No. 02-634

IN THE

Supreme Court of the United States

GREEN TREE FINANCIAL CORP. A/K/A GREEN TREE ACCEPTANCE CORP. A/K/A GREEN TREE FINANCIAL SERVICES CORP. N/K/A CONSECO FINANCE CORP.,

Petitioner,

v.

LYNN W. BAZZLE AND BURT A. BAZZLE, IN A REPRESENTATIVE CAPACITY ON BEHALF OF A CLASS AND FOR ALL OTHERS SIMILARLY SITUATED; DANIEL B. LACKEY, GEORGE BUGGS AND FLORINE BUGGS, IN A REPRESENTATIVE CAPACITY ON BEHALF OF A CLASS AND FOR ALL OTHERS SIMILARLY SITUATED,

Respondents.

On Writ of Certiorari to the Supreme Court of South Carolina

BRIEF FOR AMERICAN BANKERS ASSOCIATION, AMERICAN FINANCIAL SERVICES ASSOCIATION, AND CONSUMER BANKERS ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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FEBRUARY 2003

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This *amici curiae* brief is submitted in support of the petitioner.[1] By letters filed with the Clerk of the Court, petitioner and respondents have consented to the filing of this brief.

[1] Pursuant to Supreme Court Rule 37.6, *amici* state that the brief was prepared in its entirety by *amici curiae* and their counsel. No monetary contribution toward the preparation or submission of this brief was made by any person other than *amici curiae*, their members, and their counsel.

STATEMENT OF INTEREST OF *AMICI CURIAE*

The American Bankers Association ("ABA") is the principal national trade association of the banking industry in the United States. Its members are located in all fifty states and the District of Columbia and include banks of all types and sizes—money center banks, regional banks, and community banks. ABA members hold approximately ninety percent of the domestic assets of United States banks. The ABA frequently appears in litigation as an *amicus curiae* where the issues raised are of widespread importance to banks or consumers of banking services.

The American Financial Services Association ("AFSA") was organized in 1916 and represents more than 300 companies that engage in lending and sales financing amounting to approximately twenty percent of all consumer credit in the United States. These companies range from independently owned consumer finance firms to the nation's largest financial-services, retail, and automobile sales finance companies. AFSA's membership includes national and state banks that operate multi-state consumer credit programs.

The Consumer Bankers Association ("CBA") was founded in 1919 to provide a progressive voice for the retail banking industry. CBA members hold more than 900 bank and thrift charters, with total assets of more than $2.9 trillion, and are leaders in the areas of consumer, auto, home equity, and education finance, bank sales of investment products, small business services, and community development.

Many members of the ABA, AFSA, and CBA use standard form agreements and contracts, which include arbitration provisions. Some of those provisions authorize individual arbitration and are silent about class-action arbitration. Other arbitration provisions expressly state that class arbitrations are not permitted. Members with either sort of arbitration agreement have a strong interest in ensuring that the agreements are enforced in keeping with their terms, and that

class arbitration procedures are not imposed upon them in derogation of the Federal Arbitration Act.

SUMMARY OF ARGUMENT

Amici agree with petitioner that arbitration agreements must be enforced as written and that class arbitration procedures may not be imposed on parties who have not agreed to them. Forced class arbitration proceedings violate the Federal Arbitration Act ("FAA" or "Act"), 9 U.S.C. §§ 1-16, and are inherently unfair to defendants, in part because they cannot bind absent plaintiffs.

1. The most basic principle of the FAA is that an arbitration agreement should be enforced as written. The FAA is violated when a court determines either that parties who have agreed to do so may not arbitrate, or that they shall arbitrate under a procedure to which they did not agree. The enforceability of arbitration agreements is subject to state-law contract defenses, including unconscionability, but such a defense cannot be a mere pretext for hostility to arbitration itself and cannot be a basis for imposing a fundamentally different private decision-making process.

2. Forced class arbitrations cannot be binding on absent plaintiff class members who did not agree to, and play no part in, the particular arbitration proceeding. The decision in a judicial class action is binding on absentees because courts are created by public laws to resolve disputes. The decisions of an arbitrator have authority only because of the particular parties' agreement and cannot be imposed on other persons. Moreover, a notice of a class arbitration is not a notice to which an absent class member has an obligation to respond. And because class arbitrations are often neither public nor recorded, absent class members have little ability to protect their interests. Finally, settlements of class arbitrations are not subject to review by a neutral judge, but only by the arbitrator selected by the parties, who cannot be expected to afford absentees the protection provided by a judge under Rule 23.

3. Forced class arbitrations are fundamentally unfair to defendants. Since absent plaintiff class members cannot be bound to the result of a class arbitration, the defendant can be subjected to a series of similar claims, with no prospect of a class victory but the prospect of a class defeat the first time an arbitrator rules for a plaintiff. The absence of a written record, an explanatory opinion, or judicial review makes this ratchet all the more unfair. This kind of one-sided class procedure would obviously make arbitration an unacceptable alternative for the party (such as a lender) that must run the risk of a classwide recovery without hope of obtaining a ruling that would bar future claims.

