

**THE TOWER OF *BAZZLE*:  
WHY DUE PROCESS REQUIRES A HYBRID MODEL OF CLASSWIDE ARBITRATION**

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## I. INTRODUCTION

During the late 1970s the United States witnessed the beginning of an uncomfortable courtship between two powerful dispute resolution mechanisms: arbitration and the class action. In 2003, the U.S. Supreme Court announced its approval of their marriage, referred to as classwide arbitration,<sup>1</sup> in *Green Tree Financial Corporation v. Bazzle*.<sup>2</sup> In *Bazzle*, the Court held that where an arbitration agreement is silent regarding classwide arbitration, the arbitrator—not the court—should interpret the agreement to determine whether it permits classwide arbitration.

Unfortunately, the Court’s blessing was mixed. *Bazzle* is on infirm ground for two reasons. First, the Court could only muster a 4-1-4 plurality, and thus *Bazzle* could be easily “overruled” in the future. Subsequent changes in the composition of the Court may further destabilize the plurality that existed at the time *Bazzle* was decided. Additionally, the holding is exceedingly narrow, and leaves lower state and federal courts with wide latitude in handling classwide arbitrations. Second, and more important, subsequent developments in the area of classwide arbitration highlight infirmities in the substance of the *Bazzle* decision itself. It is not clear that *Bazzle* is sound even on its own facts because of the practical management problems it has created for courts and arbitrators, and because of the substantive legal and due process considerations it overlooked.

In light of *Bazzle*’s weaknesses, I argue that California’s “hybrid” model of compelling classwide arbitration when called for, while reserving for the courts certain substantive and due process considerations, is preferable to any “pure” model of classwide

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<sup>1</sup> In this paper I use the term “classwide arbitration,” although the terms “class arbitration” and “class action arbitration” are commonly used and are equally descriptive of the same concept.

<sup>2</sup> 539 U.S. 444 (2003)

arbitration that would preclude such judicial oversight. In that vein, the American Arbitration Association—through its promulgation of classwide arbitration rules—has pointed the way toward a workable solution of which the courts should take note.<sup>3</sup>

In Part II, I frame my argument by drawing the contours of the *Bazzle* decision. I then delve into the problems created by *Bazzle*. In particular, in Part III, I step back from *Bazzle* to provide some general background on arbitration and class actions. I then present the problem of multiple arbitration agreements and their attendant management problems that, as a practical matter, are much better handled by courts rather than arbitrators. In Part IV, I return to *Bazzle* and also introduce the California Supreme Court's decision in *Discover Bank v. Superior Court*.<sup>4</sup> In Part IV-A I argue that California's pre-arbitration use of the unconscionability doctrine, as part of a hybrid approach to classwide arbitration generally, is the appropriate way to deal with classwide arbitration waivers. In Part IV-B, I argue that the logical force that justifies the hybrid model of classwide arbitration extends to due process considerations inherent in any classwide action, including definition of the purported class, the right to notice and an opportunity to be heard, and the right to adequate representation. Indeed, I argue that constitutional procedural due process requirements may actually compel a hybrid model if the interests of absent class members are to be protected. I conclude with a brief review of my arguments in Part V.

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<sup>3</sup> American Arbitration Association Supplementary Rules for Class Arbitrations (Oct. 8, 2003). The AAA Class Arbitration Rules, promulgated shortly after the *Bazzle* decision, permit the arbitrator to make interim awards related to class certification, notice, and so forth, but require the arbitrator(s) to stay the proceedings for thirty days following such awards so that either party may appeal to a court for immediate review.

<sup>4</sup> 113 P.3d 1100 (Cal. 2005)

## II. THE TOWER OF *BAZZLE*: WHO SHOULD SPEAK FIRST?

The essential holding in *Bazzle* is quite narrow: where an arbitration agreement is silent as to classwide arbitration, “the question—whether the agreement forbids class arbitration—is for the arbitrator to decide.”<sup>5</sup> The decision, while of course binding, carries only moderate doctrinal force, as it only commanded a plurality of four Justices, with Justice Stevens concurring in the judgment. The narrow holding, the weak plurality, and subsequent changes in the Court’s personnel all suggest that *Bazzle* is not bedrock. And as will be discussed below in Part III, the practical, legal, and constitutional questions left unanswered by *Bazzle* strongly counsel in favor of its reconsideration.

In *Bazzle* the Court reviewed a decision of the South Carolina Supreme Court, which had held that South Carolina law permits classwide arbitration where the contract between the parties is silent on the matter.<sup>6</sup> In reaching its narrow holding, the Supreme Court reasoned that since the parties in that case had agreed to submit to the arbitrator “[a]ll disputes . . . relating to this contract,” and since the dispute about what the arbitration contract in each case means is a dispute “relating to this contract,” the parties thus “seem to have agreed that an arbitrator, not a judge, would answer the relevant question.”<sup>7</sup> The Court recognized certain limited circumstances where “courts assume that the parties intended courts, not arbitrators, to decide a particular arbitration-related matter,” but the Court confined those circumstances to instances that “typically involve matters of a kind that

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<sup>5</sup> 539 U.S. at 451; *see also Discover Bank v. Superior Court*, 36 Cal. 4th 148, 170-71 (2005) (deriving a “narrow holding” from *Bazzle*’s plurality opinion, when read together with Justice Steven’s concurrence); *but see* David S. Clansy and Matthew M.K. Stein, *An uninvited guest: class arbitration and the federal arbitration act’s legislative history*, 63 *Bus. Law.* 55, 68 (2007) (arguing that the Supreme Court in *Bazzle* did not explicitly *nor implicitly* validate class arbitration.)

<sup>6</sup> 539 U.S. at 447.

<sup>7</sup> *Id.* at 451-52, citing *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995) (arbitration is a “matter of contract”).

