

# **“Examining Mandatory Arbitration in Financial Service Products”**

## **U.S. Senate Committee on Banking, Housing, and Urban Affairs**

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### **Testimony of Paul Bland Executive Director, Public Justice<sup>1</sup>**

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<sup>1</sup> Public Justice pursues high impact lawsuits to combat social and economic injustice, protect the Earth’s sustainability, and challenge predatory corporate conduct and government abuses. I oversee Public Justice’s docket of consumer, worker protection, environmental and civil rights cases. I have argued or co-argued and won more than 40 reported decisions from federal and state courts across the nation, including cases in six of the federal Circuit Courts of Appeal and at least one victory in ten different state high courts. I was named the “Vern Countryman” Award winner in 2006 by the National Consumer Law Center, which “honors the accomplishments of an exceptional consumer attorney who, through the practice of consumer law, has contributed significantly to the wellbeing of vulnerable consumers.” In 2013, I received the Maryland Consumer Rights Coalition’s “Legal Champion” award. In 2010, I received the Maryland Legal Aid Bureau’s “Champion of Justice” Award. In the late 1980s, I was Chief Nominations Counsel to the U.S. Senate Judiciary Committee.

For 20 years, Public Justice has represented consumers in a large number of cases challenging abuses of forced arbitration clauses. While arbitration clauses are widely enforceable as a matter of federal law, we have successfully represented consumers and workers in cases where corporations added outrageous terms to their arbitration clauses (such as requiring consumers with small claims to travel across the country), or corporations have attempted to enforce arbitration clauses against consumers who never agreed to them, and similar abuses.

## INTRODUCTION

The vast majority of consumer financial services that are provided in America are accompanied by to a forced arbitration provision – consumers can't go to court if they're cheated or injured; they have to go to a secretive, unreviewable system selected by the corporation that wrote the contract. The use of forced arbitration clauses by lenders is grossly unfair to consumers.

My testimony will make the following key points:

- Forced arbitration harms all sorts of consumers who have been badly cheated by lenders
- By banning class actions, forced arbitration results in enabling predatory lenders to break the law and get away with it
- Congress has already banned forced arbitration in two consumer lending contexts – lending to members of the armed services and their families, and in mortgage contracts – and those steps have been enormously beneficial to consumers
- The overwhelming majority of consumers never choose arbitration, as the clauses are slipped by them in fine print that few understand
- Arbitration is a secretive, shadowy process that provides none of the openness of the public court system.
- Even if arbitrators make very egregious errors in their decisions, those decisions are almost completely unreviewable by any court.

- For about a decade, the single largest company handling consumer arbitration cases was egregiously corrupt. Despite extreme and abusive practices, it was permitted to operate, until a chance investigation by a state law enforcement agency finally shut it down. The point is that it would be very easy for this kind of abuse to recur.

My organization has represented consumers and many others in challenging forced arbitration clauses where people didn't actually consent to arbitrate, or the arbitration clause was particularly egregiously unfair, or was otherwise unenforceable. We've won dozens of cases in more than 25 states over the years. No law firm or organization in the country has won nearly as many cases as we have in challenging forced arbitration clauses. This experience helps us speak with particular authority to these issues: as a result of our history of success, over the years, literally thousands of people with legal claims who are faced with forced arbitration clauses have reached out to us, asking us if we can help them avoid having their claims forced into arbitration.

All too often, we cannot. As the Supreme Court has become more and more favorable to forced arbitration clauses, however, forced arbitration clauses are upheld now in the vast majority of cases, even when people didn't intend to agree to them or they are quite unfair. While it varies by type of case a good deal, in a great many of these cases, in our experience, people simply drop their case and give up, rather than pursue their claims in arbitration.

### **Faces of Forced Arbitration in Consumer Lending**

Akelea Edwards, of Arizona, was a student looking to help finance her education. Working through an online payday loan service, she took out a loan that quickly became

a scam. The lender had the power to renew the loan automatically, without her knowledge or consent, and the fees rapidly escalated. But she was hemmed in by the predatory lender's forced arbitration clause, with its rigged system. Ultimately she was able to defeat the clause and get into court, where she was successful, but only after a substantial fight (and one that most consumers would not win).

