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Class Action Waivers in Commercial Agreements

Comparing Their Treatment in the United States and Canada

By Jennifer Dolman and Matthew Thompson

In recent years, commercial parties such as franchisors have become increasingly proactive in addressing their exposure to class actions. One preventative measure that parties often take is to include clauses in their commercial agreements requiring that all disputes be resolved by arbitration. Many such clauses also include language specifying that a right to participate in a class action (or a class-wide arbitration) is waived. Despite agreeing to such class action waivers, plaintiffs in certain cases have nevertheless attempted to bring class actions, arguing that the waivers are unconscionable, and therefore unenforceable. While the legal status of class action waivers is evolving in the United States, largely due to a U.S. Supreme Court decision earlier this year, franchisors that operate in the United States and Canada also should be aware of the differences in how the two countries address this important element of franchise contracts.

First, a quick review. Earlier this year, the U.S. Supreme Court considered the enforceability of class action waivers in *AT&T Mobility LLC v. Concepcion et ux.*, 131 S. Ct. 1740 (2011). In that case, a clause in a cellular telephone contract specified that all disputes arising from the agreement be referred to arbitration, and prohibited class-wide arbitrations. After a dispute arose regarding a tax payable on free phones, the plaintiffs sued AT&T in California federal District Court. AT&T sought to enforce the class action waiver and stay the proceeding. The plaintiffs cited a California rule that invalidated most class action waivers in consumer contracts. Writing for a 5-4 majority, Justice Antonin Scalia overturned the California rule, enforced the waiver, and stayed the action.

Some have predicted that this decision will shelter arbitration clauses, and class action waivers particularly, from attack in the consumer context, thereby marking the demise of consumer class actions in the United States. This, of course, remains to be seen. What is clear following *AT&T Mobility*, and most relevant

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in the franchise context, however, is that class action waivers are not inherently unconscionable under American law. It remains permissible for commercial parties such as franchisors to include these waivers in their commercial agreements, and in many cases they will be enforced.

CLASS ACTION WAIVERS IN CANADA

Like their American counterparts, Canadian businesses often include class action waivers in their commercial agreements. As in the United States, these clauses have also failed to dissuade Canadian plaintiffs from pursuing class actions in many instances.

In a 2008 decision, 2038724 *Ontario Ltd. v. Quizno's Canada Restaurant Corp.*, (2008), 89 O.R. (3d) 252, (overturned on other grounds) ("*Quizno's*"), the Ontario Superior Court of Justice heard a motion to certify a franchise class action. Amongst other violations, the franchisees alleged that the franchisor was in breach of Canadian antitrust legislation. Quizno's brought a concurrent motion to stay the action on the basis of a class action waiver in the franchise agreement.

Significantly, *Quizno's* appears to represent the first occasion in which a Canadian court has considered the validity of a class action waiver. Unlike in *AT&T Mobility*, the class action waiver in *Quizno's* did not form part of an arbitration clause, but stood as its own clause. Writing for the court, Justice Paul Perell noted, however, that the distinction between a stand-alone class action waiver and a waiver incorporated into an arbitration clause was insignificant, and that the analysis of such clauses would be similar. *Id.* at 70. Perell refused to stay the action on the basis of the class action waiver, but made clear that by so doing he was not striking down all such waivers:

> An agreement to preclude class proceedings is not an obvious evil, and its enforcement should be determined by the balancing of public interests. An appropriate place to do that balancing is in the context of determining the preferable procedure. *Id.* at 77.

To clarify, the Ontario test for certification of a class action (which is similar to the test employed by courts across Canada) includes five criteria, one of which requires the moving party to establish that a class proceeding would be a preferable procedure for the resolution of the common issues. The issue is decided by reference to the three principal advantages of class actions: judicial economy, access to justice and behavior modification. While Perell clearly did not hold that class action waivers are inherently unenforceable, he also did not find them to be determinative of the issue of whether an action should be permitted to proceed. Such waivers, rather, were relegated to the position of one, amongst many, factors in the analysis of whether a class action should be certified.