4. The defects of class arbitration cannot be repaired by injecting the courts into the arbitration process to resolve questions of class definition, form and sufficiency of notice, adequacy of representation, fairness of any settlement, and so forth. The attempt to do this would sacrifice the benefits of arbitration, leaving the worst of both worlds.

5. The decision of the court below reflects the old judicial hostility to arbitration in modern and more sophisticated dress. Its premise is that courts should not enforce agreements to arbitrate disputes on an individual basis. That premise is at odds with the FAA and this Court's decisions.

ARGUMENT

I. FORCED CLASS ARBITRATION IS CONTRARY TO THE FAA.

The source of an arbitrator's power to decide a dispute is the contract between the parties to resolve their disputes in that particular way. *First Options of Chicago, Inc.* v. *Kaplan*, 514 U.S. 938, 943 (1995) ("[A]rbitration is simply a matter of contract between the parties."). The FAA makes such contracts fully enforceable, 9 U.S.C. § 2, and this Court has repeatedly held that "private agreements to arbitrate are [to be] enforced according to their terms," *Volt Info. Scis.,*

Inc. v. *Board of Trs.*, 489 U.S. 468, 479 (1989),[2] "like other contracts," *id.* at 478.[3]

Every federal court to reach the issue has held that when an arbitration agreement is silent as to class arbitration, arbitration must proceed on an individual basis and courts and arbitrators are powerless to rewrite the parties' agreement so as to compel class arbitration.[4] As this Court said in *EEOC* v. *Waffle House, Inc.*, 534 U.S. 279 (2002), "[N]othing in the

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[2] *See also Mastrobuono* v. *Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 53-54 (1995); *Perry v. Thomas*, 482 U.S. 483, 492-93 n.9 (1987)

[3] It is clear that the South Carolina court did not treat the arbitration agreement at issue "like other contracts." South Carolina contract law includes the following basic principle:

> It is elementary and needs no citation of authority that the function of courts is to adjudge and enforce contracts as they are written and entered into by the parties. The court cannot make them for the parties. . . . [T]he court cannot exercise its discretion as to the wisdom of such contract or substitute its own for that which was agreed . . . .

Charles v. *Canal Ins. Co.*, 238 S.C. 600, 608-09, 121 S.E.2d 200, 205 (1961). "Words cannot be read into a contract which impart intent wholly unexpressed when the contract was executed." *Blakeley* v. *Rabon*, 221 S.E.2d 767, 769 (S.C. 1976). But that is precisely what the South Carolina court did. Pet. App. 22a.

[4] *See, e.g.*, *Dominium Austin Partners* v. *Emerson*, 248 F.3d 720, 728-29 (8th Cir. 2001); *Champ* v. *Siegel Trading Co.*, 55 F.3d 269, 275 (7th Cir. 1995); *McCarthy* v. *Providential Corp.*, No. C 94-0627 FMS, 1994 WL 387852, at *8 (N.D. Cal. July 19, 1994); *Gammaro* v. *Thorp Consumer Disc. Co.*, 828 F. Supp. 673, 674 (D. Minn. 1993), *see also, e.g.*, *Government of United Kingdom* v. *Boeing Co.*, 998 F.2d 68, 74 (2d Cir. 1993) ("district court cannot consolidate arbitration proceedings arising from separate agreements to arbitrate, absent the parties' agreement to allow such consolidation"); *American Centennial Ins.* v. *National Cas. Co.*, 951 F.2d 107, 108 (6th Cir. 1991) ("a district court is without power to consolidate arbitration proceedings, over the objection of a party to the arbitration agreement, when the agreement is silent regarding consolidation"); *Baesler* v. *Continental Grain Co.*, 900 F.2d 1193, 1195 (8th Cir. 1990) ("absent a provision in an arbitration agreement authorizing consolidation, a district court is without power to consolidate arbitration proceedings").

[FAA] authorizes a court to compel arbitration of any issues, *or by any parties*, that are not already covered in the agreement." *Id.* at 289 (emphasis added).

The South Carolina court, however, joined a small group of state courts that have allowed one party to pursue an arbitration procedure wholly different from the one to which the parties agreed.[5] Neither the agreement between Bazzle and Green Tree nor the agreement between Lackey and Green Tree included the absent class members or provided for class arbitration. But the court asserted that "parties with nominal individual claims" would have no effective "avenue for relief" if they could not pursue their claims on a class basis. Pet. App. 22a. It therefore imposed on the parties a decision-making procedure to which neither the parties (nor the absent class members themselves) had agreed.

The Ninth Circuit recently took a different tack: it held that arbitration agreements that explicitly preclude class arbitration are void as unconscionable under state law. *See Ting* v. *AT&T*, — F.3d —, 2003 WL 292296, at *20 (9th Cir. Feb. 11, 2003). *Ting* thus denied the parties who had agreed to arbitrate the ability to do so at all, and channelled them into court proceedings. In *Ting* and the present case, the courts failed to follow the FAA's fundamental requirement that arbitration agreements be enforced in accordance with their terms.[6]

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[5] *See, e.g.*, *Keating* v. *Superior Court*, 645 P.2d 1192 (Cal. 1982), *rev'd in part on other grounds sub nom. Southland Corp.* v. *Keating*, 465 U.S. 1 (1984); *Blue Cross* v. *Superior Court*, 78 Cal. Rptr. 2d 779 (Ct. App. 1998); *Dickler* v. *Shearson Lehman Hutton, Inc.*, 596 A.2d 860 (Pa. Super. Ct. 1991).

