

Arbitration of a Data Breach Lawsuit: Defeating Class Actions with Arbitration Clauses and Class Waivers

The number of data breach class actions has surged in recent years, and this trend shows no signs of slowing down. In 2022, an average of thirty-three data breach class actions were filed in federal court every month. In June of 2023 alone, over sixty were filed. Are there alternatives to fighting battles in open, public courts? Are there options to potentially reduce the costs of litigation in lawsuits?

Arbitration clauses and class action waivers can be a possible solution. This article discusses how arbitration clauses have been used in data breach cases and whether they might be considerations in the future.

Benefits of Arbitration Clauses

Arbitration can be an effective way to avoid the expensive delays of litigation in court. Larger organizations often prefer arbitration because it bypasses lengthy hearing processes, keeps litigation confidential, and gives the parties a say on who becomes the ultimate decisionmaker. Arbitration clauses may also include class action waivers, which can prevent large groups of people from consolidating their claims. These benefits of arbitration, accompanied by class action waivers, are especially attractive to companies seeking to mitigate the costs of data breach litigation, where organizations may face huge class sizes and significant reputational damage.

Arbitration and Class Waiver Success in Recent Data Privacy Cases

Recently, a district court in Maryland certified classes of over a hundred million people following a data breach involving a customer loyalty program. The defendants soon after appealed the certification rulings. In October 2023, the Fourth Circuit vacated the certification decisions, ruling that the district court must evaluate the existence of a class waiver before a class action can proceed. The presence of an arbitration clause or class action waiver is to be considered at the initial stages of a case. In other words, a class action waiver is not a defense to liability but a defense to being required to litigate a class action at all. Upon remand, the district court reinstated the class certification orders. The court found that the class action waiver provisions

had been waived because the defendant failed to advance the waiver arguments and, instead, agreed to multidistrict litigation in a single court, which it observed was inconsistent with class action waiver.

In another case, the Northern District of California found that the representative plaintiff in a data breach lawsuit had agreed to an online dating service's terms of use which contained a class action waiver. The court then denied the plaintiff's motion for class certification. Similarly, an e-commerce website convinced the Sixth Circuit to dismiss a class action and compel arbitration where its amended terms of service included an arbitration provision. And in another case, a video gamer was prevented from bringing a class action lawsuit because the end user license agreement the plaintiff signed included an arbitration clause.

As these cases show, arbitration clauses and class action waivers can provide significant relief to avoid costly lawsuits. While not every interaction with a company may create an opportunity to include arbitration and class action waiver agreements, such instances do exist where companies enter transactions. For example, arbitration clauses are common in employment agreements and consumer-facing agreements. As mentioned above, terms of service and licensing agreements may include them as well.

Keeping Arbitration Clauses Enforceable

Not all arbitration clauses and class action waivers are enforceable. Mistakes and blind spots increase the risk that a company will be forced to litigate against a class action lawsuit it attempted to avoid with a waiver. Below is a list of steps an organization can take to prepare itself for an enforceability challenge to arbitration provisions in court.

1. **Provide Proper Notice.** When a standard form agreement includes an arbitration clause, courts often look to consent between parties to decide whether the agreement should be enforceable. Courts have found that a plaintiff consents to new or updated arbitration agreements when companies provide conspicuous notice of updates to terms of service. However, imprecise language that fails to clearly explain a consumer's rights does not provide the consumer with proper notice that they have entered an arbitration agreement. Furthermore, while some courts have found that silence from a consumer is enough to prove consent, other courts, like the Supreme Court of Indiana, require a more substantial showing of consent from the consumer, particularly where agreements are amended, and the amendment is to be effective unless rejected by the party. Companies may avoid these consent-related problems by issuing notices that clearly describe a consumer's rights and by requiring an affirmative act on the part of the consumer, like clicking an "accept" button to new terms.
2. **Do Not Waive the Arbitration Right or Class Waiver.** Whether or not a party has a valid arbitration clause, the party can inadvertently waive the right to arbitrate in litigation. The same is true of class waivers. A party waives its arbitration right or class action waiver if it has knowledge of the right and acts inconsistently with that right. Acting inconsistently with an arbitration right includes litigating on the merits without raising the arbitration right first. In a recent Ninth Circuit case, the court found the defendant could

not compel arbitration of absent class members' claims after it had already substantively challenged a representative plaintiff's claims over the course of six years. In another case in the same court, the defendant had *not* waived its arbitration right when it pleaded arbitration as an affirmative defense in its answers to the plaintiff's original and amended complaints. In a recent District of Maryland case, the court found a defendant had waived its argument to force individual actions by, among other things, agreeing to consolidate the action in a jurisdiction different from the waiver's accompanying choice of law provision. This case is a reminder that it is important to consider the full language of an arbitration clause or class waiver provision to ensure that a party does not inadvertently take steps that could invalidate it.

3. **Consider a Jurisdiction's Public Policy.** While arbitration agreements are generally enforceable under the Federal Arbitration Act, courts sometimes will strike down arbitration clauses or class action waivers if the court finds the agreements are unconscionable or contrary to public policy objectives. Public policy objectives are evidenced by laws that explicitly provide for class action rights. For example, this year the District of Rhode Island held that a class action waiver was not enforceable when a plaintiff brought an action under the Rhode Island Deceptive Trade Practices Act. In that case, the waiver ran contrary to Rhode Island's public policy objectives.
4. **Review and Revise.** If an agreement already exists without an arbitration clause or a class action waiver, a company might consider amending the agreement to add one. Courts have typically held that companies can add new arbitration clauses to already existing agreements, provided they meet certain notice requirements. It is important to stay abreast of what the jurisdictional requirements are for arbitration agreements and what the court says about public policy in the state.

Risks and "Mass Arbitration" Developments

The rise of arbitration clauses and their prevalence in the class action space is not without controversy or risk. Activist groups have criticized the prevalence of arbitration clauses and class action waivers as a sort of "get-out-of-jail-free card" that impedes the defense of an individual's right to privacy. And, in a world of "be careful what you ask for," sometimes enforcing class waivers in arbitration can be costly as well.

When a book rental website experienced a data breach, a law firm seeking to exploit an arbitration provision filed 15,107 individual arbitration demands. This "mass arbitration" can be costly for companies that promise in their agreements to bear certain arbitration costs, such as filing fees. In that case, \$300 individual filing fees would add up to approximately \$4.7 million when all the demands were totaled together. In another case, currently in the Seventh Circuit, a company is appealing a district court's order that would require it to pay about \$4 million in arbitration fees in connection with roughly 35,000 individual arbitration demands.