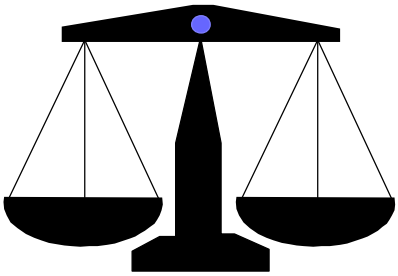

General Counsel Corner

By Peter H. Gunst, Esquire

A New Remedy in Arbitration?

Maybe the biggest problem encountered in litigation is economic imbalance. Too often, the odds are overwhelming against a wronged small business that seeks to take on a behemoth corporate defendant.

The same problems always arise. How can a small plaintiff, which suffered limited damages because of its small size, afford to take on a large corporation? How does it fund the litigation? How can it interest competent counsel if the ultimate payoff is relatively small? How does it survive years of litigation involving multiple proceedings and appeals?

One partial solution has been the class action lawsuit. Litigation may make economic sense if thousands of claims can be aggregated, so that an ultimate award of damages is large enough to whet the appetite of the plaintiffs bar.

But there are pitfalls in the class action approach as well. Because of their bulk and complexity, class actions may rattle around for years -- perhaps a decade or more -- before the defendant pays out a single dollar.

The *Allapattah* discount for cash case against ExxonMobil is a prime example. A great triumph for dealers, but it took over a decade.

In addition, because of the length, complexity and expense of class action litigation, it too often becomes attorney dominated. The plaintiffs become mere figureheads, and any recovery is sliced so thin among class members that the only true beneficiary becomes their counsel. Of course, this is not true about all class actions. But it happens too often.

The major countervailing advantage a small plaintiff has against a large defendant is a right to jury trial. If the plaintiff can survive the economic rigors of pursuing a case to trial, it is likely to find a jury that will be more sympathetic to it than to a corporate octopus.

In large part to eliminate that advantage, numerous corporations place mandatory arbitration provisions in their form contracts. Those provisions appear in everything from franchise agreements to brokerage agreements to commercial lending agreements and well beyond.

Ironically, some recent litigation suggests that a large corporation may *worsen* its litigation posture by inserting arbitration provisions in boilerplate consumer and franchise contracts.

This is because disputes are very often resolved quicker and more cheaply in arbitration than they could

be through litigation. Hence, the large corporation gives up a large part of its advantage of superior economic might and waiting power in arbitration.

The irony occurs when a defendant insists upon arbitration, but then gets hit with a class action anyway, when class treatment is permitted in arbitration. It is unusual, but it can happen.

The United States Supreme Court confronted that situation last year in a case called *Greentree Financial Corp. v. Bazzle*, 123 S.Ct. 2402 (2003). Greentree Financial entered into thousands of commercial lending contracts with mobile home purchasers. They each contained an unremarkable arbitration clause, which stated that --

> [a]ll disputes, claims, or controversies arising from or relating to this contract or to relationships which result from this contract … shall be resolved by binding arbitration by one arbitrator selected by us with consent of you.

When Greentree was faced with two consumer lawsuits filed in South Carolina state courts, it succeeded in having them placed in private arbitration. Unfortunately for Greentree, however, those disputes were resolved in arbitration on a class action basis.

The result was an award of almost $11,000,000 plus attorneys fees against Greentree in one arbitration proceeding, and an award against Greentree of over $9,000,000 and attorneys fees in the other.

Greentree appealed the arbitration awards to the South Carolina state courts. The South Carolina Supreme Court held against it, finding that there was no reason under South Carolina law why an arbitration proceeding could not be decided on a class action basis.

Greentree's final stop was the Supreme Court, where it argued that class action treatment in arbitration was foreclosed by an overriding federal statute, the Federal Arbitration Act, 9 U.S.C. §§ 1 *et seq*.

Greentree sort of lost through a decision in which the Justices showed that they were deeply divided.

Five Justices concluded that the federal act did not foreclose treating the dispute on a class action basis. Four members of that majority, however, were troubled that the class action status might have been imposed by the state court *before* sending at least one of the disputes into litigation.

This was impermissible, those Justices believed, because they concluded that the decision whether or not to resolve the dispute as a class action should have been made in the first instance by the arbitrator, and not by any judge.

They sent the proceedings back to the arbitrator to reexamine

the issue of whether the disputes should have been resolved on a class basis. Presumably, if the arbitrator so concludes, the awards will go into effect.

Three Justices dissented. They believed that class action treatment was improper as a matter of law under the arbitration statute because they interpreted the contract as giving Greentree the right to select different arbitrators in its separate disputes with each individual customer. That reading of the contract, of course, would be utterly inconsistent with class action treatment, in which a single arbitrator decides all claims as to all class members.

Significantly, even the dissenting Justices did not hold that the federal act would absolutely prohibit class actions in arbitration in all instances. Rather, their concern was with what they read to be a limitation in the specific arbitration contract at issue.

As is often the case, Justice Thomas went his own unique way. He would not have disturbed the decision of the South Carolina Supreme Court because of his belief that the federal act should never be used to disturb a state court's interpretation of a private arbitration agreement.

Of course, it may be expected that sharp-eyed corporate counsel will now revise as many of their boilerplate arbitration provisions as possible to expressly forbid arbitrators from granting class action status. Because arbitration is a matter of contract law, such a restriction would likely hold up, if agreed to by the franchisee or consumer.

But there are a multiple of arbitration agreements still in effect that contain no such limitation. It will be interesting to see if a movement arises to utilize class action remedies in arbitration to redress the economic imbalance between the small claimant and its giant adversary.

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