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## Restoring Bankruptcy's Fresh Start

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# RESTORING BANKRUPTCY’S FRESH START

*Jonathan S. Hermann\**

*The discharge injunction, which allows former debtors to be free from any efforts to collect former debt, is a primary feature of bankruptcy law in the United States. When creditors have systemically violated debtors’ discharge injunctions, some debtors have attempted to challenge those creditors through a class action lawsuit in bankruptcy court. However, the pervasiveness of class-waiving arbitration clauses likely prevents those debtors from disputing discharge injunction violations outside of binding, individual arbitration. This Note first discusses areas of disagreement regarding how former debtors may enforce their discharge injunctions. Then, it examines the types of disputes that allow debtors to collectivize in bankruptcy court. Without seeking to resolve either disagreement, this Note assumes debtors may collectivize in this context and employs an “inherent conflict” test that looks to whether disputes over discharge injunction violations are arbitrable. Because the “inherent conflict” test likely leads to the conclusion that courts must enforce class-waiving arbitration clauses, this Note argues that Congress should amend the Bankruptcy Code not only to provide debtors an express right of action under § 524 and the ability to collectivize, but also to prohibit the arbitration of these claims. Doing so will give full effect to the discharge injunction and fulfill the promise to debtors that they can truly begin anew after bankruptcy.*

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#### INTRODUCTION

Consider the case of an individual who emerges from bankruptcy. Upon the closing of his bankruptcy proceeding, the bankruptcy court absolved him of all his remaining outstanding debt by way of a "discharge injunction."<sup>1</sup> However, he soon discovers that a creditor with whom he had an outstanding balance prior to filing for bankruptcy—a credit card company, for example—has not recognized that injunction.<sup>2</sup> Perhaps the creditor failed to report the debt to consumer reporting agencies as having been discharged, resulting in

1. For a discussion of discharge injunctions in personal bankruptcy, see *infra* Part I.A.

2. See generally Jessica Silver-Greenberg, *Debts Canceled by Bankruptcy Still Mar Consumer Credit Scores*, N.Y. TIMES (Nov. 12, 2014, 9:45 PM), <https://www.dealbook.nytimes.com/2014/11/12/debts-canceled-by-bankruptcy-still-mar-consumer-credit-scores/> [https://perma.cc/JLX2-ADMV].

the debt remaining on the individual's credit reports.<sup>3</sup> Or perhaps the creditor is still attempting to collect the debt<sup>4</sup> or has even filed action in state court to collect on that debt.<sup>5</sup>

Furthermore, our former debtor has discovered that he is not alone; the same creditor has failed to recognize the debts of many other former debtors as discharged. Because it may not be cost effective to dispute the claims in court on an individual basis, he files his claim as a class action.<sup>6</sup> Yet he faces an obstacle: his credit agreement contained a class-waiving arbitration clause in which he agreed to resolve all disputes with his creditor in binding, individual arbitration.<sup>7</sup>

At first blush, it would appear this class-waiving arbitration clause has impermissibly forced the debtor to relinquish his rights. One of the primary purposes of Rule 23 of the Federal Rules of Civil Procedure, which allows plaintiffs to bring class action lawsuits in federal court,<sup>8</sup> is to allow for the “vindication of ‘the rights of groups of people who individually would be without effective strength to bring their opponents into court at all.’”<sup>9</sup> A corollary to this purpose is to allow individual consumers, for whom the cost of litigation would far exceed their potential recovery, to join forces.<sup>10</sup> As Judge Richard Posner famously observed, “The *realistic* alternative to a class action is not 17 million individual suits, but zero individual suits, as only a lunatic or a fanatic sues for \$30.”<sup>11</sup>

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3. *Id.*; see also Fair Credit Reporting Act, 15 U.S.C. § 1681s-2(a)(1)(A) (2012) (prohibiting creditors from knowingly furnishing inaccurate information to consumer reporting agencies).

4. See, e.g., Jason Green, *California Cellphone Robocalls: Debt Collection Giant iQor Sued for \$10 Million*, MERCURY NEWS (Sept. 14, 2016, 11:23 PM), <http://www.mercurynews.com/2016/09/14/santa-clara-county-debt-collection-giant-iqor-hit-with-10m-robocall-lawsuit/> [<https://perma.cc/8ZU6-FWSX>] (discussing a credit collection agency's alleged attempts to collect discharged debt by calling former debtors).

5. See, e.g., *Miller v. Chateau Cmtys., Inc. (In re Miller)*, 282 F.3d 874, 875–76 (6th Cir. 2002).

6. See Kara Bruce, *The Debtor Class*, 88 TUL. L. REV. 21, 37–38 (2013) (arguing that an individual plaintiff suing an institutional creditor for systematic misconduct may be “priced out of litigation”).

7. Indeed, arbitration clauses frequently contain class waivers. See CONSUMER FIN. PROT. BUREAU, ARBITRATION STUDY: REPORT TO CONGRESS, PURSUANT TO DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT § 1028(a) 10 (2015), [http://www.files.consumerfinance.gov/f/201503\\_cfpb\\_arbitration-study-report-to-congress-2015.pdf](http://www.files.consumerfinance.gov/f/201503_cfpb_arbitration-study-report-to-congress-2015.pdf) [<https://perma.cc/RVT4-23X4>] (finding nearly all arbitration clauses studied include class waivers); Theodore Eisenberg et al., *Arbitration's Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts*, 41 U. MICH. J.L. REFORM 871, 880, 884 (2008) (collecting a sample of consumer contracts of major telecommunications, credit, and financial services companies and finding that every consumer contract that contained a mandatory arbitration clause also included a class waiver).

8. FED. R. CIV. P. 23.

9. *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997) (quoting Benjamin Kaplan, *A Prefatory Note*, 10 B.C. INDUS. & COM. L. REV. 497, 497 (1969)).

10. See Brief for Professors of Civil Procedure & Complex Litigation as Amici Curiae Supporting Plaintiff-Appellee at 3, *Carrera v. Bayer Corp.*, No. 12-2621, 2014 WL 3887938 (3d Cir. May 2, 2014) (arguing that “small-value consumer cases . . . necessitated Rule 23”).

11. *Carnegie v. Household Int'l, Inc.*, 376 F.3d 656, 661 (7th Cir. 2004).

Federal bankruptcy law has also recognized the importance of class action lawsuits by allowing bankruptcy courts to hear class actions.<sup>12</sup> However, despite our former debtor's procedural right under federal law to sue as a representative of a class, there is a dispute as to whether he can overcome the class-waiving arbitration clause.<sup>13</sup> In 2013, the U.S. Supreme Court held in *American Express Co. v. Italian Colors Restaurant*<sup>14</sup> that Rule 23 does not establish "an entitlement to class proceedings for the vindication of statutory rights."<sup>15</sup> In other words, Rule 23 is merely a procedural mechanism and does not itself provide litigants with a substantive right to litigate as a class. Therefore, a litigant may overcome a class-waiving arbitration clause if the federal law under which he is seeking to recover creates a substantive right to class litigation.<sup>16</sup> Absent such a right, a plaintiff may only override such a clause if it were drafted to prevent a "prospective waiver of a party's right to pursue statutory remedies."<sup>17</sup> In the case of our former debtor, this would mean he must show that the Bankruptcy Code somehow indicates Congress did not intend for class-waiving arbitration clauses in credit agreements to be enforceable in bankruptcy.

However, there is uncertainty regarding the *Italian Colors* decision's impact on bankruptcy courts, both with respect to determinations of arbitrability and to the enforceability of class waivers.<sup>18</sup> Although the Bankruptcy Code does not expressly grant debtors a substantive right to litigate as a class, there remains an open question as to whether federal laws may nevertheless provide such a right absent express language. For example, some circuits have held that the National Labor Relations Act (NLRA) guarantees employee class actions, despite the lack of any express

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12. FED. R. BANKR. P. 7023 (stating that Rule 23 applies in adversary proceedings). Although many class actions in bankruptcy concern a class of creditors suing a common debtor, they may also involve a class of debtors suing a creditor for a common injury. See Bruce, *supra* note 6, at 42; see also *infra* Part III.

13. This dispute is perhaps most evident in a recent intradistrict split in the Southern District of New York, discussed in Parts I.D.2 and IV. Compare *Belton v. Ge Capital Consumer Lending, Inc.* (*In re Belton*), No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*3 (S.D.N.Y. Oct. 14, 2015) (reversing the bankruptcy court's decision denying creditor's motion to compel individual arbitration pursuant to a class-waiving arbitration clause), with *Credit One Fin. v. Anderson* (*In re Anderson*), 553 B.R. 221, 233–34 (S.D.N.Y.) (affirming the bankruptcy court's decision refusing to compel arbitration of a discharge injunction violation), *appeal docketed*, No. 16-2496 (2d Cir. July 13, 2016), and *Credit One Fin. v. Anderson* (*In re Anderson*), 550 B.R. 228, 235 (S.D.N.Y.) (declining to review the bankruptcy court's decision refusing to enforce a class-waiving arbitration clause), *appeal docketed*, No. 16-2496 (2d Cir. July 13, 2016). At present, the Second Circuit has yet to resolve this split. See generally *In re Anderson*, 550 B.R. 228.

14. 133 S. Ct. 2304 (2013).

15. *Id.* at 2309 (emphasis added).

16. *Id.* at 2309–10.

17. *Id.* at 2310 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 n.19 (1985)). Although the Court acknowledged that an arbitration forum may, in certain circumstances, be made impracticable by high filing and administrative fees, it nevertheless held that "the fact that it is not worth the expense involved in *proving* a statutory remedy does not constitute the elimination of the right to pursue that remedy." *Id.* at 2310–11.

18. See Kara J. Bruce, *Vindicating Bankruptcy Rights*, 75 MD. L. REV. 443, 475–77 (2016).

guarantee.<sup>19</sup> Therefore, assuming the full effect of *Italian Colors*, there exists somewhat of a spectrum. At one end are certain laws, such as the antitrust laws at issue in *Italian Colors*, which contain no substantive right—express or implied—to bring a class action suit. At the other end are laws such as the NLRA that may provide a substantive right to collectivize through litigation,<sup>20</sup> despite the “liberal federal policy favoring arbitration” more generally.<sup>21</sup>

This Note addresses whether a class-waiving arbitration clause bars our former debtor from challenging a discharge injunction violation as a class in light of the *Italian Colors* decision. Ultimately, it acknowledges that existing case law mandates compelling individual arbitration but argues that the guarantee of a fresh start for former debtors necessitates a legislative remedy to allow former debtors to dispute discharge injunction violations as a class in bankruptcy court.

Part I provides a brief primer of personal bankruptcy law and bankruptcy jurisdiction, the Federal Arbitration Act (FAA), and the test courts employ to resolve conflicts between federal laws—including the Bankruptcy Code—and the FAA. Next, Part II explores how courts have treated postdischarge claims of debtors seeking to enforce their discharge injunction. Such treatment may have significant consequences that could preclude debtors’ ability to dispute discharge injunction violations as a class. Part III then discusses when courts have allowed postdischarge claims to be brought by a putative class of debtors rather than by individual debtors. This discussion is particularly important, for if debtors cannot dispute a discharge injunction violation as a class, they cannot challenge a class waiver in an arbitration clause. Part IV first applies the current test of the arbitrability of federal claims to determine that discharge injunction violations are likely arbitrable. It goes on to discuss whether courts should interpret § 524 of the Bankruptcy Code, which provides for debtors’ discharge injunction, to create a substantive right to collective litigation. It then looks to the effect of *Italian Colors* on bankruptcy courts’ determinations of arbitrability of postdischarge claims brought as a class. Finally, in light of the importance of debtors’ fresh start and the need to weed out systemic debt-collection practices, Part V argues class-waiving arbitration clauses should not be enforced in a postdischarge proceeding under § 524. Because current case law likely mandates the enforcement of such clauses, this Note proposes a legislative remedy through the amendment of the Bankruptcy Code.

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19. *See Lewis v. Epic Sys. Corp.*, 823 F.3d 1147, 1151–52 (7th Cir. 2016) (holding that the NLRA’s guarantee to “engage in other concerted activities” includes the right to adjudicate employment claims as a class such that a class waiver in an employment contract was unenforceable), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-285); *Morris v. Ernst & Young, LLP*, 834 F.3d 975, 983–84 (9th Cir. 2016) (same), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-300).

20. The Supreme Court has granted certiorari to resolve whether the “concerted activities” language in the NLRA does in fact provide for such a substantive right. *See Lewis*, 137 S. Ct. 809 (2017) (No. 16-285).

21. *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

## I. RECONCILING BANKRUPTCY LAWS WITH THE FEDERAL ARBITRATION ACT

The determination of whether class-waiving arbitration clauses are enforceable in postdischarge bankruptcy disputes requires the resolution of a potential conflict of federal laws. One statute—the FAA—requires courts to enforce arbitration clauses in all but the rarest of circumstances.<sup>22</sup> The other statute—the Bankruptcy Code—provides debtors the right to a “fresh start” at the closing of their bankruptcy case.<sup>23</sup> The Bankruptcy Code also vests authority with the bankruptcy courts to resolve a range of bankruptcy matters in their own special forum separate from federal district courts.<sup>24</sup> Although the Bankruptcy Code does not expressly preclude arbitration, many debate whether enforcing class-waiving arbitration clauses in cases such as that of our former debtor nevertheless violates the Bankruptcy Code.<sup>25</sup>

This section provides background for understanding this potential conflict of laws. First, it provides a brief personal bankruptcy primer, including a discussion of the discharge injunction, as well as an overview of the jurisdiction of bankruptcy courts. Next, it outlines a brief history of the FAA. Finally, it gives an overview of the “inherent conflict” test courts employ to determine whether a federal law conflicts with the FAA such that an arbitration clause is unenforceable both generally and in the bankruptcy context.

### A. *Personal Bankruptcy Law Primer*

The voiding of debts, or a debt “discharge,” is a central concept of personal bankruptcy law in the United States.<sup>26</sup> When a bankruptcy court grants an individual debtor a discharge, his former creditors may not attempt to collect his discharged debts.<sup>27</sup> Section 524 of the Bankruptcy Code provides that a discharge “operates as an injunction against the commencement or continuation of an action . . . to collect . . . any such debt as a personal liability of the debtor.”<sup>28</sup>

22. *See infra* Part I.C.

23. *See infra* Part I.A.

24. *See infra* Part I.B.

25. *See infra* Part IV.

26. DAVID A. SKEEL, JR., *DEBT’S DOMINION* 6 (2001); *see also* John C. McCoid II, *Discharge: The Most Important Development in Bankruptcy History*, 70 *AM. BANKR. L.J.* 163, 164 (1996) (describing the discharge as “rank[ing] ahead in importance of all other[] [developments] in Anglo-American bankruptcy history”).