The issue of the enforceability of a class action waiver was also considered recently by the Supreme Court of Canada in *Seidel v. Telus Communications*, 2011 SCC 15 ("*Seidel*"). In that case, the court was asked to decide whether Seidel could bring a class proceeding against Telus, her cellular telephone service provider. Seidel alleged that Telus engaged in deceptive business practices in violation of various provisions of British Columbia's Business Practices and Consumer Protection Act, S.B.C. 2004, c. 2 ("BPCPA"). Telus argued that Seidel should not be permitted to bring the suit because her contract contained an arbitration clause that expressly waived

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any right to participate in a class action. Telus applied for a stay of the action pursuant to Section 15 of B.C.'s Commercial Arbitration Act, R.S.B.C. 1996, c. 55, s. 15, which requires that a court stay any legal proceeding commenced by a party to an arbitration agreement against another party to the agreement.

A majority of the Supreme Court of Canada stayed all of Seidel's claims, except for one brought under Section 172 of the BPCPA. Section 172 allows any individual, whether or not he or she is affected by a particular transaction, to bring an action in B.C. Supreme Court to restrain a supplier from contravening the statute. The court characterized such an individual as a "public interest litigant." Conversely, the court stayed Seidel's action under another provision of the BPCPA (Section 171) which permits a private litigant to bring an action, but makes no reference to the B.C. Supreme Court.

Rather than assert a general view as to whether class action waivers are enforceable, the Supreme Court of Canada relied upon a strict textual interpretation of the BPCPA as the basis for invalidating the class action waiver in one context but not another:

> Ms. Seidel argues that class action waivers are unconscionable in any event. Picking up on some U.S. jurisprudence, she notes that "an important number of courts, principally state courts from California and Illinois, as well as the 9th Circuit, consider pre-dispute arbitration agreements to be unconscionable, especially when they are coupled with waiver of class proceeding rights" (A.F., at para. 88). *It is not necessary on this appeal to determine whether class action waivers are unconscionable* (and I do not purport to do so) because in my view, as a matter of interpretation, the TELUS class action waiver is not severable from the arbitration clause as a whole, and as a whole it is rendered void by s. 3 of the BPCPA. [Emphasis added] *Id.* at 45.

The court thereby adopted a permissive approach with respect to class action waivers and arbitration clauses generally. It appears as though a class action brought by a party that agreed to waive its right to participate in a class action will only proceed where that party is able to cite Canadian legislation that permits it to do so.

Unlike in *Quizno's*, where the Ontario court insisted that the enforceability of a class action waiver be considered in the context of the preferable procedure analysis at certification, the Supreme Court of Canada in *Seidel* considered this issue prior to certification. Whereas the Ontario court considered the existence of the waiver as one amongst other factors in determining whether a class action should proceed, the Supreme Court of Canada considered the enforceability of the clause as a threshold question. It remains to be seen how subsequent courts will approach the issue.

On the basis of the above, we draw the following conclusions regarding the status of class action waivers in Canada:

1. Class action waivers are not inherently inconsistent with the purposes of class action legislation and are not automatically unenforceable.
2. Parties should not assume that class action waivers will shield them from class proceedings in all cases. Indeed, if these clauses were infallible, none of the plaintiff's claims in the *Seidel* case should have been permitted to proceed to certification.
3. A franchisee who wishes to escape a class action waiver will likely need to cite legislation permitting it to do so. In provinces with franchise disclosure legislation, franchisees may rely on their right to associate, which in Ontario has been interpreted by the Court of Appeal in *405341 Ontario Limited v. Midas Canada Inc.*, 2010 ONCA 478, as a right to collective action and in particular, a right to a class action.

In the event that a franchisee is able to cite such legislation, a franchisor may be forced to defend a class action waiver by arguing that its enforcement serves the purposes of judicial economy, access to justice and behavior modification.

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