FORCED ARBITRATION

CONSUMERS NEED PERMANENT RELIEF

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ABOUT THE NATIONAL CONSUMER LAW CENTER

The National Consumer Law Center®, a nonprofit corporation founded in 1969, assists consumers, advocates, and public policy makers nationwide on consumer law issues. NCLC works toward the goal of consumer justice and fair treatment, particularly for those whose poverty renders them powerless to demand accountability from the economic marketplace. NCLC has provided model language and testimony on numerous consumer law issues before federal and state policy makers. NCLC publishes an 18-volume series of treatises on consumer law, and a number of publications for consumers.

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SUMMARY

Deals valued in the tens of millions of dollars barely make ripples on Wall Street. However, one recent transaction, while relatively small by Wall Street standards, laid bare the miscarriages of justice that result from mandatory arbitration requirements buried in millions of consumer contracts. These forced arbitration clauses trap consumers in a private justice system that is rigged in favor of corporations.

Arbitration providers select supposedly neutral arbitrators, make the rules, set fees and administer consumer arbitrations. But these providers' existence depends on receipt of fees after they are chosen to arbitrate a dispute. Consumers don't choose the provider. Instead, corporations direct business and revenue to a particular provider by naming them in thousands and in some cases millions of standard form contracts. Thus supposedly neutral arbiters know that revenue will increase if the party on one side of a dispute—the corporation—is pleased with the outcome. That same arbiter knows that rulings in favor of consumers will prompt corporations to take future business elsewhere.

In 2006, a Wall Street investor decided to put this inherent bias on steroids. Not satisfied with a system in which corporations chose arbitrators and controlled their flow of fees, that investor moved to tie together through common ownership a law firm that often represented creditors with arbitration claims and the arbitration provider itself. There could hardly be a less impartial decision-maker for a consumer's dispute with a corporation.

Fortunately, this corrupt arrangement was uncovered by Minnesota Attorney General Lori Swanson in the summer of 2009. Swanson filed a lawsuit that exposed hidden financial ties by which Accretive, the Wall Street investor, simultaneously held stakes in the provider that conducted most credit card arbitrations and a law firm that led the way in pursuing collections from credit card customers through arbitration.

Since then, the net that dragged thousands of unwilling consumers into forced arbitration has unraveled. National Arbitration Forum (NAF), the purportedly impartial arbitrator with ownership ties to debt collectors, agreed to stop handling consumer cases. At least four giant banks also pledged to stop, at least temporarily, enforcement of forced arbitration clauses in credit card agreements. Mann Bracken, the giant debt collection firm, collapsed.

But these events passed nearly unnoticed outside the credit card and collections industries. Despite the complaints of consumers denied justice or a fair hearing in arbitration, and sharp criticism from advocates, too many members of the public and policy makers remain susceptible to the siren song of arbitration, with its false promises of fast, inexpensive and impartial resolution of disputes outside of court.

In practice, forced arbitration, imposed upon consumers as a condition for entering most consumer transactions, has proven to be complicated, expensive and inconvenient. Worst of all, it is inherently unfair: Consumers almost never win—even when the facts and the law are on their side. The arbitration forum depends on the corporation—and not the consumer—for its very existence. Consumers are forced into a private system of justice that is inherently biased in favor of creditors and collectors.

Swanson's exposure of the secret financial ties between collectors and purportedly "impartial" arbitrators temporarily unplugged the giant collection machine that arbitration had become. But the clock is running. Pledges by some major banks not to resort to forced arbitration are due to expire in 2013, and thousands of other businesses—from nursing homes to car dealers—still require mandatory arbitration.

Now is the time to expose the fundamentally anti-consumer, pro-creditor nature of forced arbitration, and pass legislation that will prevent creditors and collectors from restarting this inherently unfair system.

Congress must **prohibit the inclusion of forced arbitration clauses in consumer credit agreements.** Only such a prohibition will effectively prevent nominally impartial but corporation-controlled forced arbitration services.

Until Congress acts, **states must enact laws in areas not preempted by federal law to preserve consumers' rights** to join together to file class actions, limit conflicts of interest by arbitration firms and individual arbitrators, require disclosure of arbitrators' rulings, provide upfront disclosure of and relief from arbitration costs and prohibit forced arbitration clauses in all insurance contracts.

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I. BOMBSHELL: THE RETREAT FROM THE CONSUMER MARKET BY NATIONAL ARBITRATION FORUM

The year 2009 was filled with news of corporate collapses and revelations of financial scandals. So perhaps it was not surprising that the world outside the debt industry paid little notice when Minnesota Attorney General Lori Swanson announced, in July, that she had shut down forced arbitration of consumer debt by the National Arbitration Forum.