27. SKEEL, *supra* note 26, at 6. Originally, bankruptcy law existed purely to protect creditors. *See* McCoid, *supra* note 26, at 164–65. The law’s one-sided focus reflected societal scorn of debtors; the first English statute on bankruptcy, enacted in 1543, colorfully depicts debtors as conniving thieves who appropriate the wealth of creditors to support immoral, lavish lifestyles. *See* Robert Weisberg, *Commercial Morality, the Merchant Character, and the History of the Voidable Preference*, 39 *STAN. L. REV.* 3, 21 (1986). However, by the late 1600s, public opinion began to change as commentators criticized the draconian bankruptcy regime for failing to differentiate between honest and dishonest debtors and for stifling economic growth. *Id.* at 5–7.

28. 11 U.S.C. § 524(a)(2) (2012). Courts have held that the discharge injunction applies not only to direct attempts to collect discharged debt but also to any action that indirectly

The discharge acts as a reward for enduring the emotionally draining process of asset distribution to creditors seeking to collect on their debts and is a powerful incentive for entering bankruptcy.<sup>29</sup> As such, once a court closes a debtor's bankruptcy proceeding, he should be able to find comfort in knowing that his discharged debts will not come back to haunt him.<sup>30</sup>

Individual debtors may obtain a discharge one of two ways.<sup>31</sup> First, they may liquidate under Chapter 7 of the Bankruptcy Code.<sup>32</sup> When a debtor files for Chapter 7 bankruptcy, the bankruptcy court assumes control of all his assets.<sup>33</sup> A court appointee, called a "trustee," then oversees the distribution of the debtor's estate to creditors.<sup>34</sup> Even if the liquidated assets do not satisfy all of the unpaid debt, the debt is nevertheless discharged unless the debt is considered nondischargeable under § 523(a).<sup>35</sup> Alternatively, the debtor may adhere to a "rehabilitation" plan pursuant to Chapter 13 of the Bankruptcy Code.<sup>36</sup> Rather than turning over all of his assets to the court, the debtor instead retains them and promises to repay his debts over a longer period of time.<sup>37</sup> Chapter 13 is available to any debtor with a regular income.<sup>38</sup> The purpose of the discharge under both Chapter 7 and Chapter 13 is to provide the "honest but unfortunate debtor" a "fresh start" and a "completely unencumbered new beginning."<sup>39</sup>

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pressures a debtor to pay his discharged debt. *See, e.g.*, *Green Point Credit, LLC v. McLean (In re McLean)*, 794 F.3d 1313, 1322 (11th Cir. 2015) (finding that a creditor had violated § 524 when it filed a proof of claim in a bankruptcy proceeding for debt that had been discharged in an earlier proceeding).

29. *See* HOMER DRAKE, JR. & KAREN D. VISSER, *BANKRUPTCY PRACTICE FOR THE GENERAL PRACTITIONER* § 6:24 (2017) (noting that discharge is "the principal reason for an individual to declare bankruptcy"); Katherine Porter, *Life After Debt: Understanding the Credit Restraint of Bankruptcy Debtors*, 18 AM. BANKR. INST. L. REV. 1, 34 (2010) (describing filing for bankruptcy as "an emotionally draining and difficult experience").

30. *See* *Feggins v. LVNV Funding LLC (In re Feggins)*, 535 B.R. 862, 874 (Bankr. M.D. Ala. 2015) ("Bankruptcy does not resurrect dead debt."). A discharge does not preclude a debtor from voluntarily paying his discharged debts. However, courts will find improper any attempts by a creditor to coerce such payments. *See* DRAKE & VISSER, *supra* note 29, § 6:24 nn.2–5 and accompanying text.

31. Less commonly, individuals may also obtain a discharge under Chapter 11 by reorganizing and paying their debts over time, even though the primary focus of that chapter is the reorganization of businesses. *See* *Toibb v. Radloff*, 501 U.S. 157, 166 (1991).

32. SKEEL, *supra* note 26, at 6. The debtor must be an individual to receive a discharge under Chapter 7. 11 U.S.C. § 727(a)(1) (2012).

33. SKEEL, *supra* note 26, at 6.

34. *Id.*

35. Examples of nondischargeable debt are taxes, credit obtained through fraud, and domestic support obligations. *See* 11 U.S.C. § 523(a).

36. SKEEL, *supra* note 26, at 7. Chapter 13 debtors do not receive a discharge until they certify that they have paid all debts under their repayment plan. 11 U.S.C. § 1328(a); 8 ALAN N. RESNICK & HENRY J. SOMMER, *COLLIER ON BANKRUPTCY* ¶ 1328.02 (16th ed. 2017).

37. SKEEL, *supra* note 26, at 7.

38. *Id.*

39. *Grogan v. Garner*, 498 U.S. 279, 286–87 (1991) (quoting *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934)). Of course, this fresh start provides benefits to debtors. But early proponents of the discharge in American personal bankruptcy law also recognized a great cost to society if the weight of one's debts inhibited one's positive contribution to society at large. *See* John M. Czarnetzky, *The Individual and Failure: A Theory of the Bankruptcy Discharge*, 32 ARIZ. ST. L.J. 393, 428 (2000) (citing CONG. GLOBE, 26th Cong., 1st Sess. 816 (1840)).



Despite bankruptcy law's debtor-friendly evolution, it has not abandoned creditors' interests. Bankruptcy still protects creditors by allowing for the "prompt and effectual administration and settlement of the estate of all bankrupts within a limited period."<sup>40</sup> By allowing creditors to file "proofs of claim" with the bankruptcy court, bankruptcy law allows creditors to collect their outstanding debts in a centralized and orderly manner.<sup>41</sup> Although the process does not guarantee them complete recovery, it promotes equitable distribution by prioritizing their claims and allocating payments from the debtor's estate on a ratable basis.<sup>42</sup>

### B. Bankruptcy Jurisdiction

The bankruptcy courts' jurisdiction derives from the federal district courts, which have "original and exclusive jurisdiction of all cases under [the Bankruptcy Code]."<sup>43</sup> A bankruptcy "case" is an umbrella under which bankruptcy "proceedings" take place following the filing of a petition for relief.<sup>44</sup> Bankruptcy "proceedings" consist of "contested matters" or "adversary proceedings," including litigation arising after the close of a bankruptcy case.<sup>45</sup>

Federal district courts also have "original but not exclusive jurisdiction of all civil proceedings arising under" the Bankruptcy Code, as well as proceedings either "arising in or related to cases under [the Bankruptcy Code]."<sup>46</sup> A proceeding arises under the Bankruptcy Code if it is premised upon substantive bankruptcy rights conferred exclusively by the Bankruptcy Code.<sup>47</sup> Like a proceeding "arising under" the Code, a proceeding "arising in" a bankruptcy case can only arise in the context of bankruptcy, but it is typically administrative in nature.<sup>48</sup> Proceedings "related to" bankruptcy cases often involve matters under state law that "could conceivably have any effect on the estate being administered in bankruptcy."<sup>49</sup> Proceedings

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40. *Katchen v. Landy*, 382 U.S. 323, 328 (1966).

41. *See* 4 RESNICK & SOMMER, *supra* note 36, ¶ 501.01.

42. *See id.*

43. 28 U.S.C. § 1334(a) (2012). The Bankruptcy Act of 1978 broadened bankruptcy courts' jurisdiction to include original jurisdiction over most bankruptcy matters. Bankruptcy Act of 1978, Pub. L. No. 95-598, § 241(a), 92 Stat. 2549, 2668-69. However, because bankruptcy judges are not judges under Article III of the Constitution and do not have life tenure, the Supreme Court held the 1978 Act's jurisdictional grant unconstitutional for vesting them with authority reserved only for Article III judges. *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 87 (1982). Congress responded to the Court's holding in *Northern Pipeline* by vesting original jurisdiction with the federal district courts. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 101(a), 98 Stat. 333, 333.

44. 2 RESNICK & SOMMER, *supra* note 36, ¶ 301.03.

45. *Id.*

46. 28 U.S.C. § 1334(b).

47. *See* 1 RESNICK & SOMMER, *supra* note 36, ¶ 3.01[3][e][i].

48. *Id.*

49. *Pacor, Inc. v. Higgins (In re Pacor, Inc.)*, 743 F.2d 984, 994 (3d Cir. 1984). Although the Second and Seventh Circuits have adopted a slightly different test for determining "related to" jurisdiction, all circuits agree that "bankruptcy courts have no jurisdiction over proceedings

“arising under” the Code or “arising in” a bankruptcy case constitute “core” bankruptcy proceedings in which bankruptcy courts may enter an order or judgment.<sup>50</sup> Conversely, proceedings “related to” bankruptcy cases are “non-core,” and bankruptcy courts may only submit proposed findings of fact and conclusions of law to the district court.<sup>51</sup>

Although bankruptcy courts do not have original jurisdiction over bankruptcy cases—meaning they have no independent jurisdictional authority to resolve bankruptcy cases<sup>52</sup>—§ 157 of the Bankruptcy Code permits federal district courts to refer any case under the Code and any of the proceedings mentioned in 28 U.S.C. § 1334<sup>53</sup> to the bankruptcy courts of their district.<sup>54</sup> All judicial districts have entered local rules or standing orders referring all bankruptcy matters to their respective bankruptcy courts.<sup>55</sup>

### C. The FAA

In 1924, Congress passed the Federal Arbitration Act, which protected binding arbitration clauses in contracts.<sup>56</sup> Section 2 of the FAA, which the Supreme Court has called its “primary substantive provision,”<sup>57</sup> reads: “[A] contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>58</sup>

For decades, the Supreme Court interpreted § 2 narrowly. The 1953 Supreme Court decision in *Wilko v. Swan*<sup>59</sup> perhaps best represents the Court’s earlier FAA jurisprudence. In *Wilko*, the Court refused to compel arbitration of a dispute arising under the Securities Act of 1933 between partners of a securities brokerage firm and their customer despite their prior agreement to arbitrate future controversies.<sup>60</sup> The Securities Act declared void any agreement that would waive compliance with any of the Act’s provisions, and the Court held the right to select a judicial forum to be such

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that have no effect on the estate of the debtor.” *Celotex Corp. v. Edwards*, 514 U.S. 300, 308 n.6 (1995).

50. 28 U.S.C. § 157(b)(1) (2012).

51. See Paul F. Kirgis, *Arbitration, Bankruptcy, and Public Policy: A Contractarian Analysis*, 17 AM. BANKR. INST. L. REV. 503, 510 (2009).

52. See *supra* note 43 and accompanying text.

53. See *supra* notes 43–46 and accompanying text.

54. 28 U.S.C. § 157(a).

55. Bruce, *supra* note 6, at 48. For an example of a standing order of reference, see *In re Standing Order of Reference Re: Title 11, No. 12-MISC-00032* (S.D.N.Y. Feb. 1, 2012), [http://www.nysd.uscourts.gov/rules/StandingOrder\\_OrderReference\\_12mc32.pdf](http://www.nysd.uscourts.gov/rules/StandingOrder_OrderReference_12mc32.pdf) [<https://perma.cc/24N4-W8XY>].

56. Federal Arbitration Act, Pub. L. No. 68-401, 43 Stat. 883 (1925) (codified at 9 U.S.C. §§ 1–14) (2012)).

57. *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

58. 9 U.S.C. § 2.

59. 346 U.S. 427 (1953), *overruled by* *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989). One commentator calls *Wilko* “the most prominent example” of the Supreme Court’s early narrow interpretation of the FAA. Kirgis, *supra* note 51, at 512.

60. *Wilko*, 346 U.S. at 428, 438.

a nonwaivable provision.<sup>61</sup> The Court reasoned arbitration is an inadequate forum to protect securities buyers because the arbitrator's decision is not subject to judicial review and because arbitrators may not receive judicial instructions on the law.<sup>62</sup>

Despite *Wilko*'s holding, and notwithstanding scholarship indicating that Congress enacted the FAA to promote only commercial arbitration,<sup>63</sup> the Court's interpretation of the scope of the FAA has evolved and expanded.<sup>64</sup> By the 1980s, the Court widely promoted arbitration of both federal and state law claims, including arbitration of disputes involving clauses in standardized contracts of adhesion<sup>65</sup> with consumers.<sup>66</sup> The Supreme Court's current position is that the FAA was passed primarily to combat "judicial hostility to arbitration agreements" in general<sup>67</sup> and holds the FAA "establishes 'a liberal federal policy favoring arbitration.'"<sup>68</sup>

Although arbitration ordinarily involves individual parties, arbitration also allows for plaintiffs to vindicate their rights as a class. In 2003, the Supreme Court held that arbitrators may determine whether a contract precluded class arbitration, thus impliedly holding class arbitration is permissible.<sup>69</sup> In 2009, the American Arbitration Association listed 280 class arbitrations;<sup>70</sup> by 2015, that number increased by almost 50 percent.<sup>71</sup> However, with the rise of class proceedings came a rise in class waivers,<sup>72</sup> inviting the need to resolve the validity of such waivers.

61. *Id.* at 434–35.

62. *Id.* at 436.

63. See Sarah Rudolph Cole, *Incentives and Arbitration: The Case Against Enforcement of Executory Arbitration Agreements Between Employers and Employees*, 64 UMKC L. REV. 449, 467 (1996) (concluding that the FAA's legislative history indicates Congress's intent to exclude noncommercial agreements from its scope); Willy E. Rice, *Courts Gone "Irrationally Biased" in Favor of the Federal Arbitration Act?—Enforcing Arbitration Provisions in Standardized Applications and Marginalizing Consumer-Protection, Antidiscrimination, and States' Contract Laws: A 1925-2014 Legal and Empirical Analysis*, 6 WM. & MARY BUS. L. REV. 405, 445–46 (2015) (arguing that the Supreme Court's "judicial hostility" explanation overlooks critical historical factors that led to the enactment of the FAA, such as Congress's intent to reduce increasing litigation between merchants and encourage the amicable resolution of commercial disputes).

64. See Kirgis, *supra* note 51, at 512 (arguing that case law interpreting the FAA has come to dominate arbitration law).

65. See *Adhesion Contract*, BLACK'S LAW DICTIONARY (10th ed. 2014) ("A standard-form contract prepared by one party, to be signed by another party in a weaker position, [usually] a consumer, who adheres to the contract with little choice about the terms.").

66. Kirgis, *supra* note 51, at 513 (describing the Court as "firmly commit[ing] itself to arbitrability in virtually every context").

67. *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 339 (2011).

68. *CompuCredit Corp. v. Greenwood*, 565 U.S. 95, 98 (2012) (quoting *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983)).