[6] Most courts have refused to compel class arbitrations when the agreement was silent on this issue. *See* cases cited *supra* n.4. Similarly, most courts, unlike the court in *Ting*, have rejected efforts to invalidate arbitration agreements that explicitly prohibited class actions. *See, e.g.*, *Lloyd* v. *MBNA Am. Bank, N.A.*, 27 Fed. Appx. 82, 84 (3d Cir. 2002); *Snowden* v. *Checkpoint Check Cashing, Inc.*, 290 F.3d 631, 638-39 (4th Cir.), *cert denied*, 123 S. Ct. 695 (2002); *Randolph* v. *Green Tree Fin.*

Under the FAA, arbitration agreements are subject to the same defenses that state law applies to all contracts, including unconscionability. 9 U.S.C. § 2; *see also Doctor's Assocs., Inc.* v. *Casarotto*, 517 U.S. 681 (1996); *Perry*, 482 U.S. at 492 n.9. But a finding of unconscionability cannot be simply a pretext for reasserting the old judicial hostility to arbitration. It must be based on applying established state law to the facts of a particular contract, *see Perry*, 482 U.S. at 492 n.9, not a broadside ruling that an entire class of contracts, sanctioned by federal law, is inherently unconscionable.

As this Court has long recognized, parties agreeing to arbitrate their disputes are necessarily forfeiting the "procedures and opportunity for review of the courtroom," *Gilmer* v. *Interstate/Johnson Lane Corp.*, 500 U.S. 20, 32 (1991), in favor of the more efficient system of arbitration. Permitting parties to trade their right to go to court for the efficiency of arbitration lies at the very heart of the FAA.[7] To permit

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Corp.—Alabama, 244 F.3d 814, 815 (11th Cir. 2001); *Baron* v. *Best Buy Co.*, No. 99-14028, slip op. at 3 (11th Cir. June 1, 2001); *Johnson* v. *West Suburban Bank*, 225 F.3d 366, 369 (3d Cir. 2000), *cert. denied sub nom. Johnson* v. *Tele-Cash, Inc.*, 531 U.S. 1145 (2001); *Lomax* v. *Woodmen of World Life Ins. Soc'y*, 228 F. Supp. 2d 1360, 1365 (N.D. Ga. 2002); *Lozano* v. *AT&T Wireless*, 216 F. Supp. 2d 1071, 1076 (N.D. Cal. 2002); *Vigil* v. *Sears Nat'l Bank*, 205 F. Supp. 2d 566, 573 (E.D. La. 2002); *Pick* v. *Discover Fin. Servs., Inc.*, 2001 WL 1180278, at *5 (D. Del. Sept. 28, 2001); *Arriaga* v. *Cross Country Bank*, 163 F. Supp. 2d 1189, 1195 (S.D. Cal. 2001); *Hale* v. *First USA Bank, N.A.*, No. 00CIV5406JGK, 2001 WL 687371, at *7 (S.D.N.Y. June 19, 2001); *Marsh* v. *First USA Bank, N.A.*, 103 F. Supp. 2d 909, 924 (N.D. Tex. 2000); *Sagal* v. *First USA Bank, N.A.*, 69 F. Supp. 2d 627, 631-32 (D. Del. 1999), *aff'd*, 254 F.3d 1078 (3d Cir. 2001); *Zawikowski* v. *Beneficial Nat'l Bank*, No. 98C2178, 1999 WL 35304, at *2 (N.D. Ill. Jan. 11, 1999); *Brown* v. *KFC Nat'l Mgmt. Co.*, 921 P.2d 146, 166 n.23 (Haw. 1996); *Rains* v. *Foundation Health Sys. Life & Health*, 23 P.3d 1249, 1253 (Colo. Ct. App. 2001); *Stein* v. *Geonerco, Inc.*, 17 P.3d 1266, 1270-71 (Wash. Ct. App. 2001).

[7] This Court has frequently noted that a party agreeing to arbitration is agreeing to a different forum with different procedures. *See Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628

courts, or state legislatures, to label certain arbitration procedures unconscionable merely because they are alternatives to litigation would eviscerate the FAA.[8]