‘contracting parties would likely have expected a court’ to decide.”<sup>8</sup> The Court described those circumstances as “gateway matters” relating primarily to the validity or scope of the arbitration agreement. The relevant question as the *Bazze* Court saw it was “what *kind of arbitration proceeding* the parties agreed to,” which the Court held did not concern statutory or judicial procedure, but rather, concerned contract interpretation and arbitration procedure.<sup>9</sup>

*Bazze* leaves unresolved several important questions: Who is better suited to handle complicated management problems where, for example, there are multiple arbitration agreements that cover the same substantive dispute? Who should rule first—the judge or the arbitrator—on whether a classwide arbitration waiver is unconscionable and therefore unenforceable? And perhaps most fundamentally, who should decide questions of class certification, notice, adequacy of representation, and other due process-related class questions? I address each of these open questions in turn.

### **III. ARBITRATION AND CLASS ACTIONS: AN IMPERFECT FIT**

Both arbitration and representative judicial proceedings, including class actions, have relatively long histories.<sup>10</sup> However, it was only in the past 40 years that the two forms of dispute resolution began to overlap, giving birth to the concept of classwide arbitration.<sup>11</sup> In this part, I argue that while arbitration may be suitable to handle some types of class action, arbitration is fundamentally incompatible with other types of class action. In particular, class

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<sup>8</sup> *Id.* at 452, quoting *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 83 (2002).

<sup>9</sup> *Id.* at 453-44 (emphasis in original).

<sup>10</sup> Arbitration is clearly the older of the two, however. See, e.g., 1 Domke on Commercial Arbitration § 2:1 (2007) (tracing the concept of arbitration to ancient mythology, “when the three goddesses asked Paris to award the golden apple to the most beautiful among them,” and finding evidence of arbitration in ancient Egypt and in the roots of the Judeo-Christian culture).

<sup>11</sup> See *Coleman v. National Movie-Dine, Inc.*, 449 F. Supp. 945 (E.D. Pa. 1978) (allowing a class action to proceed as an arbitration).

actions where all parties are bound by the same (or at least very similar) contractual language in an arbitration agreement, may be amenable to resolution through arbitral proceedings. Such actions will usually take the form of damages class actions in the consumer and employment contexts (say against a credit card company for breach of contract, or a large employer on a classwide discrimination theory). The same cannot necessarily be said, however, for defendant class actions, limited fund class actions, injunctive relief class actions, mass torts class actions, and other types of class actions where there is no contractual basis for the dispute.

From its earliest days, arbitration has been a creature of contract. In ancient Rome, “the arbitrator acted by virtue of contract between the parties, and his authority to decide the case came from the contract between them and himself.”<sup>12</sup> Modern arbitration remains grounded in contract law, and thus “generally only parties to an arbitration agreement are bound to participate.”<sup>13</sup> Chapter one of the Federal Arbitration Act (FAA), 9 U.S.C. §§ 1-16, was originally approved by Congress in 1925, and was intended to sanction arbitration as a means of non-judicial dispute resolution in a context of general judicial hostility toward arbitration.<sup>14</sup> Congress was persuaded that arbitration, as an alternative to court proceedings, would provide certain benefits including speed, cost savings, and efficiency; that it would promote compromise between the parties because of its “face to face” nature; and that it would advanced the right of freedom of contract due to its voluntary nature.<sup>15</sup> Another

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<sup>12</sup> Domke, *supra* n. 10 § 2:2, quoting Engelmann, *A History of Continental Civil Procedure*, 259.

<sup>13</sup> *National Broadcasting Co., Inc. v. Bear Stearns & Co., Inc.*, 165 F.3d 184 (2d Cir. 1999); *see also* Domke, *supra* n. 10 § 8:4 (“The national policy fostered by the Federal Arbitration Act (FAA), favoring arbitration, does not require parties to arbitrate without having agreed to do so.”).

<sup>14</sup> David S. Clancy and Matthew M.K. Stein, *An Uninvited Guest: Class Arbitration and the Federal Arbitration Act’s Legislative History*, 64 *Bus. Law.* 55, 57 (2007).

<sup>15</sup> *Id.* at 58-61 (arguing that classwide arbitration does not have these essential characteristics).

important characteristic of modern arbitration is its confidentiality: arbitral awards are generally unpublished, and the proceedings are usually held in private.<sup>16</sup> While many of these benefits have been questioned, the Supreme Court has been firm that “[i]n enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration.”<sup>17</sup>

The class action device, unlike arbitration, is not grounded in contract law. “The class action was an invention of equity . . . mothered by the practical necessity of providing a procedural device so that mere numbers would not disable large groups of individuals, united in interest, from enforcing their equitable rights nor grant them immunity from their equitable wrongs.”<sup>18</sup> That is, the class suit, representative in nature, was created to “enable [the court] to proceed to a decree in suits where the number of those interested in the subject of the litigation is so great that their joinder as parties in conformity to the usual rules of procedure is impracticable.”<sup>19</sup> “By Rule 23 the Supreme Court has extended the use of the class action device to the entire field of federal civil litigation by making it applicable to all civil actions.”<sup>20</sup> A valid judgment or settlement reached through the class action device is

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<sup>16</sup> Michael P. Daly, *Come One, Come All: The New and Developing World of Non-signatory Arbitration and Class Arbitration*, 62 U. Miami L. Rev. 95, 124 (2007) (arguing that while parties often prefer arbitration because of its confidentiality, confidentiality is not an absolute notion, and may be inappropriate in the context of classwide arbitration).

<sup>17</sup> *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984) (discerning only two limitations on the enforceability of arbitration agreements: they must be part of a written maritime contract or a contract “evidencing a transaction involving commerce” and such clauses may be revoked on “grounds as exist at law or in equity for the revocation of any contract”).

<sup>18</sup> *Montgomery Ward & Co. v. Langer*, 168 F.2d 182, 187 (8th Cir. 1948), citing *Hansberry v. Lee*, 311 U.S. 32, 41 (1948)

<sup>19</sup> *Hansberry*, 311 U.S. at 41.