Gwendolyn Byrd, of Mississippi, is a blind woman who was pressured by a salesperson to buy new windows for her home, and was persuaded by a number of promises that would later prove to be false. Only when she hired a lawyer to challenge the deceptive promises did she discover that the Wells Fargo credit card agreement that was used to finance the sale, and which she was not able to have read, included a forced arbitration clause. Her lawsuit was dismissed, and forced into arbitration.

Aaron Brodie of Texas is one of the many people for whom Wells Fargo opened a credit card account without his authorization or permission, when he opened a checking account at Wells Fargo went he started college. He had expressly said he did not want a credit card, and when one was mailed to him, he objected, told them that he wanted to close the account, and he destroyed the card. Later he discovered that he had been hit with \$1,300 in fees, which he refused to pay. Wells Fargo then falsely reported him as having failed to pay legal debts, greatly harming his credit record. When he sued Wells Fargo, it sought to force him into arbitration.

David Rubin, of New York, applied for and was approved for an HSBC credit card. He never received the card, however, and then later discovered it had been used by someone else to make nearly \$2,000 in fraudulent purchases. Mr. Rubin contacted HSBC, and passed on these facts. But when two major credit reporting agencies began

to falsely list Mr. Rubin as being delinquent on debts from the fraudulent use of the card, HSBC verified those charges, so that his credit was unfairly and wrongly damaged by charges he had not made. When Mr. Rubin sued HSBC for violating the Fair Credit Reporting Act, the bank invoked the forced arbitration clause in the fine print of the credit card agreement.

Similarly, Gerardo Manzo of New York discovered that his identity was stolen, and a fraudster made nearly \$10,000 in purchases in his name. When Mr. Manzo contacted Citibank, it responded that it did not consider the charges to be fraudulent. Moreover, Citibank verified the fraudulent debt when it was contacted by a credit reporting agency. After multiple attempts to clear his name, including filing police reports about the fraud and tracking his location with his cell phone, Citibank finally agreed that he was not responsible for the fraudulent charges. Because of the continuing negative information on his Equifax credit report, however, Mr. Manzo sued Citibank and Equifax in a New York federal court, claiming violations of the Fair Credit Reporting Act. Citibank has invoked its forced arbitration clause to force the case out of court, however.

And a trio of additional examples of how forced arbitration has harmed consumers in New Jersey, North Carolina and Maryland will be set forth in the following section.

**By Banning Class Actions, Forced Arbitration Clauses Suppress  
Many Valid Claims and Immunize Corporations from Liability  
Even When They Have Clearly Broken the Law**

Before looking at broader statistics, let me illustrate this point with three powerful case studies. I represented a New Jersey consumer who was cheated by a bank in a case, but because the U.S. Supreme Court changed the law governing forced arbitration clauses fairly dramatically while the case was pending, our client ended up receiving nothing and none of the other consumers who were cheated in the same way

received anything. In *Homa v. American Express*, our client, Mr. Homa, agreed to purchase a credit card based on the company's offer of a specific set of conditions and terms. In fact, however, he discovered that the terms that were advertised were far better than what a cardholder could ever receive and that the credit card company was misleading people about the true cost of its loans (by exaggerating the size of the rebates the cardholders were supposed to receive).

Mr. Homa, who is far better at numbers than the average consumer, figured out the scam – that his rebate was much lower than he had been promised -- and tried to get his money back. The company rebuffed him at every turn, telling him he had miscalculated the rates and that he was not entitled to his money. He finally went to a lawyer, who told him that, while he had a valid claim, the damages in his case were so small that it did not make financial sense to pursue his claim on an individual basis. After realizing that the company had likely cheated many consumers in this bait and switch scheme, Mr. Homa sought to hold the company liable for its unfair and deceptive lending practice by filing a class action complaint in federal court.

Because the amount of individual damages was so small and the nature of the claims was so complex, no one could actually obtain a remedy on an individual basis. The company nevertheless sought to force Mr. Homa into arbitration on an individual basis, but this effort was rejected by the U.S. Court of Appeals for the Third Circuit, which found that the American Express arbitration clause's ban on class actions was "unconscionable." In other words, because the ban on class actions would gut the state of New Jersey's consumer protection laws, and give the bank a 'get of jail free' card, the court struck down the arbitration clause as unenforceable.

