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Ex rel. San Francisco City Attorney Dennis J. Herrera

CASE MANAGEMENT CONFERENCE SET

AUG 22 2008 -9:00 AM

DEPARTMENT 212

SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF SAN FRANCISCO

UNLIMITED CIVIL JURISDICTION

THE PEOPLE OF THE STATE OF CALIFORNIA, acting by and through San Francisco City Attorney Dennis J. Herrera,

Plaintiff,

vs.

NATIONAL ARBITRATION FORUM, INC.; FIA CARD SERVICES, N.A.; COLUMBIA CREDIT SERVICES, INC.; DOES 1-50 inclusive,

Defendants.

Case No. CGC-08-473569

COMPLAINT FOR INJUNCTIVE RELIEF AND CIVIL PENALTIES FOR VIOLATIONS OF BUSINESS AND PROFESSIONS CODE SECTION 17200

Plaintiff, the People of the State of California (the "PEOPLE"), acting by and through San Francisco City Attorney Dennis Herrera, is informed and believes and alleges as follows:

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INTRODUCTION AND SUMMARY OF ALLEGATIONS

1. This case challenges the unfair and unlawful business practices of defendants NATIONAL ARBITRATION FORUM, INC. ("NAF"), FIA CARD SERVICES, N.A. ("FIA"), and COLUMBIA CREDIT SERVICES, INC. ("COLUMBIA") (collectively, "DEFENDANTS"). Defendant NAF purports to act as a provider of neutral arbitration services that are fairly administered and characterized by integrity and high legal and ethical standards. In reality, NAF is retained by debt collectors and serves their interests alone in a non-neutral, biased and unfair manner. NAF is actually in the business of operating an arbitration mill, churning out arbitration awards in favor of debt collectors and against California consumers, often without regard to whether consumers actually owe the money sought by the debt collectors. NAF's arbitration process is the antithesis of fair. NAF fails to require debt collectors to provide proof that the consumers whose disputes it purports to arbitrate have been served with notice of arbitration. NAF bends or breaks its own procedural rules in favor of its debt collector clients. But when consumers who have been served request a hearing, NAF consistently ignores such requests and issues awards without consideration of the consumers' evidence or arguments. Worse, according to NAF's own disclosures, in NAF arbitrations involving claims by business entities against consumers that were disposed of by hearing in California, *the NAF arbitrator decided in favor of the business entity and against the consumer 100% of the time.* To ensure this will occur, NAF frequently ceases using arbitrators who decide in favor of consumers. Because California consumer-respondents *never* prevail in the hearings it administers, NAF cannot rightly be called a provider of neutral arbitration services at all; instead its arbitrations of consumer debt matters are a sham – the sole purpose of which is to assist its 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. Indeed, NAF goes even further to advance the interests of its debt collector clients by unlawfully allowing inflated awards in their favor, such as by awarding attorneys' fees not actually incurred and arbitration costs and fees that cannot legally be shifted to consumers under California law. FIA and COLUMBIA, in turn, participate in and benefit from this sham by forcing consumers into the NAF forum which they

know to be biased in their favor, by failing to inform consumers that the arbitration is nothing but a sham in which FIA and COLUMBIA are sure to win, by failing in many cases to serve consumers with notice of arbitration at their known address, and by seeking to obtain and collect awards against consumers to which they are plainly not entitled under California law, often including tens of thousands of dollars per arbitration in unlawful and inflated attorneys' fees, as well as stale debts long past the statute of limitations period. FIA routinely uses attorneys who are not licensed in California to conduct California arbitrations. FIA also compounds the harm of the NAF process by regularly placing consumers' personal and financial information, including social security numbers, in the public record in the course of confirming NAF's rubber-stamp arbitration awards in Superior Court, rendering consumers vulnerable to identity theft just as they are trying to rebuild their credit. A few examples of consumers' experiences with these defendants illustrate the range and type of harms suffered.

2. Anastasiya Komarova is a California resident who was the victim of mistaken identity. She had never received credit from FIA's predecessor, MBNA America Bank, N.A. ("MBNA"), but her name is very similar to that of Anastasia Komarova, an authorized user on an MBNA account. MBNA sold Anastasia Komarova's alleged debt to a third-party debt purchaser affiliated, upon information and belief, with COLUMBIA, which sought to collect against Anastasiya Komarova even after being notified that Anastasiya Komarova and Anastasia Komarova were different people living in different cities. The debt purchaser filed a claim against Anastasia Komarova, but served no notice upon her or upon Anastasiya Komarova. NAF entered an award of $11,214.33 against her, even though the debt that the third-party debt purchaser originally sought to collect was only $7,872.98, and the debt purchaser itself has been unable to explain the basis for the increased amount of the award. The debt purchaser then sought to enforce this sham arbitration award against Anastasiya Komarova. To date, no one has ever explained to Anastasiya Komarova how the alleged debt increased by $3,341.35 in the course of the NAF arbitration.

3. Elizabeth Marcotte is a California resident who had an MBNA credit card. Ms. Marcotte notified MBNA of an updated address in 2003. Her alleged debt to MBNA was

purchased by COLUMBIA sometime in 2004. COLUMBIA filed a claim against Ms. Marcotte with NAF but it served Ms. Marcotte with notice of the claim at her previous address rather than her updated address. COLUMBIA sought to recover from Ms. Marcotte the alleged balance on her credit card of $25,798.16 plus $10,631.62 in estimated attorneys' fees. The claim COLUMBIA submitted consisted of a few pages of boilerplate, signed by a COLUMBIA employee, and did not bear an attorney's name or signature. Ms. Marcotte never received notice of the arbitration because she was improperly served, and she therefore did not oppose COLUMBIA's claim. NAF awarded COLUMBIA the full amount it sought, including the estimated $10,631.62 in attorneys' fees, after an uncontested documentary review of COLUMBIA's boilerplate claims and its fee estimate. COLUMBIA never submitted, and NAF never required, proof that the estimated attorneys' fees (or indeed any attorneys' fees) were actually incurred.

