey law were applied, under *Gay* the FAA would

FAA preemption if "it is read as a blanket prohibition on unconscionability challenges to class-arbitration provisions."[98] The court noted, however, that such a reading directly conflicted with the Supreme Court's interpretation of FAA Section 2.[99] Thus, *Gay*'s holding was limited, as it purported to forbid state law contract defenses—"such as fraud, duress, or unconscionability"—to be used.[100]

2. *Third Circuit Determines that New Jersey Law Should Apply and the Class-Arbitration Waiver Is Likely Unenforceable*

After deciding the threshold FAA preemption matter, the Third Circuit turned to the critical issue of whether to apply Utah or New Jersey law.[101] The court noted that if the choice-of-law clause in the cardholder agreement was valid, Homa's appeal would fail, as Utah law "expressly allows class action waivers in consumer credit agreements."[102] AEC and AECB urged the court to apply Utah law because Utah was the place of contract, the place of performance, and the place where Homa's account was located.[103] To settle the dispute, the Third Circuit applied New Jersey's choice-of-law rules because federal courts sitting in diversity apply

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preempt us from even considering whether the class-arbitration waiver is unconscionable. . . .").

98. *See id.* (stating court's reasoning). The court also made a point to mention that *Gay*'s discussion of whether the FAA preempts state law "appears to be dicta." *See id.* at 229 (classifying *Gay*'s discussion of whether FAA preempts Pennsylvania law as dicta, "as the Court 'determined that it should enforce the terms of the choice-of-law provision selecting the application of Virginia law' and concluded that the class waiver at issue was not unconscionable under that law, but nonetheless engaged in a discussion of unconscionability under Pennsylvania law"). The court defined dictum as "'a statement in a judicial opinion that could have been deleted without seriously impairing the analytical foundations of the holding.'" *See id.* (quoting *In re* McDonald, 205 F.3d 606, 616 (3d Cir. 2000)).

99. *See id.* at 230 (stating Supreme Court clearly held that "generally applicable contract defenses, such as . . . unconscionability, may be applied to invalidate arbitration agreements without contravening [FAA] § 2").

100. *See id.* at 229-30 (limiting *Gay*'s holding).

101. *See id.* at 230 (discussing chronology of analysis).

102. *See id.* at 227 (explaining Utah law's tolerance of class action waivers in consumer credit agreements). The Utah statute allows "a creditor [to] contract with the debtor of an open-end consumer credit contract for a waiver by the debtor of the right to initiate or participate in a class action related to the open-end consumer credit contract." UTAH CODE ANN. § 70C-4-105 (2006).

103. *See Homa* 558 F.3d at 232 (stating defendants' argument that Utah law should apply). AEC and AECB further pointed to the choice-of-law clause in the cardholder agreement to demonstrate that Utah law should apply. *See id.* at 227 (discussing defendants' arguments). Among other things, the choice-of-law provision stated: "We are located in Utah, hold your Account in Utah, and entered into this Agreement with you in Utah." *See* Homa v. Am. Express Co., 496 F. Supp. 2d 440, 443 (D.N.J. 2007). For the full text of the choice-of-law provision, see *supra* note 85.

the forum state's choice-of-law rules.[104] In New Jersey, "when parties to a contract have agreed to be governed by the laws of a particular state, New Jersey courts will uphold the contractual choice *if it does not violate New Jersey's public policy*."[105] The Third Circuit noted that, when deciding whether a contractual choice-of-law provision is enforceable, the Supreme Court of New Jersey has relied on the *Restatement (Second) of Conflicts of Laws* § 187(2).[106] The *Restatement* provides that the law of the state chosen by the parties will apply unless:

> application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which . . . would be the state of the applicable law in the absence of an effective choice of law by the parties.[107]

