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Re: Revised Debt Collection Regulations

Dear Ms. Thompson and Mr. Monahan,

The American Financial Services Association ("AFSA") has significant concerns regarding the recently revised debt collection rules, Mass. Regs. Code tit. 940, §§ 7.00 *et seq*. ("Rules") generally, and Section 7.08 specifically. AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members are important sources of credit to the American consumer, providing approximately 20 percent of all consumer credit. AFSA member companies offer vehicle financing, payment cards, personal installment loans and mortgage loans. The Association encourages and maintains ethical business practices and supports financial education for consumers of all ages. Thus, AFSA represents a wide variety of creditors[1] whose input may neither have been sought nor received in the course of developing the Rules but who are directly and quite adversely impacted by the final Rules. Most AFSA members originate their own accounts or acquire accounts shortly after origination (and before any possible default) and thus do not operate like debt buyers or third party debt collectors, who appear to have been the original focus of the revisions in the Rules. When creditors collect "debts," they usually collect delinquent installments from consumers with whom they have a longer-term, ongoing and continuous relationship and who (absent acceleration) carry other (current) balances with the creditor. When debt buyers or third party debt collectors collect "debts," they usually collect only mature, static balances from consumers with whom they have no prior or ongoing relationship. Unlike creditors, debt buyers and third party debt collectors may operate with very limited information regarding the consumer or the account involved. Also, unlike creditors, debt buyers and third party debt collectors are likely to collect much older charged-off or time-barred debts.

[1] The term "creditor" as used in this letter means entities who either originate their own obligations or who take assignment of current obligations (generally shortly after origination). These entities service and collect their own debts and those of affiliated entities, and the collection of debt is not their principal business.

Serious Concerns Regarding Costs and the Impact on Future Credit

AFSA members understand that the Rules were promulgated after your Office held a public hearing and received comments from the Boston Bar Association, the Association of Credit and Collection Professionals, consumer advocates, the Office of Consumer Affairs and Business Regulation, and others, reportedly including DBA International (the debt buyers association) and the American Collectors Association, but there is no indication that your Office sought out or received input on the Rules as finally revised from creditors. Ironically, the Rules are much more onerous for creditors than for debt buyers and third party debt collectors because of the multiple times creditors would have to validate the debt.

AFSA members are greatly concerned that the Rules generally, and the new and unprecedented requirements of Section 7.08 specifically, have inadvertently created unforeseen and very difficult compliance and credit risk issues for creditors who hold and collect their own accounts. These compliance and credit risk issues are likely to lead to serious disruptions in the extension of consumer credit and increase costs for consumers. AFSA members believe that the Statements of Fiscal Effect and Small Business Impact grossly understate the expected compliance costs for creditors. Far from being "more consistent with existing state and federal laws," the Rules establish new burdens on creditors that have not previously been imposed by any other state or federal law.

Purpose of Revisions

As stated in your Office's press release on March 1, 2012, the purported purpose of the revisions was to provide guidance and make Massachusetts' laws "more consistent with existing state and federal laws." However, no federal law, and to our knowledge no statewide law, currently require creditors who collect accounts that they own or originate to validate debts with established customers. Creditors, with narrow exception (*e.g.*, creditors collecting in a name other than their own that suggests the involvement of a third party), are not required to provide validation of debt notices that are required of debt collectors and debt buyers under federal and other states' laws. As Congress recognized in establishing the federal Fair Debt Collection Practices Act ("FDCPA"), creditors "generally are restrained by the desire to protect their good will when collecting past due accounts," which means are distinguishable from independent collectors who are "likely to have no future contact with the consumer and often are unconcerned with the consumer's opinion of them."[2] The previously applicable inspection requirement adequately addressed consumer needs for information without imposing undue burdens on creditors. Validation notices do not make rational sense in ongoing credit relationships, particularly those involving both current and past due balances.

If, for example, a consumer obtains a motor vehicle installment loan from a bank (or enters into a motor vehicle retail installment sales contract with a dealer who immediately assigns the contract to a sales finance company) and makes payments for a period of time to the same creditor, it would not appear to serve any useful consumer purpose for a creditor to (i) incur the

[2] *See, e.g.*, S. Rep. No. 382, 95th Cong., 1st Sess. 2, *reprinted in* [1977] U.S.C.C.A.N. 1695.

additional cost to send a notice informing the consumer of a right to validate the debt before proceeding to collect an individual delinquent installment; nor (ii) suspend repossession efforts and risk the loss of collateral pending a consumer's request to validate the debt; nor (iii) suspend collection efforts until documents that were previously provided to the consumer as required by law in the ordinary course of the relationship are re-provided upon request. In the context of a creditor collecting an account it originated or obtained immediately after origination, validation serves no rational purpose justifying the additional cost and risk in the credit or context.

Because creditors do not face similar validation requirements in any other state, they currently lack the existing infrastructure, policies and procedures to implement a Section 7.08 notice and will need to make significant investments of time and resources to create the necessary new processes to do so. Moreover, as there is no precedent for the requirement, there are many unanswered questions for creditors regarding implementation. The attendant delays in collection will increase risks and costs to creditors, which risks and costs will necessarily be passed on the consumers in the form of higher costs, delays and limited choice.