69. *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 452–53 (2003). Justice John Paul Stevens argued in his concurring opinion that the FAA permitted class arbitration. *Id.* at 454–55 (Stevens, J., concurring).

70. See Judith Resnik, *Diffusing Disputes: The Public in the Private of Arbitration, the Private in Courts, and the Erasure of Rights*, 124 YALE L.J. 2804, 2888 (2015).

71. *Id.* at 2888 n.412.

72. *Id.*

*D. McMahon and the “Inherent Conflict” Test*

Both bankruptcy courts and Article III courts<sup>73</sup> rely on the same Supreme Court precedent when determining whether to enforce an arbitration clause. However, despite similar origins, the test in bankruptcy courts has evolved as similar to but distinct from that of Article III courts. It has closely tracked the Article III test, and bankruptcy courts have at times looked to elements of the other test to guide their determinations of enforceability. Ultimately, to reach a conclusion about the effect of recent Supreme Court case law on bankruptcy courts’ approach to class-waiving arbitration clauses, it is important to look at each test in turn. This Part will first focus on the test of Article III courts and then turn to that employed by bankruptcy courts.

1. Article III Courts:  
The “Inherent Conflict” Test and Class Waivers

Considering the “liberal federal policy favoring arbitration,”<sup>74</sup> contractual agreements to arbitrate a dispute arising out of federal law are largely unassailable. Nevertheless, the Supreme Court held in *Shearson/American Express v. McMahon*<sup>75</sup> that certain claims may be nonarbitrable as a matter of federal law.<sup>76</sup> That case involved a group of plaintiffs who alleged their former brokerage firm violated the Racketeer Influenced and Corrupt Organizations Act (RICO) and the antifraud provisions of section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5.<sup>77</sup> In response, the brokerage firm filed a motion to compel arbitration pursuant to its prior contracts with the plaintiffs.<sup>78</sup> The Court held the plaintiffs’ claims to be arbitrable, but in doing so it established a test for determining the arbitrability of claims under federal law.<sup>79</sup> Accordingly, a party may rebut the presumption of arbitrability by showing a “contrary congressional command” limiting or prohibiting arbitration waivers in certain contexts.<sup>80</sup> This congressional command should, the Court indicated, “be deducible from [the statute’s] text or legislative history,” or from an *inherent conflict* between arbitration and the statute’s underlying purposes.”<sup>81</sup>

Since *McMahon*, courts have applied the “inherent conflict” test to a range of areas of federal law, from consumer product warranties to employee benefit plans and credit repair services.<sup>82</sup> Although circuits have arrived at

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73. This Note uses the term “Article III courts” to refer to federal district and circuit courts, as well as the Supreme Court, which derive their power from Article III of the Constitution.

74. *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

75. 482 U.S. 220 (1987).

76. *Id.* at 226–27, 238.

77. *Id.* at 223.

78. *Id.*

79. *Id.* at 226–27, 238.

80. *Id.* at 226.

81. *Id.* at 227 (emphasis added) (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 632–37 (1985)).

82. *E.g.*, *Gay v. CreditInform*, 511 F.3d 369, 378–79 (3d Cir. 2007) (applying the “inherent conflict” test to the Credit Repair Organizations Act); *Cunningham v. Fleetwood Homes of Ga., Inc.*, 253 F.3d 611, 613–17 (11th Cir. 2001) (applying the “inherent conflict”

various conclusions as to whether certain federal laws inherently conflict with the FAA, they have applied similar versions of the test. For example, the Seventh Circuit recently analyzed whether the NLRA allows class arbitration, holding the “fundamental right” of employees to collectively bargain justified a refusal to enforce the class-waiving arbitration clause at issue.<sup>83</sup> And although the Eighth Circuit found there to be no such conflict between the FAA and the NLRA in a similar case, it nevertheless similarly applied the “inherent conflict” test of *McMahon* to reach its conclusion.<sup>84</sup>

Class waivers within arbitration clauses have added a layer of complexity to the “inherent conflict” test. For a time, parties opposing the enforcement of class-waiving arbitration clauses looked to two defenses that worked in tandem with the Court’s “inherent conflict” test. The first looked to the common law doctrine of unconscionability.<sup>85</sup> By finding class waivers unconscionable, a court could refuse to enforce the arbitration clause pursuant to the exception within § 2 of the FAA.<sup>86</sup> For example, the Supreme Court of California held that class-waiving arbitration clauses in contracts of adhesion are unenforceable under California state law notwithstanding the federal policy favoring arbitration.<sup>87</sup> However, in 2011, the Supreme Court limited the unconscionability defense in *AT&T Mobility LLC v. Concepcion*,<sup>88</sup> holding the FAA preempts state laws that abrogate the enforceability of class-waiving arbitration clauses based on doctrines of unconscionability.<sup>89</sup>

The second defense to enforceability relied on the “effective vindication” doctrine established by the Supreme Court in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*<sup>90</sup> In contrast to the evaluation of a competing *substantive* federal right under the “inherent conflict” test, the “effective vindication” doctrine evaluates the *procedural* adequacy of arbitration, allowing for the enforcement of an arbitration clause only if “the prospective litigant effectively may vindicate its statutory right of action in the arbitral

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test to the Magnuson-Moss Warranty Act after a mobile home dealership sought to compel arbitration of plaintiff’s breach of warranty claim); *Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 7 F.3d 1110, 1113–15 (3d Cir. 1993) (applying the “inherent conflict” test to the Employee Retirement Income Security Act of 1974).

83. *Lewis v. Epic Sys. Corp.*, 823 F.3d 1147, 1160 (7th Cir. 2016) (quoting *Allen-Bradley Local No. 1111 v. Wis. Emp’t Relations Bd.*, 315 U.S. 740, 750 (1942)), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-285). The phrase “inherent conflict” was perhaps inapt in this case. The Seventh Circuit held the statute’s preclusion of class waivers to mean any such waivers were illegal, thus falling squarely within the FAA’s exception to the presumption of enforceability. To that end, the FAA and the NLRA “work hand in glove.” *Id.* at 1157.

84. *Owen v. Bristol Care, Inc.*, 702 F.3d 1050, 1053 (8th Cir. 2013).

85. *See generally* 7 JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 29.4 (rev. ed. 2016).

86. As discussed in Part I.C, *supra*, § 2 of the FAA provides that arbitration clauses are enforceable except under “such grounds as exist at law or in equity for the revocation of any contract.” 9 U.S.C. § 2 (2012).

87. *Discover Bank v. Superior Court*, 113 P.3d 1100, 1103 (Cal. 2005), *abrogated by AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011).

88. 563 U.S. 333 (2011).

89. *Id.* at 341.

90. 473 U.S. 614 (1985).

forum.”<sup>91</sup> In other words, if an arbitration clause acts as a “prospective waiver of a party’s right to pursue statutory remedies,” then it is unenforceable.<sup>92</sup> Under this doctrine, the Court has recognized prohibitively high arbitration fees as potential grounds for refusing to enforce an arbitration clause even if the Court finds no inherent conflict between the substantive statutory right and the FAA.<sup>93</sup> A class-waiving arbitration clause may lead to such a finding, as an individual plaintiff is unable to spread the fees across the class.

However, the Supreme Court’s decision in *Italian Colors* took much of the wind out of the “effective vindication” doctrine’s sails.<sup>94</sup> Although the Court recognized the possibility that excessive arbitration fees may act as an impermissible waiver of a litigant’s rights, that litigant carries a heavy burden of showing the arbitration clause all but completely closes the door to adjudication.<sup>95</sup> The plaintiffs in that case were unable to meet this burden, even though they stood to recover an amount less than the cost of litigating individually.<sup>96</sup> In so holding, the *Italian Colors* Court fell back on its analysis under *McMahon* and determined that the federal antitrust law at issue contained no “contrary congressional command” requiring the Court to reject the class waiver.<sup>97</sup> By relying on *McMahon* to do the heavy lifting not only for the analysis of the arbitrability of the claim but also for the validity of the class waiver, the Supreme Court all but merged these analyses into one.

## 2. Bankruptcy Courts’ “Inherent Conflict” Test

Bankruptcy courts have also looked to *McMahon* for guidance and have relied on the same “inherent conflict” language as the Article III courts when determining the enforceability of arbitration clauses.<sup>98</sup> However, the

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91. *Id.* at 637.

92. *Id.* at 637 n.19.

93. *Green Tree Fin. Corp.-Ala. v. Randolph*, 531 U.S. 79, 90 (2000).

94. *Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2309 (2013); *see Resnik, supra* note 70, at 2886 n.397 (arguing that, in the wake of *Concepcion* and *Italian Colors*, lower courts have retreated from finding arbitration clauses invalid under the “effective vindication” doctrine).

95. *Italian Colors*, 133 S. Ct. at 2310–11.

96. Specifically, the plaintiffs only stood to recover \$38,549 individually, while the cost of expert analysis necessary to prove their claims was at least several hundred thousand dollars. *Id.* at 2308.

97. *Id.* at 2309.

98. Some bankruptcy courts have looked to whether the discharge renders the arbitration clause invalid—that is, whether the arbitration clause survives the discharge of the debtor’s obligations—before applying the *McMahon* test. *See, e.g., Williams v. Navient Sols., LLC (In re Williams)*, 564 B.R. 770, 775 (Bankr. S.D. Fla. 2017) (“The entry of a chapter 7 discharge does not vitiate the effectiveness of an otherwise binding agreement to arbitrate matters relating to a claim that may or may not be subject to the discharge.”); *Belton v. Ge Capital Consumer Lending, Inc. (In re Belton)*, No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*3 (S.D.N.Y. Oct. 14, 2015) (citing *Rent-A-Ctr., W., Inc. v. Jackson*, 561 U.S. 63, 70–71 (2010)) (holding an arbitration clause is severable from the underlying contract and remains in force postdischarge). For the purposes of analysis, this Note assumes the arbitration clause survives discharge.

“inherent conflict” test in bankruptcy courts has evolved with some distinctions.

To begin, the Supreme Court’s unequivocal message to enforce arbitration clauses in all but the rarest of circumstances creates a unique tension in bankruptcy courts.<sup>99</sup> Much of this tension can be explained by the jurisdictional evolution of the bankruptcy courts. Under the Bankruptcy Act of 1898, the scope of bankruptcy courts’ jurisdiction was limited, and many bankruptcy matters were resolved in state courts.<sup>100</sup> In 1973, the congressionally authorized National Bankruptcy Review Commission proposed expanding the scope of matters over which bankruptcy courts had jurisdiction.<sup>101</sup> Although Congress did not incorporate all of the commission’s recommendations into the Bankruptcy Code in 1978,<sup>102</sup> the Code’s current jurisdictional structure reflects a greater centralization of bankruptcy matters in bankruptcy court.<sup>103</sup> Therefore, unlike federal district courts, the centralizing pull of bankruptcy courts’ jurisdiction bears upon the question of whether to allow resolution of a claim in another forum such as arbitration.

A critical distinguishing attribute of the “inherent conflict” test in bankruptcy is the deference accorded to the bankruptcy courts’ determination of arbitrability.<sup>104</sup> Courts have long agreed that arbitration clauses are enforceable when a “non-core” claim is at issue.<sup>105</sup> Because a bankruptcy court lacks jurisdiction to decide “non-core” claims on their merits, there cannot be a countervailing interest for the bankruptcy court, rather than an arbitrator, to resolve the matter. In this regard, the deference to a determination of arbitrability of “non-core” claims is similar to that accorded to federal district courts; on an appeal of a district court’s determination of arbitrability in a nonbankruptcy setting, the court reviews the decision *de novo*.<sup>106</sup> However, at least in the context of the arbitrability of “core”

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99. See Kirgis, *supra* note 51, at 516 (arguing that the determination of claims’ arbitrability “create[s] a dilemma for [bankruptcy] judges who have been conditioned to enforce arbitration clauses without a second thought, but who are also highly sensitive to the centralizing pull of the bankruptcy process”).

100. SKEEL, *supra* note 26, at 147. Bankruptcy courts had broader “summary” jurisdiction over the debtor’s property but a more limited “plenary” jurisdiction over other matters. Accordingly, state courts often resolved matters not directly implicating the debtor’s property, such as claims against the debtor for preference or for alleged fraudulent transfer of the debtor’s assets to shelter them against collection. *Id.*

101. *Id.* at 139, 141.

102. *Id.* at 141.

103. For a discussion of bankruptcy jurisdiction, see *supra* Part I.B.

104. However, some have argued that the Court did not intend for *McMahon* to help courts determine which forum is best for hearing a case that may be arbitrated but rather merely to resolve the question of whether a federal claim is arbitrable. See, e.g., Kirgis, *supra* note 51, at 523–24 (arguing that the Court did not intend for *McMahon* to help courts determine which forum is best for hearing a case that may be arbitrated but rather to merely resolve whether a federal claim was arbitrable).

105. *Id.* at 517.

106. See, e.g., *Laster v. AT&T Mobility LLC*, 584 F.3d 849, 853 (9th Cir. 2009), *rev’d sub nom.* *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011); *Randolph v. Green Tree Fin. Corp.-Ala.*, 178 F.3d 1149, 1152 (11th Cir. 1999), *aff’d in part, rev’d in part*, 531 U.S. 79 (2000).

claims,<sup>107</sup> which do not dispose of the enforceability of an arbitration agreement, most circuits employ an abuse of discretion standard after reviewing de novo whether the bankruptcy court had discretion.<sup>108</sup>

Although most circuits defer to bankruptcy courts' decisions of arbitrability in "core" proceedings, they are divided regarding the circumstances under which to defer. After holding that neither the Bankruptcy Code's text nor its legislative history evinced a congressional intent to preclude arbitration of "core" claims, the Fifth Circuit in *In re National Gypsum Co.*<sup>109</sup> employed a two-part inquiry under *McMahon*'s "inherent conflict" test.<sup>110</sup> First, the court looked to the "underlying nature of the proceeding" to determine "whether [the claim] derives exclusively from the provisions of the Bankruptcy Code."<sup>111</sup> It was careful to distinguish "federal rights conferred by the Bankruptcy Code" from the jurisdiction of bankruptcy courts as the first step of its "inherent conflict" test.<sup>112</sup> Second, it held the bankruptcy court "retains significant discretion to assess whether arbitration would be consistent with the purpose of the Code" if the claim at issue concerns rights derived exclusively from the Bankruptcy Code.<sup>113</sup> Finally, it held such purposes to include "the goal of centralized resolution of purely bankruptcy issues, the need to protect creditors and reorganizing debtors from piecemeal litigation, and the undisputed power of a bankruptcy court to enforce its own orders."<sup>114</sup>

The Third Circuit adopted the Fifth Circuit's approach, holding that a bankruptcy court has no discretion to assess whether arbitration is consistent with the purposes of the Bankruptcy Code when the debtor "has failed to raise any statutory claims that were created by the Bankruptcy Code."<sup>115</sup> Similarly, when evaluating the arbitrability of a "core" claim, the Ninth Circuit in *In re Thorpe Insulation Co.*<sup>116</sup> first noted that the underlying claim originated in the Bankruptcy Code, then held that the bankruptcy court had discretion to deny arbitration in light of the policies implicated by the underlying claim.<sup>117</sup>

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107. To reiterate, "core" claims include claims "arising under" the Bankruptcy Code as well as claims "arising in" a bankruptcy case. *See supra* Part I.B.

