December 20, 2024

New Jersey Supreme Court affirms class action waiver untethered to an arbitration agreement

by C. Allen Garrett Jr.

Takeaway: Following the U.S. Supreme Court's landmark decision in *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011), numerous courts have upheld class action waiver clauses in mandatory arbitration agreements. But relatively few decisions have addressed the enforceability of class action waivers untethered to arbitration agreements. Earlier this year, however, the New Jersey Supreme Court upheld a class action waiver in a residential lease agreement that did not contain an arbitration agreement. *Pace v. Hamilton Cove*, 317 A.3d 477 (N.J. 2024). The *Pace* decision introduces a new variable into the calculus of whether companies that face class actions must utilize mandatory arbitration agreements to avoid class litigation.

In *Pace*, residential tenants signed leases that included a broad class action waiver—expressly waiving their right to "bring, represent, join, or otherwise maintain a Class Action or similar proceedings against us or our agents in forum"—but did not include an arbitration agreement. 317 A.3d at 482. After allegedly discovering that, contrary to its advertising, the apartment complex did not provide "24/7 security," the tenants filed a putative class action against the complex that alleged common law fraud and a violation of New Jersey's Consumer Fraud Act ("CFA"). *Id.* The complex moved to dismiss or, alternatively, to strike the plaintiffs' class allegations based on the class action waiver. In response, the tenants challenged the lease agreements as "unconscionable and contracts of adhesion." *Id.*

The trial court denied the complex's motion and the Appellate Division affirmed, holding that "'a class action waiver in a contract that does not contain a mandatory arbitration provision' is unenforceable as a matter of law and public policy." *Id.* at 483 (quoting *Pace v. Hamilton Cove*, 295 A.3d 1251, 1258 (N.J. App. Div. 2023)). The New Jersey Supreme Court granted leave to appeal. *Id.* at 484.

The Supreme Court first disagreed with the Appellate Division's bright-line rule requiring class action waivers to be linked with mandatory arbitration agreements. While class action waivers "are frequently paired with arbitration provisions to prevent class arbitration," that fact "does not mean that an arbitration provision is necessary to a class waiver's enforceability." *Id.* at 487. And even if class actions "advance several important policy goals," that alone does not preclude waiver: "Our law supports the contractual waiver of many rights that advance important goals, such as the constitutional right to a jury trial, provided that the requisite procedural safeguards surrounding the waiver are met." *Id.*

Despite New Jersey's "'strong public policy in favor of freedom to contract,'" legislatures "can override the freedom to contract in specific settings." *Id.* (quoting *Boyle v. Huff*, 314 A.3d 793, 802 (2024)). Thus, courts construing the Fair Labor Standards Act (which specifically authorizes class action) and similar state statutes expressly authorizing class actions have refused to enforce class action waivers. *Id.* at 487-89. But in *Pace*, there was "neither a controlling statutory provision that expressly permits class actions" nor a "clear statement of public policy disfavoring class action waivers." *Id.* at 489. In such a case, the absence of a mandatory arbitration agreement does not render a class action waiver "per se unenforceable," but rather requires individualized review to determine enforceability "under general contract principles." *Id.*

Turning to an examination of the lease agreements' unconscionability, the Supreme Court listed the four factors New Jersey courts consider: "(1) the subject matter of the contract, (2) the parties' relative bargaining positions, (3) the degree of economic compulsion motivating the adhering party, and (4) the public interests affected by the contract." *Id.* Factor one implicated the CFA, which applies to a "consumer contract for housing." *Id.* at 492. But factor two did not "particularly favor plaintiffs or defendants," because the tenants "had time to consult with an attorney" regarding the "take-it-or-leave-it" lease agreement and "were free to seek out alternative housing arrangements if they did not agree with the lease's terms." *Id.*

For similar reasons, factor three (economic compulsion) did not favor plaintiffs, who "did not face 'a monopolistic market,' and likely had the ability to choose from 'a vast selection' of apartments available for a monthly rent comparable to the $3,700 rent at issue here." *Id.* (citation omitted). Nor did factor four (public interests) support invaliding the lease agreements as unconscionable: "The class action waiver here does not prohibit plaintiffs, and similarly situated tenants of Hamilton Cove, from individually vindicating their statutory rights under the CFA, which allows for treble damages and recovery of attorneys' fees for successful claims." *Id.* at 493. Because the class action waiver "does not functionally operate as an exculpatory clause," the *Pace* court held that, "on balance, the waiver is not unconscionable." *Id.*

By upholding a class action waiver not contained within a mandatory arbitration agreement, the New Jersey Supreme Court increased the complexity of a potential class action defendant's analysis regarding potential utilization of an arbitration agreement. The recent rise in "mass arbitrations" has created a potential cost for arbitration agreements in at least some circumstances, particularly since courts have not yet settled upon an enforceable mass arbitration framework palatable to potential defendants. Assuming other courts follow *Pace* and enforce class action waivers outside of arbitration agreements, defendants concerned about mass arbitrations can evaluate whether a class action waiver untethered to an arbitration agreement in their consumer agreements would be found unconscionable. If it appears such a waiver would be enforced, these defendants could omit a mandatory arbitration agreement and thereby avoid the risk of a mass arbitration.