4. Jane Roe (a pseudonym) is a California resident who had an MBNA credit card. MBNA filed a claim against her with NAF concerning an alleged unpaid balance. In October 2004, NAF entered an arbitration award against her in the amount of $17,887.47. In 2005, MBNA sought to confirm this arbitration award with a petition in the Superior Court of a Bay Area county. In the course of seeking to confirm the award, MBNA, through its attorney, included in public court filings – and thereby posted in the public record – Ms. Roe's credit history, including her social security number, date of birth, mother's maiden name, annual salary, previous salary, and various account balances. To date, this sensitive private information – which could easily be used to commit identity theft against Ms. Roe – remains in the public record, as does private information of many other California residents who were the victims of identical practices by MBNA.

5. John Sheakley is a California resident who had an MBNA credit card. He refused to make payments on a charge that he protested repeatedly to MBNA. MBNA filed a notice of claim against Mr. Sheakley with NAF. After receiving notice of the arbitration, Mr. Sheakley wrote to NAF seeking a hearing on MBNA's claims so that he could explain why he contested the balance on his card and why he did not owe the balance based on the terms of his

cardmember agreement. NAF never responded to Mr. Sheakley's request for a hearing. Instead, it issued an arbitration award against him based on MBNA's papers alone.

6. Troy Cornock is a New Hampshire resident whose wife, from whom he was separating, opened an MBNA account in his name. Mr. Cornock was unaware of this account and the balance that his wife had accumulated on it until he started to receive collections calls from MBNA, which refused to remove his name from the account. MBNA filed a case against Mr. Cornock with NAF and served him with notice of its claim at his wife's address. Nonetheless Mr. Cornock received the notice and wrote a letter to NAF, under his current address, and explaining that the account had been opened by his wife and he had never consented to it. Unbeknownst to Mr. Cornock, and disregarding his claim of identity theft, NAF entered an arbitration award against him that it served on him at his wife's address, even though Mr. Cornock had notified NAF directly of his new address. The first notice Mr. Cornock had of the award came after MBNA obtained a default judgment against him, confirming the arbitration award of nearly $10,000. Upon information and belief, NAF and MBNA have followed the same practices of ignoring allegations of identity theft and of making or tolerating defective service on consumers in numerous California arbitrations.

7. John Newsom is a Mississippi resident in whose name an identity thief opened an MBNA credit card account. Mr. Newsom received notice that the account was in default and he explained to MBNA that the account was not his. Nonetheless MBNA initiated a NAF arbitration against Mr. Newsom. Mr. Newsom received notice that MBNA's claim had been filed with NAF and was given 14 days to respond to the claim. On the 12th day, Mr. Newsom's attorney filed an answer to the claim with NAF, describing the identity theft. NAF never forwarded the answer to the arbitrator who decided the case, claiming that it had been received on the 15th day, and the arbitrator received Mr. Newsom's case with a stack of what NAF called "uncontested" cases. The arbitrator entered an award against Mr. Newsom of $17,759.65. Upon information and belief, NAF has followed the same practice of ignoring allegations of identity theft and failing to convey consumer responses to the arbitrator in numerous California

arbitrations, and MBNA has followed the same practice of ignoring allegations of identity theft with regard to numerous California consumers.

8. The injustices experienced by Ms. Komarova, Ms. Marcotte, Ms. Roe, Mr. Sheakley, Mr. Cornock, Mr. Newsom, and the tens of thousands of California consumers who have been subjected to unfair NAF arbitration proceedings share a common thread: the scheme of defendants NAF, FIA, COLUMBIA, and DOES 1-50 to pervert the arbitration process to serve their unlawful and unfair ends.

9. Arbitration is a mode of alternative dispute resolution that can offer significant benefits in efficiency and access to justice to parties who have contracted to resolve their disputes in this manner. This mode also benefits the public by conserving scarce judicial resources. For these and other reasons, arbitration has a special place in California's (and the nation's) justice system. Arbitration awards are subject to review only in special and narrowly defined circumstances, unlike the decisions of the trial courts who would typically adjudicate debt collection claims like those brought by FIA and COLUMBIA. Indeed, it is settled law in California that parties to an arbitration award are bound by it even if the arbitrator's decision was wrong.

10. But in light of the deference paid to arbitration awards, as the United States Supreme Court noted in 1968, "we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free rein to decide the law as well as the facts and are not subject to appellate review." (*Commonwealth Coatings Corp. v. Continental Cas. Co.* (1968) 393 U.S. 145, 148-49.) California law underscores the importance of arbitrator impartiality with a series of consumer-protection measures contained in the California Arbitration Act, Code of Civil Procedure sections 1280 *et seq.* Respected arbitration organizations safeguard this essential impartiality by retaining unbiased arbitrators, by complying with the California Arbitration Act in letter and in spirit, and by treating opposing parties to a dispute with fairness and equality.

11. NAF, by contrast, has turned arbitration's paradigm of impartiality on its head in the manner described in this Complaint, and FIA and COLUMBIA participate in and benefit

from this scheme as described in this Complaint. DEFENDANTS' scheme harms California citizens by depriving them of the fair arbitration process to which they are entitled under the law, by undermining public trust in quasi-adjudicatory processes, and by costing California citizens hundreds of thousands dollars in fees, forum costs, and stale debts – money that debt collectors like FIA and COLUMBIA are not entitled to receive. The PEOPLE bring this action to reform DEFENDANTS' unfair and unlawful scheme.

PARTIES

12. Plaintiff the PEOPLE OF THE STATE OF CALIFORNIA, by and through San Francisco City Attorney Dennis J. Herrera, prosecute this action pursuant to California Business and Professions Code sections 17204 and 17206.

13. Defendant NAF is a Minnesota corporation with offices located at 8000 Norman Center Drive, Suite 1000, Minneapolis, Minnesota 55437. NAF does business in California and sponsors arbitrations in California involving California residents. NAF also maintains an office in California.

14. Defendant FIA is a national bank with offices located at 1100 North King Street, Wilmington, Delaware, 19801. FIA supplies credit cards to California consumers, makes loans to California consumers, requires California consumers to submit to arbitrations sponsored by NAF, uses California courts to confirm NAF arbitration awards against California consumers, and does business in California.

15. Defendant COLUMBIA is a California corporation with offices located at 1731 Howe Avenue, Suite 360, Sacramento, California 95825. COLUMBIA purchases debts owed by California consumers, collects and attempts to collect debts allegedly owed by California consumers, requires California consumers to submit to arbitrations sponsored by NAF, uses California courts to confirm arbitration awards against California consumers, and does business in California.