108. For a discussion of the circuit courts' approaches to the "inherent conflict" test in bankruptcy, see *infra* notes 109–24 and accompanying text.

109. 118 F.3d 1056 (5th Cir. 1997).

110. *Id.* at 1067.

111. *Id.*

112. *Id.* at 1068–69 (noting that the Court in *McMahon* was concerned primarily with the purposes of and rights conferred by a particular federal statute, rather than the jurisdiction of federal courts). Accordingly, under the Fifth Circuit's "inherent conflict" test, whether a "core" claim "arises under" or "arises in" the Bankruptcy Code has no direct bearing on its arbitrability.

113. *Id.* at 1069.

114. *Id.*

115. *Mintze v. Am. Gen. Fin. Servs., Inc. (In re Mintze)*, 434 F.3d 222, 231 (3d Cir. 2006).

116. 671 F.3d 1011 (9th Cir. 2012).

117. *Id.* at 1022. Unlike the approach of the Fifth Circuit, however, the Ninth Circuit appears to rely on the purposes of the Bankruptcy Code to find an inherent conflict sufficient to give the bankruptcy court discretion, notwithstanding whether the claim itself derives exclusively from the Bankruptcy Code. *See id.*



By contrast, the Second and Fourth Circuits only undertake the policy-based second inquiry of the Third, Fifth, and Ninth Circuits' test<sup>118</sup> and decline to look to whether a claim "derives exclusively from the provisions of the Bankruptcy Code."<sup>119</sup> By excluding the inquiry of whether the claim itself is a "statutory claim[] . . . created by the Bankruptcy Code,"<sup>120</sup> the potential to find a conflict is arguably greater in these circuits. For example, in *MBNA America Bank, N.A. v. Hill*,<sup>121</sup> the Second Circuit established a case-by-case inquiry that looks to whether arbitration of the claim would "seriously jeopardize the objectives of the Bankruptcy Code."<sup>122</sup> The Fourth Circuit also adopted a purpose-driven approach in *In re White Mountain Mining Co.*<sup>123</sup> when it analyzed whether arbitration conflicted with the purposes of certain provisions of the Bankruptcy Code and ultimately deferred to the bankruptcy court's decision.<sup>124</sup>

Like the "inherent conflict" test employed by Article III courts, the introduction of class-waiving clauses into the analysis adds complexity. However, few courts have analyzed class waivers under the "inherent conflict" test in bankruptcy.<sup>125</sup> The Second Circuit's decision in *Hill* is one such example. Rather than treat the class-waiving question as separate from that of the arbitrability of the claim, the Second Circuit held the plaintiff's choice to file as a putative class was evidence that her claim "lack[ed] the direct connection to her own bankruptcy case" necessary to show arbitration would "seriously jeopardize the objectives of the Bankruptcy Code."<sup>126</sup>

In addition, two recent cases in the Southern District of New York relied on *Hill* to review bankruptcy decisions refusing to compel arbitration of class claims, although the courts disagreed over its holding. In one of these decisions, *In re Anderson*,<sup>127</sup> the court held the enforceability of the class waiver to be independent of the question of arbitrability, thereby declining to review the bankruptcy court's decision relating to the class waiver's

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118. Indeed, in *MBNA America Bank, N.A. v. Hill*, 436 F.3d 104, 108 (2d Cir. 2006), the Second Circuit relied explicitly on the factors of the second prong articulated by the Fifth Circuit in *In re National Gypsum Co.*

119. *In re Nat'l Gypsum Co.*, 118 F.3d at 1067.

120. *In re Mintze*, 434 F.3d at 231.

121. 436 F.3d 104 (2d Cir. 2006).

122. *Id.* at 109. In finding that arbitration would "not seriously jeopardize the objectives of the Bankruptcy Code," the court gave three reasons:

(1) [The debtor's] estate has now been fully administered and her debts have been discharged, so she no longer requires protection of the automatic stay and resolution of the claim would have no effect on her bankruptcy estate; (2) as a purported class action, [the debtor's] claims lack the direct connection to her own bankruptcy case that would weigh in favor of refusing to compel arbitration; and (3) a stay is not so closely related to an injunction that the bankruptcy court is uniquely able to interpret and enforce its provisions.

*Id.*

123. 403 F.3d 164 (4th Cir. 2005).

124. *Id.* at 170–71.

125. See Bruce, *supra* note 18, at 475–76.

126. *Hill*, 436 F.3d at 109.

127. 550 B.R. 228 (S.D.N.Y.), *appeal docketed*, No. 16-2496 (2d Cir. July 13, 2016).

unenforceability.<sup>128</sup> In the other decision, *In re Belton*,<sup>129</sup> the court first relied on *Hill* in holding that the class of plaintiffs contributed to the finding that arbitration did not jeopardize the Bankruptcy Code.<sup>130</sup> The court then relied on *Italian Colors*, holding individual arbitration of the debtors' claim would not eliminate "the[ir] right to pursue" a remedy.<sup>131</sup>

Bankruptcy courts' approach to the "inherent conflict" test and the circuits' different analyses of class waivers together provide the framework for analyzing the enforceability of class-waiving arbitration clauses in a postdischarge dispute.

## II. ENFORCING DISCHARGE INJUNCTIONS

To determine the enforceability of class-waiving arbitration clauses, it is necessary to determine whether a violation of § 524 is actionable—that is, whether the Bankruptcy Code allows our former debtor to bring a claim at all. It is axiomatic that there can be no inherent conflict between the FAA and the Bankruptcy Code if he has no federal right to vindicate.

Fortunately for our former debtor, courts generally agree that he has avenues for recourse. Just what jurisdictional grant allows bankruptcy courts to render a judgment, however, is disputed. Courts also disagree about how to enforce a discharge injunction violation.

While an individual debtor-plaintiff may be indifferent to the court's interpretation of its jurisdiction or its method of enforcement, the treatment of § 524 has more significant consequences for a class of debtors. Although this Note does not seek to resolve either question, a preliminary discussion of the varying approaches to jurisdiction and enforcement is critical to identifying those methods that ultimately allow for class proceedings. The following section discusses in greater detail the ways in which courts treat matters involving violations of § 524.

### A. *The Jurisdictional Authority of Bankruptcy Courts to Enforce Discharge Injunctions Under § 524*

It is uncontroverted that the violation of a discharge injunction implicates a bankruptcy court's "core" jurisdiction, which allows bankruptcy judges to render a final judgment.<sup>132</sup> Nevertheless, courts disagree about the source of their jurisdiction over postdischarge disputes under § 524. Some courts interpret § 524 to grant substantive rights to a debtor such that a discharge injunction dispute "arises under" the Bankruptcy Code.<sup>133</sup> Other courts hold

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128. *Id.* at 235.

129. No. 15-CV-1934 (VLB), 2015 WL 6163083 (S.D.N.Y. Oct. 14, 2015).

130. *Id.* at \*8.

131. *Id.* at \*9 (quoting *Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2311 (2013)).

132. *See* *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 71 (1982) ("[R]estructuring of debtor-creditor relations . . . is at the core of the federal bankruptcy power.").

133. *See, e.g.,* *Ins. Co. of N. Am. v. NGC Settlement Tr. & Asbestos Claims Mgmt. Corp.* (*In re Nat'l Gypsum Co.*), 118 F.3d 1056, 1063–64 (5th Cir. 1997) (holding that § 524 confers

more obliquely that any violation of the Bankruptcy Code constitutes a “core” proceeding, the remedy for which, at least impliedly, “arises under” the Code.<sup>134</sup> Alternatively, some courts hold the bankruptcy court that issued an injunction has the inherent authority to render final judgment when a party has violated it.<sup>135</sup>

The interpretation of a bankruptcy court’s jurisdiction in this context has a significant impact on the opportunity for our former debtor to bring his postdischarge claim on behalf of a class. If, on the one hand, a court adopts the view that a debtor may only seek relief on an individual basis from the bankruptcy court that discharged his debts, the court forecloses his ability to seek relief as part of a class, regardless of any class-waiving arbitration clauses. On the other hand, if a court interprets its jurisdiction to originate in a substantive right within the Bankruptcy Code rather than an individual debtor’s bankruptcy case, a debtor may be able to proceed as a class.

### *B. Approaches to Enforcing Discharge Injunctions Under § 524*

The treatment of the discharge injunction under § 524 is particularly important to answering the ultimate question of the enforceability of class-waiving arbitration clauses, as it may ultimately frame how courts apply their “inherent conflict” test. Yet courts disagree over exactly how to enforce a discharge injunction. A minority of courts have held that § 524 creates an implied right of action, allowing a debtor to file a complaint in any federal district court and implying the right to receive a trial by jury.<sup>136</sup> Without explicitly disagreeing that § 524 creates a private right of action to remedy violations of this injunction, other courts hold that § 524 is only enforceable through § 105, which grants the bankruptcy court that issued the injunction flexibility in enforcing the Bankruptcy Code.<sup>137</sup> In between are both broad and narrow interpretations of debtors’ substantive rights and the extent of the bankruptcy courts’ contempt powers. This section analyzes these various approaches by looking to three topics of dispute: (1) the nature of the rights § 524 confers on debtors, (2) the nature of the rights § 105 confers on debtors, and (3) the inherent contempt powers of the bankruptcy courts.

#### 1. Debtors’ Rights Under § 524

Both federal district courts and bankruptcy courts begin their analysis of § 524 violations by determining whether § 524 creates a private right of

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a substantive right to the discharged debtor, the dispute over which arises under the Bankruptcy Code).

134. *See, e.g.,* Walls v. Wells Fargo Bank, N.A., 276 F.3d 502, 505–06 (9th Cir. 2002) (holding that claims alleging a violation of the Bankruptcy Code constitute “core” proceedings).

135. *See, e.g.,* Alderwoods Grp., Inc. v. Garcia, 682 F.3d 958, 970 (11th Cir. 2012) (holding that a bankruptcy court, much like a federal district court, “possesses the inherent power to sanction contempt of its orders”).

136. *See* Molloy v. Primus Auto. Fin. Servs., 247 B.R. 804, 819 (C.D. Cal. 2000).

137. *Barrientos v. Wells Fargo Bank, N.A.*, 633 F.3d 1186, 1188 (9th Cir. 2011); *Cox v. Zale Del., Inc.*, 239 F.3d 910, 917 (7th Cir. 2001); *see also* 11 U.S.C. § 105 (2012).

action.<sup>138</sup> A majority of the courts have held § 524 does not provide for a private right of action.<sup>139</sup> This determination may be dispositive of a court's decision to permit debtor class actions, as a debtor who cannot successfully bring a claim as an individual cannot bring the claim as a class.

For example, in *Pertuso v. Ford Motor Credit Co.*,<sup>140</sup> the Sixth Circuit affirmed the district court's dismissal of a debtor's claim for relief under § 524 holding that a private right of action does not exist under that section.<sup>141</sup> The plaintiffs, who were former debtors, brought a class action lawsuit in federal district court against defendant Ford Motor Credit Company for attempting to collect discharged debt in violation of § 524.<sup>142</sup> The district court did not grant class certification and dismissed the complaint without leave to amend.<sup>143</sup> On appeal, the Sixth Circuit held that "the traditional remedy for violation of an injunction lies in contempt proceedings, not in a lawsuit such as this one."<sup>144</sup> The court was silent as to whether bankruptcy courts may preside over contempt proceedings involving a class of debtors.<sup>145</sup> At the very least, its decision foreclosed the possibility of class proceedings as an enforcement mechanism for § 524 in federal district court.

The reasoning of the Sixth Circuit relies in large part on the language of § 524(a)(2), which provides that a discharge "operates as an injunction," but is otherwise silent as to any remedies.<sup>146</sup> This language is comparable to that of the Bankruptcy Code's § 362, which governs automatic stays.<sup>147</sup> Like a discharge, an automatic stay prevents creditors from seeking to collect debts outside the bankruptcy process.<sup>148</sup> Creditors seeking repayment must file "proofs of claim" with the bankruptcy court, which notify the court of the amount of money the debtor owes to them.<sup>149</sup> When a debtor emerges from bankruptcy, the stay is lifted and the discharge takes its place.<sup>150</sup>

Despite similar functions, the prescribed remedies for violating § 524 and § 362 differ. While § 362 expressly provides for a private right of action, § 524 is silent to any such right. Section 362(k)(1) allows any "individual injured by any willful violation of a stay" to "recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, [to]

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138. A statute creates a private right of action when it allows an individual to "sue in a personal capacity to enforce a legal claim." *Private Right of Action*, BLACK'S LAW DICTIONARY (10th ed. 2014). Private rights of action may be "express" or "implied." See 33 CHARLES ALAN WRIGHT & CHARLES H. KOCH, JR., FEDERAL PRACTICE AND PROCEDURE: JUDICIAL REVIEW § 8324 (2006).

139. See, e.g., *Jones v. CitiMortgage, Inc.*, 666 Fed. App'x 766, 774–75 (11th Cir. 2016); *Walls*, 276 F.3d at 509; *Cox*, 239 F.3d at 917; *Pertuso v. Ford Motor Credit Co.*, 233 F.3d 417, 422–23 (6th Cir. 2000).

140. 233 F.3d 417 (6th Cir. 2000).

141. *Id.* at 422–23.

142. *Id.* at 420.

143. *Id.*

144. *Id.* at 421.

145. *Id.*

146. 11 U.S.C. § 524(a)(2) (2012).

147. *Id.* § 362 (stating that a petition of bankruptcy "operates as a stay").

148. *Id.* § 362(a).

149. 4 RESNICK & SOMMER, *supra* note 36, ¶ 501.01.