Yet Swanson's action, which was part of a consent judgment that settled a lawsuit that had been filed only four days earlier, suddenly and dramatically changed the debt collection industry: It brought to a halt a forced arbitration production line that had denied hundreds of thousands of consumers basic rights and propelled them toward garnishment, attachment and other harsh measures to enforce collection orders. "It is good for consumers that this company will no longer be able to administer credit card and consumer debt collection arbitrations," Swanson said in an understated announcement of the settlement.[1]

But Swanson's victory did more. It validated the long-standing claims by advocates that the structure and conduct of forced arbitration was biased against consumers, expensive and unfair. Further, Swanson exposed hidden financial ties between NAF and one of the biggest customers for its supposedly "impartial" services: Mann Bracken, a huge law firm specializing in the collection of consumer debts.

Swanson effectively shut down a huge and powerful machine that had become a major tool for collectors. By the time of the settlement, tens of millions of credit card contracts named NAF as the arbitrator of all disputes between consumers and their credit card providers. Each year NAF and its arbitrators processed hundreds of thousands of disputes over credit cards and other consumer debts.[2]

Forced arbitration played a growing role in an often hidden but important sector of the economy: the collection of consumer debts. Fueled by the growth in outstanding credit card debt to a peak of nearly $1 trillion, debt collection has become a multi-billion dollar industry in its own right.

Collection businesses have different focuses and business models. Some collectors get paid commissions equal to a portion of the debt that they collect. Others seek to profit from collections of consumer debts they purchased from banks and others for pennies on the dollar.

Key players in the industry include law firms that provide muscle to modern collections by securing judgments that creditors can use to garnish wages and attach property and bank accounts. To get such judgments, collectors typically file claims against alleged debtors in state courts.

In recent years, forced arbitration emerged as another tool to give collectors even more leverage against consumers. By inserting forced arbitration clauses in credit card agreements and other consumer contracts, creditors opened the door to file claims in mass with private, secretive arbitrators. That often

[1] "National Arbitration Forum Barred from Credit Card and Consumer Arbitrations under Agreement with Attorney General Swanson," release dated July 19, 2009.

[2] "National Arbitration Forum Barred from Credit Card and Consumer Arbitrations Under Agreement with Attorney General Swanson," news release dated July 19, 2009.

proved a quicker and cheaper route to getting judgments against consumers.

Consumer advocates have campaigned against forced arbitration and exposed its fundamental unfairness to consumers. A recent study found that more than 94 percent of arbitrated disputes with alleged debtors were resolved in favor of creditors.[3] Even some former arbitrators began to speak out about pressures to rule in favor of creditors and an arbitration process sharply biased against consumers.

The shutdown of NAF will not in itself prevent future forced arbitration abuses. "The troubling practices in which the NAF engaged may well reappear before too long," said Paul Bland, a lawyer for Public Justice, a public interest law firm, and an expert on abuse of forced arbitration in consumer contracts. "So long as there is money to be made in debt collection arbitrations, arbitration providers will try to make it, even if their efforts mean that consumers are deprived of fair hearings."[4]

II. WHAT'S THE MATTER WITH FORCED ARBITRATION?

Arbitration refers to an agreement between parties to a dispute to let an outside party resolve that dispute. Arbitration is "binding" when the disputing parties "agree" to follow the arbitrator's decision.

In 1925 the Federal Arbitration Act was enacted in order "to overcome the reluctance of federal courts to entertain or enforce arbitration clauses in contracts between commercial business entities."[5] "In a series of decisions toward the end of the 20th century, the Supreme Court concluded that the FAA established a 'federal policy favoring arbitration.'"[6]

Promoters of arbitration argued that it sped up and cut the costs of resolving disputes. While that might have had some validity in cases where parties to a dispute voluntarily chose to arbitrate, consumers forced into arbitration made no such choices and almost always found themselves bound into a one-sided, expensive system established by creditors to deny consumers legal and due process rights.

Any rationale for arbitration vanishes when a dispute pits an individual consumer against a powerful bank or corporation and the weaker party—the individual consumer—is trapped in the arbitration process by a contract clause imposed long before the dispute arose.

A myriad of practices transformed arbitration into a system of forced arbitration that is inherently unfair and unfriendly to consumers. Filing fees of $250 and up, combined with three-figure hourly rates by arbitrators, other fees and loser pay rules, made arbitration prohibitively expensive for consumers. Limits on discovery made it difficult for consumers to build and present their cases. Arbitrations

[3] "The Arbitration Trap: How the Credit Card Companies Ensnare Consumers" by John O'Donnell, Public Citizen, Sept. 2007, p. 13.

