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Arbitration awards across the country may be set aside

By Sylvia Hsieh
Staff writer
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In a stunning turn of events, the kingpin of consumer debt arbitration, the National Arbitration Forum, has been knocked out of the consumer debt business amidst allegations of consumer fraud, throwing into jeopardy hundreds of thousands of arbitration awards.

That it all happened faster than an average consumer can decipher his or her credit card agreement only added to the drama.

[Click here](#) to read a related article: "Where will all the arbitration go?"

On July 14, Minnesota Attorney General Lori Swanson [filed a complaint](#) against the National Arbitration Forum (NAF), alleging that it had concealed its financial ties to the largest debt collection agency and worked behind the scenes with creditors against the interests of consumers.

Five days later, [NAF agreed as part of a consent decree](#) that it would cease consumer debt arbitration by July 24.

The ink was barely dry on the settlement when the American Arbitration Association announced on July 22 that it too would be getting out of debt collection arbitration until it can develop standards of practice.

Consumer lawyers reacted swiftly.

"Tons of consumer lawyers are investigating lawsuits right now," said

Paul Bland, staff attorney with Public Justice in Washington, D.C. and co-author of *Consumer Arbitration Agreements*.

NAF handled an estimated 200,000 arbitrations per year, according to the Attorney General's complaint.

Dan Edelman, a consumer rights attorney with Edelman, Combs, Lattner & Goodwin in Chicago, has already filed [the first class action](#) against credit giant MBNA/FIA and the debt collection law firm Mann Bracken, alleged to have financial ties to NAF, seeking to set aside thousands of arbitration awards and judgments entered against Illinois consumers since 2007.

Bland expects more to be filed soon.

Lawyers handling individual consumer debt cases are also planning to use the recent revelations to get judgments overturned and sue for damages.

NAF spokesperson Christina Doucet released a statement citing "increasing challenges to arbitration on all fronts" and "mounting legal costs" as reasons for its sudden exit from the consumer arbitration arena.

The company did not admit liability in the consent decree.

Meanwhile, on July 22 a Congressional subcommittee heard testimony on the issue.

Swanson testified that her investigation found that debt collection claims were routinely steered to arbitrators who regularly ruled in favor of debt collectors.

"There is tremendous pressure on arbitration companies" to rule in favor of creditors, she said. "It's a very lucrative, profitable business. Companies know that if an arbitration company isn't friendly to corporate litigants, they'll take their business elsewhere."

Michael Kelly, Chief Operating Officer of NAF, testified that the firm's practice of marketing its services to debt collectors doesn't mean its arbitrators are biased.

"We don't shy away from saying that we do market our services," Kelly said. "The majority of the clients are debt collectors, and we

market that - [or] I should say we did.”

He said that if mandatory arbitration for consumer contracts was not available, consumers would be harmed because they would be forced to deal with complicated rules in civil court.

Lawmakers introduced the Arbitration Fairness Act of 2009 in the House (H.R. 1020) and Senate (S. 931) earlier this year. The bill would prohibit pre-dispute mandatory binding arbitration in most contracts, but the measure has not advanced out of committee in either house of Congress.

‘Complex web’

Even to veteran consumer lawyers, the Attorney General’s complaint was a shocker.

“It’s huge. It’s incredible,” said Santa Fe, N.M. attorney Richard Rubin, emeritus chair of the National Association of Consumer Advocates.

“I was shocked to find out who owned the NAF,” said Bland.

[The complaint](#) mapped out a “complex web” which boiled down to a cozy financial relationship: the arbitration services of NAF and sister organizations as well as the debt collection services of the law firm Mann Bracken and other companies have all been owned by the same New York hedge fund since 2007.

The complaint alleged that the NAF violated state consumer fraud, deceptive trade practices and false advertising statutes through “complex and opaque corporate structuring” that concealed its financial ties and represented itself as a neutral party.

“Consumers also do not know that - despite representing to the public that it has ‘no relationship with any party’ and does not ‘counsel our users’ - [NAF] works closely with creditors behind the scenes,” the complaint said.

It further alleged that the NAF encouraged creditors to file arbitration claims, helped creditors draft arbitration clauses and sometimes collection claims against consumers, and referred creditors to debt collection law firms, including Mann Bracken, which then filed arbitration claims before the NAF.

Swanson announced at the time of the consent decree that other state attorneys general have contacted her.

The city of San Francisco is also litigating [a suit it filed last year](#) claiming that NAF ran an "arbitration mill" that was biased against consumers and that MBNA/FIA forced consumers into a "sham" process, failed to provide proper notice and collected amounts they were not entitled to under state law.

'Tainted' judgments

The consent decree does not address what will happen to the massive number of arbitration awards issued by NAF over the years.

"Literally hundreds of thousands of consumers have NAF awards entered against them - tons of them way past the statute of limitations, many of them with junk fees and illegal interest, some of them against victims of identity theft - that are now severely tainted by the news that the same people prosecuting the cases owned a large part of the firm that picked the judges," charged Bland.

Aurora Harris, a consumer attorney in Los Angeles who has been challenging the NAF's rubber stamping procedures and awards based on faulty affidavits and digital signatures from out-of-state lawyers, said that the allegations against NAF will be persuasive in individual cases.

"I can go to judges and attach the [Attorney General's] complaint and the consent decree to every case. It creates a huge inference," she said.

State laws vary on when an arbitration award or judgment confirming an award can be overturned.

"Generally, states would allow an attack on a judgment on the ground of fraud by nondisclosure of the fact that the arbitrator had a financial interest in the matter," Edelman said.

But Rubin said that class actions will be an uphill battle.

"The ability of a class action litigant to get all of these other court cases undone is limited because of comity. Definitely a federal court will not be able to tell state courts to set aside judgments," said Rubin, who hopes that other state attorneys general or the Federal

Trade Commission will step in and order that profits be disgorged.

Lawyers can also pursue damages under state consumer laws, such as unfair trade practices statutes, and some attorneys are considering RICO charges in federal court, Bland said.