Considering the *Restatement*, the court agreed with the *Muhammad* principle that a class-arbitration waiver can violate New Jersey public policy where the waiver is found in a contract of adhesion and where the anticipated individual recovery involves a particularly small amount of asserted damages.[108] The Third Circuit determined that, as in *Muhammad*, the contract at issue had the characteristics of an adhesion contract.[109] Furthermore, the court stated that Homa's underlying claim involved a "predictably small amount of damages" because the claim implicated less than five percent of his total credit card balance.[110] Therefore, the court found

104. *See Homa*, 558 F.3d at 227 ("In evaluating whether a contractual choice-of-law clause is enforceable, federal courts sitting in diversity apply the choice-of-law rules of the forum state, which in this case is New Jersey.").

105. *Id.* (emphasis added) (describing New Jersey method of analyzing choice-of-law issue).

106. *See id.* (examining New Jersey choice-of-law rules).

107. RESTATEMENT (SECOND) OF CONFLICTS OF LAWS § 187(2)(b) (1969).

108. *See Homa*, 558 F.3d at 231 (explaining "prediction" that Supreme Court of New Jersey would find that class-arbitration waiver violates fundamental public policy of New Jersey).

109. *See id.* (comparing contract at issue to contract in *Muhammad*). The court stated that the contract at issue possessed the "hallmarks of a contract of adhesion" because it was "'presented on a take-it-or-leave-it basis . . . in a standardized printed form, and without opportunity for the 'adhering party' to negotiate except perhaps on a few particulars.'" *Id.* (citation omitted) (analyzing contract at issue against indicia of contracts of adhesion).

110. *See id.* (explaining why class-arbitration waiver violates New Jersey's fundamental public policy). The amount in dispute was foreseeably capped at five percent of Homa's total credit card balance because the original claim involved the Blue Cash card promotion, which purported to provide cardholders with five percent cash back on purchases made with the card. *See id.* at 226-27 (stating case's facts). Still, because the district court made no findings of fact as to the potential value of Homa's claims (it treated AEC's Motion to Compel Arbitration as a Motion to Dismiss) the case had to be remanded. *See id.* at 233 (explaining that district court still had to determine whether "the claims at issue are of such a low value as effectively to preclude relief if decided individually").

that the class-arbitration waiver violated New Jersey's fundamental public policy as applied to small-sum claims.[111]

The Third Circuit then turned to the remaining portion of the *Restatement* and analyzed whether New Jersey or Utah had a materially greater interest in resolving the issue.[112] The court's analysis considered each state's contacts with the parties to the litigation, and the policy reasons underlying the states' conflicting laws.[113] The court determined that, given these considerations—"particularly New Jersey's interest in protecting its consumers' ability to enforce their rights under the [NJCFA]"—the Supreme Court of New Jersey would find that New Jersey had a materially greater interest than Utah in the dispute.[114] Thus, the court held that "if this is a small-sum case, then the Supreme Court of New Jersey would apply New Jersey law to the class-arbitration waiver."[115]

Lastly, the court applied New Jersey law to Homa's unconscionability claim.[116] The court held: "[I]f the claims at issue are of such a low value as effectively to preclude relief if decided individually, then, under *Muhammad*, the application of Utah law to the class-arbitration waiver is

111. *See id.* (stating court's holding). This was not the end of the court's analysis, as it still had to discuss the rest of the test enumerated in the *Restatement*. *See id.* (acknowledging next step in choice-of-law analysis).

112. *See id.* at 231 (stating that court combined remaining *Restatement* analysis, namely "that New Jersey law would apply in the absence of the parties' choice-of-law provisions and that New Jersey has a materially greater interest that Utah in the determination of the waiver's validity"). The court combined the remaining analysis because "as New Jersey choice-of-law rules 'require application of the law of the state with the greatest interest in resolving the particular issue that is raised in the underlying litigation,' New Jersey Law will necessarily apply in the absence of an agreement if New Jersey has a materially greater interest." *Id.* (explaining court's rationale).