150. See *id.*

recover punitive damages.”<sup>151</sup> Section 524 goes no further than stating that a discharge “operates as an injunction.”<sup>152</sup> Some courts have pointed to this language to conclude that Congress did not intend for § 524 to provide a private right of action.<sup>153</sup>

This conclusion is further bolstered by the fact that Congress did not amend § 524 when it added a subsection to § 362 providing for a private right of action as part of Bankruptcy Amendments and Federal Judgeship Act of 1984.<sup>154</sup> Some have argued that, by adding this provision to the automatic stay provision but not to § 524, Congress did not intend § 524 to provide a similar remedy.<sup>155</sup>

Despite the absence of any language providing an express private right of action, some courts and commentators have argued that such a right exists. One argument relies on an expansive reading of the discharge injunction as a complete bar to any attempts by creditors to collect discharged debt, whether in or out of court.<sup>156</sup> This expansive reading is supported by Congress’s apparent intent “to give complete effect to the discharge and to eliminate any doubt concerning the effect of the discharge as a total prohibition on debt collection efforts.”<sup>157</sup> Another argument looks to the policies furthered by the discharge injunction, such as the need to protect debtors from harassment by creditors, as evidence of legislative intent to create a private right of action.<sup>158</sup>

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151. 11 U.S.C. § 362(k)(1).

152. *Id.* § 524(a)(2).

153. *See Walls v. Wells Fargo Bank, N.A.*, 276 F.3d 502, 508–09 (9th Cir. 2002) (holding that § 362 is evidence that “Congress certainly knows how to create a private right of action when it wants to”); *Pertuso v. Ford Motor Credit Co.*, 233 F.3d 417, 422 (6th Cir. 2000) (holding that “[t]he contrast [between §§ 362 and 524] is instructive” in finding no right of action in § 524).

154. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 304, 98 Stat. 333, 352 (codified at 11 U.S.C. § 522(b)). Congress amended § 362 to provide for such a right following criticism of the use of the court’s contempt power to remedy violations of the automatic stay. *See Peterson v. Wells Fargo Bank, N.A.*, No. 99-CV-6389 (REC/SMS), 2000 WL 1225788, at \*5 (E.D. Cal. Aug. 17, 2000).

155. *See Walls*, 276 F.3d at 509 (“Had Congress meant to create a private right of action for violations of § 524, it could easily have done so; that it did not is a strong [indication] that it did not intend any such remedy.”); *Pertuso*, 233 F.3d at 422 (concluding Congress’s failure to amend § 524 when it amended § 362 to provide for a private right of action evinced an intent not to provide a private right of action under § 524); *Cohen v. HSBC Mortg. Servs., Inc.*, No. 8:15-CV-01922-T27-EAJ, 2016 WL 3748659, at \*2 (M.D. Fla. Mar. 24, 2016) (holding that Congress acted intentionally when amending § 362 to provide for a private right of action but did not similarly amend § 524); *cf. Garfield v. Ocwen Loan Servicing, LLC*, 811 F.3d 86, 92 n.7 (2d Cir. 2016) (comparing the absence of an express right of action in § 524 with the language of § 362(k), but declining to rule on an implied right of action).

156. Robert P. Wasson, Jr., *Remedying Violations of the Discharge Injunction Under Bankruptcy Code § 524, Federal Non-Bankruptcy Law, and State Law Comports with Congressional Intent, Federalism, and Supreme Court Jurisprudence for Identifying the Existence of an Implied Right of Action*, 20 BANKR. DEV. J. 77, 105 (2003).

157. *Id.* (quoting H.R. REP. NO. 95-595, at 365 (1977)).

158. *See Rogers v. NationsCredit Fin. Servs. Corp.*, 233 B.R. 98, 109 (N.D. Cal. 1999).

However, for all the attention courts give the private-right-of-action question, it has little practical impact on the outcome of the dispute.<sup>159</sup> Whether a federal statute creates a private right of action is incredibly important for Article III courts; absent a private right of action, those federal courts likely lack federal question jurisdiction to grant relief.<sup>160</sup> Yet a § 524 dispute’s “core” nature—at least when a debtor does not seek to enforce his discharge injunction as a class<sup>161</sup>—resolves the jurisdictional question for bankruptcy courts.<sup>162</sup>

The absence of a private right of action might cause federal district courts to dismiss a debtor’s complaint for failure to state a claim on which they can grant relief, but that does not leave the debtor without recourse. Some courts dismiss the claim without prejudice, preserving the debtor’s ability to refile in bankruptcy court.<sup>163</sup> Other courts refer the matter to the bankruptcy court pursuant to its district’s local rule or standing order and pursuant to 28 U.S.C. § 1412, which allows courts to transfer cases to other venues “in the interest of justice or for the convenience of the parties.”<sup>164</sup> Nevertheless, the absence of any prescribed remedy invites interpretation of the Bankruptcy Code to determine how it gives the discharge injunction teeth.

## 2. Section 105 as an Enforcement Mechanism

Despite holding that § 524 does not create a private right of action, many courts have concluded that the debtor may have other avenues of recourse. These courts rely on § 105, which allows the bankruptcy court<sup>165</sup> to “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title,” and “mak[e] any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.”<sup>166</sup> The discharge injunction of § 524 is arguably a

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159. See Transcript of Status Conference; Pre-Trial Conference; Motion to Dismiss Adversary Proceeding, to Compel Arbitration, to Strike Class Allegations, to Stay Proceedings at 45, *Anderson v. Credit One Bank, N.A.*, No. 15-08214 (Bankr. S.D.N.Y. May 5, 2015) (calling the issue of a private right of action a “red herring”).

160. See, e.g., *Merrell Dow Pharm. Inc. v. Thompson*, 478 U.S. 804, 814 (1986) (holding that the absence of a congressionally prescribed remedy for violation of a federal statute “is tantamount to a congressional conclusion that the presence of a claimed violation of the statute as an element of a state right of action is insufficiently ‘substantial’ to confer federal-question jurisdiction”).

161. See *infra* Part III.C (discussing how some courts view class action proceedings as “non-core” proceedings).

162. See *supra* Part II.A.

163. See *Cox v. Zale Del., Inc.*, 242 B.R. 444, 446 (N.D. Ill. 1999), *aff’d*, 239 F.3d 910 (7th Cir. 2001).

164. 28 U.S.C. § 1412 (2012); see also *Jones v. CitiMortgage, Inc.*, 666 Fed. App’x 766, 775 (11th Cir. 2016).

165. Courts debate whether § 105 similarly grants federal district courts this authority. Compare *Bessette v. Avco Fin. Servs., Inc.*, 230 F.3d 439, 446 (1st Cir. 2000) (“[A] district court sitting in bankruptcy is similarly authorized to invoke its equitable powers under § 105 when necessary to carry out the provisions of the Bankruptcy Code.”), with *Pertuso v. Ford Motor Credit Co.*, 233 F.3d 417, 423 (6th Cir. 2000) (holding that a federal district court cannot invoke § 105 to remedy a discharge violation).

166. 11 U.S.C. § 105(a) (2012).

provision of the Bankruptcy Code, and the collection of discharged debt is certainly an abuse of process.<sup>167</sup> Indeed, many courts have relied on § 105 to hold contempt proceedings and sanction offenders,<sup>168</sup> offer compensatory damages,<sup>169</sup> grant attorney's fees,<sup>170</sup> and sometimes award punitive damages.<sup>171</sup>

Holding that § 524 is only remediable through contempt proceedings under § 105 is not necessarily fatal to classes of debtors. Although generally only the court that issued an injunction may hold a violator in contempt,<sup>172</sup> some courts have presided over contempt proceedings involving classes of debtors.<sup>173</sup>

### 3. Inherent Contempt Authority

Finally, some courts hold that bankruptcy courts possess an inherent authority to hold contempt proceedings.<sup>174</sup> Reliance on this theory of the bankruptcy courts' power effectively leads to the same result reached by those courts that rely on § 105 to enforce § 524, although 524's inherent authority is "inherent to all courts, while [§ 105's authority] is rooted in statute."<sup>175</sup> One interpretation of a court's inherent contempt authority is that a bankruptcy court has the inherent authority to enforce its own orders.<sup>176</sup> Another more expansive interpretation holds that bankruptcy courts have the inherent authority to enforce provisions of the Bankruptcy Code, regardless of the issuing court.<sup>177</sup> It follows from this view that bankruptcy courts' inherent authority may allow debtors to seek relief in jurisdictions other than the court in which they received their discharge injunction.<sup>178</sup> This interpretation may provide one avenue for debtors to seek relief as a nationwide class.

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167. See *Bessette*, 230 F.3d at 445 (holding that a bankruptcy court may invoke § 105 to enforce § 524).

168. See, e.g., *Hardy v. United States ex rel. Internal Revenue Serv. (In re Hardy)*, 97 F.3d 1384, 1391 (11th Cir. 1996).

169. See, e.g., *Otero v. Green Tree Servicing, LLC (In re Otero)*, 498 B.R. 313, 318, 321–22 (Bankr. D.N.M. 2013) (awarding an amount to a debtor equal to the discharged debt a creditor coerced the debtor into paying).

170. See, e.g., *Watkins v. Guardian Loan Co. (In re Watkins)*, 240 B.R. 668, 683 (Bankr. E.D.N.Y. 1999).

171. See, e.g., *Nibbelink v. Wells Fargo Bank, N.A. (In re Nibbelink)*, 403 B.R. 113, 121–22 (Bankr. M.D. Fla. 2009).

172. See *Baker ex rel. Thomas v. Gen. Motors Corp.*, 522 U.S. 222, 236 (1998).

173. See *infra* Part III.C.

174. See, e.g., *In re Biery*, 543 B.R. 267, 298–99 (Bankr. E.D. Ky. 2015); *Cano v. GMAC Mortg. Corp. (In re Cano)*, 410 B.R. 506, 538 (Bankr. S.D. Tex. 2009); *In re Perviz*, 302 B.R. 357, 370 (Bankr. N.D. Ohio 2003).

175. See *In re Cano*, 410 B.R. at 538.

176. See *Bessette v. Avco Fin. Servs., Inc.*, 230 F.3d 439, 445 (1st Cir. 2000) (holding that a bankruptcy court has inherent contempt powers in addition to its statutory contempt powers under § 105); *Mapother & Mapother, P.S.C. v. Cooper (In re Downs)*, 103 F.3d 472, 477 (6th Cir. 1996) ("Bankruptcy courts, like Article III courts, enjoy inherent power to sanction parties for improper conduct.").

177. See, e.g., *Aiello v. Providian Fin. Corp. (In re Aiello)*, 231 B.R. 693, 702 (Bankr. N.D. Ill. 1999), *aff'd*, 257 B.R. 245 (N.D. Ill. 2000), *aff'd*, 239 F.3d 876 (7th Cir. 2001).

178. See *id.*

### III. COMBATTING § 524 VIOLATIONS AS A CLASS OF DEBTORS

As discussed in the previous section, a court cannot reach the question of a class-waiving arbitration clauses' enforceability unless the debtor is permitted, at the very least, to seek relief individually. Similarly, a court cannot reach this question unless the Bankruptcy Code permits a class of debtors in this context.

This Part discusses classes of debtors in bankruptcy. It explores the different reasons that a debtor may seek relief as a class, such as cost efficiency and the greater availability of legal services. Next, it concludes the Bankruptcy Code does not necessarily preclude a debtor from seeking relief as a class in contested matters such as postdischarge disputes. Finally, it explores the different approaches of bankruptcy courts when deciding whether to allow for a debtor to contest a discharge injunction violation as part of a class. Like the previous Parts, this Part does not seek to resolve which approach is correct. Rather, it merely explains the possible justifications for allowing or denying debtor classes. This is essential to understanding how courts may apply the "inherent conflict" test in the context of discharge injunction violations.

#### *A. Reasons Debtors May Want to Dispute Discharge Injunction Violations as a Class*

There are many practical reasons why a debtor may want to dispute postdischarge misconduct as a class. Most importantly, such class actions are a powerful means to uncover systemic violations of discharge injunctions.<sup>179</sup> Centralizing multiple claims against one creditor may help the court to discover abusive patterns and practices.<sup>180</sup> In addition, litigating as a class allows debtor-plaintiffs to realize economies of scale if the cost of disputing a creditor's conduct outweighs the relatively small amount of a single debtor's damages.<sup>181</sup> The presiding bankruptcy court also benefits from economies of scale by not having to hold multiple proceedings involving the same creditor's misconduct.<sup>182</sup>

Another reason specific to § 524 for forming debtor classes is that reopening one's bankruptcy case may not always be easy. It is likely that a debtor's bankruptcy attorney no longer represents him, leading him to

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179. See *In re Biery*, No. 10-23338, 2014 WL 1431947, at \*6 (Bankr. E.D. Ky. Apr. 14, 2014) ("First and most importantly, class procedures would enhance the chance that the potential class members' contempt claims are adjudicated and any systemic violation of discharges on Respondents' part is discovered.").

180. *In re Melendez*, 224 B.R. 252, 264 (Bankr. D. Mass. 1998) (discerning a creditor's "disturbing pattern" of interference with debtors' ability to receive a "fresh start").

181. See, e.g., *Brannan v. Wells Fargo Home Mortg., Inc. (In re Brannan)*, 485 B.R. 443, 460 (Bankr. S.D. Ala. 2013) (certifying class of debtors); *Montano v. First Light Fed. Credit Union (In re Montano)*, 398 B.R. 47, 58–59 (Bankr. D.N.M. 2008) (same).

182. Cf. *In re Melendez*, 224 B.R. at 271 (consolidating evidentiary hearings of numerous debtors alleging similar claims against the same creditor).



reengage counsel to proceed with his motion to the court.<sup>183</sup> A related reason is that, absent representation, the debtor may not realize the creditor's actions violate his discharge rights under § 524.<sup>184</sup> A class action will protect such debtors. Additionally, attorneys, who are often paid a contingent fee, have little incentive to pursue the claim if the potential compensatory damages are nominal.<sup>185</sup>

### *B. Class Actions in the Bankruptcy Code*

The idea of a class of debtors perhaps seems antithetical to the notion of bankruptcy. After all, one of bankruptcy's primary functions is to equitably allocate the estate of an individual debtor to his creditors.<sup>186</sup> Under this view of bankruptcy, the court derives its authority to preside over a debtor's bankruptcy proceedings through its jurisdiction in rem—that is, over the property of a debtor.<sup>187</sup> If a court may exercise only in rem jurisdiction over a debtor's estate, then it cannot be that debtors may bring a proceeding as a putative class when a particular bankruptcy court does not have jurisdiction over the equitable distribution of the estates of other class members.

This jurisdiction is different from in personam jurisdiction, which allows the court to exercise jurisdiction over individuals.<sup>188</sup> Under this view of the bankruptcy court's jurisdiction, class actions of creditors are not antithetical to the bankruptcy process. Bankruptcy proceedings often involve multiple creditors seeking to recover from the same debtor.<sup>189</sup> Therefore, creditors may file as a class.