Individual arbitration of small claims is not an unconscionable process. On the contrary, as Congress recognized when it passed the FAA, arbitration is typically both faster and cheaper than litigation, *see* S. Rep. No. 68-536, at 3 (1924), and Congress has reiterated that view in more modern times.[9] *See also* Lewis L. Maltby, *Private Justice: Employment Arbitration and Civil Rights*, 30 Colum. Hum. Rts. L. Rev. 29, 55, 56-57 (1998); Robert A. Gorman, *The Gilmer Decision and the Private Arbitration of Public Law Disputes*, 1995 U. Ill. L. Rev. 635, 646; Christopher R. Drahozal, *"Unfair" Arbitration Clauses*, 2001 U. Ill. L. Rev. 695, 755 (2001) (noting the cost for consumers to arbitrate is decreasing "as arbitration institutions compete to provide low-cost arbitration") (footnote omitted); *cf. Green Tree Financial Corp.-Alabama* v. *Randolph*, 531 U.S. 79, 95 & n.2 (2000) (Ginsburg, J., concurring) (discussing the low cost of arbitration). As the Court noted in *Allied-Bruce*, arbitration is par-

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(1985); *see also Gilmer*, 500 U.S. at 26, 32; *Rodriguez de Quijas* v. *Shearson/American Express, Inc.*, 490 U.S. 477, 480 (1989); *Shearson/American Express, Inc.* v. *McMahon*, 482 U.S. 220, 229-30 (1989).

[8] *See Doctor's Assocs.*, 517 U.S. at 687 (holding that States are "precluded . . . from singling out arbitration provisions for suspect status"); *Perry*, 482 U.S. 483 (striking California statute prohibiting arbitration of wage collection actions); *Southland Corp.* v. *Keating*, 465 U.S. 1, 13 (1984) ("[T]he purpose of the [FAA] was to assure those who desired arbitration and whose contracts related to interstate commerce that their expectations would not be undermined by . . . state courts or legislatures.") (alterations in original).

[9] *See* H.R. Rep. No. 97-542, at 13 (1982) ("The advantages of arbitration are many: it is usually cheaper and faster than litigation; it can have simpler procedural and evidentiary rules; it normally minimizes hostility and is less disruptive of ongoing and future business dealings among the parties; [and] it is often more flexible in regard to scheduling . . . ."); *see also Allied-Bruce Terminix* v. *Dobson*, 513 U.S. 265, 280 (1995).

ticularly "helpful to individuals . . . complaining about a product, who need a less expensive alternative to litigation." *Allied-Bruce*, 513 U.S. at 280 (citation omitted). Thus, "for smaller, simpler, more routine cases, it is hard to beat administered arbitration." Berthold H. Hoeniger, *Commercial Arbitration Handbook* § 3.10 (1st ed. 1990, rev. 1-1991); *see also* Anne Brafford, *Arbitration Clauses in Consumer Contracts of Adhesion: Fair Play or Trap for the Weak and Unwary?*, 21 J. Corp. L. 331, 333 (1996) (citation omitted) ("Many consumer disputes, which often involve simple factual issues, can be resolved quickly and relatively cheaply through arbitration."). Finally, studies suggest both that arbitration is fair to consumers[10] and that those who participate in arbitration are widely satisfied that their cases were handled fairly.[11]

II. FORCED CLASS ARBITRATION CANNOT BIND ABSENT CLASS PLAINTIFFS.

By allowing each plaintiff to pursue a forced class arbitration, the South Carolina court not only rewrote the arbitration agreements that Bazzle and Lackey each had with Green Tree but also purportedly altered the rights of each absent class member. *Bazzle* upheld a process that imposed upon absent class members a proceeding they did not choose to bring, before a decision maker not selected in accordance

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[10] *See* Maltby, 30 Colum. Hum. Rts. L. Rev. at 46-48 (comparing Lisa Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 Employment Rts. & Employment Pol'y J. 189 (1997) with data from federal district courts) (comparing the results individuals obtain in arbitration with the results they obtain in court for similar cases and finding that individuals are four times more likely to prevail in arbitration than in traditional litigation); *see also* Jessica Pearson, *An Evaluation of Alternatives to Court Adjudication in Consumer Dispute Resolution* 322 (ABA Special Comm. on Dispute Res. 1983)

[11] *See* Gary Tidwell et al., *Party Evaluation of Arbitrators: An Analysis of Data Collected from NASD Regulation Arbitrations* 25 (Aug. 5, 1999) (presented to the National Meeting of the Academy of Legal Studies in Business).

with their own arbitration agreements or any other rule or agreement binding on them. That process also required absent class members to opt out or to proceed with a large number of parties and claims that they did not agree could be included in the resolution of any disputes they may have.

Such a proceeding plainly cannot bind absent plaintiff class members. "It is a principle of general application in Anglo-American jurisprudence that one is not bound by a judgment . . . in which he is not designated as a party or to which he has not been made a party by service of process." *Hansberry* v. *Lee*, 311 U.S. 32, 40 (1940); *see also Pennoyer* v. *Neff*, 95 U.S. 714, 733 (1877) (mem.). Judicial class actions represent a narrow exception to this "deep-rooted historic tradition." *Martin* v. *Wilks*, 490 U.S. 755, 762 (1989) (internal quotations omitted); *see Hansberry*, 311 U.S. at 41. At equity, the "necessary parties" rule required that all parties be joined to an action, no matter how "numerous they may be." *West* v. *Randall*, 29 F. Cas. 718, 721 (C.C.D.R.I. 1820) (No. 17,424) (Story, J.). Because this rule made litigation simply unmanageable in some instances, equity developed an exception, the predecessor to the modern class action. *Ortiz* v. *Fibreboard Corp.*, 527 U.S. 815, 832 (1999); *West*, 29 F. Cas. at 722; *see also* J. Story, *Commentaries on Equity Pleading* § 97 (J. Gould 10th rev. ed. 1892). From these roots, the modern class action has further evolved to address certain problems.[12]