16. The transactions and practices described herein involve additional entities whose identities and involvement are unknown to the PEOPLE. The true names and capacities, whether corporate, associate, individual, partnership or otherwise, of Defendants Does 1 through 50,

inclusive, are unknown to the PEOPLE, which therefore sue said defendants by such fictitious names. The PEOPLE will seek leave of court to amend this complaint to allege their true names and capacities when the same are ascertained.

17. The PEOPLE are informed and believe and thereupon allege that all of the acts and omissions described in this Complaint by any defendant were duly performed by, and attributable to, all DEFENDANTS, including Doe Defendants, each acting as agent and/or under the direction and control of the others, and such acts and omissions were within the scope of such agency, direction, and/or control. Any reference in this complaint to any acts of "DEFENDANTS" shall be deemed to be the acts of each and every defendant acting individually, jointly or severally.

JURISDICTION AND VENUE

18. The Superior Court has jurisdiction over this action. DEFENDANTS are conducting unlawful and deceptive business practices in San Francisco and the City Attorney has the right and authority to prosecute these cases on behalf of the PEOPLE.

19. Venue is proper in this Court because DEFENDANTS transact business in the City and County of San Francisco and some of the acts complained of occurred in this venue.

FACTUAL ALLEGATIONS:

NAF'S ARBITRATION MILL IS BIASED IN FAVOR OF DEBT COLLECTORS

20. Upon information and belief, and based on NAF's own reporting, NAF handled 33,933 arbitration matters in California involving consumer collections during the period January 1, 2003 through March 31, 2007.

21. Of these 33,948 matters, 16,425 were brought by FIA or its predecessor MBNA, and at least 1667 additional matters were brought by assignees of FIA or MBNA. (Hereinafter, FIA and its predecessor MBNA are referred to simply as FIA.) But NAF's self-reported figures are probably woefully shy of the true total of consumer collections arbitrations in California handled by NAF, because, as discussed below, NAF omits many arbitrations from its reporting, including all arbitrations it has handled for COLUMBIA, an assignee of FIA.

22. Even NAF's self-reported, likely inaccurate statistics demonstrate that consumers had no chance of prevailing in NAF collections arbitrations brought by business entities. Again based on NAF's own reporting, a total of 18,075 consumer arbitration matters it handled were disposed of by a participatory or paper hearing before an arbitrator. (In its statistics, NAF includes cases where the consumer does not appear or contest a claim as "hearings" conducted by an arbitrator on the papers. Cases where the consumer contests a claim but no in-person, participatory hearing is conducted are also called "hearings" on the papers by NAF. For clarity and following NAF's terminology, this Complaint refers to in-person hearings as "participatory hearings" and to document review hearings, including those where the consumer has not appeared or contested a claim, as "paper hearings.") Of the matters that went to hearing, including to a paper hearing, only 30 out of 18,075 – or less than 0.2% of the total – resulted in a victory by the consumer. Each and every one of these consumer victories was a matter where a consumer had brought a claim against a business entity – a very small number of the total number of claims decided by NAF arbitrators. But in each and every case where a business entity brought a claim against a consumer and the matter was disposed of by hearing, the NAF arbitrator ruled in favor of the business entity – a 100% success rate that any litigant would be overjoyed to have.

23. NAF accomplishes this astonishing result in favor of its corporate clients in part by establishing incentives for arbitrators to favor debt collectors rather than consumers. Upon information and belief, NAF arbitrators handling consumer collections matters are not salaried but are paid by the number of arbitrations that they handle. This gives them incentives to decide matters quickly with little review. Moreover, NAF arbitrators who reliably decide in favor of businesses are rewarded with more business from NAF – a repeat player effect that the California Supreme Court has recognized as pernicious. (*Armendariz v. Foundation Health Psychcare Services Inc.* (2000) 24 Cal.4th 83, 111 ["[I]t is not the fact that the employer may pay an arbitrator that is most likely to induce bias, but rather the fact that the employer is a 'repeat player' in the arbitration system that is more likely to be a source of business for the arbitrator."].)

24. The repeat player effect in NAF arbitrations is amply borne out by NAF's reported statistics. For example, one California arbitrator, during the period January 1, 2003 through March 31, 2007, handled 1290 consumer collections matters that were disposed of by participatory or paper hearing. This arbitrator decided every single one of these matters in favor of the business entity. Upon information and belief, a total of 28 California arbitrators handled nearly 90 percent of all of consumer collections cases, and they too decided every matter disposed of by participatory or paper hearing in favor of business entities. NAF also makes it easy for its arbitrators to decide cases in favor of debt collectors by giving them pre-printed award forms in favor of the business and against the consumer; all the arbitrator needs to do is sign.

25. In case its positive incentives are insufficient for NAF to assure debt collectors that they will win arbitrations, NAF also dumps arbitrators who decide in favor of consumers. Harvard Law School professor Elizabeth Bartholet, who served for a time as an arbitrator for NAF in Massachusetts, has provided sworn deposition testimony that NAF ceased using her services after she awarded money to a consumer and against a credit card company on a counterclaim. In fact, for at least one arbitration that was scheduled to be heard by Professor Bartholet after her pro-consumer award, NAF sent a letter to the parties to that arbitration stating that Professor Bartholet was unavailable due to a scheduling conflict. In fact, Professor Bartholet testified, she had no scheduling conflict and had never told NAF that she was unavailable for the pending arbitration. Professor Bartholet was informed by NAF staff that her pending arbitrations were reassigned because of the award she made in favor of the consumer.

26. In addition to NAF's practice of giving arbitrators incentives to decide in favor of debt collectors, debt collectors' 100% success rate in NAF hearings is further ensured by the extraordinarily high rate of consumer defaults in these hearings. Upon information and belief, out of the 18,075 NAF arbitrations disposed of by paper or participatory hearings, 16,055 were cases where the consumer defaulted on the claim. As discussed below, FIA and COLUMBIA employ outdated addresses for consumers in serving them with NAF claims, which ensures that defaults remain high. NAF, in turn, tolerates these extraordinary default rates by allowing

service by certified mail or private delivery service rather than effective personal or substituted service. Moreover, in practice, NAF does not require proof of service on the consumer at all.