Nevertheless, the Bankruptcy Code does not expressly prohibit debtors from forming a class in a dispute against a common creditor. The Bankruptcy Code incorporates Rule 23 of the Federal Rules of Civil Procedure through Rule 7023 to allow for class actions in “adversary proceedings.”<sup>190</sup> Importantly, the Bankruptcy Code contains no express language limiting the right to form a class to creditors.<sup>191</sup> Part VII of the Bankruptcy Rules governs adversary proceedings, which are distinct from “contested matters” governed

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183. *In re Biery*, 2014 WL 1431947, at \*6 (“By that point, his relationship with his bankruptcy counsel will have concluded, and he will need to re-engage counsel to file a contempt motion.”).

184. *Id.* (“Lacking counsel, he may not realize that a prohibited collection attempt violates his discharge and may believe that he is obligated to pay an otherwise discharged debt.”).

185. *Id.*

186. *See supra* notes 40–42 and accompanying text.

187. *See In Rem*, BLACK'S LAW DICTIONARY (10th ed. 2014).

188. *See In Personam*, BLACK'S LAW DICTIONARY (10th ed. 2014).

189. *See Bruce, supra* note 6, at 42–43.

190. 11 U.S.C. § 7023 (2012).

191. *See Wilborn v. Wells Fargo Bank, N.A. (In re Wilborn)*, 609 F.3d 748, 754 (5th Cir. 2010) (“[I]f bankruptcy court jurisdiction is not permitted over a class action of debtors, Rule 7023 is virtually read out of the rules. This would ascribe to Congress the intent to categorically foreclose multi-debtor class actions arising under the Bankruptcy Code without a clear indication of such intent.”).

by Part IX of the Bankruptcy Rules.<sup>192</sup> In short, adversary proceedings are lawsuits within a particular bankruptcy case.<sup>193</sup>

If, as a majority of courts hold, a bankruptcy court must treat a postdischarge dispute under § 524 as remediable through contempt proceedings rather than through a standalone lawsuit,<sup>194</sup> then the dispute could not be an adversary proceeding. Rule 7001 provides an exclusive list of matters considered adversary proceedings under the Code.<sup>195</sup> Disputes not contained in this list are considered contested matters, which may only be initiated by motion.<sup>196</sup> Rule 9020 expressly provides that contested matters include contempt proceedings.<sup>197</sup>

The characterization of a postdischarge dispute under § 524 as a contested matter does not foreclose debtors' ability to seek relief as a class. However, Rule 9014 states that several of the rules applicable to adversary proceedings "shall apply" in contested matters.<sup>198</sup> Although Rule 7023 is not named in this list, courts have nevertheless read Rule 9014 to incorporate Rule 7023.<sup>199</sup>

Rule 9014 specifically states that certain discovery rules incorporated into adversary proceedings by Bankruptcy Rule 7026 "shall not apply" in contested matters.<sup>200</sup> If the list in Rule 9014 were meant to be exclusive, it would have been superfluous to include this express limitation. The permissive wording in Rule 9014 also supports this reading. It provides that certain rules shall apply "unless the court directs otherwise"<sup>201</sup> and that "[t]he court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply."<sup>202</sup> The upshot is that a bankruptcy court has the discretionary authority to apply Rule 7023 in contested matters and allow a class action in such proceedings.<sup>203</sup> Indeed, at least five circuits have read Rule 9014 to incorporate Rule 7023 into contested matters.<sup>204</sup>

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192. FED. R. BANKR. P. pts. VII, IX.

193. 10 RESNICK & SOMMER, *supra* note 36, ¶ 7001.01.

194. *See supra* Part II.B.

195. FED. R. BANKR. P. 7001.

196. *See Barrientos v. Wells Fargo Bank, N.A.*, 633 F.3d 1186, 1191 (9th Cir. 2011) ("[C]ontempt proceedings for a violation of § 524 must be initiated by motion in the bankruptcy case under Rule 9014 and not by adversary proceeding.").

197. FED. R. BANKR. P. 9020.

198. *Id.* 9014(c).

199. *See, e.g., In re Biery*, No. 10-23338, 2014 WL 1431947, at \*4 (Bankr. E.D. Ky. Apr. 14, 2014).

200. FED. R. BANKR. P. 9014(c).

201. *Id.*

202. *Id.*; *see also In re Biery*, 2014 WL 1431947, at \*3 (noting that bankruptcy courts have greater discretion than federal district courts to allow classes of debtors in contempt proceedings in light of Rule 9014).

203. *See In re Biery*, 2014 WL 1431947, at \*4.

204. *See Gentry v. Siegel*, 668 F.3d 83, 89–91 (4th Cir. 2012) (allowing creditors to file proofs of claim as a class pursuant to Rules 7023 and 9014); *Reid v. White Motor Corp.*, 886 F.2d 1462, 1469–70 (6th Cir. 1989) (same); *Certified Class in the Charter Sec. Litig. v. Charter Co. (In re Charter Co.)*, 876 F.2d 866, 867 (11th Cir. 1989) (same); *In re Am. Reserve Corp.*, 840 F.2d 487, 488 (7th Cir. 1988) (same); *Birting Fisheries, Inc. v. Lane (In re Birting Fisheries, Inc.)*, 178 B.R. 849, 851 (W.D. Wash. 1995) (same), *aff'd*, 92 F.3d 939 (9th Cir. 1996).

### C. Allowing Debtors to Proceed as a Class

Just as it would be fruitless to challenge the class-waiving arbitration clause if our former debtor has no legal remedy under § 524,<sup>205</sup> our former debtor would also be unable to challenge it if he cannot dispute a discharge injunction violation as part of class. Courts disagree over a debtor's ability to bring a claim as a class. Those courts that would allow our former debtor to bring his claim as a class may permit a nationwide class or may limit the class to debtors within the same federal district. Conversely, some courts may hold that they have no jurisdiction to settle postdischarge disputes of debtors with no connection to our former debtor's estate. The following discussion summarizes the different treatment of classes of debtors in this context.<sup>206</sup>

#### 1. Nationwide Classes of Debtors

Some courts have allowed for nationwide classes of debtors by relying on the contempt power of the courts.<sup>207</sup> For example, the First Circuit held that debtors can maintain a class to seek enforcement of a § 524 discharge injunction in either bankruptcy court or district court.<sup>208</sup> It first reasoned that both the district court and bankruptcy court may rely on their inherent contempt powers as well as their statutory contempt power under § 105 to enforce § 524.<sup>209</sup> Next, it held that § 524 creates a "statutory injunction" applicable to all debtors, which differs from a court-ordered injunction applicable only to a simple debtor that is "individually crafted by the bankruptcy judge, and in which that judge's insights and thought processes may be of particular significance."<sup>210</sup> Accordingly, the First Circuit held that

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205. See *supra* Part II.B.

206. This section limits its discussion to the ability for debtors to dispute discharge injunction violations as a *putative* class. It is important to note that classes of debtors may find it difficult to meet the certification requirements of Rule 23(b)(3) in contesting systemic discharge injunction violations. It may be that the resolution of the debtors' claims would require the court to conduct too many individualized inquiries, such that the plaintiffs fail to meet the predominance and superiority requirements, and possibly even the commonality requirement. See *Wal-Mart Stores, Inc. v. Dukes*, 564 U.S. 338, 350 (2011) (holding that commonality requires a contention "that it is capable of classwide resolution," and that plaintiffs cannot simply allege they "have all suffered a violation of the same provision of law"); *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 624–25 (1997) (holding that a class of plaintiffs who were or would someday be injured by asbestos exposure did not satisfy the predominance requirement, as there was significant variation in the manner of their exposure and the types of their injuries). A more complete discussion of class certification, however, is beyond the scope of this Note.

207. See *Bruce*, *supra* note 6, at 63–66 (discussing "contempt power" cases that look to the limits of judicial authority rather than to their basis for subject matter jurisdiction).

208. *Bessette v. Avco Fin. Servs., Inc.*, 230 F.3d 439, 445 (1st Cir. 2000).

209. *Id.*

210. *Id.* at 446; see also *Walls v. Wells Fargo Bank, N.A. (In re Walls)*, 262 B.R. 519, 528 (Bankr. E.D. Cal. 2001) (noting that the discharge injunction is a "Code created, statutory injunction[]" that "does not depend on individual orders for injunctive relief fashioned by individual bankruptcy judges"); Elizabeth Warren & Jay L. Westbrook, *Class Actions for Post-Petition Wrongs: National Relief Against National Creditors*, 22 AM. BANKR. INST. J. 14, 46 (2003) (arguing the characterization of § 524 as an "'injunction' is a legal fiction, a

enforcement of the discharge injunction of § 524 need not be confined to the issuing tribunal.<sup>211</sup> Finally, the First Circuit held that § 7023 allowed the debtors to seek relief in contempt proceedings as a class in either district or bankruptcy court.<sup>212</sup>

Courts have also relied on their § 1334 subject matter jurisdiction to allow for a nationwide class of debtors.<sup>213</sup> Some have interpreted § 1334(b), which provides for bankruptcy courts' subject matter jurisdiction,<sup>214</sup> to allow a bankruptcy court to preside over any bankruptcy action, regardless of the court in which it originated.<sup>215</sup> Other courts have adopted an expansive view of § 1334(e) of the Bankruptcy Code, which grants the district court in which a bankruptcy case is filed "exclusive jurisdiction . . . of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate."<sup>216</sup> According to the latter view, § 1334(e) does not merely grant in rem jurisdiction; rather, its primary purpose is to prevent multiple judgments relating to the same estate and thus undermining orderly distribution of assets.<sup>217</sup> Because a discharge injunction violation necessarily occurs after the distribution of debtors' estates, there is no risk of interference with the courts' administration.<sup>218</sup>

## 2. Classes of Debtors in "Home Courts"

Some courts allow debtors to seek relief as a class, but have limited the members of the class to those within the district of the "home court"<sup>219</sup> in

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point buttressed by the fact that the usual findings for an injunction do not have to be made and the usual notice and a hearing are not needed to bind the entire world").

211. *Bessette*, 230 F.3d at 446.

212. *Id.*

213. *See, e.g.*, *Bank United v. Manley*, 273 B.R. 229, 232, 246–47 (N.D. Ala. 2001); *Noletto v. Nationsbank Mortg. Corp. (In re Noletto)*, 244 B.R. 845, 849 (Bankr. S.D. Ala. 2000).

214. *See supra* note 46 and accompanying text.

215. *See, e.g.*, *Cano v. GMAC Mortg. Corp. (In re Cano)*, 410 B.R. 506, 551 (Bankr. S.D. Tex. 2009) ("The jurisdictional test for bankruptcy court jurisdiction is not whether each cause of action relates to or arises in or under an individual bankruptcy case. The test is whether each cause of action relates to or arises in or under *any* bankruptcy case.").

216. 28 U.S.C. § 1334(e) (2012).

217. *See, e.g.*, *Chiang v. Neilson (In re Death Row Records, Inc.)*, No. ADV. 10-02574, 2012 WL 952292, at \*12 (B.A.P. 9th Cir. Mar. 21, 2012) (holding that claims that are not solely in rem may be brought outside their "home court," but holding contempt proceedings must remain with the issuing tribunal); *Manley*, 273 B.R. at 247 (holding that § 1334(e) only affects the bankruptcy court's jurisdiction "when a judgment converts the disputed claim into a finite unit of estate property" (citation omitted)).

218. Other provisions of the Code may support a departure from the view that § 1334(e) grants a bankruptcy court only in rem jurisdiction. For example, § 541, which defines the property of the debtor's estate in bankruptcy, exempts any wages the debtor earns after the case's commencement. 11 U.S.C. § 541(a)(6) (2012). However, a creditor seeking to recover these wages postdischarge would nevertheless be violating the discharge injunction, even though those wages were not part of the debtor's estate. *See In re Dickerson*, 510 B.R. 289, 292, 298 (Bankr. D. Idaho 2014) (holding that a creditor's attempts to collect debtor's postdischarge wages violated his discharge injunction).

219. *See* Richard H. Gibson, *Home Court, Outpost Court: Reconciling Bankruptcy Case Control with Venue Flexibility in Proceedings*, 62 AM. BANKR. L.J. 37, 38 (1988).

which the bankruptcy petition was filed.<sup>220</sup> Similar to courts that have allowed nationwide classes of debtors, these “home court” cases have allowed debtor classes under two theories. The first adheres to an interpretation of § 1334(e) that supports that provision’s intended prevention of multiple judgments relating to the same estate.<sup>221</sup> Restricting a debtor class to those whose estates have been administered by the same court do not implicate this concern, despite a departure from a rigid interpretation of the court’s in rem jurisdiction.<sup>222</sup>

The second theory views § 524 as enforceable only through contempt proceedings. Unlike those courts that have certified nationwide classes of debtors, however, the “home court” cases that rely on contempt proceedings conclude that an injunction may only be enforced by its issuing court.<sup>223</sup> Although classes of debtors necessarily involve aggregation of debtors from different bankruptcy cases, the theory holds these debtors may seek class relief if they all received an injunction from the same court.<sup>224</sup>

### 3. Classes of Debtors Not Permitted

Finally, there are many courts that do not recognize debtor-plaintiff class actions. They hold that a bankruptcy court may only preside over claims with a sufficient nexus to the debtor’s bankruptcy estate.<sup>225</sup> In reaching this conclusion, these courts rely on the bankruptcy court’s in rem jurisdiction and administration of a particular debtor’s estate.<sup>226</sup> Accordingly, courts adopting this interpretation of bankruptcy subject matter jurisdiction are unlikely to allow a class action aggregating multiple debtors’ causes of action, regardless of how similar. This would require collective treatment across multiple estates that were not previously consolidated in the same case.<sup>227</sup>

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220. For a discussion of “home court” cases, see Bruce, *supra* note 6, at 56–62.

221. See, e.g., *Williams v. Sears, Roebuck & Co. (In re Williams)*, 244 B.R. 858, 866 (S.D. Ga. 2000), *aff’d sub nom. Williams v. Sears Roebuck, Co.*, 34 F. App’x 967 (11th Cir. 2002).

222. However, these courts do not go as far as those that allow for nationwide classes of debtors. See *supra* Part III.C.1.

223. See *Beck v. Gold Key Lease, Inc. (In re Beck)*, 283 B.R. 163, 167 (Bankr. E.D. Pa. 2002) (citing *Waffenschmidt v. MacKay*, 763 F.2d 711, 716 (5th Cir. 1985)); see also *Montano v. First Light Fed. Credit Union (In re Montano)*, No. 7-04-17866 SL, 2007 WL 2688606, at \*1–2 (Bankr. D.N.M. Sept. 10, 2007) (holding that debtors may enforce § 524 through the court’s contempt powers but that the class must be limited to those who received their discharge from the District of New Mexico).