Then the U.S. Supreme Court intervened, with its notorious decision in *Concepcion v. AT&T Mobility*, 131 S. Ct. 1740 (2011). In this 5-4 decision, Justice Scalia invented a new rule of federal law that wiped away state contract laws that refused to enforce contracts that undermined consumer protection or civil rights laws. After *Concepcion*, the district court was provided with a powerful evidentiary record that proved no consumer could effectively vindicate his or her statutory rights relating to the claims at issue in the case under American Express's arbitration clause, including expert testimony, testimony from Mr. Homa, and records of the paltry number of arbitrations pursued. This evidence, as well as the plaintiff's briefs, is available at our website, [www.publicjustice.net](http://www.publicjustice.net), on the page dedicated to the *Homa* case. American Express did not bother to challenge the evidentiary record, taking the position that these facts did not matter, after *Conception*. Notwithstanding this evidence, the district court dismissed the case and enforced the arbitration clause without comment.

On a final appeal to the Third Circuit, the Court of Appeals accepted the factual record showing that American Express's ban on class actions would gut Mr. Homa's case: "We accept this characterization, for the record demonstrates that the significant cost of arbitrating Homa's claim and the likelihood that there would be a limited recovery even if his arbitration was successful makes it unlikely that an attorney would take his case. Furthermore, in view of the complexity of the issues pertaining to the merits of Homa's claim, it would be very difficult for him to prosecute the case without the aid of an attorney whether in a judicial proceeding or in arbitration."

Notwithstanding these facts, in light of the *Concepcion* case, the Third Circuit said that American Express's arbitration clause should be enforced even though the

arbitration offered only an “illusory remedy”: “Even if Homa cannot effectively prosecute his claim in an individual arbitration **that procedure is his only remedy, illusory or not**. Though some persons might regard our result as unfair, [the Federal Arbitration Act] requires that we reach it.” 494 Fed. Appx. 191 (2012).

Similarly, I was co-counsel in a class action that was litigated in Maryland state court, *Wells v. Chevy Chase Bank*. The credit card issuer had promised in promotional materials and in its contract that it would “never” raise its interest rates above 24%, and then it did raise its interest rates (as well as add a number of other charges) for a number of people. It was a classic bait-and-switch. The case was settled for \$16.1 million (as well as actions taken to remove improper negative information from class members’ credit records), and checks were mailed to more than 200,000 class members. (Compare this, again, to the 411 people who take cases to arbitration each year against lenders throughout the entire United States.)

During the challenge to the arbitration clause in the *Wells* case, however, evidence was put before the trial court that if the arbitration clause had been enforced, no consumers would have been able to pursue their claims on an individual basis. This evidence was never challenged or refuted by the defendant, who argued that this did not matter. Our clients had approached a number of lawyers without finding any willing to handle the case, and the case was only filed shortly before the limitations period ended. This was an important case that needed to be brought, and which resolved very favorably for the consumers, but if the arbitration clause had been enforced, no consumers would have received any recovery.

As one further example, I was co-counsel in five cases brought against payday



lenders in North Carolina state court. While payday lending is legal in many states, it was not in North Carolina. The judge divided the five cases into two groups, to better manage them. The first three cases were litigated and resolved before the *Concepcion* decision. We settled those cases for \$45 million, and sent checks to more than 200,000 class members. The second two cases were thrown out because of the payday lenders' class action bans, and so far as I know, not a single one of the consumers pursued their claims in arbitration and recovered anything. The contrast is striking: 200,000 consumers who retained their constitutional rights to go to court recovered \$45 million and received checks, and tens of thousands of consumers who were subject to forced arbitration clauses with class action bans received nothing.

These examples will not be surprising to anyone even slightly familiar with consumer law in the U.S. When corporations can simply ban their customers from banding together in a class action, the consequence is often that the corporation can simply break the law and get away with it. The Consumer Financial Protection Bureau study, mandated by the Dodd-Frank Act, provided ample empirical proof of this fact.

In recent years, for example, if a bank systematically cheated 10,000 customers in the same way, the bank could use its arbitration clause to stop those customers from going to court together. Each individual had to figure out the scam, figure out what their rights were and then spend time and money fighting the bank. In the incredibly inefficient system that banks foisted on their own customers, everyone was essentially on their own. In contrast, a class action could offer all 10,000 people a fair shot at justice.