<sup>20</sup> *Montgomery Ward*, 168 F.2d at 187.

generally binding on all class members, even those who do not participate directly in the litigation.<sup>21</sup>

Certification of a class action under Rule 23 is a two step process. First, the class action must meet four prerequisites, generally termed numerosity, commonality, typicality, and adequacy of representation.<sup>22</sup> If the prerequisites are met, the court must then place the dispute into a one of four functional categories of class action, often referred to as “incompatible standards,”<sup>23</sup> “limited fund,”<sup>24</sup> “injunctive relief,”<sup>25</sup> and “damages” or “(b)(3)”<sup>26</sup> class actions. These four categories are not mutually exclusive; there can be a great deal of overlap, and the lines between each category are often blurry. Although a class is usually comprised of plaintiffs, Rule 23 can also be used to bind a class of defendants. The “damages” class action under Rule 23(b)(3) has two important additional prerequisites: first, common questions of law or fact must “predominate” over individualized questions, and second, the class action device must be “superior” to other available methods of dispute resolution.<sup>27</sup> If a damages class action is certified, there are two further additional requirements: the court must direct notice of the action to all class members, and must provide them with an opportunity to opt out of the action if they so choose.<sup>28</sup>

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<sup>21</sup> See generally *Hansberry v. Lee*, 311 U.S. 31; see also Fed. R. Civ. P. 23(c)(2)(B).

<sup>22</sup> Fed. R. Civ. P. 23(a).

<sup>23</sup> Fed. R. Civ. P. 23(b)(1)(A).

<sup>24</sup> Fed. R. Civ. P. 23(b)(1)(B).

<sup>25</sup> Fed. R. Civ. P. 23(b)(2).

<sup>26</sup> Fed. R. Civ. P. 23(b)(3). The term “damages” class actions is underinclusive of all of the kinds of class action that can be certified under Rule 23(b)(3); thus the reference to the more comprehensive but less descriptive “(b)(3)” class actions.

<sup>27</sup> Fed. R. Civ. P. 23(b)(3).

<sup>28</sup> Fed. R. Civ. P. 23(c)(2)(B). The notice and opt-out requirements, mandatory under Rule 23(b)(3), are merely permissive under Rules 23(b)(1) and (b)(2). See Fed. R. Civ. P. 23(c)(2)(A). While Constitutional due process requirements and the Rule 23 notice requirements are not coextensive, see *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 177 (1974), it is arguable that the Constitution requires some minimum amount of notice under any type of class action in certain circumstances. See *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950) (“An elementary and fundamental requirement of due process in any proceeding which is to be

### A. A brief history of classwide arbitration

Overlap between the class action device and arbitration (at least under the FAA) is a relatively recent development. The first known example of a court allowing a class action to proceed as an arbitration under the FAA was the 1978 case of *Coleman v. National Movie-Dine, Inc.*<sup>29</sup> There, the federal district court for the Eastern District of Pennsylvania allowed a class action to proceed as an arbitration, reasoning that doing so would advance the federal policy favoring arbitration, especially where the parties' contract contained no "express provision excluding class actions from arbitration and because there is no forceful evidence of a purpose to exclude such a claim from arbitration."<sup>30</sup> However, the *Coleman* court provided very little reasoning for its decision, merely citing two cases from the First and Second circuits for the proposition that "[a]rbitration should not be foreclosed simply by adding persons to a civil action who are not parties to the arbitration agreement because such an inclusion would thwart the federal policy in favor of arbitration."<sup>31</sup> However, the cases the court relied on had addressed a fundamentally different question: whether a judicial proceeding should be stayed pending arbitration where one or more of the defendants were not party to the arbitration agreement between the plaintiff and another defendant. The courts in those cases were comfortable allowing arbitration to run its course before deciding the dispute between the plaintiff and the remaining defendants. That is quite a different matter from compelling arbitration as a class action. Thus—despite its thin analysis—the

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accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections.”)

<sup>29</sup> 449 F. Supp. 945; *see also* Ian R. Macneil, Richard E. Speidel, Thomas J. Stipanowich, *Federal Arbitration Law: Agreements, Awards, and Remedies under the Federal Arbitration Act* § 18.9.2 (1999) (citing *Coleman* as the earliest known classwide arbitration under the FAA).

<sup>30</sup> 499 F. Supp. at 948.

<sup>31</sup> *Id.*, citing *Hilti, Inc. v. Oldach*, 392 F.2d 368, 369 n. 2 (1st Cir. 1968), *followed by* *Lawson Fabrics, Inc. v. Akzona, Inc.*, 355 F. Supp. 1146, 1151 (S.D.N.Y.), *aff'd mem.*, 486 F.2d 1394 (2d. Cir. 1973). However,

*Coleman* case represents a dramatic move on the part of the court by compelling arbitration as a representative action.

The true watershed moment came in 1982, when the California Supreme Court held that classwide arbitration was available under California law, and provided the analytical framework that was missing from *Coleman* in the now well-known case of *Keating v. Superior Court*.<sup>32</sup> The court emphasized that the same principles that favor class actions generally also favor classwide arbitration. This is especially true in the context of widely used adhesion contracts, which present “ideal cases for class adjudication; the contracts are uniform, the same principles of interpretation apply to each contract, and all members of the class will share a common interest in the interpretation of an agreement to which each is a party.”<sup>33</sup> In this context, and in others, the class suit serves to reduce repetitious litigation and provide small claimants with a means of redress that otherwise would not warrant individual litigation or arbitration. The court’s overriding concern was to avoid situations where “gross unfairness would result from the denial of an opportunity to proceed on a classwide basis.”<sup>34</sup> In holding that classwide arbitration was available under California law, the court pointed to California Code of Civil Procedure section 1281.3, which expressly authorizes consolidation of separate arbitrations under certain circumstances. Citing to both federal and state court decisions for support, the court extended the logic of consolidation of arbitration proceedings to justify classwide arbitration. The court thus found it unlikely that the California Legislature, in adopting section 1281.3, “intended to preclude a court from

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<sup>32</sup> 31 Cal. 3d 584, 645 P.2d 1192 (1982), rev’d in part on other grounds by *Southland Corp. v. Keating*, 465 U.S. 1, 104 S.Ct. 852 (1984).

<sup>33</sup> 31 Cal. 3d at 609, quoting *La Sala v. American Sav. & Loan Assn.*, 5 Cal. 3d 864, 877 (1971).