27. NAF's practices of giving arbitrators incentives to decide in favor of debt collectors, and of turning a blind eye to the defective methods that its business customers use to serve consumers, are unlawful under Code of Civil Procedure section 1297.181 ("The parties [to an arbitration] shall be treated with equality ....") and constitute unfair and unlawful business practices.

NAF ENSURES AWARDS IN FAVOR OF DEBT COLLECTORS WITH BUSINESS PRACTICES THAT ARE UNFAIR AND VIOLATE CALIFORNIA LAW

28. Although NAF's arbitrations are nominally conducted according to the NAF "Code of Procedure" ("NAF Code"), upon information and belief NAF disregards the rules contained in this document when it would benefit debt collectors to do so. For example, NAF routinely allows late filings by debt collectors, while enforcing the NAF Code's time limits against consumers. This practice violates Code of Civil Procedure section 1297.191.

29. Upon information and belief, NAF also routinely ignores consumers' requests for participatory hearings and consumers' motions, even though such requests and motions are allowed by the NAF Code. This practice violates Code of Civil Procedure sections 1297.191 and 1297.242 ("the arbitral tribunal shall hold oral hearings at an appropriate state of the proceedings, if so requested by a party"). Upon information and belief, in some cases where NAF actually sets a matter for a hearing before an arbitrator, the arbitrator is not informed that the hearing will take place and does not actually conduct any hearing.

30. NAF routinely administers consumer arbitrations under agreements that provide that the consumer must pay the attorneys' fees and costs of the opposing party if the opposing party prevails in arbitration. Indeed, NAF arbitrators routinely award thousands of dollars in fees and costs to debt collectors who prevail in NAF's biased arbitrations. This practice is unfair as well as unlawful under Code of Civil Procedure section 1283.4, which prohibits private arbitration companies and neutral arbitrators from administering consumer arbitrations under agreements requiring fee- and cost-shifting.

31. Upon information and belief, NAF permits debt collectors like FIA to have ex parte contacts with NAF, which in turn are passed on by NAF to the arbitrator, concerning substantive aspects of the debt collectors' claims. For example, at the request of certain debt collectors, NAF informs arbitrators of the cost of the arbitration itself, so that the arbitrator can include the forum cost in the total award. But this information is not provided to the consumer. This practice violates NAF's own rules and Code of Civil Procedure sections 1297.191 and 1297.244 ("All statements, documents, or other information supplied to, or applications made to, the arbitral tribunal by one party shall be communicated to the other party, and any expert report or evidentiary document on which the arbitral tribunal may rely in making its decision shall be communicated to the parties."). Moreover, as discussed in paragraph 32, it is unlawful for NAF to administer arbitrations where the consumer must pay the costs of the prevailing party – and NAF compounds this unlawful conduct by hiding its unlawful fee-shifting from consumers through these ex parte contacts.

32. The NAF Code requires every claimant to submit with its claim an affidavit stating that the information in the claim is accurate. But for FIA, COLUMBIA, and other debt collectors, upon information and belief, NAF overlooks this rule and allows the claimant to submit inadequate affidavits that do not attest to the truth of the claim – such as affidavits by an attorney who swears that his or her client informed the attorney that the claim was true. NAF's practice of ignoring its affidavit requirement to suit its debt collection customers violates Code of Civil Procedure section 1297.191.

33. Upon information and belief, NAF often does not convey consumer responses to a debt collector's claims to the arbitrator. For example, in the case of John Newsom, discussed in paragraph 7 above, NAF did not convey Mr. Newsom's attorney's description of the identity theft Mr. Newsom had suffered to the arbitrator who decided the case. Instead, NAF submitted the case to the arbitrator as "uncontested." This practice is unfair and unlawful under Code of Civil Procedure section 1287.191.

34. California law and the NAF Code require arbitrators to decide all cases on their merits regardless of whether one party to the arbitration does not appear. Yet the practice of

NAF arbitrators, upon information and belief, is to decide automatically cases where the consumer does not appear in favor of debt collectors – indeed, one arbitrator admitted as much in recent public statements, saying that "[b]ecause they're defaults, the power of the arbitrator is such that you have no choice as long as the parties have been informed." Upon information and belief, NAF encourages this practice by, *inter alia*, designating cases submitted to its arbitrators as uncontested, paying arbitrators per arbitration regardless of the amount of time they spend on the matter, and giving them pre-printed forms that allow them to render awards in favor of debt collectors simply by signing their names. NAF's practices are unfair and unlawful under Code of Civil Procedure sections 1297.252 and 1297.253.

NAF ARBITRATIONS ARE INADEQUATE TO PROTECT CONSUMER RIGHTS UNDER CALIFORNIA LAW

35. In addition to breaking its own rules in order to assist debt collectors, NAF has adopted rules and procedures that are simply inadequate to allow consumers to vindicate their rights under the California Fair Debt Collection Practices Act, Civil Code sections 1788 *et seq.* (the "Rosenthal Act"), and other California consumer protection laws and policies. The Rosenthal Act guarantees nonwaiveable rights to California debtors who face debt collection efforts, such as the right to be free of false representations that they will be liable for attorneys' fees, the right to receive adequate service of process, and the right to receive written verification of the validity of the debt in some circumstances. The Rosenthal Act is intended to prohibit debt collectors from engaging in unfair or deceptive acts or practices and applies to actions debt collectors take in arbitrations.

36. NAF awards that are entered against consumers are presented as a lump sum and do not break out the components of the award. Thus, a consumer who reviews an NAF award does not know how much of the award is principal, how much is interest, how much is fees or penalties charged by the debt collector, how much is attorneys' fees awarded to the debt collector, and how much is arbitration fees recovered by the debt collector. NAF's practice of rendering lump sum awards allows abuses by debt collectors like FIA and COLUMBIA, who roll into their claims items they are not entitled to receive, such as unreasonable and estimated

attorneys' fees and such as arbitration fees, as discussed further below. The experience of Anastasiya Komarova, whose alleged debt jumped from $7,872.98 to $11,214.33 in an arbitration conducted by NAF – when even the debt collector could not provide any justification for how the debt grew by $3,341.35 during the course of the arbitration – illustrates the potential for abuse created by NAF's failure to break out components of arbitration awards. NAF thereby aids and abets FIA's and COLUMBIA's unlawful and unfair practice of obtaining inflated awards.