This Court has carefully guarded the rights of persons who are absent from, yet bound by, this exceptional process. Absent class members may be bound only if a court has followed procedures established by law, including a judicial de-

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[12] As this Court stated in *United States Parole Commission* v. *Geraghty*, 445 U.S. 388, 402-03 (1980), these problems include: "the protection of the defendant from inconsistent obligations, the protection of the interests of absentees, the provision of a convenient and economical means for disposing of similar lawsuits, and the facilitation of the spreading of litigation costs among numerous litigants with similar claims."

termination that they are "adequately represented" by the participants. *See Ortiz*, 527 U.S. at 846; *Martin*, 490 U.S. at 762 n.2; *see also Hansberry*, 311 U.S. at 42. This due process requirement is now embodied, in federal judicial proceedings, in Federal Rule of Civil Procedure 23. This rule was adopted pursuant to the Constitution and the laws of the United States, and determines what is necessary, and generally sufficient, to protect the rights of absent parties (and therefore to make it appropriate they be bound to the result of the class action).

A forced class arbitration lacks any such fundamental protections for absent class members. We emphasize four points: (a) lack of participation in the selection of the arbitrator; (b) the inadequacy of class notice from an arbitrator; (c) the closed proceedings; and (d) the impossibility of assuring the fair settlement of claims on a class basis. *See generally* Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 Wm. & Mary L. Rev. 1, 112 (2000).

a. An absent class member cannot be bound by the decision of an arbitrator chosen by the named plaintiff and defendant. Absent class members may be bound by the decisions in judicial class actions because courts are established by laws binding on all relevant persons. But arbitrators derive their powers solely from the particular parties' private contract. *Cf. United Steelworkers of Am.* v. *Enterprise Wheel & Car Corp.*, 363 U.S. 593, 597 (1960). When a person has not agreed to have his claims decided by a particular arbitrator, there is no basis by which that arbitrator can assert authority over that person. This point has been made by consumer advocates: "arbitral resolution of the claims of a plaintiff class cannot have preclusive effect on absent class members since arbitrators have no authority to bind absent parties." *See* Brief *Amicus Curiae* of Public Citizen at 23-24, *Green Tree Fin. Corp.—Alabama* v. *Randolph*, No. 99-1235 (U.S. 2000).

Here, the arbitration clause specifically reserved the selection of the arbitrator to the parties whose claims were at issue. ("All disputes, claims, or controversies . . . shall be resolved by binding arbitration by one arbitrator selected by us with consent of you." Pet. App. 110a.) Such a provision is useful. Such a provision is useful in resolving individual disputes, but flawed when applied to a class arbitration. Absent class members cannot be bound by the ruling of an arbitrator they had "absolutely no role in selecting." Sternlight, 42 Wm. & Mary L. Rev. at 112.

This is not merely a procedural nicety. One function of a court in a judicial class action is to protect the absent plaintiff class members against the possibly contrary interests of the named plaintiffs who are supposed to be their representatives. A decisionmaker selected by the named plaintiffs and defendants is not well positioned to play that role. As Professor Sternlight notes, "the arbitrator will have been selected at least in part by the named plaintiffs or their attorneys, not by the absent class members. Thus, it is difficult to see how such an arbitrator would play the role of the court in checking possible self-dealing." *Id.* at 113 (citations omitted).

b. An arbitrator selected by one of the parties is under no obligation to send any particular notice, in any particular manner, to "absent" persons. Moreover, there is no established procedure for judicial determination of the adequacy of either the contents or the method of delivery of an arbitrator's notice. And a notice of a class arbitration is not a notice to which an absent class member has an obligation to respond. In view of the fundamental importance of notice, *see Mullane* v. *Central Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950), these multiple uncertainties about the giving of notice are a further substantial obstacle to binding absent plaintiff class members.

c. The fact that arbitrations are frequently not public and their results are often confidential creates additional problems. Unlike court proceedings, which are presumptively

open, *see, e.g.*, *Press-Enter. Co.* v. *Superior Court*, 464 U.S. 501, 507-08 (1984), arbitration is a private dispute resolution mechanism, whose proceedings are not necessarily memorialized even in a transcript, *e.g.*, Sternlight, 42 Wm. & Mary L. Rev. at 114, and whose resolution is often not supported by a written opinion.[13] This is not a problem (and may be an advantage) in resolving one-on-one disputes, but private proceedings are wholly unworkable where the rights of "absent class members" are being decided. *See Hansberry*, 311 U.S. at 41. Absent class members could have no confidence in the final decision and could not as a practical matter challenge it.

d. Settlements, also, cannot be made demonstrably fair to absent class members. One important objective of the protections afforded in judicial class actions is to prevent "the fraudulent and collusive sacrifice of the rights of absent parties." *Id.* at 45; Alba Conte & Herbert B. Newberg, 2 *Newberg on Class Actions* § 11.65 (4th ed. 2002). The trial judge plays a critical role in preventing class representatives and defendants from engineering a course of litigation or settlement that is unfair to absent class members. But because arbitrators who are selected only by the present parties lack tenure, and have no jurisdiction beyond what the parties have conferred on them, they may be far less willing or able to protect absentees against collusion by the parties who appointed them.