<sup>34</sup> 31 Cal. 3d at 613.

ordering classwide arbitration in an appropriate case.”<sup>35</sup> The California Supreme Court did not leave trial courts without a role in a classwide arbitration however: “The court would have to make initial determinations regarding certification and notice to the class, and if classwide arbitration proceeds it may be called upon to exercise a measure of external supervision in order to safeguard the rights of absent class members to adequate representation and in the event of dismissal or settlement.”<sup>36</sup> The case was ultimately appealed to the U.S. Supreme Court, which held in part that because the California Supreme Court’s decision was purely a matter of state law and not federal law, the High Court was without jurisdiction to rule on the availability of classwide arbitration under the FAA.<sup>37</sup> That question would be left for another day.

Meanwhile, some courts began to adopt California’s “hybrid”<sup>38</sup> model of classwide arbitration, often approving classwide arbitration in certain so-called “negative expected value” cases, but reserving for the court “such determinations as are necessary to certify the class and provide proper notices,” and requiring trial courts to “retain such supervisory jurisdiction as is necessary to safeguard the interests of the absent class members.”<sup>39</sup> Several federal courts, however, refused to permit classwide arbitration absent an express agreement to arbitrate class claims. Those courts took the view that a United States district court had no

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<sup>35</sup> 31 Cal. 3d at 613.

<sup>36</sup> *Id.*

<sup>37</sup> 465 U.S. at 9.

<sup>38</sup> The word “hybrid” is commonly used to describe California’s approach to classwide arbitration. See *Discover Bank*, 36 Cal. 4th at 157 (“It is [the] important role of class action remedies in California law that led this court to devise the *hybrid* procedure of classwide arbitration in *Keating*...”) (emphasis added) (internal citation omitted).

<sup>39</sup> *Lewis v. Prudential-Bache Securities, Inc.*, 179 Cal. App. 3d 935, 946 (1986); see also *Dickler v. Shearson Lehman Hutton, Inc.*, 408 Pa. Super. 286, 288-89 (1991) (approving classwide arbitration where all contracts in that case contained arbitration clauses, but reserving for the court issues of certification, notice, and adequacy of representation); *Blue Cross of California v. Superior Court of Los Angeles*, 67 Cal. App. 4th 42 (1998) (holding that the FAA does not preempt application of the California classwide arbitration rule).

such authority under Section 4 of the FAA, which requires a federal district court to enforce arbitration agreements “in accordance with the terms of the agreement.”<sup>40</sup>

More than twenty years after *Keating*, the U.S. Supreme Court finally had the opportunity to clarify whether state law classwide arbitration procedures were compatible with the FAA in *Bazzle*.<sup>41</sup> While the Court was unable to form a majority to decide the issue, the four-justice plurality implicitly held that there was no problem of preemption.<sup>42</sup> The Court ultimately held, as discussed in Part II above, that where an arbitration agreement is silent as to classwide arbitration, the question of whether the agreement forbids classwide arbitration is for the arbitrator—not the court—to decide.<sup>43</sup>

## **B. The challenge of multiple arbitration agreements**

A fundamental aspect of all of the classwide arbitration cases to date, from *Keating* to *Bazzle*, is that the purported class of plaintiffs was defined in part in terms of its contractual relationship to the defendant(s). The Supreme Court, in *Bazzle*, was especially mindful of that point, noting that “insofar as the other class members agreed to proceed in class arbitration, they consented as well.”<sup>44</sup> But while courts and commentators have approved of classwide arbitrations where the parties have all agreed to the same arbitration agreement,

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<sup>40</sup> 9 U.S.C. § 4. See, e.g., *Champ v. Siegel Trading Co., Inc.*, 55 F.3d 269, 271 (7th Cir. 1995) (also finding that the FAA precludes consolidation, absent an express agreement to the contrary); accord, *Randolph v. Green Tree Financial Corp.*, 991 F. Supp. 1410, 1423-1424 (M.D. Ala. 1997); *Howard v. Klynveld Peat Marwick Goerdeler*, 977 F. Supp. 654, 665 n. 7 (S.D.N.Y. 1997); but see *New England Energy Inc. v. Keystone Shipping Co.*, 855 F.2d 1, 3 (1st Cir. 1988) (holding that a district court does have the power to order consolidated arbitration where the agreement is silent as to consolidation, but that state law must supply the procedure).

<sup>41</sup> 539 U.S. 444 (2003).

<sup>42</sup> *Id.* Justice Thomas dissented on the ground that the FAA does not apply to proceedings in state courts, thus adding a sixth vote in favor of permitting classwide arbitration under state law. See also *Garcia v. DIRECTV*, 115 Cal. App. 4th 297, 304 n. 4 (2004) (“Implicit in *Bazzle* is the notion that, absent a class action waiver, classwide arbitration is proper under the FAA—but the Supreme Court has yet to say that it is so.”).

<sup>43</sup> 539 U.S. at 451-52 (explaining that courts are to decide certain “gateway” issues such as the validity and scope of the arbitration agreement, but that arbitrators must decide other questions, including “what *kind of arbitration proceeding*” the parties agreed to) (italics in original).

<sup>44</sup> 539 U.S. at 451.

there has been very little—if any—consideration of whether classwide arbitration is suitable for all possible forms of class actions.

At one end of the spectrum, there are a few easy cases where the incompatibility of arbitration and class action is obvious. The defining characteristic of such a class action is the absence of any arbitration agreement between any of the parties. Take, for example, the mass tort case of *Jenkins v. Raymark Industries, Inc.*,<sup>45</sup> where the 5th Circuit approved certification of a class of about one thousand plaintiffs claiming damages for asbestos-related personal injuries. Clearly such a class action would not be referable to arbitration because there was no arbitration agreement between the defendant and any of the plaintiffs. Likewise a class claim for injunctive relief under Rule 23(b)(2), say against a city charged with violating the civil rights of a certain class of its citizens, would not be arbitrable where there was no arbitration agreement between the city and its citizens.

On the other end of the spectrum is a category of class claims that clearly would be amenable to arbitration. The essential element in this category is the existence of an identical arbitration agreement between the defendant and all purported plaintiff class members. Classic examples might include a contractual dispute between a credit card company and its card holders,<sup>46</sup> or an employment dispute between a large employer and a tightly defined class of its employees who all signed the same arbitration agreement.