The CFPB conducted an extensive empirical study of forced arbitration. Its

results, reported to Congress in March of 2015, are entirely consistent with what most experts in consumer law would have predicted: Incredibly few consumers ever actually take cases to arbitration, and very few of them recover much. The CFPB looked at *every single arbitration* conducted by the American Arbitration Association (by far the largest private arbitration company in the United States that handles consumer cases) over a period of three years in cases against lenders. In those three years, the TOTAL number of cases that consumers arbitrated against lenders was 411 per year. Out of hundreds of millions of arbitration clauses, and compared to the legal system, where more than 13 million consumers received recoveries in class actions. That is not a typo. *Throughout the entire United States*, the total number of arbitrations against lenders each year was 411. Sec. 1, p. 11.

Over those three years, and again for the entire United States, 32 (thirty-two) consumers won recoveries from arbitrators in cases against lenders, where the arbitrators issued decisions. Sec. 1, p. 11. In those 32 cases, the consumers recovered 12 cents for every dollar of their legal claims. Sec. 5, p. 13.

By contrast, in a study of 400 private lawsuits that were brought in court and litigated as class actions, more than 13 million customers received more than \$2.7 billion in recoveries. Sec. 1, p. 16. The attorneys' fees in those class actions amount to 16% of the gross relief received by the consumers. Sec. 8, pp. 23, 32-33.

This study is consistent with Public Justice's experience: Very few consumers have any interest in bringing cases in arbitration. There are a number of factors that we see again and again:

- The arbitration system is foreign and confusing to consumers. Most

consumers don't know what the word means, or wrongly assume they can still go to court.

- The rules of the arbitration providers are lengthy, hard to find, and often it's not clear which set of rules apply. The American Arbitration Association has many different sets of rules, and cases are often litigated for some time as to which set of rules will govern in a given case.
- Consumers often must pay up front expenses that exceed what they'd have to pay in a court. It is not at all uncommon for corporations to refuse to pay their share of arbitrators' fees (even when their customer contracts promise that they will pay most of the costs of arbitration), so when consumers do go to arbitration there are often extensive delays while the arbitration company collects fees from the company.
- There are a number of examples of arbitrators requiring consumers to pay enormous "loser pays" awards (meaning that even if a consumer brought a well-grounded case and they end up losing before the private corporate arbitrator, they are forced to pay the corporation's attorneys' fees, in some cases amounting to several hundred thousand dollars), which makes consumers reluctant to go to arbitration.
- Most private consumer lawyers are very reluctant, or completely unwilling, to represent clients in a system that they believe is rigged against consumers. Unlike the banking industry lawyers, consumer lawyers generally only get paid if they win cases. Many of them have a reasonable, earned distrust of forced arbitration, and extensive surveys of consumer lawyers consistently show that most will walk away from a case rather than go to arbitration.

## **Congress Has Already Banned Forced Arbitration for Two Types of Consumer Financial Contracts**

Congress has already banned forced arbitration in two significant types of consumer lending. The first is mortgage contracts. In the wake of the 2008 financial crisis, one of whose major causes was fraud in the mortgage markets, the Congress banned the use of forced arbitration clauses in mortgage agreements in the Dodd Frank Act. This crucial protection has permitted fraud cases to go forward in court, and has been enormously beneficial to consumers.

In addition, in the Military Lending Act, passed by the Congress in 2008, the Congress made it illegal for lenders to charge members of the armed services, or their families, interest rates exceeding 36%. In order to make sure that this protection would actually be implemented, the Congress made it a misdemeanor for a lender to include an arbitration clause in a high cost loan to a member of the armed services! In other words, the Congress recognized that it was so unfair to members of the armed services for a lender to use a forced arbitration clause, that it was literally a crime to do so!

These examples are very important, because they show a key point. If Congress actually wants a law to be enforced, it needs to ban forced arbitration of claims relating to the law. After the financial crisis of 2008, the Congress wanted to stop widespread fraud in the mortgage market – it really mattered to end this – so Congress banned forced arbitration in mortgage documents. When Congress wanted to stop predatory lending to members of the military, it banned forced arbitration of claims relating to the new protections.

By contrast, look at laws where forced arbitration continues to operate. So

New Mexico just passed its own new statute, banning high cost loans. But as a state statute, it's impossible for the New Mexico legislature to ban forced arbitration of claims relating to the law. (The U.S. Supreme Court would certainly find such a protection to be preempted by the Federal Arbitration Act.) As a result, the new New Mexico law will end up having very little impact – lenders can continue to make higher cost loans, and rely upon their forced arbitration clauses to enable them to break the law and get away with it.