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[13] *See* Steven A. Meyerowitz, *The Arbitration Alternative*, 71 A.B.A. J. 78, 80 (1985) (noting that in general, arbitrations are not open to the public and no record of the proceedings is kept); *see also, e.g.*, *United Steelworkers of Am.*, 363 U.S. at 598 ("[a]rbitrators have no obligation . . . to give their reasons for an award"); *Raytheon Co.* v. *Automated Bus. Sys., Inc.*, 882 F.2d 6, 8-9 (1st Cir. 1989) (holding that arbitrators are not required to issue written opinions); *Sobel* v. *Hertz, Warner & Co.*, 469 F.2d 1211, 1214-15 (2d Cir. 1972) (same). By contrast, objectors in court are free to review the record to assist themselves in attacking any settlement. *See generally* 2 *Newberg on Class Actions* §§ 11.57, 11.58 (discussing the rights of objectors to class settlements).

III. FORCED CLASS ARBITRATION IS UNFAIR TO DEFENDANTS.

Because forced class arbitration decisions cannot be binding on absent plaintiff class members, class arbitration is fundamentally unfair to the defendant. A defendant may face a series of proceedings in which it has no prospect of winning more than the named plaintiff's individual dispute. But the first defeat will purport to provide relief to the entire remaining class. This problem is exacerbated by the lack of requirements for a written record, or an opinion explaining the decision, or an opportunity for substantive review.

This Court has recognized that it is "unfair to allow members of a class to benefit from a favorable judgment without subjecting themselves to the binding effect of an unfavorable one." *American Pipe & Constr. Co.* v. *Utah*, 414 U.S. 538, 547 (1974).[14] Defendants have "a distinct and personal interest in seeing the entire plaintiff class bound by *res judicata* just as [the defendant] is bound." *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 805 (1985); *see also Geraghty*, 445 U.S. at 402-03 (noting that one of the benefits of class actions is "the protection of the defendant from inconsistent obligations"). Preventing defendants who prevail from being subjected to collateral attacks on decisions "is not a mere matter of practice or procedure inherited from a more technical time than ours. It is a rule of fundamental and substantial justice, of public policy and of private peace, which should be cordially regarded and enforced by the courts." *Federated Dep't Stores* v. *Moitie*, 452 U.S. 394, 401 (1981) (citation and internal quotation marks omitted); *see also Parklane Hosiery Co.* v. *Shore*, 439 U.S. 322, 332-33 (1979). Indeed, "central to the purpose for which civil courts have been established, [is] the conclusive resolution of disputes

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[14] The 1966 amendments to the Federal Rules of Civil Procedure were specifically designed to eliminate this sort of one-sidedness, which had been a feature of the so-called "spurious" class action. *See American Pipe*, 414 U.S. at 547.

within their jurisdictions." *Montana* v. *United States*, 440 U.S. 147, 153 (1979) (citations omitted). The important public policies underlying these rules of finality include protecting parties from "the expense and vexation attending multiple lawsuits, conserv[ing] judicial resources, and foster[ing] reliance on judicial action by minimizing the possibility of inconsistent decisions." *Id.* at 153-54; *see also, e.g.*, *Kremer* v. *Chemical Constr. Corp.*, 456 U.S. 461, 467 n.6 (1982); *Allen* v. *McCurry*, 449 U.S. 90, 94 (1981); *Parklane Hosiery*, 439 U.S. at 326.

In a judicial class action "[a] judgment in favor of either side is conclusive in a subsequent action between them on any issue actually litigated and determined, if its determination was essential to that judgment." *Cooper* v. *Federal Reserve Bank of Richmond*, 467 U.S. 867, 874 (1984); *see also, e.g.*, *Phillips Petroleum*, 472 U.S. at 801; *Hansberry*, 311 U.S. at 41-42. As this Court held in *Cooper*, "[u]nder elementary principles of prior adjudication a judgment in a properly entertained class action is binding on class members in any subsequent litigation." 467 U.S. at 874. The requirement is made clear in Rule 23: "'[a]ll members of the class . . . are bound by the judgment entered in the action unless, in a rule 23(b)(3) action, they make a timely election for exclusion.'" *Matsushita Elec. Indus. Co.* v. *Epstein*, 516 U.S. 367, 379 (1996) (citation omitted); *see also Devlin* v. *Scardelletti*, 122 S. Ct. 2005, 2011 (2002) ("appealing the approval of a settlement is [a class member's] only means of protecting himself from being bound by a disposition of his rights he finds unacceptable").

All of these principles are violated by forced class arbitration. Because any decision rendered in a class arbitration cannot be binding on absent plaintiffs, a defendant will achieve finality through a class arbitration only if he loses and each absent class member is satisfied by the amount of damages awarded.