113. *See id.* at 232 (discussing court's analysis). First, the court documented that "New Jersey's governmental-interest analysis requires an initial inquiry into whether there is an actual conflict between the laws of Utah and New Jersey." *Id.* The court found that there was a stark conflict between the states' laws. *See id.* ("Comparison of *Muhammad*, which declared unconscionable a class-arbitration waiver that would preclude relief under New Jersey's Consumer Fraud Act, with UTAH CODE ANN. § 70C-4-105, which explicitly states that class-action waivers in open-end consumer credit contracts are valid, reveals such a conflict."). Finding an actual conflict, the court sought to "identify the governmental policies underlying the law of each state and how those policies [were] affected by each state's contacts to the litigation and to the parties' so that [it could] determine which state [had] the greater interest." *Id.*

114. *See id.* at 232-33 ("Given [each state's contacts and policy reasons], 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 under the NJCFA."). The court determined that New Jersey's strong consumer protection laws trumped Utah's pro-business stance on class-arbitration waivers. *See id.* at 232 (discussing which state had materially greater interest).

115. *Id.* (stating court's holding).

116. *See id.* at 233 (explaining final portion of court's decision).

unconscionable."[117] The Third Circuit's decision reversed the district court's order dismissing the case in favor of arbitration, and the case was remanded for further proceedings consistent with the decision.[118]

IV. THE STORM SURGE: ANALYZING *HOMA*'S IMPACT

The *Homa* decision is consistent with the growing trend among circuit courts to invalidate contractual class-arbitration waivers in consumer contracts.[119] The decision is significant to the Third Circuit's treatment of class-arbitration waivers and, more broadly, to federal class-arbitration waiver jurisprudence in two primary ways.[120] First, by voiding AECB's class-arbitration waiver, *Homa* instructs companies to adopt extensive risk prevention measures in consumer contracts in order to enhance the likelihood that an arbitration provision will be enforced.[121] Second, by holding that the FAA does not preempt consideration of state law contract defenses, it eliminates the circuit split on the preemption issue that *Gay* purportedly created.[122]

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117. *Id.* (stating court's holding).

118. *See id.* (stating court's disposition). Judge Weis, in his concurrence, stated that the court remanded essentially because the district court's ruling was constrained by FED. R. CIV. P. 12(b)(6) and thus "did not fully address all of the matters relevant to the contention that the Cardmember Agreement contain[ed] an unconscionable class-action waiver." *See id.* at 233 (Weis, J., concurring) (discussing reason for remand). The lower court on remand was to consider the question of unconscionability under New Jersey law. *See id.* ("Because all of the factors bearing on [the unconscionability] issue are not pertinent to our limited review in this case, the question of unconscionability under New Jersey law remains open for consideration on remand."). Nonetheless, the Third Circuit went through the requisite analysis and predicted that the lower court would find the class-arbitration waiver to be unconscionable. *See id.* at 233 (majority opinion) (finding class-arbitration waiver unconscionable).

119. *See* Laster v. AT&T Mobility LLC, 584 F.3d 849, 854-55 (9th Cir. 2009) (finding class-arbitration waiver unconscionable). The *Laster* court implemented a three-part test to determine whether a class-arbitration waiver in a consumer contract is unconscionable: "(1) is the agreement a contract of adhesion; (2) are disputes between the contracting parties likely to involve small amounts of damages; and (3) is it alleged that the party with superior bargaining power has carried out a scheme deliberately to cheat large numbers of consumers out of individually small sums of money." *See id.* (analyzing class-arbitration waiver's validity); Dale v. Comcast Corp., 498 F.3d 1216, 1224 (11th Cir. 2007) ("[W]e conclude the Comcast class action waiver is unconscionable to the extent it prohibits the subscribers from bringing a class action alleging state law claims based on a violation of the Cable Act's franchise fee provisions."); Kristian v. Comcast Corp., 446 F.3d 25, 64 (1st Cir. 2006) (holding class-arbitration waiver unenforceable). For a complete discussion of the *Kristian* decision, see *supra* notes 48-57 and accompanying text.