[4] Testimony of F. Paul Bland Jr., staff attorney, Public Justice, Domestic Policy Subcommittee, Oversight and Government Reform Committee, hearing on "'Arbitration' or 'Arbitrary': The Misuse of Arbitration to Collect Consumer Debts," July 22, 2009, p. 1.

[5] "Arbitration Abuse: an Examination of Claims Files of the National Arbitration Forum," Staff Report of the Domestic Policy Subcommittee Majority Staff, Oversight and Government Reform Committee, House of Representative, July 21, 2009, p. 3.

[6] "Arbitration's Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts," by Theodore Eisenberg, Geoffrey P. Miller and Emily Sherwin, Cornell Law School Legal Studies Research Papers, 2008, p. 23.

were often held at distant locations that made it impossible for consumers to attend their own cases. Secret proceedings and the lack of published or written decisions drew a curtain across an arbitration process where arbitrators are not obligated to follow the law or even their own rules.

Forced arbitration denied other important rights to consumers. Opportunities to appeal were very limited, even when arbitration proceedings violated basic legal protections or due process. Forced arbitration clauses usually prohibited class actions, which made it almost impossible for consumers to challenge unfair practices embedded in business models where profits came from imposing relatively small extra costs on thousands or millions of transactions. The secrecy of arbitration proceedings and orders and the lack of clear rules on conflicts of interest created an untenable system with pro-creditor or anti-consumer biases.[7]

By its very nature, forcing arbitration upon a consumer prior to the emergence of a dispute systematically favors creditors and collectors. Arbitration companies, anxious to compete for case filings by giant lenders, blatantly favor corporate customers. Similarly, individual arbitrators who operate as subcontractors depend upon arbitration companies for referrals and know that adverse decisions in any given case can make them subject to blackball in the future by large lenders.

Arbitrators' biases are reinforced by the high volume and percentage of their revenue that comes from a handful of big creditors and collectors. Forced arbitration of consumer debts "puts decisions in the hands of arbitrators who have a strong incentive to favor the arbitration companies' clients," a 2007 report by Public Citizen, a nonprofit consumer advocacy group, found.[8]

Forced arbitration procedures also favor creditors and collectors over consumers, who are unlikely to be familiar with notice requirements, understand that default judgments can be issued if they fail to respond prior to deadlines or know which information to submit or the proper form. High fees, "loser pays" rules and filings at distant locations also add to the burdens on consumers in arbitration.

Lawyers representing consumers were often confused by complex NAF rules of procedure, jargon and timetables. Consumer lawyers also found that factually and legally clear defenses were often ignored or compromised by NAF arbitrators.

Meanwhile, debt collectors learned to use forced arbitration to expedite the high-volume production of judgments that extend the life of debt and make it collectible through garnishment, attachment of bank accounts or liens.

"Arbitrations of consumer debt matters are a sham—the sole purpose of which is to assist (NAF's) debt collector clients in collecting money from consumers by creating an appearance that a fair and neutral arbitration has occurred and resulted in an enforceable award," the City Attorney of San Francisco said in a 2008 lawsuit.[9]

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[7] Consumer Arbitration Agreements: Enforceability and Other Topics, Fifth Edition, by Paul Bland, Leslie A. Bailey, Michael J Quirk, Richard H. Frankel and Jonathan Sheldon, pp. 3-11.

[8] "The Arbitration Trap: How Credit Card Companies Ensnare Consumers," by John O'Donnell, Public Citizen, September 2007, p. 29.

[9] Complaint for Injunctive Relief and Civil Penalties for Violations of Business and Professions Code Section 17200, p. 2, filed Aug. 22, 2008 in the People of the State of California, acting by and through San Francisco City Attorney Dennis J. Herrera vs. National Arbitration Forum Inc., et al, Case No. CGC-08-473569, in Superior Court of California, County of San Francisco.

In California, virtually all of the nearly 34,000 cases processed by NAF during a 51-month period were filed by collectors, the Public Citizen study found. Creditors prevailed in 94 percent of the 19,300 cases that were completed.[10]

A later review by Congressional investigators of 239 NAF case files from California, the only state that requires detailed disclosure of arbitration outcomes, found that in more than two-thirds of the cases consumers were not properly served notice. All of the cases lacked anything more than "hearsay" as evidence to support the debt claims, investigators concluded.[11]

III. FORCED ARBITRATION: NO JUSTICE, NO RECOURSE

Consumers are often blind-sided by arbitration. Few understand the procedure or how abbreviated and final it can be, with the results being virtually equivalent to a court judgment, but with far fewer rights to appeal an unjust result. Despite the widespread placement of forced arbitration clauses in credit card and other consumer contracts, most consumers believe they still have the right to sue a corporation when a dispute arises.[12]

[10] "The Arbitration Trap: How Credit Card Companies Ensnare Consumers," by John O'Donnell, Public Citizen, September 2007, p. 15.