The importance of this point is illustrated in a related context. Under Federal Rule of Civil Procedure 23(f), a court's decision to certify a case as a class action may be immediately appealed. The rule was adopted to address the concern that "[a]n order granting certification . . . may force a defendant to settle rather than incur the costs of defending a class action and run the risk of potentially ruinous liability." Fed. R. Civ. P. 23 (Advisory Committee Notes).[15] But a defendant in a forced class arbitration faces a far worse threat: it has no offsetting chance to *win* a class victory, and it typically has no avenue for immediate appeal of the class determination and has only limited judicial review after an arbitration award has been entered. *See* 9 U.S.C. § 10; *see also, e.g.*, *Flexible Mfg. Sys. Pty. Ltd.* v. *Super Prods. Corp.*, 86 F.3d 96 (7th Cir. 1996); *A1 Ainsworth* v. *Skurnick*, 960 F.2d 939 (11th Cir. 1992).[16]

IV. THE DEFECTS OF FORCED CLASS ARBITRATION CANNOT BE REPAIRED BY INJECTING THE COURTS INTO THE ARBITRATION PROCESS.

Some courts and commentators have suggested that the defects of forced class arbitration can be overcome by significant judicial participation in the arbitration process. *See, e.g.*, Daniel R. Waltcher, Note, *Classwide Arbitration and 10B-5 Claims in the Wake of Shearson/American Express, Inc.* v. *McMahon*, 74 Cornell L. Rev. 380, 404 (1989)

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[15] *See also* Henry J. Friendly, *Federal Jurisdiction: A General View* 120 (1973) (discussing the problem of "blackmail settlements" involved in large scale multistate class actions); *cf. In re Rhone-Poulenc Rorer Inc.*, 51 F.3d 1293, 1294, 1298 (7th Cir 1995) (granting the "extraordinary" relief of mandamus to review district court decision on class certification because of "pressure to settle" even in case where previous similar suits had been won by defendant).

[16] Of course, if *amici* are wrong and defendants can be forced to participate in class arbitrations, fairness would require binding absent class members.

("Classwide arbitration . . . may sacrifice due process protections if court involvement in the proceedings decreases or ceases upon certification."). But this is a suggestion to destroy the arbitration process in order to save it.

Courts that have compelled class arbitration have recognized that "[w]ithout doubt a judicially ordered classwide arbitration would entail a greater degree of judicial involvement than is normally associated with arbitration." *Keating* v. *Superior Court*, 645 P.2d 1192, 1209 (Cal. 1982), *rev'd in part on other grounds sub nom. Southland Corp.* v. *Keating*, 465 U.S. 1 (1984); *see also Blue Cross* v. *Superior Court*, 78 Cal. Rptr. 2d 779, 786-87 (Ct. App. 1998); *Dickler* v. *Shearson Lehman Hutton, Inc.*, 596 A.2d 860, 866 (Pa. Super. Ct. 1991). They have acknowledged that it will be difficult "to avoid judicial intrusion upon the merits of the dispute, or upon the conduct of the proceedings themselves and to minimize complexity, costs, or delay." *Keating*, 645 P.2d at 1209 (citing *Class Wide Arbitration: Efficient Adjudication or Procedural Quagmire?*, 67 Va. L. Rev. 789 (1981)).

This does not adequately state the difficulty. Courts will be compelled "to make initial determinations regarding certification and notice to the class." *Keating*, 645 P.2d at 1209; *see also* Pet. App. 3a (noting that the trial court certified the class in *Bazzle*). But to do so, "it may be necessary for the court to probe behind the pleadings before coming to rest on the certification question." *General Tel. Co.* v. *Falcon*, 457 U.S. 147, 160 (1982). Courts considering certification must understand "the claims, defenses, relevant facts, and applicable substantive law." *Castano* v. *Am. Tobacco Co.*, 84 F.3d 734, 744 (5th Cir. 1996). Courts considering notice proposals would need to understand the entire dispute well enough to approve "the best notice practicable under the circumstances." *Cf.* Fed. R. Civ. P. 23(c)(2). To assure fairness, courts would also be required to "exercise a measure of external supervision" over dismissals and settlements. *Keating*, 645 P.2d at 1209. Such "careful court monitoring" would likely have to continue throughout the litigation. 1 *Newberg*

on Class Actions § 1.13. And of course judicial determinations would be potentially subject to review by higher courts.

All of this would require lawyers, time, and expense, defeating the very purposes arbitration was designed to serve. As the Fourth Circuit noted in another context, such judicial participation would "reduce arbitral proceedings to the status of preliminary hearings. Parties would cease to utilize a process that no longer had finality." *Remmey* v. *PaineWebber, Inc.*, 32 F.3d 143, 146 (4th Cir. 1994).

Forced class arbitration with heavy judicial participation lacks the advantages of either arbitration or judicial class actions. It eliminates the efficiencies of arbitration. And at the same time, as long as there is any substantial role for an arbitrator selected by the parties, and any remaining informality in the process, class arbitration cannot possibly provide the full protections for absent parties that are afforded by the painstakingly worked out procedures for judicial class actions.