37. The NAF Code allows consumers to obtain a breakdown of the components of an arbitration award, and a written statement of the arbitrator's decision, but only for a fee. Additionally, NAF allows consumers to have participatory hearings before an arbitrator rather than paper hearings only on payment of a fee. NAF's practices of charging fees for participatory hearings and for documents that consumers need in order to vindicate their rights under the Rosenthal Act and other California laws and policies are unfair.

38. Under the NAF Code, consumers are allowed no discovery to learn about the claims against them unless the arbitrator grants requests for discovery. Upon information and belief NAF arbitrators, rarely or never grant discovery to consumers. Although arbitration is a streamlined procedure intended to offer time and cost efficiencies over litigation, the inability of consumers to obtain even minimal information about the claims against them means that they are unable to vindicate their rights under the Rosenthal Act and other California laws and policies. NAF's practice of disallowing discovery is unfair.

39. Under the NAF Code, debt collector claimants are allowed to serve consumers with their claims by certified mail or private delivery service rather than the in-person service that litigants are entitled to in most cases. Such service may be sufficient to protect respondents' rights in some kinds of arbitration proceedings. But in the kind of consumer collection arbitration that NAF practices, these means of service are inadequate to ensure that consumers are given notice of the claims against them. NAF's service rules constitute unfair practices because they are so lax that the do not give consumers an adequate opportunity to protect their rights under the Rosenthal Act and other California laws and policies.

40. Under the NAF Code, NAF staff hear and decide some of the motions made by parties to California arbitrations, including, for example, motions by consumers to waive arbitration fees. By doing so, NAF staff act as arbitrators and are subject to the requirements of the California Arbitration Act, Code of Civil Procedure sections 1280 *et seq.* Yet NAF does not require its staff to comply with the California Arbitration Act, such as by disclosing their identities and their prior business with parties to the arbitrations they assist in deciding. This practice is unlawful under, inter alia, Code of Civil Procedure section 1297.121.

41. The result of NAF's practices, including those described in paragraphs 22-42 above, is that NAF awards against consumers are unfair and unlawful. Consumers are routinely given defective notice of claims against them, as NAF knows or should know. Consumers are subject to proceedings where they cannot vindicate their rights under the Rosenthal Act and other California laws and policies because they are not given discovery, full information about the claims against them, or full information about the awards entered against them. NAF enforces its rules against consumers but breaks its own rules where it serves the needs of debt collectors. Consumers in NAF proceedings are certain to lose – as evidenced by the 100% win rate that business entities have against consumers in claims that are disposed of by participatory or paper hearing before an NAF arbitrator, according to NAF's own statistics. The biased and unfair nature of the NAF forum, moreover, results in harms to more than justice and fair play. As described below, consumers who are victimized by NAF arbitration awards often must pay thousands of dollars to debt collectors that the collectors are not entitled to receive – through collectors' practices of seeking bogus attorneys' fees and stale debts and of unlawfully shifting arbitration fees onto consumers, all of which is enabled by the rubber stamp that NAF arbitration awards provide.

42. In the course of carrying out these business practices, NAF has abdicated its role as the sponsoring organization of neutral arbitrations. Instead, its business model with regard to consumer debt collection matters consists exclusively of assisting debt collectors in recovering money against consumers – such that it is no longer acting as an arbitration sponsoring

organization at all, and its arbitration panelists can no longer be said to be engaging in arbitrations.

NAF FAILS TO COMPLY WITH CALIFORNIA DISCLOSURE STATUTES AND OTHER CALIFORNIA LAWS AND POLICIES

43. Code of Civil Procedure section 1281.96 requires any private company administering consumer arbitrations to disclose, on a quarterly basis, certain information regarding its consumer arbitrations for the past five years, such as the name of the business entity bringing claims against consumers, the number of times that business entity has used the private arbitration sponsor in the past, and the outcome of the arbitration. This information is to be disclosed on the arbitration sponsor's website.

44. Since the first quarter of 2007, NAF has openly flouted this disclosure requirement by failing to disclose any information at all concerning arbitrations that it administered from April 1, 2007 through the present. This practice is unlawful under Code of Civil Procedure section 1281.96.

45. Moreover, even before NAF ceased making disclosures at all, it violated section 1281.96 by making incomplete disclosures. For example, NAF disclosed no arbitrations involving COLUMBIA, yet court dockets reveal numerous cases where COLUMBIA sought to confirm NAF arbitration awards against consumers. Upon information and belief, NAF also disclosed no arbitrations involving other debt collectors that used its services, such that its 1281.96 disclosures were woefully incomplete.

46. Prior to the first quarter of 2007, NAF also violated section 1281.96 by making false disclosures of the share of arbitration fees that consumers paid for NAF arbitrations. Generally business entities in California are not permitted to shift the business's share of arbitration fees (along with attorneys' fees) to consumers, even when the consumer loses in the arbitration. (Code of Civil Procedure section 1284.3.) Upon information and belief, in numerous NAF awards, debt collectors sought and received their arbitration fees as part of the award – yet NAF folded the arbitration fees into the award itself without providing a breakdown of the cost-shifted arbitration fees. NAF then claimed in its 1281.96 disclosures that the

consumer had not paid the collector's share of the arbitration fees. This practice violated section 1281.96 and was deceptive, unfair, and unlawful.

47. NAF also violated section 1281.96 by making misleading disclosures about the number of times it had conducted arbitrations involving particular business entities. Section 1281.96(a)(4) requires arbitration sponsors to disclose "[o]n how many occasions, if any, the nonconsumer party has previously been a party in an arbitration or mediation administered by the private arbitration company." In each of its quarterly disclosures prior to April 2007, NAF disclosed only the number of times a business entity had been involved in arbitrations before NAF in that quarter, rather than the total number of times the business entity had previously arbitrated or mediated before NAF. This practice, a violation of section 1281.96, meaningfully harms consumers. For example, a consumer facing an arbitration against FIA in 2007 would have learned from NAF's 2007 disclosures that FIA had been a party before NAF 782 times in the past – but the real number of times FIA had appeared before NAF arbitrators in the last four years was 16,425.

48. Although nearly all of NAF's arbitrations are initiated by businesses against consumers, upon information and belief NAF is also used by business entities as a forum for consumers to bring affirmative claims against those entities. Upon information and belief, NAF has never permitted California consumers to bring affirmative claims in the form of class actions. Yet for many potential claims that California consumers have against credit card companies like FIA, class treatment is the only feasible mechanism for pursuing affirmative claims. NAF's failure to permit class actions when class treatment is the only way to vindicate certain consumer claims is an unfair business practice.