120. For a discussion of the significance of *Homa* on class-arbitration waiver jurisprudence, see *infra* notes 123-48 and accompanying text.

121. For a discussion of *Homa*'s impact on corporate contract drafting, see *infra* notes 123-36 and accompanying text.

122. *See Homa*, 558 F.3d at 230 (rejecting argument that, under *Gay*, FAA precludes court from applying state law unconscionability principles to void class-arbitration waiver). For a discussion of the implications of the court's holding

A. *The Impact of* Homa*'s Implied Lessons*

In light of *Homa*, companies must now review and modify the arbitration clauses in their consumer contracts to enhance the likelihood that such provisions will survive litigation.[123] There are a number of preventative practices companies should implement to withstand *Homa*'s precedent.[124] Most importantly, because *Homa* appears to sever the unenforceable class-arbitration waiver from the remainder of the arbitration clause, companies should include nonseverability provisions in their arbitration clauses.[125] Such provisions should state that the entire arbitration clause is null and void if the class-arbitration waiver is invalidated.[126] Failing to include a nonseverability provision would put a company in the precarious position of being unable to appeal a potentially unfavorable class-arbitration verdict.[127]

Additionally, *Homa* impliedly recommended several steps that companies can take to draft more enforceable class-arbitration waivers.[128] These steps are reflected in the factors the *Homa* court considered in voiding the class-arbitration waiver: the parties' relative bargaining positions; whether

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regarding the FAA preemption issue, see *infra* notes 137-41 and accompanying text.

123. For a discussion of *Homa*'s impact on corporate contract drafting and the contract modifications that corporations should make, see *infra* notes 123-36 and accompanying text.

124. For a discussion of preventative practices for companies, see *infra* notes 121-41 and accompanying text.

125. *See Homa*, 558 F.3d at 233 (relying on *Muhammad* to invalidate class-arbitration waiver). Reliance on *Muhammad* would lead the Third Circuit to sever the unenforceable class-arbitration waiver while enforcing the rest of the arbitration clause. *See* Muhammad v. County Bank of Rehoboth Beach, 912 A.2d 88, 91 (N.J. 2006) ("[T]he appropriate remedy in these circumstances is to sever the unconscionable provision and enforce the otherwise valid arbitration agreement."); *see also* Dawson, *supra* note 35 (detailing that one preventative drafting practice is to "include language that the mandatory arbitration provision will be rendered null and void in its entirety if a court (or arbitrator) determines that the waiver of class . . . relief is unenforceable").

126. *See* Dawson, *supra* note 35, at 13 (providing language that should be included in nonseverability provision); Roger A. Lewis & Jonathan H. Claydon, *Class Arbitration Waiver Provisions Under Attack in Third Circuit*, GOLDBERG KOHN ALERT (Mar. 9, 2009), http://www.goldbergkohn.com/news-alerts-133.html ("As a primary protection, it is advisable to include a nonseverability clause in the arbitration provision stating that the arbitration provision cannot be enforced if the class arbitration waiver is invalidated.").

127. *See* Lewis & Claydon, *supra* note 126 ("Most companies do not want to find themselves in 'class' arbitration, which has all or more of the usual risks of class litigation but without the protection of a meaningful right of appeal."). AECB included a nonseverability provision in its arbitration clause, although it is unclear whether the district court will honor it on remand. *See Homa*, 558 F.3d at 234 (Weis, J., concurring) ("[S]hould any portion of th[e] '*Restrictions on Arbitration*' provision be deemed invalid or unenforceable, then the entire Arbitration Provision (other than this sentence) shall not apply.").