V. FORCED CLASS ARBITRATION IS AN ATTACK ON ARBITRATION ITSELF.

The decision below reflects a modern and more sophisticated form of the old judicial hostility toward arbitration, "a judicial disposition inherited from then-longstanding English practice." *Circuit City Stores, Inc.* v. *Adams*, 532 U.S. 105, 111 (2001). Congress passed the FAA "to overcome courts' refusals to enforce agreements to arbitrate." *Allied-Bruce Terminix Cos.* v. *Dobson*, 513 U.S. 265, 270 (1995) (citation omitted); *see also Gilmer* v. *Interstate/Johnson Lane Corp.*, 500 U.S. 20, 28 (1991). In keeping with the FAA, this Court has emphatically rejected the earlier hostility. *See Rodriquez de Quijas* v. *Shearson/American Express, Inc.*, 490 U.S. 477, 480-81 (1989) (citations omitted). "[S]uspicion of arbitration as a method of weakening the protections afforded in the substantive law . . . has fallen far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes." *Id.* at 481 (citation omitted).

Parties enter into arbitration agreements to avoid the expense and delay of litigation. "The desire to avoid the delay and expense of litigation persists. The desire grows with time and as delays and expenses increase." S. Rep. No. 68-536, at 3 (1924). Over the twentieth century, arbitration evolved to provide a quick, inexpensive, and fair alternative to litigation. H.R. Rep. No. 97-542, at 13 (1982). But parties simply will not offer or agree to arbitration provisions that courts have rendered unfair and unworkable. In agreeing to arbitrate, parties weigh costs and benefits. For a court "to read such a [class proceedings] term into the parties' agreement would disrupt the negotiated risk/benefit allocation and direct the parties to proceed with a different sort of arbitration." *Champ* v. *Siegel Trading Co.*, 55 F.3d 269, 275 (7th Cir. 1995) (internal quotation marks, brackets, and citations omitted).

Amici's members, who use standard form lending agreements throughout the United States, face a particular difficulty. They do not know where a customer will reside in the future or where he will initiate proceedings if a dispute arises. They cannot afford to offer arbitration anywhere, if doing so may sometimes subject them to forced class arbitration.

The loss of arbitration would also harm the customers of *amici*'s members. These customers benefit not only because their own disputes are resolved more efficiently, but also because lending companies, including amici's members, can avoid much of the otherwise enormous cost of litigation.

Finally, we note that parties cannot necessarily avoid the threat of forced class arbitration by stating explicitly in their agreements that arbitration will not be done on a class basis. The court below suggested (Pet. App. 22a n.21) that it might reject such a proposition as unconscionable. Some other courts have already done so. Such courts' hostility to arbitration could hardly be more clear, resulting in either forced class arbitration or even court proceedings. *See, e.g.*, *Ting*,

2003 WL 292296, at *20 (arbitration agreement struck because, *inter alia*, it prohibited class proceedings); *Comb* v. *PayPal, Inc.*, 218 F. Supp. 2d 1165, 1175-76 (N.D. Cal. 2002) (same); *ACORN* v. *Household Int'l, Inc.*, 211 F. Supp. 2d 1160, 1171, 1174 (N.D. Cal. 2002) (same); *Lozada* v. *Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087, 1104-05 (W.D. Mich. 2000) (same); *Leonard* v. *Terminix Int'l Co.*, — So. 2d —, 2002 WL 31341084, at *8 (Ala. Oct. 18, 2002) (striking arbitration agreement because it prohibited class proceedings); *Szetela* v. *Discover Bank*, 118 Cal. Rptr. 2d 862, 867-68 (Ct. App. 2002) (compelling arbitration, but striking prohibition on class proceedings), *cert. denied*, 71 U.S.L.W. 3400 (U.S. Feb. 24, 2003) (No. 02-829); *cf. Lytle* v. *CitiFinancial Servs., Inc.*, 810 A.2d 643, 667-68 (Pa. Super. Ct. 2002) (remanding for consideration of whether prohibition on class proceedings was unconscionable).[17]

This Court has held that arbitration agreements are enforceable so long as the parties can effectively vindicate their substantive rights. *See, e.g.*, *Shearson/American Express, Inc.* v. *McMahon*, 482 U.S. 220, 229-30 (1987); *see also Gilmer*, 500 U.S. at 32 (rejecting a claim that "arbitration procedures cannot adequately further the purposes of the ADEA because they do not provide for . . . class actions"). The combination of the cases cited above and the rulings in *Bazzle* is to supply another condition: arbitration agreements must provide for class arbitrations. This is precisely the sort of condition to the enforcement of an arbitration agreement that is forbidden under the FAA.

[17] The majority rule is that arbitration agreements that prohibit class arbitrations or class actions in favor of individual arbitration are fully enforceable under the FAA. *See, e.g.*, cases cited *supra* n.6.

CONCLUSION

For the foregoing reasons, the judgment of the South Carolina Supreme Court should be reversed.

Respectfully submitted,

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FEBRUARY 2003