In between these two endpoints is a murky middle, characterized by the problem of an evolving arbitration agreement. A simple variation on the employment dispute example above illustrates the point. Say the large employer bound all of its employees to a common

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<sup>45</sup> 782 F.2d 468 (5th Cir. 1986).

<sup>46</sup> See, e.g., *Discover Bank v. Superior Court*, 37 Cal. 4th 148 (2005).

arbitration clause during the period of 1970 to 1980, requiring all disputes to be resolved under the rules of the National Arbitration Forum (NAF) by a single arbitrator. But imagine that from 1980 to 1990, it used a different arbitration clause, requiring all disputes to be resolved pursuant to the American Arbitration Association's (AAA) rules by a three-member panel of arbitrators. And imagine further that from 1990-2008, the employer's lawyers once again tinkered with the language of the arbitration clause, changing the applicable law from California to Delaware. Finally, assume that—perhaps due to chronic sloppiness in the Human Resources department—a large number of employees never signed arbitration agreements at all. Now suppose a wage and hour dispute arises that affects a class of employees who were hired at various points between 1970 and 2008, and the employer moves to compel arbitration? Ignore for the moment (and *only* for a moment) the complicating fact that *Bazze* requires the arbitrator(s) to interpret the various arbitration clauses in the first instance to determine whether they prohibit classwide arbitration. What does the court do? Does it refer the case to arbitration under the AAA rules or the NAF rules, where the former specifically provide for classwide arbitration, but the latter do not? Does it create subclasses, referring one class of plaintiffs to arbitration before the AAA, another before NAF, and allowing a third class of non-signatory plaintiffs to proceed in court? If the court does create three such subclasses, who should decide the California-versus-Delaware-choice-of-law issue? Should further subclasses be created along choice-of-law lines? Should the court use its equity powers to “consolidate” the AAA and NAF arbitrations into one proceeding? Can the non-signatory plaintiffs be folded into one of the arbitrations? Or should the motion to compel arbitration be denied, even in the face of the strong national policy favoring arbitration? Or would the variations in the arbitration clauses

cause the class claim to fail under the “commonality” test of Rule 23(a)(2)? Clearly the employer, under these circumstances, might choose to withdraw its motion to compel arbitration. But what if the three groups of plaintiffs were to bring three separate class claims: two demands for classwide arbitration (one before the AAA and one before NAF) and one class action complaint before the court? Would the employer be forced to defend the same substantive claim in three separate forums, potentially facing three inconsistent judgments? Clearly the problem of the evolving arbitration clause is one that could create extremely complicated problems for the classwide arbitration mechanism.

These questions expose a fundamental tension between arbitration and class actions, derived from the fact that the former is a creature of contract, and the latter is a representative action borne of the courts’ equity power. An arbitrator’s jurisdiction is fundamentally derived from the consent of the parties. A judge’s jurisdiction is much broader, and does not require consent. Instead, it ultimately flows from the federal and state constitutions and the laws that Congress and the state legislatures pass pursuant thereto. In the case of multiple arbitration agreements that, despite their procedural differences, cover the same dispute, it is nearly impossible to imagine that an arbitrator could manage the sorting problems outlined above without help from a court. Further, the policy aims of speed, efficiency, and controlling costs would be advanced by permitting judges, not arbitrators, to play the management role when faced with multiple arbitration agreements.

Now recall *Bazzele*, which directs that the arbitrator should decide in the first instance whether the parties’ agreement permits classwide arbitration. It is conceivable that the resolution of that question could turn on what arbitral procedure—the AAA rules or the NAF

rules—was required by the agreement.<sup>47</sup> While the Supreme Court observed that the arbitrators in *Bazzle* were “well situated” to determine “what kind of arbitration proceeding” the parties agreed to in that case,<sup>48</sup> the same would not be true in the context of multiple arbitration agreements. Rather, it is the courts, with their broader power to bring all the parties before them, who are better situated to manage such a situation.

#### IV. UNCONSCIONABILITY AND DUE PROCESS: QUINTESSENTIAL GATEWAY ISSUES

The problem of multiple arbitration agreements is essentially one of management. It is a practical problem posed by a hypothetical that is concededly unlikely to arise very often. But it is not the only problem left unsolved by *Bazzle*.

Two other open questions are whether *Bazzle* would require a trial court to defer to the arbitrator on the unconscionability of classwide arbitration waivers,<sup>49</sup> and on questions of class certification, notice, and adequacy of representation.<sup>50</sup> The few commentators who have addressed the issue tend to take the view that the unconscionability of class action

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<sup>47</sup> As noted above, the AAA rules have special provisions designed to handle classwide arbitration, whereas the NAF rules do not. Should the availability of classwide arbitration turn on whether the rules chosen specifically provide for classwide procedures? Should the parties’ agreement be construed in light of the procedure the parties chose?

<sup>48</sup> *Bazzle*, *supra*, 539 U.S. at 453.

<sup>49</sup> For an excellent argument that the separability doctrine requires the court, not the arbitrator, to decide the unconscionability issue, see Jack Wilson, “No-class-action arbitration clauses,” *State-law unconscionability, and the Federal Arbitration Act: A case for federal judicial restraint and Congressional action*, 23 *Quinnipiac L. Rev.* 737 (2004); see also Monica T. Nelson, *Discover Bank v. Superior Court: the unconscionability of classwide arbitration waivers in California*, 30 *Am. J. Trial Advoc.* 649 (2007); Kathleen M. Scanlon, *Classwide arbitration waivers: the “severability” doctrine and its consequences*, 62-APR Disp. Resol. J. 40 (2007); but see *Hawkins v. Aid Ass’n for Lutherans*, 338 F.3d 801, 801 (7th Cir. 2003) (holding that an unconscionability challenge “must first be considered by the arbitrator”).