### **Very Few Americans Genuinely Agree to Arbitration**

Forced arbitration clauses are ubiquitous in financial services. From credit cards to payday loans, clauses informing consumers that they are surrendering their Constitutional right to court are hidden in fineprint. They are often presented in long, complex forms, or in a paragraph or two hidden in a large agreement. Many on-line contracts bury the arbitration clause hundreds of lines deep in fine print; the corporations know that nearly all people will just click “agree” rather than scroll down so far. Unsurprisingly, consumers are typically unaware of these provisions, or if by some chance they are aware of them, they do not understand the implications.

In our experience of talking to many consumers, nearly everyone first learns that they have supposedly agreed that they don't want to take their case to a jury or court only after the dispute arises. In most cases, when someone first learns of an arbitration clause, it is a bitter surprise. I've had innumerable conversations where people – often very angry and dissatisfied people – were utterly unaware that they had supposedly agreed to such a clause.

Based on survey data, the Consumer Financial Protection Bureau (which in 2016 released an extensive and thoughtful study of forced arbitration in lending contracts)

has found that “consumers are generally unaware of whether their credit card contracts include arbitration clauses. Consumers with such clauses in their agreements generally do not know whether they can sue in court or wrongly believe that they can do so.” When they do read the arbitration clauses, it turns out that most consumers misunderstand them. For example, “less than 7% of consumers whose credit card agreements included pre-dispute arbitration clauses stated that they could not sue their credit card issuers in court.”<sup>3</sup> And most consumers with such clauses “wrongly believe that they can participate in class actions.”<sup>4</sup> In fact, misunderstanding is so commonplace that when researchers at St. John’s Law School pointed consumers to the arbitration clause and asked them to read it, only “approximately 13% understood that the contract they had just been shown prohibited them from participating in a class action lawsuit.” Amy J. Schmitz, “Consideration of ‘Contracting Culture’ in Enforcing Arbitration Provisions,” 81 St. John’s L. Rev. 123, 160 (2007).

Even when consumers do learn of arbitration clauses, based on Public Justice’s experience, consumers often don’t understand the clause even after they read it. In other words, our experience strongly supports the conclusions of the Consumer Financial Protection Bureau (“CFPB”) study on forced arbitration. Few people know what arbitration means, or wrongly assume they can still go to court. If individuals do notice the arbitration clause, and try to figure out what it means and how it would work, our experience is that they generally quickly become confused and discouraged. The arbitration rules are also lengthy, hard to find, and it’s often unclear which set of rules apply to the consumer’s case. Consumers also often must pay up front expenses absent in a court, and often face extensive delays when (as they often do) corporations refuse to pay their share of arbitrators’ fees.

## **Forced Arbitration is a Secretive, Non-transparent System**

Forced arbitration creates a culture of secrecy, where largely unaccountable arbitrators hear disputes behind closed doors and render decisions without being bound to follow legal precedents and often without publishing a written decision that explains their reasoning. This culture of secrecy prevents consumers and employees who are having a dispute from learning whether others have experienced a similar problem before and how that problem was resolved. It also leads to arbitrary and inconsistent results in the arbitral forum because arbitrators, unlike judges, are not required to follow precedents created by earlier-decided cases with similar facts. Most arbitration companies, and most arbitration clauses, impose varying levels of secrecy on individual workers, consumers and others who are subject to the clauses – it is very common for people to be barred from discussing the facts of their case, or the arbitrator’s decision, publicly.

But while arbitration remains cloaked in secrecy from the perspective of outsiders, the employers and companies that participate in multiple arbitrations, and the lawyers who represent those companies, are not outsiders. This repeat player bias benefits employers and other corporate participants in arbitration in many ways, from giving them a sense of what arguments an arbitrator is likely to favor to allowing them to select, in advance, an arbitrator who they believe will support their position.