[11] "Arbitration Abuse: an Examination of Claims Files of the National Arbitration Forum," Staff Report of the Domestic Policy Subcommittee Majority Staff, Oversight and Government Reform Committee, House of Representative, July 21, 2009, p. 9.

[12] See "Forced Arbitration: Unfair and Everywhere" by Public Citizen, Sept. 14, 2009, p. 1.

Eleanor Schiano obtained an MBNA credit card in 1997. Two years later MBNA sent her a bill stuffer that she probably never noticed that obligated her to give up the right to a judge and jury and instead required that all disputes be settled by the National Arbitration Forum, an entity that was selected solely by MBNA.[13]

So in 2003, when Schiano faced severe debt problems in the wake of her husband's lay-off from a job in a New Jersey textile factory and illness, NAF was lined up to referee any disputes between Schiano and her credit card issuer.[14]

According to the Schianos, MBNA agreed to settle her husband's credit card account but required her to default on her payments before it would come to a settlement on her account.[15] But after Eleanor Schiano defaulted, MBNA refused to settle her account. Instead, it sold her account to a law firm that would later merge into Mann Bracken.[16]

[13] See "Affidavit in Support of Motion to Compel Arbitration" on pages 34-40 of "Plaintiffs' Appendix in Opposition to Defendant, NAF, Motion to Dismiss and In Support of Plaintiffs' Motion to Amend Complaint" filed Sept. 13, 2005 in Eleanor and Ralph Schiano vs. MBNA et al, 05cv1771 in U.S. District Court for the District of Newark, N.J.

[14] See Second Amended Complaint, filed April 15, 2008, in Eleanor and Ralph Schiano vs. MBNA et al, 05cv1771 in U.S. District Court for the District of Newark, N.J. p. 5.

[15] See Complaint for Violation of 15 U.S.C.1692, et seq. and 9 U.S.C. 1-4 and Fraud, filed April 4, 2005 in Eleanor and Ralph Schiano vs. MBNA et al, 05cv1771 in U.S. District Court for the District of Newark, N.J.

[16] See Report and Recommendation issued Nov. 16, 2005; Brief in Opposition to Defendant, NAF, Motion to Dismiss and In Support of Plaintiffs' Motion to Amend Complaint filed Sept. 13, 2005, p.5; and Certification, filed Sept. 13, 2005, all in Eleanor and Ralph Schiano vs. MBNA et al, 05cv1771 in U.S. District Court for the District of Newark, N.J.

That firm, called Wolpoff & Abramson, then brought an arbitration action against her before NAF to collect on the credit card debt. Wolpoff brought the arbitration action under MBNA's name, even though MBNA no longer owned the debt and was no longer a proper party to sue. No hearing was ever held, Wolpoff submitted some kind of minimal documents to NAF, Eleanor Schiano never had a chance to raise the reneged settlement offer, and some months later an individual Schiano had never heard of issued an arbitration award against her for $35,000—$25,000 that was allegedly owed on the credit card and $10,000 to the law firm for "attorney fees"—a handsome payment for just mailing some minimal documents to NAF.

Of course, the law firm was bringing thousands of cases before the NAF, a firm with which it would soon have a special relationship after a Wall Street investor acquired ownership stakes in both the law and arbitration firms. Moreover, the law firm was representing itself in the matter, so NAF awarded Wolpoff attorney fees for bringing its own case.

Incredibly, under existing law, consumers have few rights to contest such outrageous results — even though the action was brought in the name of the wrong party and even though the attorney fees were beyond all reason. The law allows the collector to turn this arbitration award into a court judgment with few if any rights for the consumer to challenge that award. Moreover, most collectors eliminate even those few rights by waiting three months to confirm their arbitration award. The law actually states that if collectors wait three months, consumers have no right to raise defenses to the award being turned into a court judgment that can lead to wage garnishment, property seizures, and liens on homes.

Eleanor Schiano, faced with continual harassment and threats to pay the arbitration award, refinanced her home mortgage with a subprime lender and used the proceeds to pay off the debt. Yet the debt continued to appear on her credit report. The whole matter is now in litigation.