<sup>50</sup> For an argument that California’s post-*Keating* “hybrid” model of classwide arbitration is no longer available after *Bazzle*, see Carole J. Buckner, *Toward a pure arbitral paradigm of classwide arbitration: Arbitral power and federal preemption*, 82 *Denv. U. L. Rev.* 301 (2004); see also Kristen M. Blankley, *Class actions behind closed doors? How consumer claims can (and should) be resolved by class-action arbitration*, 20 *Ohio St. J. on Disp. Resol.* 451, 457 (2005) (noting that *Bazzle* does not address the role of courts in a class arbitration, but suggesting that “[i]t would not be surprising if the Court were to later hold that an arbitrator, rather than the court, should handle not only the merits of the claim but also the issues of certification and notice”).

waiver clauses should be for the courts, but that the class certification, notice, and adequacy of representation issues should be left to the arbitrator. However, the California Supreme Court's decisions in *Keating*, and more recently in *Discover Bank*, suggest that at least California courts will proceed with the hybrid model in both cases. Furthermore, they would be correct in doing so: courts should have an early role in addressing unconscionability and due process issues both as a practical matter, to encourage finality by reducing the likelihood of subsequent collateral attacks on the arbitral award by absent class members, and to protect the interests of those same absent class members. Indeed, at least in the context of procedural due process, that result may be constitutionally compelled.

#### **A. Unconscionability**

In *Discover Bank*, the California Supreme court held that “under some circumstances the law in California is that class action waivers in consumer contracts of adhesion are [unconscionable and thus] unenforceable, whether the consumer is being asked to waive the right to class action litigation or the right to classwide arbitration.”<sup>51</sup> In other words, the right to class relief is a substantive right in certain circumstances. The Court held that this might be true even where the parties' agreement selects a governing law, such as Delaware's, that permits class arbitration waivers.<sup>52</sup>

In reaching its holding, the *Discover Bank* court noted that the *Bazzle* court did not address the question “whether that determination of unconscionability should be made by a

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<sup>51</sup> 36 Cal. 4th at 152, 162-63.

<sup>52</sup> 36 Cal. 4th at 173-74 (suggesting that California's unconscionability jurisprudence should weigh heavily in a trial court's choice of law analysis, and instructing that “[i]f California has a materially greater interest than the chosen state, the choice of law shall not be enforced, for the obvious reason that in such circumstance we will decline to enforce a law contrary to this state's fundamental policy”) (internal quotation marks and citation omitted).

court or an arbitrator.”<sup>53</sup> Noting the *Bazzle* Court’s judgment that certain “gateway” or “fundamental” matters are to be left for courts, the California Supreme Court held that “determinations of whether arbitration agreements or portions thereof are deemed to be unconscionable or contrary to public policy” clearly fall within that category.<sup>54</sup>

While the *Discover Bank* holding reflects a minority view,<sup>55</sup> it is completely consistent with the unconscionability jurisprudence in California,<sup>56</sup> and is also correct as a matter of public policy. If courts find that class arbitration or other collective action waivers are enforceable (as they often do), corporations will logically seek to include them in all of their contracts, where possible. Indeed, it would be in their self interest to shield themselves from classwide liability. Such a trend could possibly contribute to the ultimate demise of classwide arbitration, and perhaps the class action itself.<sup>57</sup> Thus one of the best ways for courts to protect classes of consumers, employees, and other parties to widely used adhesion contracts is to use the doctrine of unconscionability the way California does. For courts that

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<sup>53</sup> 36 Cal. 4th at 171.

<sup>54</sup> *Id.*

<sup>55</sup> See *Johnson v. West Suburban Bank*, 225 F.3d 366 (3d Cir. 2000) (enforcing arbitration clause that prevented pursuit of class actions); *Snowden v. CheckPoint Check Cashing*, 290 F.3d 631 (4th Cir. 2002) (holding collective action waivers are not unconscionable); *Livingston v. Associates Fin. Inc.*, 339 F.3d 553 (7th Cir. 2003) (enforcing class action and class arbitration waiver); *Jenkins v. First Am. Cash Advance of Ga.*, 400 F.3d 868 (11th Cir. 2005), *cert. denied*, 126 S.Ct. 1457 (2006) (finding that class action waiver was not unenforceable); *Iberia Credit Bureau v. Cingular Wireless LLC*, 379 F.3d 159 (5th Cir. 2004) (class arbitration waiver not unconscionable under Louisiana law); *but see Kristian v. Comcast Corp.*, 446 F.3d 25 (1st Cir. 2006) (holding a class arbitration unenforceable where it deprives claimant with opportunity to vindicate statutory rights); *Ingle v. Circuit City Stores*, 328 F.3d 1165 (9th Cir. 2003) (class waiver part of unconscionable arbitration clause); *Leonard v. Terminix International Co.*, 854 So. 2d 529 (Ala. 2002) (finding a classwide arbitration waiver unconscionable); *State ex rel. Dunlap v. Berger*, 567 S.E. 2d 265, 278-79 (W. Va. 2002), *cert. denied*, 537 U.S. 1087 (“permitting the proponent of a [contract of adhesion] to include a provision that prevents an aggrieved party from pursuing class action relief would go a long way toward allowing those who commit illegal activity to go unpunished, undeterred, and unaccountable.”).

<sup>56</sup> See *Armandariz v. Found Health Psychcare Servs., Inc.*, 24 Cal. 4th 83 (2000).

<sup>57</sup> For a compelling (and charming) argument that class actions and class arbitrations are on their way to extinction due in part to the success of collective action waivers in adhesion contracts, see Myriam Gilles, *Opting out of liability: The forthcoming, near-total demise of the modern class action*, 104 Michigan L. Rev. 373, 376 (2005) (noting that challenges to such waivers on unconscionability grounds have failed “everywhere except California”).

are serious about advancing the policy at the very core of the class action mechanism, which is “to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action,”<sup>58</sup> they must give serious consideration to more expansive use of the unconscionability doctrine.

That very policy was at the core of the California Supreme Court’s decision “to devise the hybrid procedure of classwide arbitration in *Keating*” as well.<sup>59</sup> However, while it is clear that California courts will continue to use the unconscionability doctrine to protect the rights of consumers and employees to obtain classwide relief (at least until told otherwise by the Supreme Court), not everyone is convinced that California’s hybrid classwide arbitration procedure has survived *Bazzle* as well. Some commentators contend that *Bazzle* and its progeny have completely foreclosed the hybrid model of classwide arbitration.<sup>60</sup> That conclusion, however, is both undesirable and premature.