## **Arbitration Tends to Favor Corporations Over People**

There are a number of different private arbitration companies who compete to be selected by corporations in their standard form contracts with consumers and employees. Arbitration work is often very lucrative, and arbitrators know that if they rule against a corporate defendant too frequently or too generously (from the standpoint of

that corporation), they will lose the work. Companies imposing arbitration clauses on their employees and consumers through standard form contracts of adhesion sometimes justify their actions with rhetoric about arbitration being cheaper and faster and fairer than litigation in court. From numerous conversations with lawyers both for corporations and advocates for individuals generally, and participation in multiple mediations and settlement negotiations, I can unequivocally testify that the nearly universal perception among both plaintiff-side and defense-side lawyers is that arbitrators are more likely to have a pro-defense attitude than are judges or juries.

Companies help their advantage further by “blackballing” arbitrators who have even the slightest indication that they may rule against them. This was revealed in a study of arbitration in managed care cases in California, which found a small number of cases where an arbitrator awarded a plaintiff more than \$1 million against an HMO. In each case, it was the only HMO case that the arbitrator handled, indicating that when the arbitrator rules against the HMO, he can no longer get any work from them. The study also found that arbitrators were twenty times more likely to enter summary judgment for HMOs than a judge. California Managed Health Care Systems 22 23 (2000).

### **Arbitrators’ Decisions Are Not Subject to Meaningful Judicial Review**

Sometimes even very smart, hardworking people make mistakes. But arbitrators’ decisions are nearly always final, no matter how unfair or wrong they may be. The general rule is that judicial review of arbitrators’ decisions “is very narrow; one of the narrowest standards of judicial review in all of American jurisprudence.” *Lattimer-Stevens Co. v. United Steelworkers of Am. Dist. 27*, 913 F.2d 1166, 1169 (6th Cir. 1990).



For example, Judge Richard Posner wrote for the Seventh Circuit that courts should not review arbitrators' interpretations of contracts even if they are "wacky," so long as the arbitrator attempted to "interpret the contract at all." *Wise v. Wachovia Securities, Inc.*, 450 F.3d 265, 269 (7th Cir. 2006). And when the Third Circuit considered an arbitrator's decision that "inexplicably" cited and relied upon language that was not included in a key document, the court held that "such a mistake, while glaring, does not fatally taint the balance of the arbitrator's decision in this case. ...." *Brentwood Medical Associates v. United Mine Workers of America*, 396 F.3d 237 (3d Cir. 2005). The Supreme Court itself has held that "courts are not authorized to review the arbitrator's decision on the merits" even if the fact finding was "silly." *Major League Baseball Players Ass'n v. Garvey*, 532 U.S. 504, 509 (2002). The California Supreme Court found that even when an arbitrator's decision would "cause substantial injustice" on its face, it was not subject to judicial review. *Moncharsh v. Heily & Blase*, 3 Cal. 4th 1 (1992).

**IMPORTANT HISTORICAL POINT: THE COMPANY THAT WAS THE LARGEST PRIVATE ARBITRATION PROVIDER IN THE U.S. FOR ABOUT 10 YEARS WAS SHUT DOWN FOR CORRUPT AND ILLEGAL BEHAVIOR**

This Committee should look back at the history of the late (but not lamented) National Arbitration Forum (NAF). Here are the key things to know:

- For about a decade, NAF was by far the largest provider of arbitration services to lenders for consumer arbitration;
- NAF's operations were outrageously unfair to consumers, and favorable to lenders, to a degree where words such as "corrupt" are entirely fair characterizations;
- The overwhelming majority of courts took no action with respect to the NAF, as courts were reluctant or unwilling to probe into the fairness of a major arbitrator

who was used by many corporations, in the wake of the Supreme Court's rush to favor mandatory arbitration; and

O The exact same factors that gave rise to the NAF – corporate desire for immunity from consumer protection law; a willingness by some actors to do ANYTHING to favor corporations if this would bring them substantial income; and the unwillingness of courts to meaningfully police arbitration – could easily give rise to a very similar actor down the road.

There is no reason whatsoever that this disgrace could not easily happen again. The NAF cloaked itself in respectability by spending a ton of money on articles and studies praising itself, hiring former judges and prominent political figures, fighting off discovery into its operations, and getting secrecy orders covering any documents that did become public, etc. Indeed, if the Minnesota Attorney General had not happened to discover that the NAF had crossed the most blatant line of inappropriate conduct – taking tens of millions of dollars for shares of a wholly owned corporation from entities who were currently litigating tens of thousands of cases in front of NAF – the NAF might well still be operating corruptly. I pose the question: “How can mandatory arbitration by lenders be fair when by far the largest provider of arbitration services for a decade operated in a dishonest and lawless manner, nothing happened, and there is nothing to stop this from happening again?”