224. See *In re Beck*, 283 B.R. at 175.

225. One scholar has described these as “nexus” cases, in which the bankruptcy court has jurisdiction only over the debtor’s estate. Bruce, *supra* note 6, at 51–52.

226. *Id.*

227. See, e.g., *Barrett v. AVCO Fin. Servs. Mgmt. Co.*, 292 B.R. 1, 2 (D. Mass. 2003); *Singleton v. Wells Fargo Bank, N.A. (In re Singleton)*, 284 B.R. 322, 324 (D.R.I. 2002).

IV. ANALYZING THE ARBITRABILITY OF  
POSTDISCHARGE § 524 DISPUTES UNDER THE  
“INHERENT CONFLICT” TEST

As previously discussed, this Note does not seek to resolve the disagreements over the jurisdictional and enforcement considerations of § 524.<sup>228</sup> In addition, it does not propose the best way to consider classes of debtors.<sup>229</sup> Rather, for the purpose of analysis, it assumes our former debtor may bring his dispute as a class. Under this assumption, it proposes to resolve how courts should apply the “inherent conflict” test to determine whether to enforce a class-waiving arbitration clause in this context.

Because of the frequency with which class waivers appear in arbitration clauses of consumer contracts,<sup>230</sup> the determination of whether debtors may waive their procedural right to collectivize is inextricably tied to the arbitrability of their claim. However, as discussed in Part I.D, courts disagree over the way in which class waivers figure into their arbitrability analysis. This Part will first apply the “inherent conflict” test to determine that a postdischarge dispute under § 524 is arbitrable and that the Bankruptcy Code does not provide debtors with a substantive right to collectivize.<sup>231</sup> It will then address the enforceability of class waivers in bankruptcy in light of *Italian Colors* and will conclude that the “effective vindication” does not render such class waivers unenforceable.

A. Applying the “Inherent Conflict” Test to § 524

Because both the text and the legislative history of the Bankruptcy Code are silent as to the arbitrability of postdischarge disputes under § 524, courts must employ the “inherent conflict” test to determine (1) whether § 524 disputes are arbitrable and (2) whether the class-waiving arbitration clauses inherently conflict with a substantive right to collectivize.<sup>232</sup>

1. The Arbitrability of Postdischarge Disputes Under § 524

Although the circuits are split on the application of the “inherent conflict” test under *McMahon*,<sup>233</sup> it is likely that either approach should lead to the same conclusion that § 524 disputes are arbitrable.

Under the “inherent conflict” test of the Third, Fifth, and Ninth Circuits, the first step in finding a dispute not arbitrable is to look to what, if any, rights

228. *See supra* Part II.

229. *See supra* Part III.

230. *See supra* note 7 and accompanying text.

231. This Note uses the term “arbitrable” in this context to mean the bankruptcy court does not have discretion to refuse to compel arbitration. *See supra* note 108 and accompanying text.

232. *See* *Belton v. Ge Capital Consumer Lending, Inc. (In re Belton)*, No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*6 (S.D.N.Y. Oct. 14, 2015); *see also* *Lewis v. Epic Sys. Corp.*, 823 F.3d 1147, 1158 (7th Cir. 2016) (finding a class-waiving arbitration clause was unenforceable because it “ran up against the substantive right to act collectively that the NLRA gives to employees,” despite holding the claim itself was arbitrable), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-285).

233. *See supra* Part I.D.2.

derive from § 524.<sup>234</sup> In addition to the disputed treatment of § 524,<sup>235</sup> the different language used by each of these circuits at this step perhaps complicates the analysis. For example, the Fifth Circuit in *In re National Gypsum* first looked to whether the claim “derives exclusively from the provisions of the Bankruptcy Code.”<sup>236</sup> The discharge injunction undoubtedly meets this test. However, the Third and Ninth Circuits both refer to a claim “created by the Bankruptcy Code.”<sup>237</sup> Strictly construed, courts may find that § 524 fails this test if they first conclude that § 524 creates no actionable claim.<sup>238</sup> If, however, these courts consider a “claim” in a less formal sense, it is likely they will find the first inquiry of the “inherent conflict” test satisfied.

Under the approaches of the Second and Fourth Circuits, courts may avoid the thorny question of whether the discharge injunction of § 524 is a “claim” for purposes of the test by relying only on the second policy-based inquiry of the Third, Fifth, and Ninth Circuits.<sup>239</sup> Therefore, if there is no dispute that § 524 satisfies the first inquiry of the Third, Fifth, and Ninth Circuits, the tests employed by all circuits merge. Accordingly, any court undertaking this inquiry will look to the purposes of the Bankruptcy Code to determine whether an inherent conflict with the FAA necessitates a refusal to enforce an arbitration clause.

Perhaps because the Supreme Court has not weighed in on the “inherent conflict” test in bankruptcy, there is a debate as to whether this second purposive approach should find that the FAA conflicts with the purposes of a discharge injunction. Nowhere is this debate more apparent than in the Southern District of New York, where a recent case on this very matter created an intradistrict split. That case, *In re Anderson*, held a dispute of a discharge injunction violation not arbitrable under the “inherent conflict” test.<sup>240</sup> Eight months earlier, the Southern District decided *In re Belton*, the facts of which were almost identical to those of *In re Anderson*.<sup>241</sup> However, unlike the court in *In re Anderson*, the court in *In re Belton* held a discharge injunction violation to be arbitrable.<sup>242</sup>

The disagreement concerned an interpretation of the Second Circuit’s holding in *Hill*, which applied the “inherent conflict” test to a violation of the

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234. See *supra* Part I.D.2.

235. See *supra* Part II.

236. *Ins. Co. of N. Am. v. NGC Settlement Tr. & Asbestos Claims Mgmt. Corp. (In re Nat’l Gypsum Co.)*, 118 F.3d 1056, 1067 (5th Cir. 1997).

237. *In re Mintze*, 434 F.3d 222, 231 (3d Cir. 2006); see also *supra* Part I.D.2.

238. See *supra* Part II.B.1 (discussing cases in which courts found that § 524 provides no private right of action).

239. See *supra* Part I.D.2.

240. *Credit One Fin. v. Anderson (In re Anderson)*, 553 B.R. 221, 231–34 (S.D.N.Y.), appeal docketed, No. 16-2496 (2d Cir. July 13, 2016). The court declined to review the bankruptcy court’s decision that the class waiver was unenforceable. See *supra* note 128 and accompanying text.

241. *Belton v. Ge Capital Consumer Lending, Inc. (In re Belton)*, No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*1–2 (S.D.N.Y. Oct. 14, 2015).

242. *Id.* at \*6–9.

Bankruptcy Code's automatic stay provision.<sup>243</sup> However, that disagreement also brings into focus a larger dispute over how bankruptcy courts should apply the "inherent conflict" test. The court in *In re Anderson* reasoned that a discharge is "so fundamentally related to a debtor's fresh start" and that "arbitration is inadequate to protect such core, substantive rights granted by the Code."<sup>244</sup> The court in *In re Belton*, however, looked to whether the FAA "severely conflicted" with § 524 such that debtors could not vindicate their rights under the Bankruptcy Code.<sup>245</sup>

As discussed in Part I.D.2, the Third Circuit proposed, and the Second Circuit adopted, three policy factors to consider: (1) "the goal of centralized resolution of purely bankruptcy issues," (2) "the need to protect creditors and reorganizing debtors from piecemeal litigation," and (3) "the undisputed power of a bankruptcy court to enforce its own orders."<sup>246</sup> Notably, these factors look not to the adequacy of arbitration as a forum but rather to the extent to which arbitration could disrupt the bankruptcy process. The court in *In re Belton* similarly did not consider the adequacy of arbitration as a forum but instead held that arbitration does not "necessarily or seriously jeopardize the objectives of the Bankruptcy Code" when a dispute "'would not interfere with or affect the distribution of the estate' and would not 'affect an ongoing reorganization.'"<sup>247</sup> In contrast, the court in *In re Anderson* looked to potential "high barriers" debtors may face in arbitration, including inefficient resolution of their claims.<sup>248</sup>

In light of what the Supreme Court has held to be a "liberal federal policy favoring arbitration,"<sup>249</sup> the court's approach in *In re Belton* was likely the correct one. Indeed, a recent bankruptcy decision held that *In re Belton* was "better aligned with the federal policy favoring arbitration" and adopted its analysis over that of *In re Anderson*.<sup>250</sup> It held that the enforcement of a class-waiving arbitration clause did not inherently conflict with § 524.<sup>251</sup>

The Supreme Court has made clear that arbitrators are just as capable as courts of efficiently resolving complex matters.<sup>252</sup> It held in *McMahon* that a court's ability to refuse to compel arbitration is not grounded in the adequacy of arbitration as a forum but, rather, in the finding of an "irreconcilable conflict between arbitration and [a federal statute's]

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243. *MBNA Am. Bank, N.A. v. Hill*, 436 F.3d 104, 108–10 (2d Cir. 2006).

244. *In re Anderson*, 553 B.R. at 232–33.

245. *In re Belton*, 2015 WL 6163083, at \*6.

246. *Ins. Co. of N. Am. v. NGC Settlement Tr. & Asbestos Claims Mgmt. Corp. (In re Nat'l Gypsum)*, 118 F.3d 1056, 1069 (5th Cir. 1997).

247. *In re Belton*, 2015 WL 6163083, at \*8 (quoting *Hill*, 436 F.3d at 109–10).

248. *In re Anderson*, 553 B.R. at 232 n.9. The court reasoned that potential costs associated with arbitration could also act as a high barrier. Because the Supreme Court included arbitration costs as part of its class waiver analysis in *Italian Colors*, this Note will discuss cost considerations in Part IV.B, *infra*.

249. *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

250. *Williams v. Navient Sols., LLC (In re Williams)*, 564 B.R. 770, 783 (Bankr. S.D. Fla. 2017).

251. *Id.*

252. *See Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 240 (1987) (holding that an arbitration tribunal is capable of handling complex antitrust matters).



underlying purposes.”<sup>253</sup> Since *McMahon*, the “inherent conflict” test outside of bankruptcy has led to the presumption of arbitrability, and a party opposing arbitration faces a high hurdle in persuading the court to find an inherent conflict.<sup>254</sup>

Bankruptcy courts are not insulated from *McMahon* and its progeny. Despite the unique considerations in bankruptcy, such as the centralizing pull of the bankruptcy courts’ jurisdiction and the deference given to them on review of arbitrability determinations,<sup>255</sup> bankruptcy courts must look only to a conflict of laws. And although a court may conclude the discharge injunction is a court order that the issuing court alone may enforce,<sup>256</sup> it may also conclude that the discharge order is not handcrafted such that the issuing court alone is qualified to interpret it.<sup>257</sup> Indeed, the discharge injunction is not tailored to individual debtors even though each individual debtor receives his own discharge. The discharge injunction has the universal effect of enjoining former creditors from pursuing any discharged debt and requires no bankruptcy expertise to interpret.<sup>258</sup> Therefore, in light of the current state of FAA jurisprudence, discharge injunction violations are likely arbitrable.

## 2. A Substantive Right to Class Actions in Bankruptcy?

The “inherent conflict” test also requires determining whether the Bankruptcy Code grants debtors a substantive right to challenge discharge injunction violations as a class. However, no such right exists.

Although the Supreme Court has yet to find an inherent conflict based on a substantive right for plaintiffs to collectivize under federal law, some circuits have refused to enforce class-waiving arbitration clauses. Recently, the Seventh Circuit found in *Lewis v. Epic Systems Corp.*<sup>259</sup> a “contrary congressional command” in the NLRA sufficient to preclude class-waiving arbitration clauses in labor contracts.<sup>260</sup> In that case, the court held that the statute’s legislative history supported the reading of its guarantee to workers to “engage in other concerted activities” to include the right to litigate as a class.<sup>261</sup> The Ninth Circuit reached a similar holding, relying heavily on the analysis of the Seventh Circuit in *Lewis*.<sup>262</sup>

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253. *Id.*

254. *See supra* Part I.D.1.

255. *See supra* Part I.D.2.

256. *See supra* note 176 and accompanying text. Ironically, under this approach, the arbitrability of a claim and the ability for debtors to bring their claim as a nationwide class may be mutually exclusive. If the bankruptcy court that issued the injunction is the only court that may enforce it, then that court necessarily cannot enforce discharge injunctions issued by other bankruptcy courts.

257. *See Belton v. Ge Capital Consumer Lending, Inc. (In re Belton)*, No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*8 (S.D.N.Y. Oct. 14, 2015); *see also supra* note 210 and accompanying text.

258. *See In re Belton*, 2015 WL 6163083, at \*8.

259. 823 F.3d 1147 (7th Cir. 2016), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-285).

260. *Id.* at 1152, 1156.

261. *Id.* at 1152–53.

262. *Morris v. Ernst & Young, LLP*, 834 F.3d 975, 983–84 (9th Cir. 2016), *cert. granted*, 137 S. Ct. 809 (2017) (No. 16-300).

In contrast, no such right exists in bankruptcy. The Bankruptcy Code does not contain any language similar to the NLRA guaranteeing debtors any right to collectivize. Although the Bankruptcy Code may allow for debtor class actions,<sup>263</sup> its permissiveness is a far cry from a guarantee. This point is further supported by both the infrequency of debtor class actions and the disagreement over whether to allow debtors to dispute discharge injunction violations as a class.<sup>264</sup> In light of this reading, bankruptcy courts should find class-waiving arbitration clauses enforceable in this context.

*B. The Effect of Italian Colors on the  
“Inherent Conflict” Test in Bankruptcy*

Although the Supreme Court weakened the “effective vindication” doctrine with its decision in *Italian Colors*,<sup>265</sup> some argue that the “inherent conflict” test in bankruptcy is largely insulated from its holding.<sup>266</sup> One argument is that the “inherent conflict” test is more sensitive to costs incurred by debtors in bankruptcy than by ordinary plaintiffs.<sup>267</sup> When a class-waiving arbitration clause saddles debtors with steeper litigation costs, a court may hold such a clause unenforceable under the “inherent conflict” test, as the debtor is unable to effectively vindicate his rights.<sup>268</sup>

The argument that the “inherent conflict” test insulates bankruptcy courts from *Italian Colors* relies on finding that the test in bankruptcy postdischarge is sufficiently different from Article III courts’ analysis of class waivers. This interpretation, however, is not supported by the *Italian Colors* decision. In its holding, the Supreme Court relied on the language of *McMahon* to hold that the antitrust claim at issue was arbitrable and that the class waiver was enforceable.<sup>269</sup> It held that “arbitration is a matter of contract” and that “courts must ‘rigorously enforce’ arbitration agreements according to their terms.”<sup>270</sup> A party’s only proverbial escape hatch to any arbitration agreement—including one in which he waived his right to litigate as a class—is a showing of an inherent conflict of laws. No part of the *Italian Colors* holding indicated the Court’s intention to cabin its decision to antitrust law specifically or areas outside of bankruptcy more generally.