NAF ENGAGES IN UNFAIR AND DECEPTIVE MARKETING PRACTICES

49. Although its real function is to deliver arbitration awards to debt collectors, NAF engages in unfair and deceptive marketing practices by advertising itself to consumers as fair and neutral. For example, NAF's website includes the claims that NAF's "dispute resolution processes are designed to provide both parties with an equal opportunity to prevail," that the NAF Code "ensures all parties a fair, unbiased dispute resolution process," and that NAF is "not

beholden to any company or individual that utilizes [its] services." NAF's website further claims that NAF's "mission is simple: to provide a fair, efficient, and effective system for the resolution of commercial and civil disputes," that it aspires to "high legal and ethical standards," and that it brings people together to solve conflict "in the most fair and appropriate manner." NAF's website also contends, "We are guided by experience, integrity and innovation. Our commitment to professional and legal standards produces clear, unbiased rules, and we accord disputing parties rights and privileges consistent with those of the judicial system. The former judges and experienced attorneys who hear and decide our cases review the facts and render decisions based on known rules and substantive law." In light of the 100% win rate that debt collectors have in NAF hearings in California, and in light of NAF's unfair business practices, these advertisements are unfair and deceptive and violate Business and Professions Code section 17500.

50. NAF's deceptive marketing practices extend to mischaracterizing reports that have analyzed arbitration outcomes. For example, a 2005 press release still available on NAF's website describes a study conducted by Ernst & Young as "demonstrat[ing] that consumers do as well in arbitration as they do in court, but in much less time and at a much lower cost, and that their satisfaction with arbitration is very high." NAF also states on its website that the Ernst & Young study shows that "the majority of consumers are satisfied with the speed, simplicity and cost benefits of arbitration." What NAF neglects to mention about the Ernst & Young report is that it studied only 226 consumer-initiated arbitration proceedings, which are unrepresentative of NAF's arbitration practice as a whole. In California arbitrations reported by NAF, consumer-initiated proceedings amount to less than one third of one percent of the total number of arbitrations administered by NAF. Moreover, Ernst & Young attempted to contact only 40 consumers to determine their satisfaction levels with their arbitration proceedings, and only 29 consumers responded. NAF's characterization of the Ernst & Young study as demonstrating consumer satisfaction with NAF arbitrations constitutes unfair and deceptive advertising and violates Business and Professions Code section 17500.

51. NAF also misleads consumers about the nature of arbitration itself, by claiming on its website that arbitration decisions are reviewed by a judge to determine if "the procedures used, the hearing conducted, and the award issued were fair and just under the applicable law." As NAF knows or should know, "neither the merits of the controversy nor the sufficiency of the evidence to support the arbitrator's award are matters for judicial review [in California]." (*DeMello v. Souza* (1973) 36 Cal.App.3d 79 at 86-87.) Instead, parties to an arbitration "are bound by the award even if the decision of the arbitrator is wrong." (*Id.*) NAF's website advertisement concerning the extent of judicial review of arbitration awards is unfair and deceptive and violates Business and Professions Code section 17500.

52. NAF also misleads the public about its arbitrators. Its website claims that its arbitrations "are decided by former judges and experienced attorneys." But a number of the arbitrators disclosed by NAF in its 1281.96 disclosures have never been licensed to practice law in California. Worse still, other arbitrators disclosed by NAF have been suspended from the practice of law or are otherwise ineligible to practice in California – yet they decided cases for NAF in California after they became ineligible or suspended. NAF's advertisements concerning its arbitrators and their qualifications are unfair and deceptive and violate Business and Professions Code section 17500.

53. Some of the only truthful advertisements that NAF publishes are those that are exclusively directed at debt collectors and other business entities. In trade magazines and letters to corporate general counsels, NAF makes claims concerning its arbitrations that imply (truthfully) that businesses overwhelmingly win in cases brought before NAF. For example, NAF advertises that "[a]rbitration can save up to 66% of your collection costs." It tells businesses that its arbitrations feature limited discovery and limited pre-hearing maneuvering, and that its arbitrations will make a positive impact on the company's bottom line. And, in letters to corporate counsels, it provides references consisting entirely of business representatives and their lawyers, with no references by consumers or consumer attorneys. These marketing practices, while candid about whose interests NAF exists to serve, are unlawful or otherwise unfair because they violate the Judicial Council's Ethics Standards for Neutral Arbitrators in

Contractual Arbitration, which forbid advertisements that imply favoritism toward any party to an arbitration.

FIA AND COLUMBIA COMMIT UNFAIR AND UNLAWFUL BUSINESS PRACTICES IN CONNECTION WITH NAF ARBITRATIONS

54. Debt collection companies who use NAF arbitrations have understood the message of NAF's pro-business marketing; they know that the odds in NAF arbitrations overwhelmingly favor them. Indeed, in trial testimony in *Komarova v. National Credit Acceptance, Inc.*, San Francisco Superior Court No. 456-891 (December 19, 2007), the president of one debt collection firm expressed surprise at the concept that debt collectors could ever lose NAF cases. For debt collectors to use NAF arbitrations to collect debts, with awareness of the favorable odds they face in this biased forum, is an unfair business practice.

55. FIA and COLUMBIA are two debt collectors who use NAF in just this way: they force consumers to arbitrate before this biased forum. From January 1, 2003 through March 31, 2007, FIA used NAF in 16,425 collections matters in California – assuming that NAF's reported data is correct. It is impossible to know how many times COLUMBIA used NAF for arbitrations during that same period, because NAF unlawfully omitted COLUMBIA arbitrations from its 1281.96 disclosures, but court dockets reveal numerous cases brought by COLUMBIA seeking to confirm arbitration awards made by NAF arbitrators. For FIA and COLUMBIA to use a biased arbitration provider is an unfair business practice. This practice is moreover a breach of the covenant of good faith and fair dealing between collectors and consumers: when consumers enter into agreements to arbitrate disputes with debt collectors, implied in those agreements is a promise by the collectors not to force consumers into an unfair and biased forum. Finally, by using NAF to recover awards they are not entitled to, FIA and COLUMBIA instigate quasi-judicial proceedings in bad faith.