IV. AN AUDACIOUS SCHEME

With billions of dollars in debt collection revenue at stake, it is hardly surprising that creditors and collectors have used forced arbitration to strip unfortunate debtors like the Schianos of their rights and resources.

What is surprising is that an audacious scheme to consolidate and systematize the use of forced arbitration as a disguise for strong-arm collection operations had financial backing from the federal government and some of the nation's most prestigious universities, including Princeton and Yale.

Swanson's lawsuit uncovers and documents the plan: National Arbitration Forum would provide a cover of "impartiality" even as it launched a sales push to convince credit card issuers and other lenders to pay for its arbitration services and encouraged its customers to engage Mann Bracken to do collections.

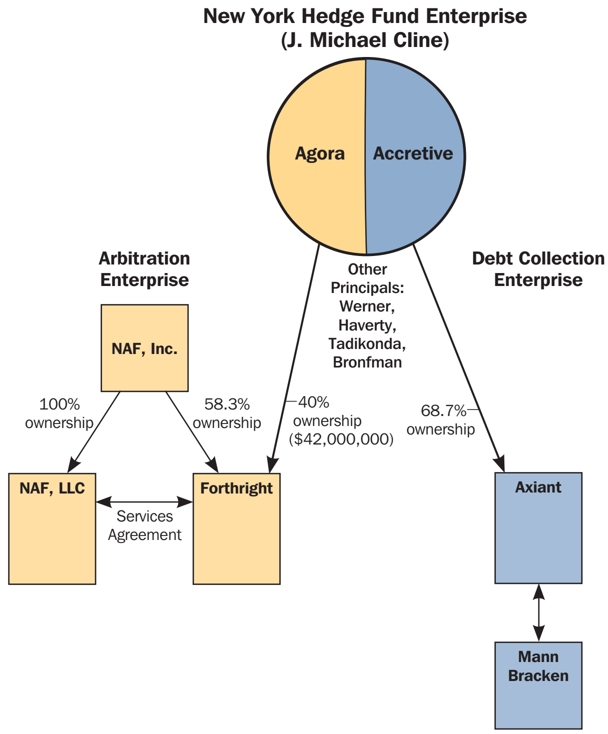
The coordinated effort was overseen by a Wall Street equity investor known as Accretive Partners. According to Swanson's lawsuit, Accretive "simultaneously took control of one of the country's largest debt collectors and became affiliated with . . . the country's largest debt collection arbitration company."[17]

[17] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No.

Accretive paid $42 million for a 40 percent stake in its new joint venture with NAF and an as-yet undisclosed amount for a 69 percent stake in another joint venture with the lawyers who owned Mann Bracken. [18]

Money for the investments was wreathed in Ivy. Specifically, much of the money came from a $233 million investment fund organized by Accretive that pooled investments from Princeton, Yale and a mutual fund for colleges and foundations called Common-Fund. [19] Additional funding for Accretive's stake in the Mann Bracken affiliate came from a $100.5 million financial package backed by the U.S. Small Business Administration. [20]

For years, consumer advocates used evidence of forced arbitration's complexity, expense and economic biases to show that it was inherently unfair to consumers. Data that showed that creditors and collectors nearly always won, while consumers nearly always



27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al., p. 2.

[18] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 in Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 20, 28, Exhibit 5.

[19] See Form D Notice of Sale of Securities, p. 2, filed June 8, 2006 by Accretive II L.P. with the U.S. Securities and Exchange Commission; Common Fund for Nonprofit Organizations, Information for Members June 2009, p. 29; Association of Yale Alumni, Directory of Organizations, p. 223, posted on-line at http://www.yale.edu/directory/FinalUpdates/DirectoryOrgs.pdf.

The partnership, known as Accretive II, roster of investors included J. Michael Cline, the general or managing partner; the Trustees of Princeton University; another limited partnership affiliated with the Common Fund for Nonprofit Organizations, which described itself as "a tax-exempt organization operated by and for its Member colleges, universities and independent schools" and has on its 11-member board of trustees includes executives from Brown and Pepperdine universities and William and Flora Hewlett Foundation; and another limited partnership called A II Holdings located on the fifth floor at 55 Whitney Avenue in New Haven, which is Yale University's investment office.

A spokesman for Accretive and the Common Fund declined to comment on the investments, and referred all questions to the parties in the lawsuit. Fund management executives at Princeton and Yale did not respond to requests for comment.

Swanson's lawsuit said that through the portion of the investment that drew upon the Small Business Administration financing "the federal government effectively distributed money to help fund the debt collection enterprise. An SBA spokesman declined to comment because the agency was not a party to Swanson's lawsuit.