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263. See *supra* Parts III.B, III.C.

264. See *supra* Part III.C.

265. See *supra* Part I.D.1.

266. See Bruce, *supra* note 18, at 477 (arguing that the Supreme Court’s “reject[ion of] similar financial considerations in the context of an effective vindication challenge to a class arbitration waiver” should not “have any bearing on bankruptcy courts’ inherent conflict analysis”).

267. *Id.* at 477–78.

268. The court in *In re Anderson* adopts a similar argument: Without mentioning the *Italian Colors* decision or the “effective vindication” doctrine, it held arbitration to be an inadequate forum to protect a debtor’s fresh start in part because of potential arbitration costs. *Credit One Fin. v. Anderson (In re Anderson)*, 553 B.R. 221, 232 & n.9 (S.D.N.Y.), *appeal docketed*, No. 16-2496 (2d Cir. July 13, 2016).

269. See *supra* Part I.D.1.

270. *Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2309 (2013) (quoting *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 221 (1985)).

The *In re Belton* decision provides a model for properly incorporating the *Italian Colors* decision.<sup>271</sup> First, it looked to the debtors' claim under § 524.<sup>272</sup> Upon finding no conflict between § 524 and the FAA, it then turned to the "effective vindication" doctrine of *Italian Colors* and found no impediment to the debtors' right to pursue a statutory remedy in individual arbitration.<sup>273</sup> Indeed, other courts that have interpreted *Italian Colors* in bankruptcy have come to a similar conclusion about the "inherent conflict" test.<sup>274</sup>

## V. WHERE DOES OUR FORMER DEBTOR GO FROM HERE?

Although the Supreme Court is comfortable deferring to arbitration if parties have agreed to resolve their disputes before an arbitrator, many have criticized arbitration as inadequate to protect consumers' rights. Class-waiving arbitration clauses may stifle claims that consumers would otherwise bring absent barriers imposed by individual arbitration. Accordingly, this section proposes a legislative remedy to provide debtors a nonwaivable private right of action that would allow them to litigate discharge injunction violations as a class in bankruptcy court.

### A. The Shortcomings of Individual Arbitration

If the Supreme Court's confidence in the adequacy of arbitration is not misplaced, our former debtor might not worry about individually arbitrating his dispute over a discharge injunction violation. In addition, even if he incurs arbitration fees, he likely does not face the same barrier to relief as the plaintiffs in *Italian Colors*;<sup>275</sup> his dispute merely becomes more expensive.<sup>276</sup>

Not all share the Supreme Court's stance, however. Some question the fairness of arbitrating many consumer-related disputes.<sup>277</sup> Specifically, there

271. *Belton v. Ge Capital Consumer Lending, Inc. (In re Belton)*, No. 15-CV-1934 (VLB), 2015 WL 6163083, at \*4 (S.D.N.Y. Oct. 14, 2015).

272. *Id.*

273. *Id.* at \*9–10.

274. *See, e.g., Campos v. Bluestem Brands, Inc.*, No. 3:15-CV-00629-SI (MHS), 2016 WL 297429, at \*11 (D. Or. Jan. 22, 2016) (enforcing a class-waiving arbitration clause by finding that there was no inherent conflict between the policies underlying an automatic stay and the FAA and that the Bankruptcy Code does not guarantee economically viable paths to resolving disputes); *Williams v. Navient Sols., LLC (In re Williams)*, 564 B.R. 770, 783 (Bankr. S.D. Fla. 2017) (adopting the analysis of *In re Belton*).

275. *See supra* note 96 and accompanying text.

276. Because he is not entirely unable to vindicate his rights, a court is unlikely to override the class-waiving arbitration clause even under Justice Kagan's characterization of the "effective vindication" doctrine in her *Italian Colors* dissent. *See Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2313 (2013) (Kagan, J., dissenting) (justifying a refusal to enforce an arbitration clause only when "such a clause . . . operates to confer immunity from potentially meritorious federal claims").

277. *See generally* Jessica Silver-Greenberg & Robert Gebeloff, *Arbitration Everywhere, Stacking the Deck of Justice*, N.Y. TIMES (Oct. 31, 2015), [http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html?\\_r=0](http://www.nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html?_r=0) [<https://perma.cc/CCA8-VPLG>] (arguing that arbitration

is evidence that arbitration does not always provide an easy path to resolution for individual consumers.<sup>278</sup> In a recent article, Professor Judith Resnik reported that very few individual consumers pursue claims through arbitration relative to those eligible to bring claims.<sup>279</sup> In contrast, a greater number of individual consumers pursue their claims in court relative to those eligible to bring claims indicating that courts are more accessible than arbitration.<sup>280</sup> She therefore argues that mandatory class-waiving arbitration clauses serve to restrict consumers' ability to pursue their rights despite some predictions that the clauses would lead to "thousands of separate proceedings."<sup>281</sup>

In addition, class-waiving provisions hinder the enforcement of many small-value claims. Professor Resnik found that consumers rarely imagine they would themselves bring cases and concluded that private enforcement therefore depends on collective action.<sup>282</sup> The inability to spread costs across a class may support consumers' sentiments, particularly if the cost of bringing a claim exceeds the amount they stand to recover individually. As Justice Kagan argued in her *Italian Colors* dissent, "No rational actor would bring a claim worth tens of thousands of dollars if doing so meant incurring costs in the hundreds of thousands."<sup>283</sup> The inability to spread these costs all but prevents individuals from filing such claims in the first place.<sup>284</sup>

This justification for class proceedings is as important in bankruptcy as in other areas of the law. Because the costs of disputing a discharge injunction violation may very well exceed the likely recovery, individual debtors face the same barriers to recovery without the ability to collectivize.<sup>285</sup>

Further, public enforcement by government entities on behalf of consumers likely depends on claims filed by private parties to bring companies' illegal activities to the government's attention.<sup>286</sup> Although the Bankruptcy Code authorizes the Department of Justice to investigate creditor misconduct through the U.S. Trustee Program,<sup>287</sup> many incidents of

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clauses in consumer contracts represent a "far-reaching power play orchestrated by American corporations").

277. *Id.*

278. Resnik, *supra* note 70, at 2817.

279. *Id.* at 2893.

280. *Id.* at 2903–04.

281. *Id.* at 2892–93 (quoting *AT&T v. Concepcion*, 563 U.S. 333, 363 (2011) (Breyer, J., dissenting)).

282. *Id.* at 2904.

283. *Am. Express Co. v. Italian Colors Rest.*, 133 S. Ct. 2304, 2316 (2013) (Kagan, J., dissenting).

284. *Id.*

285. *See, e.g., In re Biery*, 543 B.R. 267, 302 (Bankr. E.D. Ky. 2015) (classifying debtors' postdischarge claims as "low-value," thereby allowing them to pursue their claims as class).

286. Resnik, *supra* note 70, at 2909–10 (finding that in approximately two-thirds of consumer class actions also pursued by the government, the government filed its complaints after private parties had brought suit).

287. *See generally* 28 U.S.C. § 586(a)(3) (2012).

misconduct are nevertheless likely to slip through the cracks absent private enforcement.<sup>288</sup>

### B. A Legislative Solution

In light of the considerations discussed in Part V.A, it is very likely that our former debtor will face significant hurdles to vindication of his right to a fresh start. It is problematic, therefore, that present case law likely mandates the enforcement of the class-waiving arbitration clause in his credit agreement. The evolution of bankruptcy law from a mere means to protect creditors to a regime that also protects the “honest but unfortunate debtor” demonstrates the importance of the discharge injunction.<sup>289</sup> But the purpose of the discharge injunction is defeated if, in practice, creditors can use class-waiving arbitration clauses as roadblocks to debtors’ attempts to fight systemic violations of § 524.

The Bankruptcy Code grants substantial authority to bankruptcy courts to handle matters “arising under” the Code or “arising in” a bankruptcy proceeding.<sup>290</sup> Indeed, in their “inherent conflict” test, most circuit courts recognize the bankruptcy courts’ ability to enforce their own orders as justification for refusing to allow arbitrators to resolve certain matters in bankruptcy.<sup>291</sup> The wide disagreement over how to treat discharge injunction disputes demonstrates that, at present, § 524 does not grant bankruptcy courts sufficient authority to protect former debtors.<sup>292</sup> And although a majority of courts agree that courts may enforce § 524 through contempt proceedings,<sup>293</sup> their interpretation of § 524 and their application of the “inherent conflict” test is muddled when a debtor seeks to dispute systemic discharge injunction violations as a class.

In finding an inherent conflict by reasoning that a bankruptcy court may enforce its own orders,<sup>294</sup> courts may do one of two things. First, they may treat the discharge injunction as a court order tailored to an individual debtor’s proceeding.<sup>295</sup> By doing so, they would necessarily preclude classes of debtors. Second, they may characterize the discharge injunction as a “statutory injunction” and ground bankruptcy jurisdiction in the enforcement of the Bankruptcy Code rather than in the administration of an individual debtor’s estate.<sup>296</sup> Accordingly, in the context of a discharge injunction violation, courts must read between the lines of the Bankruptcy Code and bend the meaning of an injunction to allow for class enforcement if they wish to avoid foreclosing the possibility of debtor class actions.

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288. See Bruce, *supra* note 18, at 449 (arguing that the U.S. Trustee Program is “poorly positioned to discover small but pervasive incidences of lender misconduct”).

289. *Grogan v. Garner*, 498 U.S. 279, 287 (1991) (quoting *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934)); see *supra* notes 27, 39 and accompanying text.

290. See *supra* Part I.B (discussing the jurisdiction of bankruptcy courts).

291. See *supra* Part I.D.2 (discussing the “inherent conflict” test in bankruptcy).

292. See *supra* Part II.B.

293. See *supra* Part II.B.

294. See *supra* note 256 and accompanying text.

295. See *supra* note 256 and accompanying text.

296. See *supra* note 210 and accompanying text.

By allowing debtors to dispute systemic discharge injunction violations as a class, courts may avoid the problems of underenforcement and underdetection, as debtors have the financial incentive to bring suit. Congress should therefore amend § 524 of the Bankruptcy Code to create a private right of action that debtors may bring as a class in bankruptcy court.

Congress has already recognized the potential for abuse of debt collections. In 1977, it enacted the Fair Debt Collection Practices Act (FDCPA),<sup>297</sup> which creates a private right of action that allows consumers to directly sue abusive debt collectors,<sup>298</sup> including on behalf of a class.<sup>299</sup> However, the FDCPA limits debtors' ability to seek relief by regulating only third-party debt collectors.<sup>300</sup> In addition, although another statute—the Fair Credit Reporting Act—prohibits creditors from reporting inaccurate information to consumer reporting agencies,<sup>301</sup> it does not prevent other forms of abuse.<sup>302</sup> As such, our former debtor is left without an express statutory grant to bring a class action against an abusive creditor under § 524. By providing for an express right of action, Congress would close this gap and guarantee our former debtor the fresh start he deserves.

An express private right of action does not resolve the arbitrability of the dispute, nor does it address the enforceability of a class waiver. It has long been evident that the current state of the “inherent conflict” test in bankruptcy is uncertain and that clarity is needed.<sup>303</sup> Accordingly, Congress should heed the proposals to enact legislation prohibiting class-waiving arbitration clauses in core proceedings.<sup>304</sup> This bright-line rule, operating in conjunction with a debtor's right to bring a class action, would bring much needed clarity to a muddy area of bankruptcy law and allow debtors to enjoy the full protection of their discharge injunctions.

#### CONCLUSION

A discharge injunction is a powerful incentive for consumers plagued by debt to enter into bankruptcy. For some former debtors, however, the promise of a fresh start is illusive, as creditors continue to pursue discharged

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297. Fair Debt Collection Practices Act, Pub. L. No. 95-109, 91 Stat. 874 (1977) (codified at 15 U.S.C. § 1692–1692p (2012)).

298. 15 U.S.C. § 1692k.

299. *See, e.g.,* Santoro v. Aargon Agency, Inc., 252 F.R.D. 675, 687 (D. Nev. 2008).

300. 15 U.S.C. § 1692k(a).

301. 15 U.S.C. § 1681s-2(a)(1)(A) (2012).

302. *See supra* notes 2–5 and accompanying text.

303. Alan N. Resnick, *The Enforceability of Arbitration Clauses in Bankruptcy*, 15 AM. BANKR. INST. L. REV. 183, 185 (2007) (arguing that the many different approaches to the “inherent conflict” test in bankruptcy has led to “uncertainty and confusion . . . with respect to the interplay between arbitration and bankruptcy and whether an arbitration clause should be enforced in a particular proceeding in a bankruptcy case”).

304. *Id.* at 214. Bankruptcy is not the only area in which there have been calls to reform arbitration clauses. The Consumer Financial Protection Bureau recently issued a rule prohibiting class-waiving arbitration agreements in certain consumer financial agreements. However, the prohibition will only apply prospectively and to agreements entered over 180 days after the rule's promulgation. *See* CFPB Arbitration Agreements, 12 C.F.R. § 1040 (2017).

debt in violation of § 524. To add insult to injury, these debtors find themselves forced to dispute discharge injunction violations in individual arbitration pursuant to an arbitration clause in their credit agreements. In light of these class-waiving arbitration clauses, debtors cannot collectivize to spread litigation or arbitration costs, thereby jeopardizing their ability to vindicate their rights under the Bankruptcy Code.

There is widespread disagreement over whether debtors may even dispute discharge injunction violations as a class in the first place. Not only do courts disagree about how to enforce discharge injunctions, they also disagree over the types of disputes that allow for debtors to collectivize. Even if courts were to agree that debtors may in fact collectivize to combat systemic violations of discharge injunctions, however, the Supreme Court's "inherent conflict" test, which allows courts to refuse to enforce class-waiving arbitration clauses in certain contexts, likely leads to a finding that such clauses are enforceable in this context.

Without debtors' ability to collectivize, discharge injunction violations will be underenforced. Given the importance of granting debtors a clean slate after discharge, Congress should take notice of the obstacles debtors face while attempting to combat a systemic violation of discharge injunctions. By amending the Bankruptcy Code not only to provide debtors an express right of action under § 524 and the ability to collectivize but also to prohibit the arbitration of these claims, Congress will provide much needed clarity to this area of the law. Such an amendment will fulfill the promise to debtors that they can truly begin anew after bankruptcy.