Before it was shut down by a law enforcement action brought by the Minnesota Attorney General, however, very few courts ever struck down NAF arbitration clauses on the basis of bias, and the organization operated on a large scale for about a decade after the first evidence emerged that its neutrality was questionable. It took the

discovery that NAF had a substantial undisclosed conflict of interest before it was shut down. On July 14, 2009, the Attorney General of Minnesota sued the NAF and its corporate affiliates for consumer fraud, deceptive trade practices, and false advertising based on the NAF's undisclosed financial relationship with one of the country's largest debt collection law firms. See Compl. at ¶ 5, *State v. Nat'l Arbitration Forum, Inc.* (Minn. Dist. Ct. July 14, 2009). Within days, the NAF announced that it would cease conducting consumer arbitrations. See Robin Sidel and Amol Sharma, *Credit-Card Disputes Tossed Into Disarray*, Wall Street Journal (July 21, 2009).

Although the NAF did not initially acknowledge any wrongdoing after the Minnesota action was filed, a year and a half later the company *did* admit that the key allegations in the Minnesota complaint were true:

On April 6, 2011 the NAF executed a settlement agreement in which it formally stipulated that effective June 27, 2007 it became a holding company, transferred its operations to two subsidiaries and sold a 40% ownership interest in one of the subsidiaries to participants in the consumer debt collection industry for \$42 million.

*Torrence v. Nationwide Budget Finance*, No. 05-0047, 2012 WL 335947 at ¶ 30 (N.C. Super. Ct. Jan. 25, 2012).

NAF aggressively marketed itself to credit card companies and debt collectors. See Caroline E. Mayer, *Win Some, Lose Rarely? Arbitration Forum's Rulings Called One-Sided*, Wash. Post, Mar. 1, 2000, at E1 (“[A]rbitration industry experts say [that] the forum's business involves more corporate-consumer disputes, in large part because of

the company's aggressive marketing.”).

While NAF trumpeted itself to the public as fair and neutral, “[b]ehind closed doors, NAF sells itself to lenders as an effective tool for collecting debts.” Robert Berner & Brian Grow, *Banks v. Consumers (Guess Who Wins)*, BusinessWeek, June 5, 2008. See also Sean Reilly, *Supreme Court Looks at Arbitration in Alabama Case This Week*, Mobile Reg., Oct. 1, 2000, at A1 (“In marketing letters to potential business clients, [NAF’s] executives have touted arbitration as a way of eliminating class action lawsuits, where thousands of small claims may be combined.”); Sarah Ovaska, *3 Cases Cite Payday Lending: Consumer Groups Say Arbitration Clauses Deny People Recourse to Courts*, News & Observer, Jan. 7, 2007 (“[NAF], which in 2006 resolved \$3 billion worth of claims involving debts and other disputes, has been singled out by consumer advocates, who criticize it for advertising its services to businesses.”). In its solicitations and advertising, NAF “has overtly suggested to lenders that NAF arbitration will provide them with a favorable result.”<sup>13</sup> Ken Ward, Jr., *State Court Urged to Toss One-Sided Loan Arbitration*, Charleston Gazette & Daily Mail, Apr. 4, 2002, at 5A.

BusinessWeek described a September 2007, PowerPoint presentation aimed at creditors—and labeled “confidential”—that promises “marked increase in recovery rates over existing collection methods.”<sup>14</sup> Robert Berner & Brian Grow, *Banks v. Consumers (Guess Who Wins)*, BusinessWeek, June 5, 2008 The presentation also “boasts that creditors may request procedural maneuvers that can tilt arbitration in their favor. ‘Stays and dismissals of action requests available without fee when requested by Claimant—allows claimant to control process and timeline.’” Speaking on condition of anonymity, an NAF arbitrator told BusinessWeek that these tactics allow creditors to file actions

even if they are not prepared, in that “[i]f there is no response [from the debtor], you’re golden. If you get a problematic [debtor], then you can request a stay or dismissal.”

BusinessWeek also highlighted another disturbing NAF marketing tactic: NAF “tries to drum up business with the aid of law firms that represent creditors.” Neither AAA nor JAMS cooperate with debt-collection law firms in such a manner.