[20] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 26.

lost, further shattered forced arbitration's veneer of impartiality.

Despite the compelling case compiled by its critics, NAF had grown rapidly as most of the largest credit card issuers wrote forced arbitration clauses into more and more agreements with customers. In 2006, NAF processed 214,000 consumer debt cases for a list of customers that included five of the nation's six largest credit card issuers: Bank of America, JPMorgan Chase, Citigroup, Discover and American Express.[21] Mann Bracken and law firms that it later acquired filed 125,000 of those claims, or 60 percent of the consumer debt cases processed by NAF that year.[22]

Mann Bracken had been created by the merger of three large collections firms into a single enterprise. As part of the arrangement, most of the merged law firms' operations and assets were assigned to a company called Axiant LLC. Axiant held Mann Bracken's files, office leases, computer systems and telephones and employed its support staff.[23] Axiant's customers included Discover and American Express.[24]

Mann Bracken's web site described itself as "a national law firm that combines (via recent merger) 3 of the top 5 law firms specializing in the practice of collections and creditors' rights law." Axiant's web site said that it and Mann Bracken "work in concert to serve our common clients." Besides filing lawsuits, that work encompassed call center collections, arbitration cases, "skip tracing" elusive alleged debtors and execution of garnishments and liens.

In 2008, Mann Bracken and its Axiant affiliate had more than 1,000 employees and 24 offices, operated two call centers and "had an infrastructure that supported 35,000 lawsuits per month, 20,000 arbitration filings per month and $55 million in collections per month."[25]

Meanwhile, Accretive, NAF and Mann Bracken worked hard to hide their conjoined interests. Accretive created a separate corporation, called Agora, to hold its stake in Forthright, its joint venture with NAF.

But Accretive executives played a pivotal role in the effort to grow NAF. They took seats on Forthright's board, got involved in executive hiring and worked up strategies for sales and lobbying. Their goal was to build NAF, which posted 2006 net income of $10 million on revenue of $39 million,[26] into a billion-dollar corporation that would capture half of the

[21] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 5.

[22] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al., p. 2.

[23] "Mann Bracken in receivership" by Jamie Smith Hopkins in the Baltimore Sun, Feb. 27, 2010.

[24] Complaint of Chapter 7 Trustee filed March 31, 2010 in Case No. 09-14118 in U.S. Bankruptcy Court for the District of Delaware, p. 12.

[25] Declaration of Keith Bolt in Support of Chapter 11 Petition and First Day Motions, filed Nov. 20, 2009 in re Axiant LLC debtor in the United States Bankruptcy Court for the District of Delaware, Case No. 09-14118, p. 2, and "Debt Law Firm's Fall Brings Chaos" by Jamie Smith Watkins and Andrea K. Walker in the Baltimore Sun, Jan. 16, 2010, p. 8A.

[26] "BANKS VS. CONSUMERS (GUESS WHO WINS); The business of revolving credit-card disputes is booming. But critics say the dominant firm favors creditors that are trying to collect from unsophisticated debtors," by Robert Berner and Brian Grow with Susann Rutledge in Business Week, June 16, 2008, p. 72.

collections claims currently filed in state courts and become "a comprehensive, alternative legal system."[27]

To do that, NAF would continue to present itself as "impartial," Swanson observed. Its "neutral decision-makers constitute a system that satisfies or exceeds objective standards of fairness," an NAF news release proclaimed.[28]

But the company's business plans and pitches to creditors told a different story. "You have all the leverage," proclaimed an NAF PowerPoint presentation to a financial services company."[29] "Starting with a simple clause—an arbitration clause—in your contracts, you take control of collections and claims . . . without a lawyer . . . from your office," NAF said in materials for prospective clients. "You have all the leverage and the customer really has little choice but to take care of this account," another NAF presentation said.[30]

Accretive guided NAF to step up marketing efforts aimed at encouraging creditors to file arbitration claims and helping lenders draft and insert forced arbitration clauses into credit card and other consumer loan contracts.[31] NAF actually formed a team of executives, led by a "vice president of clause placement," who were "partially compensated on a commission basis for convincing companies to place clauses in their customers agreements requiring arbitration of any disputes" by NAF.[32]

It was as if the rich owner of a National Football League team had secretly formed a joint venture with the league's referees. A court-appointed officer overseeing the liquidation of Axiant concluded that Accretive and controlling manager J. Michael Cline carried out "an illegal scheme to defraud potentially millions of consumers by requiring them to agree to arbitrate, on a binding basis, disputes with their creditors (at NAF even though it) was secretly and illegally controlled, manipulated and/or operated in such a way as to unfairly benefit credit card companies."[33]

Swanson alleged the investors had intentionally hidden the financial stakes that linked the interests of a debt collector that was a party to hundreds of thousands of claims against consumers to the interests of the supposedly neutral arbitration firm that ruled on those claims. That violated Minnesota laws against "consumer fraud, deceptive trade practices, and false advertising," her lawsuit

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[27] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p.13.