56. FIA and COLUMBIA both take advantage of the cursory review that NAF arbitrators give to their claims by working further unfairness on consumers in the arbitration process. Upon information and belief, both FIA and COLUMBIA frequently use outdated addresses to serve consumers with notice of the NAF arbitration claim – such as the case of

Elizabeth Marcotte, who was served by COLUMBIA at an outdated address even though she had supplied an updated address to FIA before COLUMBIA purchased her alleged credit card debt from FIA. This practice of using defective addresses ensures that consumers will default on debt collectors' claims and is an unfair business practice.

57. Additionally, upon information and belief, FIA and COLUMBIA have ex parte contacts with NAF and NAF arbitrators during the arbitration of their claims. For example, on their behalf, NAF tells the arbitrators and FIA and COLUMBIA the total amount of arbitration fees so that arbitrators can roll those fees into the arbitration award, but this information is never conveyed to the consumer. This is an unfair business practice.

58. Perhaps most egregiously, FIA and COLUMBIA take advantage of the biased NAF forum to obtain awards from consumers that are grossly inflated and well above what the collectors are entitled to. Such awards can amount to tens of thousands of dollars in an individual case – multiplied by tens of thousands of arbitrations. The manner in which FIA and COLUMBIA obtain these inflated awards is described below.

59. Upon information and belief, FIA routinely seeks attorneys' fees of approximately 15% or more of the amount of the consumer's alleged debt. But Code of Civil Procedure section 1284.3 makes it unlawful for an arbitration company like NAF to administer an arbitration that shifts fees and costs to the consumer when the consumer loses. Thus, it is an unfair business practice for FIA to seek such fees, and an unlawful business practice for FIA to aid and abet NAF's violation of 1284.3 by seeking such fees.

60. Moreover, even if section 1284.3 did not prohibit the shifting of attorneys' fees to consumers who lose in NAF arbitrations, FIA's practice of seeking attorneys' fees of approximately 15% of the consumer's alleged debt would nonetheless be an unfair and unlawful business practice because the amount of such fees is often or always objectively unreasonable for the work that FIA's attorneys perform in NAF arbitrations. Such fees are vastly higher than what a reasonable attorney would charge to provide the minimal services required to represent FIA in an arbitration before NAF. These services frequently consist solely of submitting electronically a few pages of boilerplate claim information using an electronic form supplied by NAF. For

such trivial activity, FIA requests and obtains thousands to tens of thousands of dollars in attorneys' fees. For FIA to seek these unreasonable attorneys' fees from consumers, particularly in such a biased forum, is an unfair business practice and is unlawful under the Rosenthal Act and other California laws.

61. For FIA to seek even reasonable attorneys' fees before NAF would in many cases be an unfair and unlawful business practice for an additional reason. Upon information and belief, FIA uses out-of-state attorneys who are not licensed to practice in California to represent it before NAF. These practitioners do not comply with procedures for seeking permission to practice before an arbitrator in California, and therefore they are not entitled to any fees at all for their unlicensed work. For FIA to seek to recover these practitioners' fees from consumers is unfair and unlawful under, *inter alia*, Code of Civil Procedure section 1282.4(b).

62. Upon information and belief, FIA also seeks to recover its arbitration fees from consumers in NAF proceedings. But in California, businesses that prevail in arbitrations against consumers are not permitted to recover their arbitration fees pursuant to Code of Civil Procedure section 1284.3. FIA's practice of seeking and obtaining these fees before NAF is an unfair business practice and is unlawful under the Rosenthal Act and the California Arbitration Act.

63. Upon information and belief, FIA also seeks to recover stale debts from consumers that are outside of the statute of limitations period. FIA is not entitled to recover these funds, and seeking an award of such funds before NAF is an unfair business practice and is unlawful under the Rosenthal Act.

64. FIA's practice of obtaining awards to which it is not entitled is possible in part because it brings these claims in the biased NAF forum – but it is also possible in part because FIA submits defective affidavits to its NAF arbitrators. For example, upon information and belief, FIA's affidavits in support of its claims routinely aver not that the affiant swears to the truth of the claim – but rather that the affiant is an attorney or other agent who swears that the claim contains an accurate account of what his or her client has told him or her. Even under NAF's lax rules of evidence and procedure, such an affidavit is inadequate. Nonetheless FIA

routinely submits such affidavits in support of its claims, and NAF arbitrators routinely make awards based on them. These practices are unfair.

65. COLUMBIA also seeks and obtains grossly inflated arbitration awards. These awards include COLUMBIA's attorneys' fees. But Code of Civil Procedure section 1284.3 makes it unlawful for an arbitration company like NAF to administer an arbitration that shifts fees and costs to the consumer when the consumer loses. Thus, it is an unfair business practice for COLUMBIA to seek such fees, and an unlawful business practice for COLUMBIA to aid and abet NAF's violation of 1284.3 by seeking such fees.

66. Moreover, even if it were not per se unfair and unlawful for COLUMBIA to seek and obtain attorneys' fees in NAF arbitrations, COLUMBIA's conduct would nonetheless violate section 17200. This is because, upon information and belief, COLUMBIA routinely submits claims to NAF that include its estimated attorneys' fees – in some cases amounting to tens of thousands of dollars. Yet COLUMBIA does not submit documentation to prove that these estimated attorneys' fees were actually incurred, and NAF's arbitrators do not require such documentation. These estimated attorneys' fees are particularly outrageous where the consumer does not appear before the arbitrator or contest the claim (such as in cases where COLUMBIA has used an outdated address for service of the claim) – in such cases, no further work beyond preparing a claim is required. Moreover, upon information and belief, COLUMBIA does not even use the services of an attorney to prepare its claims. This is precisely what happened to Elizabeth Marcotte: COLUMBIA submitted a claim to NAF that consisted of computer-generated boilerplate that was not signed by an attorney and bore no indication of being prepared under an attorney's supervision. COLUMBIA served Ms. Marcotte with the claim at an outdated address, and Ms. Marcotte did not receive the claim in time to contest it. Nonetheless COLUMBIA sought "estimated" attorneys' fees of $10,631.62, and NAF awarded every penny of that estimate, without requiring COLUMBIA to submit documentation that the estimated fees were actually incurred. These practices are unfair and are unlawful under the Rosenthal Act.