NAF had an arsenal of other ways of letting potential clients know that NAF can immunize them against liability. One NAF advertisement depicted NAF as “the alternative to the million-dollar lawsuit.” Nadia Oehlsen, *Mandatory Arbitration on Trial, Credit Card Mgmt.*, Jan. 1, 2006, at 38. Additionally, NAF sent marketing letters to potential clients in which it “tout[s] arbitration as a way of eliminating class action lawsuits, where thousands of small claims may be combined . . . .” *Supreme Court Looks at Arbitration in Alabama Case This Week, Mobile Reg.*, Oct. 1, 2000, at A1. NAF’s marketing letters also urged potential clients to contact NAF to see “how arbitration will make a positive impact on the bottom line” and told corporate lawyers that “[t]here is no reason for your clients to be exposed to the costs and risks of the jury system.” See Caroline E. Mayer, *Win Some, Lose Rarely? Arbitration Forum’s Rulings Called One-Sided*, *Wash. Post*, Mar. 1, 2000, at E1.

The NAF also manipulated the process for selecting arbitrators, so that favored clients got better results. The Center for Responsible Lending analyzed this data and reached two conclusions: (a) companies that arbitrated more cases before certain arbitrators consistently got better results from those arbitrators, and (b) individual arbitrators who favored creditors over consumers got more cases. Joshua M. Frank, Center for Responsible Lending, *Stacked Deck: A Statistical Analysis of Forced Arbitration* (2009), <http://www.responsiblelending.org/credit-cards/research->

analysis/stacked\_deck.pdf.

Similarly, the Christian Science Monitor analyzed one year of data and found that NAF's ten most frequently used arbitrators—who were assigned by NAF to decide nearly three out of every five cases—ruled for the consumer only 1.6% of the time. In contrast, arbitrators who decided three or fewer cases during that year found in favor of the consumer 38% of the time. Simone Baribeau, *Consumer Advocates Slam Credit-Card Arbitration*, Christian Sci. Monitor, July 16, 2007. One particular arbitrator, Joseph Nardulli, handled 1,332 arbitrations and ruled for the corporate claimant 97% of the time. On a single day—January 12, 2007— Nardulli signed 68 arbitration decisions, giving debt holders and debt buyers every cent of the nearly \$1 million that they demanded. Public Citizen, *The Arbitration Trap: How Credit Card Companies Ensnare Consumers* 17 (2007), <http://www.citizen.org/documents/ArbitrationTrap.pdf>. One former NAF arbitrator boasted, “I could sit on my back porch and do six or seven of these cases a week and make \$150 apop without raising a sweat, and that would be a very substantial supplement to my income. I'd give the [credit-card companies] everything they wanted and more just to keep the business coming.” Chris Serres, *Arbitrary Concern: Is the National Arbitration Forum a Fair and Impartial Arbiter of Dispute Resolutions?* Star Trib. (Minneapolis), May 11, 2008, at 1D.

NAF also blackballed arbitrators who dared to rule in favor of consumers. Harvard law professor Elizabeth Bartholet went public with her concerns that, after she awarded a consumer \$48,000 in damages, NAF removed her from 11 other cases, all of which involved the same credit card company, on the credit card company's objection.

As Bartholet described her experience, “NAF ran a process that systematically serviced the interests of credit card companies.” Similarly, former West Virginia Supreme Court Justice Richard Neely stopped receiving NAF assignments after he published an article accusing the firm of favoring creditors.

Is this all ancient history? Maybe. But maybe not. Nothing has changed since these events to prevent another corrupt arbitration firm from springing into existence. Arbitrators’ decisions are just as unreviewable as they’ve ever been, and the U.S. Supreme Court’s love affair with forced arbitration has only strengthened. We’re all just waiting to see what happens here, unless the Congress takes action.

### **Conclusion**

Forced arbitration clauses are pervasive in nearly every aspect of consumer financial services, and most consumers are unaware of, or do not fully understand, the consequences of agreeing to such provisions. As a result, millions of consumers are locked out of the court system and forced into secretive proceedings that overwhelmingly favors corporate defendants.

Through ending forced arbitration in this sector, Congress can ensure countless Americans are no longer denied their day in court and are no longer forced into a system where they are unlikely to prevail or, even if they do, to facilitate meaningful changes in how corporations and employers treat their customers and employees or compensate them for abuse.