128. For a discussion of *Homa*'s implied lessons, see *infra* notes 129-36 and accompanying text.

the waiver was presented in a contract of adhesion; and whether the size of the damages effectively precluded the plaintiff from bringing an individual claim.[129] First, the court's inherent disapproval of adhesion contracts may be assuaged by presenting the contract to the consumer as fairly as possible.[130] This involves ensuring that the class-arbitration waiver is included in the contract in a manner that is "prominent, clear, conspicuous and understandable."[131] Further, by ensuring that the consumer knowingly agreed to the waiver, a company can balance the parties' relative bargaining positions.[132] To do so, companies should both employ procedural mechanisms and provide the consumer with the option to reject the arbitration agreement.[133]

Finally, a company can alleviate the impractical costs for consumers who bring an individual claim by contractually agreeing to bear the cost of the individual arbitration.[134] As the *Homa* decision was primarily predicated on the low-value claim's effect on the viability of an individual action, the inclusion of a reimbursement or cost-shifting provision arguably

129. *See Homa*, 558 F.3d at 231-32 (stating court's analysis); *id.* at 233 (Weis, J., concurring) (noting additional factors considered by court).

130. *See id.* at 231 (majority opinion) (noting that class-arbitration waivers that are found in contracts of adhesion can be "problematic"); Lewis & Claydon, *supra* note 126 (instructing companies that, in *Homa*'s wake, "the contract containing the class arbitration waiver [should be] presented to the consumer in as fair a manner as possible").

131. *See* Dawson, *supra* note 35 (urging corporations to draft language in arbitration agreements in particular way).

132. *See Homa*, 558 F.3d at 233 (Weis, J., concurring) (listing "the parties' relative bargaining positions" among factors relied on by *Muhammad* court—and in turn considered by *Homa* court—in determining whether to strike class-arbitration bans); Pivoris v. TCF Fin. Corp., No. 07 C 2673, 2007 U.S. Dist. LEXIS 90562, at *12 (N.D. Ill. Dec. 7, 2007) (explaining substantial steps company took to ensure consumer understood and knowingly agreed to class-arbitration waiver). In *Pivoris*, the class-arbitration waiver was enforced, among other reasons, because the corporate defendant had required the plaintiff to separately initial the clause and because the contract cautioned the plaintiff to "read this Arbitration provision carefully." *See Pivoris*, 2007 U.S. Dist. LEXIS 90562, at *2-3 (describing characteristics of enforceable class-arbitration waiver).

133. *See Pivoris*, 2007 U.S. Dist. LEXIS 90562, at *3 ("[The plaintiff] was entitled to reject the arbitration clause by 'mailing a written rejection notice' within thirty days."); Dawson, *supra* note 35 (explaining choice that should be given to consumers). For a discussion of the procedural mechanisms in *Pivoris*, see *supra* note 132 and accompanying text.

134. *See* Dawson, *supra* note 35 (arguing that "the company should bear the cost of the arbitration of individual disputes"); *see also* Daniel R. Higginbotham, *Buyer Beware: Why the Class Arbitration Waiver Clause Presents a Gloomy Future for Consumers*, 58 DUKE L.J. 103, 133 (2008) ("Another way to lower consumers' costs is to shift some or all of the arbitration filing fees to the drafting party."). *Cf. Pivoris*, 2007 U.S. Dist. LEXIS 90562, at *5 (indicating that arbitration clause provided that company would not seek to recover arbitration or attorney's fees); Higginbotham, *supra*, at 134 ("Perhaps the easiest way to lower costs is to require losing businesses to reimburse all of a claimant's reasonable attorney's fees.").

would have changed the outcome of the case.[135] Such a provision would have required AECB to cover the fees associated with the arbitration and would have effectively allowed Homa to bring the low-value claim individually.[136]

