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ISSUE BRIEF

National Arbitration Forum Settlement with Minnesota Attorney General

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On July 20, 2009, Minnesota Attorney General Lori Swanson announced that the country's largest arbitrator of credit-card and consumer-collection disputes would no longer handle consumer arbitrations.

The National Arbitration Forum's decision to end its consumer-arbitration business resulted from a settlement it reached with the State of Minnesota less than a week after Attorney General Swanson sued the company in Ramsey County, Minnesota, accusing the company of violating Minnesota's consumer-fraud, deceptive-trade-practices, and false-advertising statutes.

The attorney general's complaint accused the company of holding itself out to the public as an independent arbitration company, while at the same time working against the interests of consumers. The complaint also alleged that the company advocated for the inclusion of mandatory arbitration clauses in consumer agreements and went so far as to assist in the drafting of such clauses. Additionally, the State of Minnesota accused the company of hiding from the public its affiliation with a New York hedge fund group that owns a major debt-collection enterprise, which generated considerable business for the company. The settlement was followed within days by the filing of a class-action complaint in Minnesota federal district court against the National Arbitration Forum and several finance companies, including Bank of America, Wells Fargo, and JPMorgan Chase. In its one dozen causes of action, ranging from antitrust to fraud to breach of contract claims, the lawsuit similarly alleges that the National Arbitration Forum did not administer fair consumer arbitrations.

As the financial-sector collapsed during the past two years, private arbitration of consumer-creditor disputes has been subjected to increased scrutiny as lawmakers and consumer advocates contended that creditors and arbitration companies take advantage of unsophisticated consumers. Last summer, *BusinessWeek* spotlighted the National Arbitration Forum in a cover story detailing the company's business tactics, some of which surfaced in the Minnesota complaint. The *BusinessWeek* story revealed, among other things, that the company issued arbitration rulings, as well as had close relations with creditors appearing in arbitrations administered by the company. The *BusinessWeek* story also included withering testimonials about the company's business practices from consumer-debtors and former company arbitrators. The company defended itself throughout the *BusinessWeek* story as fair, diligent, and neutral in the consumer arbitrations it administered.

In addition to the Minnesota lawsuit, in March 2008 the National Arbitration Forum was sued in California by San Francisco City Attorney Dennis Herrera. In that lawsuit, the City of San Francisco similarly accused the company of running an "arbitration mill, [and] churning out arbitration awards in favor of debt collectors... without regard to whether consumers actually owe the money sought." The San Francisco lawsuit alleged that less than 0.2 percent of the arbitration hearings conducted by the company in California between Jan. 1, 2003 and March 31, 2007 were resolved in favor of the consumer. And, where the individual consumer did prevail at arbitration, the consumer only

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prevailed when he or she initially filed the claim. In cases where a business initially filed the claim, the company's arbitrators uniformly ruled in favor of the business. The National Arbitration Forum denied the allegations and stated that it "acted reasonably and in good faith at all times."

The increased scrutiny of arbitration companies could have a profound effect on the widespread use of alternative dispute resolution in the United States. The United States Supreme Court has consistently reinforced its preference that disputes be settled through arbitration rather than litigation. Just last year, in *Preston v. Ferrer*, the Court observed that the Federal Arbitration Act established a national policy favoring arbitration and foreclosed state legislative attempts to undercut judicial enforcement of arbitration agreements. The prime objective of arbitration agreements, the Court reiterated, is to achieve streamlined results. In 2000, the Supreme Court cited the National Arbitration Forum as an example of an organization that had developed fair arbitration procedures at a low cost to the participants.

The Supreme Court's preference for arbitrating disputes, however, may not stem the increasing tide against enforcing mandatory consumer arbitrations. Congress has recently introduced legislation that would limit the scope of consumer arbitration agreements. The Arbitration Fairness Act of 2009, introduced in March 2009, would render invalid any pre-dispute consumer arbitration agreement. In addition, the Fairness in Nursing Home Arbitration Act, introduced around the same time, also would render unenforceable pre-dispute arbitration agreements between long-term care facilities and residents. Finally, the Consumer Financial Protection Agency Act of 2009 would empower a newly created agency to "prohibit or impose conditions or limitations on the use of agreements [involving] a consumer that require the consumer to arbitrate any future disputes [under] any enumerated consumer law if [the agency] finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of consumers."

The National Arbitration Forum's settlement with the State of Minnesota requires the company to stop handling current consumer arbitrations and to not process or administer new consumer arbitrations, the practical effect of which is that the company will immediately cease administering consumer arbitrations after July 24. According to the Minnesota Attorney General's press release announcing the settlement, however, the company may still arbitrate Internet domain disputes, personal injury protection claims, and cargo disputes.

In the company's own press release, National Arbitration Forum CEO Mike Kelly stated that given the current economic climate, legislative uncertainty, and increasing challenges to its arbitration business from state attorneys general and class-action attorneys, "[t]he costs of providing consumer arbitration services far exceed the revenue generated." The company, however, pointed out that the Minnesota complaint did not allege that the company's arbitration proceedings were inherently unfair, and noted that, the "fairness of arbitration is ensured by the independence of the neutral arbitrators." Additionally, the company's press release described its services as "the faster, lower cost, and superior alternative to litigation[] that ensures parties receive the same outcomes they would in court."

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