The very questions left unanswered by *Bazzle* demonstrate why abandoning the hybrid model would be undesirable. While *Bazzle* held that arbitrators should interpret arbitration clauses that are silent as to classwide arbitration waivers, and while some courts (especially California courts) may reserve questions of unconscionability and class certification for themselves, the *Bazzle* court gives little guidance on what should happen where an arbitrator decides that a “silent” arbitration agreement does contain a classwide arbitration waiver. Logically, for a court to determine whether such an implicit waiver would be enforceable, there would either be a stay of arbitration so that the plaintiff could seek judicial review, or the plaintiff would arbitrate individually and challenge the enforceability

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<sup>58</sup> *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 617 (1997).

<sup>59</sup> *Discover Bank*, 36 Cal. 4th at 157, citing *Keating*, *supra*, 31 Cal. 3d 584.

<sup>60</sup> *See, e.g.,* Buckner, *Toward a pure arbitral paradigm*, *supra*, 82 Denv. L. Rev. at 304.

of the implicit waiver after the arbitrators issue a final award.<sup>61</sup> The latter option is clearly undesirable, as it raises the specter of having to completely re-arbitrate the issue on a classwide basis should the court find the implicit waiver unenforceable.<sup>62</sup>

As one commentator has observed, the Supreme Court has often invoked practical considerations when determining whether an issue is a substantive, gateway matter related to arbitrability that is for a court, or whether it is purely procedural or otherwise a matter for the arbitrator.<sup>63</sup> Some practical considerations the Court has considered relate to “duplication of effort,” and whether the arbitrator is “comparatively more expert” or “well situated” to answer a particular question.<sup>64</sup> The plurality decision in *Bazzle* is itself an example of the fine line between what are questions of arbitrability and what are not. There, the Court observed that arbitrators are “well situated” to determine “what kind of arbitration proceeding” the parties agreed to because that question involves contract interpretation and arbitration procedures.<sup>65</sup> That practical consideration may have tipped the balance in *Bazzle*.

But practical considerations raised in light of *Discover Bank* could easily tip the balance back in the other direction. That is, the tension between *Bazzle* and *Discover Bank* creates a serious practical difficulty by leaving one threshold question (whether the contract contains a classwide arbitration waiver) for the arbitrator, and another threshold question (whether such a waiver is unconscionable) for the court. In light of *Bazzle*'s status as a weak

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<sup>61</sup> Jack Wilson, “No-class-action arbitration clauses”, *supra*, 23 Quinnipiac L. Rev. at 782.

<sup>62</sup> *See id.* (also arguing that the former option is also suboptimal, as it “requires litigants to bounce inefficiently between court and arbitration).

<sup>63</sup> *Id.* at 783-785.

<sup>64</sup> *Id.* citing *John Wiley & Sons v. Livingston*, 376 U.S. 543, 556-57 (1964) (holding that a court should decide whether an employer is bound by an arbitration agreement between a union and a company that merged with the employer), *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 85 (2002).

<sup>65</sup> *Bazzle, supra*, 539 U.S. at 453.

plurality opinion, it is possible that Court, with its new composition, could “overrule” *Bazzle* if the full force of the practical morass it created were brought to its attention.<sup>66</sup>

## B. Due Process

Practical considerations are not the only reason why *Bazzle* should be reconsidered, and why predictions about the demise of the hybrid model are premature. Courts would be correct to retain supervisory jurisdiction over class matters on due process grounds as well.

A close reading of *Discover Bank* suggests that at least California will likely continue with its hybrid model unless and until the Supreme Court rules that it may not. In deciding that classwide arbitration waivers are, in certain circumstances, unconscionable under California law, the California Supreme Court recalled its decision in *Keating*, emphasizing that “[w]ithout doubt a judicially ordered classwide arbitration would entail a greater degree of judicial involvement than is normally associated with arbitration.”<sup>67</sup> The court re-asserted that trial courts “would have to make initial determinations regarding certification and notice to the class, and . . . to exercise a measure of external supervision in order to safeguard the rights of absent class members to adequate representation and in the event of dismissal or settlement.”<sup>68</sup> In considering the impact of *Bazzle* on its prior decision, the court could not find “anything concrete that would cause us to reconsider *Keating*’s holding over 20 years ago . . . .”<sup>69</sup> Although it did not specifically hold as much, if the California Supreme Court were presented with an argument that all such issues of class treatment should be left to the

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<sup>66</sup> See Wilson, *supra*, at 791 (suggesting this result).

<sup>67</sup> *Discover Bank*, 36 Cal. 4th at 157, quoting *Keating*, 31 Cal. 3d at 613 (internal citations omitted).

<sup>68</sup> *Id.*

<sup>69</sup> *Id.* at 172 (citing to *Bazzle v. Green Tree Financial Corp.*, 351 S.C. 244 (adopting the California approach to classwide arbitration); *Dickler v. Shearson Lehman Hutton, Inc.*, 408 Pa. Super. 286 (same); American Arbitration Association, Supplementary Rules for Class Arbitrations (Oct. 8, 2003) (providing supplemental rules for classwide arbitration)).

arbitrator, the court would almost certainly rule that such issues are properly construed as “gateway” issues under *Bazzle*, which “contracting parties would likely have expected a court to decide.”<sup>70</sup> That would be a true statement, as well, at least in California where the courts have decided such issues in the classwide arbitration context since *Keating* was decided more than twenty years ago.