B. *Elimination of the Circuit Split on the FAA Preemption Issue*

The *Homa* decision clarified the muddled precedent the Third Circuit established in *Gay*.[137] *Gay* had prompted companies across the nation to argue that a circuit split existed as to the enforceability of class-arbitration waivers and that the FAA preempted state law contract defenses.[138] In response, many lower courts, particularly in the Third Circuit, reached decisions that barred class actions in the arbitral setting.[139] The *Homa* decision, however, clarified that *Gay*'s FAA preemption language was merely dicta and, in so doing, effectively eliminated the purported circuit split on the issue.[140] Had the Third Circuit declined to limit *Gay*'s hold-

135. *See Homa*, 558 F.3d at 233 (holding class-arbitration waiver unconscionable if claims at issue "are of such low value as effectively to preclude relief if decided individually"). Some arbitration organizations have predetermined cost shifting rules. *See* Am. Arbitration Ass'n, Consumer Arbitration Costs, http://www.adr.org/sp.asp?id=22039 ("If the consumer's claim . . . does not exceed $10,000, then the consumer is responsible for one-half the arbitrator's fees up to a maximum of $125."). Nevertheless, even such consumer-protective cost shifting strategies do not help with very small claims. *See* Higginbotham, *supra* note 134, at 133 ("For many consumers, the $125 fee alone prevents filing a claim. As a result, the rules should provide that, for consumers with low-value claims, the business must pay the consumer's fees.").

136. *See Homa*, 558 F.3d at 231 (holding that class-arbitration waiver violated New Jersey public policy—namely, consumers' ability to effectively pursue their rights under consumer protection law—because of small value of claim).

137. *See* Bland & Prestel, *supra* note 9, at 390-91 (explaining *Homa*'s limiting effect on *Gay*).

138. *See, e.g.*, Petition for Writ of Certiorari, T-Mobile USA, Inc. v. Laster, 128 S. Ct. 2500 (2008) (No. 07-976) (arguing that, under *Gay*, state law is preempted by FAA).

139. *See, e.g.*, Shubert v. Wells Fargo Auto Fin., Inc., No. 08-3754, 2008 U.S. Dist. LEXIS 105198, at *25 (D.N.J. Dec. 31, 2008) (holding class-arbitration waiver enforceable on basis that "*Gay* [court] distinctly analyzed the no-class action arbitration [clause] and found that federal law preempted the conflicting state law"); *Kudos to the Third Circuit for Preserving Class Actions*, LABOVICK INJURY LAW BLOG (Feb. 25, 2009), http://injurylaw.labovick.com/tags/homa-v-american-express-compan/ ("[*Gay*] prompted several U.S. district courts in New Jersey to dismiss class actions in the last year.").

140. *See* Homa v. Am. Express Co., 558 F.3d 225 (3d Cir. 2009) (finding *Gay*'s preemption language to be dicta and not barrier to court's application of state law); *see also Visions of Circuit Split*, MORRISON FOERSTER FIN. SERVS. REPORT (Mar. 9, 2009), http://www.mofo.com/financial-services-report-spring-2009-03-09-2009/#9 ("Class waiver enthusiasts thought they'd discovered the Holy Grail for Supreme Court review when the Third Circuit issued *Gay*, a murky decision that seemed to stand for the proposition that state law class waiver analysis was preempted by the FAA."); Deepak Gupta, *Third Circuit Strikes Down Class-Action Ban, Eliminates Claimed Circuit Split*, PUBLIC CITIZEN CONSUMER LAW & POLICY BLOG (Feb. 26, 2009, 1:26 PM), http://pubcit.typepad.com/clpblog/2009/02/third-circuit-strikes-down-clas-

ing, corporate defendants in many jurisdictions would continue to have a strong argument that plaintiffs are precluded from arguing state law contract defenses—conceivably the most effective argument that plaintiffs possess.[141]

V. CONCLUSION: THE CASE FOR AN "UNWAIVERING" JUDICIAL STANDARD

The enforceability of class action bans in mandatory arbitration clauses remains one of the most hotly contested issues in consumer litigation.[142] A growing number of courts have held such waivers unenforceable under an array of theories.[143] While the circuit courts now seem fully aware that the plight of consumers has been exacerbated by the proliferation of class-arbitration waivers, the courts are lacking a uniform judicial standard to address the problem.[144]

The approach used by the *Homa* court provides a standard to effectively adjudicate the issue.[145] Adopting *Homa*'s indicia involves a totality of

saction-ban-eliminates-claimed-circuit-split.html (discussing rise and fall of "claimed circuit split" on FAA preemption issue).