67. Upon information and belief, COLUMBIA also seeks to recover its arbitration fees from consumers in its NAF claims. But COLUMBIA is not entitled to shift this fee to

consumers under Code of Civil Procedure section 1284.3. COLUMBIA's practice of seeking and obtaining these fees before NAF is an unfair business practice and is unlawful under the Rosenthal Act and the California Arbitration Act.

68. The grossly inflated arbitration awards that COLUMBIA obtains are possible in part because of NAF's biased and cursory review of these claims. But they are also possible because COLUMBIA submits defective affidavits and paltry supporting evidence to bolster these claims. Although arbitration is a streamlined proceeding that does not require compliance with the Evidence Code, COLUMBIA's practice of submitting affidavits that do not competently attest to the facts they purport to prove, or even establish the basic fact of the arbitrability of the dispute in question, and its practice of submitting documentary evidence that does not support its claims, is an unfair business practice that does not allow consumers to vindicate their rights under the Rosenthal Act. Similarly, NAF's practice of accepting such "evidence" is also an unfair business practice.

69. In addition to acting unfairly and unlawfully in the course of submitting its claims to NAF, defendant FIA commits unfair and unlawful business practices in the course of seeking confirmation of arbitration awards before superior courts in California. When consumers contest these confirmations, FIA's attorneys routinely post sensitive and private consumer information in public court documents. For example, in the case of Jane Roe, discussed in paragraph 4 above, FIA's attorneys placed into the public record her social security number, mother's maiden name, and credit history. Such abuses have occurred in dozens of other confirmation cases. FIA's practice of publicizing private consumer information in contested award confirmation cases – with no other apparent purpose but to intimidate or harass consumers who resist confirmation of NAF awards – is an unfair business practice and is unlawful under numerous California laws, including Article I, section 1 of the California Constitution; Civil Code sections 1798.81.5 and 1798.85; and California Rule of Court 1.20(b)(2). It is also an unfair business practice because FIA's privacy policies promise consumers that their personal information will be protected, but FIA does not keep this promise.

70. Finally, FIA's cardmember agreements with consumers, which force consumers to bring any affirmative claims against FIA in an arbitral forum, are contracts of adhesion that disallow class actions. Under established California law, requiring consumers to consent to this provision as a condition of obtaining credit is in the context of FIA's cardmember agreements an unfair business practice.

CAUSES OF ACTION:

FIRST CAUSE OF ACTION FOR VIOLATION OF BUSINESS AND PROFESSIONS CODE SECTION 17200 AGAINST NAF

71. The PEOPLE incorporate by reference paragraphs 1 through 70 inclusive.

72. California Business and Professions Code section 17200 prohibits any "unlawful, unfair or fraudulent business act or practices." NAF has engaged in unlawful, unfair and deceptive business acts and practices in violation of section 17200. Such acts and practices include but are not limited to the following:

a. NAF has violated the California Arbitration Act, Code of Civil Procedure sections 1280 *et seq.*; the Rosenthal Act, Civil Code sections 1788 *et seq.*; Business and Professions Code section 17500; and the Judicial Council's Ethics Standards for Neutral Arbitrators, or aided and abetted violations of the California Arbitration Act, the Rosenthal Act, and the Ethics Standards for Neutral Arbitrators, by the acts and practices set forth in this Complaint;

b. NAF's arbitration administration practices constitute unfair business practices because they offend established public policy, and because the harm they cause to consumers in California greatly outweighs any benefits associated with those practices; and

c. NAF has engaged in misleading and unfair advertising.

SECOND CAUSE OF ACTION FOR VIOLATION OF BUSINESS AND PROFESSIONS CODE SECTION 17200 AGAINST FIA

73. The PEOPLE incorporate by reference paragraphs 1 through 72 inclusive.

74. California Business and Professions Code section 17200 prohibits any "unlawful, unfair or fraudulent business act or practices." FIA has engaged in unlawful, unfair and

deceptive business acts and practices in violation of section 17200. Such acts and practices include but are not limited to the following:

a. FIA has violated the California Constitution, the California Arbitration Act, the Rosenthal Act, Civil Code sections 1798.81.5 and 1798.85, and California Rule of Court 1.20(b)(2); and/or has aided and abetted violations of the California Constitution, the California Arbitration Act, the Judicial Council's Ethics Standards for Neutral Arbitrators, the Rosenthal Act, Civil Code sections 1798.81.5 and 1798.85, and California Rule of Court 1.20(b)(2) by the acts and practices set forth in this Complaint; and

b. FIA's practices in connection with NAF arbitrations constitute unfair business practices because they offend established public policy, and because the harm they cause to consumers in California greatly outweighs any benefits associated with those practices.

THIRD CAUSE OF ACTION FOR VIOLATION OF BUSINESS AND PROFESSIONS CODE SECTION 17200 AGAINST COLUMBIA

75. The PEOPLE incorporate by reference paragraphs 1 through 74 inclusive.

76. California Business and Professions Code section 17200 prohibits any "unlawful, unfair or fraudulent business act or practices." COLUMBIA has engaged in unlawful, unfair and deceptive business acts and practices in violation of section 17200. Such acts and practices include but are not limited to the following:

a. COLUMBIA has violated the California Arbitration Act and the Rosenthal Act; and/or has aided and abetted violations of the California Arbitration Act, the Judicial Council's Ethics Standards for Neutral Arbitrators, and the Rosenthal Act, by the acts and practices set forth in this Complaint; and

b. COLUMBIA's practices in connection with NAF arbitrations constitute unfair business practices because they offend established public policy, and because the harm they cause to consumers in California greatly outweighs any benefits associated with those practices.

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PRAYER FOR RELIEF

The PEOPLE pray for judgment against DEFENDANTS as follows:

1. Preliminary and permanent injunctive relief by which the Court prohibits the DEFENDANTS from performing or proposing to perform or aiding and abetting any acts of unfair competition or deceptive advertising in California, and by which the Court requires DEFENDANTS to conform their business practices to California law and policy;

2. An order that DEFENDANTS pay $2,500.00 in civil penalties for each violation of Business and Professions Code section 17200, including but not limited to violations occurring in each arbitration conducted by NAF;

3. Costs of suit; and

4. For such further and additional relief as the Court deems proper.

Dated: March 24, 2008

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