[28] See "Banks vs. Consumers (Guess Who Wins)" by Robert Berner & Brian Grow with Susann Rutledge in Business Week, June 16, 2008.

[29] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 35.

[30] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 35, 37.

[31] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 33.

[32] Complaint by Attorney General Lori Swanson filed in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al, p. 33.

[33] Complaint of Chapter 7 Trustee filed March 31, 2010 in Case No. 09-14118 in U.S. Bankruptcy Court for the District of Delaware, p. 9.

said. Within days of its filing, NAF signed a consent judgment in which it agreed to stop arbitrating disputes between consumers and creditors or collectors and pay the cost of the Minnesota investigation. The judgment included a stipulation that it would not be "construed as an admission of wrongdoing or liability" by NAF.[34]

V. COLLAPSE OF THE "ALTERNATIVE LEGAL SYSTEM"

After National Arbitration Forum announced its retreat from consumer arbitration, the collections business of Mann Bracken and its Axiant affiliate began to unravel. In November 2009, Axiant announced that it had agreed to be acquired by NCO Group, the nation's largest debt collector, and that it had filed a voluntary petition for Chapter 11 "to facilitate this transaction." But 18 days later NCO Group (which itself is controlled by an equity investment unit of JPMorgan Chase) walked away from the deal, and Axiant converted its bankruptcy into a Chapter 7 liquidation.[35]

The court-appointed official overseeing the liquidation of Axiant estimated that fall-out from the failed bid by Accretive and Cline to extend their control of the arbitration business ended up costing Axiant tens of millions of dollars in lost revenue and exposed it to hundreds of millions of dollars of potential liability in civil lawsuits.[36]

Mann Bracken collapsed in the wake of its operating affiliate. On Jan. 14, 2010, Maryland regulators, noting that a Mann Bracken lawyer had notified state court clerks that it would be shutting down by the end of the month and transferring creditor-clients to other lawyers, ordered the firm to stop debt collection activities in that state.[37] Mann Bracken reportedly shut down its two dozen offices around the country and said in a statement that it was insolvent and planning its own bankruptcy filing.[38]

On Feb. 26, 2010, a Maryland judge appointed a receiver to liquidate Mann Bracken.[39] While some debtors gained breathing room from the shutdown of Mann Bracken, which had been the subject of many complaints about abusive collections practices, others were left in limbo after they made payments and reached agreements with a firm that had stopped functioning.[40]

NAF's retreat also cleared the way for progress in a class action lawsuit claiming that six credit card banks had illegally colluded to promote forced arbitration.

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[34] Consent Judgment signed July 17, 2009, in Fourth Judicial District Court, Hennepin County Minnesota, on July 14, 2009 by Case No. 27-CV-09-18550, State of Minnesota vs. National Arbitration Forum, et al.

[35] See "Axiant to be Purchased by NCO Group" on Nov. 20, 2009 and "NCO Terminates its Proposal to Acquire Axiant" on Dec. 8, 2009, both released on PR Newswire.

[36] Complaint of Chapter 7 Trustee filed March 31, 2010 in Case No. 09-14118 in U.S. Bankruptcy Court for the District of Delaware, p 14.

[37] Summary Order to Cease and Desist and Summary Suspension of Collection Agency Licenses filed Jan. 11, 2010 in the Matter of Mann Bracken LLP, before the Maryland State Collection Agency Licensing Board in the Office of the Commissioner of Financial Regulation, DFR-FY-2010-216.

[38] "Debt Law Firm's Fall Brings Chaos" by Jamie Smith Hopkins and Andrea K. Walker in the Baltimore Sun, Jan. 16, 2010, p. 8A.

[39] "Mann Bracken in receivership" by Jamie Smith Hopkins in the Baltimore Sun, Feb. 27, 2010.

[40] "After the Fall" by Jamie Smith Hopkins and Andrea K. Walker in the Baltimore Sun, March 21, 2010.