More fundamentally, Supreme Court precedent (*Bazzle* notwithstanding) suggests that the hybrid model of classwide arbitration may be constitutionally compelled. While the Supreme Court has not directly addressed the due process requirements of classwide arbitration, it has laid out a framework for analysis in its decisions dealing with class actions generally. In *Phillips Petroleum Co. v. Shutts*, the Court listed minimal procedural due process requirements a class action money judgment must meet if it is to bind absent members of the class; those requirements include notice, an opportunity to be heard, a right to opt out, and adequate representation.<sup>71</sup>

In *Matsushita v. Epstein*, the Court reaffirmed the due process principles applicable to class actions as outlined in *Phillips Petroleum*.<sup>72</sup> Justice Ginsberg, concurring in the judgment, wrote separately to emphasize those due process considerations, especially in the context of a class member’s collateral attack on a prior judgment. Joined by Justices Stevens and Souter, she wrote that, “this Court has recognized the first line responsibility of the states

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<sup>70</sup> *Id.* at 169 (quoting *Bazzle, supra*, 539 U.S. at 452). The Court has, however, shown it is willing to vitiating any arbitration procedure that violates the due process clause of the Fourteenth Amendment. See *United Steelworkers of America v. United States*, 361 U.S. 39, 74-5 (1959) (“Some years ago this Court struck down as unconstitutional state statutes making arbitration of labor disputes mandatory.” (citing *Wolff Packing Co. v. Industrial Relations Court*, 262 U.S. 522 (1923); *Dorchy v. State of Kansas*, 264 U.S. 286 (1924))).

<sup>71</sup> *Phillips Petroleum Co. v. Shutts*, 472 U.S. 798, 812 (1985) (citing *Hansberry v. Lee*, 311 U.S. 32, 42-43, 45 (1940)).

<sup>72</sup> *Matsushita v. Epstein*, 516 U.S. 367, 379-79 (1996) (quoting *Phillips Petroleum* for the proposition that due process for class action plaintiffs requires “notice plus an opportunity to be heard and participate in the litigation,” and “that the named plaintiff at all times adequately represent the interests of the absent class members”).

themselves for assuring that the constitutional essentials are met.”<sup>73</sup> Notwithstanding the obligation of states to ensure that due process rights are protected from the beginning of the class action proceeding, “[f]inal judgments,” she continued, “remain vulnerable to collateral attack for failure to satisfy the adequate representation requirement.”<sup>74</sup>

This due process framework is readily extended to the context of classwide arbitration. There, the “first line responsibility” for ensuring that the minimum constitutional requirements are met lies with the trial court. While those who call for a “pure” arbitral model of classwide arbitration would suggest that the first line responsibility lies with the arbitrator, that conclusion is doubtful. It is not clear that contracting parties can contract away their due process rights, much less the due process rights of those they might later seek to represent in a class action. What is clear is that state and federal trial courts have developed straightforward, tested, and most importantly *transparent* procedures for protecting the due process rights of absent parties. These are outlined in Federal Rule of Civil Procedure 23 and its state law cousins. With the exception of the rules of the American Arbitration Association and JAMS, it is not clear that any other arbitration rules explicitly provide due process protections for absent class members in a classwide arbitration. Instead, issues of class certification, notice, opt-out rights, and adequacy of representation may be left to the discretion of the arbitrator. Arbitrators, unlike judges, get paid only when they take cases, usually on an hourly basis. Thus there are inherent dangers lurking when the

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<sup>73</sup> 516 U.S. at 396 (citing *Hansberry*, 311 U.S. at 42).

<sup>74</sup> *Id.* (citing *Hansberry*, 311 U.S. at 40, 42); *see also* Restatement (Second) of Judgments §§ 42(1)(d) and (e), Comments e and f, pp. 406, 410-412 (1982) (noting, *inter alia*, that judgment is not binding on purportedly represented person where, to the knowledge of the opposing party, the representative seeks to advance his own interest at the expense of the represented person); *see also id.*, § 41, Comment a, p. 394 (if § 42 circumstances exist, “the represented person may avoid being bound either by appearing in the action before rendition of the judgment or by attacking the judgment by subsequent proceedings”).

protection of due process rights is left to the discretion of an arbitrator who arguably has an interest adverse to the absent parties.<sup>75</sup> Courts may therefore be justified in inquiring into the adequacy of the protections afforded by the arbitration rules themselves, as well as any initial decisions made by the arbitrator with respect to the class issues.

There are some who would nevertheless contend that a pure arbitral model is adequate to the task because the arbitrators' award will ultimately be subject to challenge either in a nullification proceeding or in an enforcement action. However, the grounds upon which a court may rely in vacating or refusing to enforce an arbitral award are exceedingly narrow, limited to a showing of fraud, corruption, arbitrator misconduct, or other egregious grounds.<sup>76</sup> Courts are almost never permitted to review the merits of an arbitral award. Thus it is highly doubtful that a retrospective court inquiry into the adequacy of due process protections will truly protect the interests of absent class members.

The better course—and I argue the constitutionally required course—is for courts to make determinations regarding class certification, notice, and adequacy of representation at the front end of the arbitration, leaving the merits of the dispute and other non-due process related procedural matters to the arbitrators.

In addition to meeting the “first line responsibility” of protecting due process rights, there is efficiency to be gained as well. Performing a court-based due process inquiry at the outset will help to shield the arbitrators' award from collateral attack, and will therefore help achieve the finality that all parties (particularly defendants) tend to seek in the class context. And to the extent a meritorious collateral attack does arise after the fact, the plaintiff will

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<sup>75</sup> Similar concerns are inherent in the settlement of any classwide arbitration.

<sup>76</sup> *See, e.g.*, 9 U.S.C. § 10.

have a court record to point to in support of her claim (which would not necessarily be available following a confidential arbitration proceeding).

## **V. CONCLUSION**

On balance there is much to commend the hybrid model of classwide arbitration. It recognizes the fundamentally public aspects of classwide arbitration, and ensures that the court is there to represent those public interests. Classwide arbitration, while not suitable for all class actions, is an important tool for the vindication of certain class claims, primarily in the consumer and employment contexts. However, classwide arbitration is a blend of two very different procedural mechanisms, one which promotes speed, efficiency, simplicity, and confidentiality, and the other which promotes global settlement of small claims alleging widespread harm in the aggregate. Such a blended regime requires compromise. On the class action side, it must be conceded that some kinds of class action are fundamentally incompatible with classwide arbitration. On the arbitration side, the notion that arbitration is completely private must also give way. In a representative action, due process compels a public component, and it is only through court supervision at the outset of a classwide arbitration proceeding that the public dimension can be protected.