141. *See, e.g.*, Brief for CTIA – The Wireless Ass'n as Amicus Curiae Supporting Petitioners, T-Mobile USA, Inc. v. Laster, 128 S. Ct. 2500 (2008) (No. 07-976) (arguing that "the text and history of the FAA make clear that Congress never intended for state policy judgments about what is substantively unfair to provide a ground for invalidating an otherwise proper arbitration clause.").

142. *See* Bland & Prestel, *supra* note 9, at 370 (commenting on vigorous debate surrounding enforceability of class-arbitration waivers); Duffy, *supra* note 38, at 848 ("The validity of class action waivers in consumer contracts of adhesion has been a hotly contested topic in contract law."); Lewis & Claydon, *supra* note 126 (noting that enforceability of class action waiver provisions in mandatory arbitration clauses is "[o]ne of the most contentious issues in consumer class action litigation in recent years").

143. For a discussion of the contract defenses that have voided class-arbitration waivers, see *supra* notes 92-118 and accompanying text. For further background on the arguments available to plaintiffs, see Rice, *supra* note 3, at 246-52 (listing several arguments).

144. *See* Higginbotham, *supra* note 134, at 115 (noting that Supreme Court has yet to decide issue); *see also* Rice, *supra* note 3, at 256 (explaining need for judicial standard, and proposing two-prong analysis to Supreme Court). Rice's proposed test elaborates upon tests implemented in past circuit court decisions:

> This analysis would begin with determining if the contract was a product of a negotiation between sophisticated parties with similar bargaining positions. If the Court so determined, the agreement would be valid and enforceable. If, however, the Court determined the contract is one in which there was little or no negotiation or it was a standard-form or adhesion contract and the plaintiff had no reasonable alternative to the transaction, the Court would then step through an analysis of the agreement and determine whether it restricts the plaintiff's substantive rights.

Rice, *supra* note 3, at 256 (proposing judicial standard).

145. For a discussion of the Third Circuit's rationale in *Homa*, see *supra* notes 92-118 and accompanying text. The issue could also be resolved by pending congressional legislation that seeks to void specific types of arbitration provisions. *See* Wilson, *supra* note 1 ("The Arbitration Fairness Act of 2009 would ban provisions requiring arbitration of (1) an employment, consumer, or franchise dispute, or (2) a dispute arising under any statute intended to protect civil rights.").

the circumstances analysis that assesses whether: (1) the claim involves a presumably small amount of damages; (2) the class-arbitration waiver is presented in a contract of adhesion; (3) the parties enjoy relatively equal bargaining positions; and (4) the waiver provision affects the public interests involved in the case.[146] Implementation of such a standard, coupled with modified consumer contracts that take into account the risk prevention measures discussed in Part IV.A, could resolve the class-arbitration waiver issue.[147] Widespread adoption of this standard would ensure that: (1) companies can continue to use the class-arbitration waiver mechanism, thereby remaining protected from colossal class action judgments; and (2) consumers can vindicate their statutory rights without being taken advantage of by unconscionable contracts of adhesion.[148]

Steven D. Millman

146. *See* Homa v. Am. Express Co., 558 F.3d 225, 230-34 (3d Cir. 2009) (identifying factors used to reach decision).

147. For a discussion of how the standard would solve the problem, see *supra* note 146 and accompanying text.

148. For a complete discussion of how the standard would achieve these results, see *supra* notes 107-13, 123-36 and accompanying text.