The lawsuit, Ross vs. Bank of America, was filed in August 2005 in federal court in Manhattan, and includes allegations that the banks had begun meeting in 1999 and formed an illegal conspiracy to promote the widespread adoption of forced arbitration clauses in credit card contracts. The aim of the conspiracy, according to the lawsuit, was to deny consumers key safeguards including the right to file class action lawsuits against credit card issuers: "By forcing cardholders to arbitrate, (the banks) collectively intended to and have succeeded in reducing their legal exposure for widespread patterns of egregious and unlawful conduct."[41]

Four of the banks—JPMorgan Chase, Bank of America, Capital One and HSBC—have reached tentative settlements in which they denied wrongdoing but agreed to immediately stop enforcing existing forced arbitration clauses in credit card agreements. The banks have also agreed that forced arbitration clauses and class action lawsuit bans would be kept out of their contracts with credit card holders until at least 2013.[42]

The banks had initially asked the judge to send the plaintiffs away to pursue their claims in arbitration. The banks persuaded a district court judge to dismiss the lawsuit in September 2006, but in May 2008 the plaintiffs' appeal was upheld by a 2nd Circuit Court of Appeals panel that included current Supreme Court Justice Sonia Sotomayor. The lawsuit is proceeding against three other defendants: Citigroup, Discover and NAF.

However, Public Citizen, the consumer advocacy organization, recently warned that "the use of forced arbitration remains rampant" in credit card contracts and in other consumer transactions including with providers of cellular telephone service, home builders and securities dealers.[43]

V. TIME TO ACT

Consumers stood to reap many short and medium term benefits from the Minnesota lawsuit settlement that suddenly halted operations of National Arbitration Forum's multimillion dollar machine that ground out default judgments for creditors and collectors.

Yet the Minnesota victory and subsequent settlements in the Ross class action lawsuit against banks that imposed forced arbitration upon credit card customers will result in only limited and temporary protections and relief for consumers. So long as creditors, collectors and debt buyers see potential for profit in the use of forced arbitration, they will continue to promote and implement new forms and pretexts for "alternative dispute resolution."

The capture of the purportedly neutral NAF by a debt collector and buyer whose claims it was adjudicating is only the most extreme manifestation of the bias inherent in the current arbitration system. Under current law, creditors or other big players have the ability to insert arbitration clauses in contracts that affect millions of consumers. When selecting

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[41] Class Action Complaint filed Aug. 11, 2005 in U.S. District Court, Southern District of New York, 05cv7116, Robert Ross, et al vs. Bank of America N.A. et al, p.3.

[42] See Order filed Dec. 18, 2009 in U.S. District Court, Southern District of New York, 05cv7116, Robert Ross, et al vs. Bank of America N.A. et al and "Settlement Reached with Four Credit Card Companies to Drop Mandatory Arbitration Clauses," news release posted at www.bergermontague.com/newsitem.cfm?id=91, viewed Jan. 25, 2010.

[43] "Forced Arbitration: Unfair and Everywhere" by Public Citizen, Sept. 14, 2009, p. 3.

the arbitration provider, these corporations have enormous bargaining power. They will only choose an arbitration provider that favors them, and the arbitration forum's business is dependent on corporations designating that forum in their standard form consumer contracts. It is no surprise that even before it was purchased by the parent of a collection firm, NAF explicitly marketed itself to creditors based on how it would benefit them to choose NAF arbitration. These same market forces infect all consumer arbitration.

To make permanent and consolidate gains in the fight against forced arbitration, Congressional action if needed to prevent the reemergence of a forced arbitration system that functions mainly as a tool to boost creditors' profits, expedite collections and deny consumers their rights. **The Arbitration Fairness Act of 2009** (filed as H.R. 1020 and S. 931) or similar legislation would prohibit the insertion of forced arbitration clauses into consumer credit agreements and ensure that courts, rather than arbitrators, would decide disputes between consumers and credit card companies.

VI. CONCLUSION

The shutdown of the pro-creditor forced arbitration machine run by National Arbitration Forum, Axiant and Mann Bracken was a milestone in the struggle for consumer justice. That victory, which resulted from the settlement of the lawsuit filed by Minnesota's Attorney General, provided consumers temporary relief from abusive use of forced arbitration as a debt collection tool.

However, Congressional action remains urgently needed to protect consumers and prevent the reemergence, in new forms, of abusive debt collection using forced arbitration.

Otherwise, as Paul Bland, a leading critic of forced arbitration, warned, "The circumstances that allowed NAF to profit from credit card arbitration remain unchanged, and it would be all too easy for another company to start up where NAF left off."[44]

[44] Testimony of F. Paul Bland Jr., staff attorney, Public Justice, Domestic Policy Subcommittee, Oversight and Government Reform Committee, hearing on "'Arbitration' or 'Arbitrary': The Misuse of Arbitration to Collect Consumer Debts," July 22, 2009, p. 22,