Evolution of Section 7.08: From Inspection to Validation

AFSA members do not understand the rationale for Section 7.08 as revised. The provision previously stated:

> 7.08: Inspection. It shall constitute an unfair or deceptive act or practice for a creditor to fail to allow a debtor or an attorney for a debtor to inspect and copy the following materials regarding a debt during normal business hours of the creditor and *upon notice* given to such creditor not less than five business days preceding the scheduled inspection:
>
> (1) All papers or copies of papers in the possession of the creditor, which bear the signature of the debtor and which concern the debt being collected;
>
> (2) A ledger, account card, or similar record in the possession of a creditor, which reflects the date and amount of payments, credits, and charges concerning the debt.

(Emphasis supplied.) The March 2011 proposal would have re-captioned and expanded the provision to read:

> 7.08: Validation of Debts. It shall constitute an unfair or deceptive act or practice for a creditor to fail to provide to a debtor or an attorney for a debtor within five business days of receipt of a *request* the following materials in the possession, custody, or control of the creditor regarding a debt:
>
> (1) All papers or copies of papers, including electronic records, which bear the signature of the debtor and which concern the debt being collected;
>
> (2) A ledger, account card, or similar record, whether paper or electronic, which reflects the date and amount of payments, credits, balances, and charges

concerning the debt, including but not limited to interest, fees, charges or expenses incidental to the principal obligation which the creditor is expressly authorized to collect by the agreement creating the debt or permitted to collect by law;

(3) The name and address of the original creditor, if different from the collecting creditor;

(4) A copy of any judgment against the debtor.

A creditor shall provide such documentation by first-class mail to the debtor if the debtor makes such a request.

(Emphasis supplied.) The final rule, however, completely changes the process and scope of disclosure:

7.08: Validation of Debts. (1) It shall constitute an unfair or deceptive act or practice for a creditor to fail to provide to a debtor or an attorney for a debtor the following *within five business days after the initial communication* with a debtor in connection with the collection of a *debt*, unless the following information is contained in the initial communication or the debtor has paid the debt:

(a) The amount of the debt;

(b) The name of the creditor to whom the debt is owed;

(c) A statement that unless the debtor, within 30 days after receipt of the notice, disputes the validity of the debt, or any portion thereof, the debt will be assumed to be valid by the creditor; and

(d) A statement that if the debtor notifies the creditor in writing within 30 days after receipt of this notice that the debt, or any portion thereof is disputed, the creditor will obtain verification of the debt and provide the debtor, or an attorney for the debtor, additional materials described in 940 CMR 7.08(2).

(2) If the debtor, or any attorney for the debtor, notifies the creditor in writing within the 30-day period described in 940 CMR 7.08(1), that the debt, or any portion thereof, is disputed, the creditor shall cease collection of the debt, or any disputed portion thereof, until the creditor *verifies the debt and provides* the debtor, or any attorney of the debtor, by first class mail, *the following materials*:

(a) All documents, including electronic records or images, which bear the signature of the debtor and which concern the debt being collected;

(b) A ledger, account card, account statement copy, or similar record, whether paper or electronic, which reflects the date and amount of payments, credits,

> balances, and charges concerning the debt, including but not limited to interest, fees, charges or expenses incidental to the principal obligation which the creditor is expressly authorized to collect by the agreement creating the debt or permitted to collect by law;
>
> (c) The name and address of the original creditor, if different from the collecting creditor; and
>
> (d) A copy of any judgment against the debtor.
>
> Pursuant to 940 CMR 7.08(2), the creditor must provide those materials described in 940 CMR 7.08(2)(a) through (d) which are in the possession, custody or control of the creditor. If the creditor does not possess, have custody of, or control the materials described in 940 CMR 7.08(2)(a) through (d), the creditor shall cease collection of the debt until the creditor has made reasonable efforts to obtain the necessary information and provide this information to the debtor.

(Emphasis supplied.) It is understandable that a broad range of records could and should be made available for "inspection" and copying at a creditor's place of business. However, depending upon how long a consumer has been the customer of a creditor, the number of documents for potential production may in fact be quite substantial and costly to produce and mail in hard copy.[3]

Moreover, the historical concept of "validation" is considerably narrower than "inspection." The federal FDCPA does not explain what a debt collector must do in order verify a debt in response to a consumer's dispute, but the United States Court of Appeals for the Fourth Circuit stated in *Chaudhry v. Gallerizzo*[4] that:

> [V]erification of a debt involves nothing more than the debt collector confirming in writing that the amount being demanded is what the creditor is claiming is owed; the debt collector is not required to keep detailed files of the alleged debt. Consistent with the legislative history, verification is only intended to "eliminate the . . . problem of debt collectors dunning the wrong person or attempting to collect debts which the consumer has already paid. There is no concomitant obligation to forward copies of bills or other detailed evidence of the debt.[5]

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[3] Open-end credit, for example, involves a continuing offer to extend credit that is accepted and contractually completed only as each purchase, cash advance or balance transfer is effected, which may entail a signed sales slip in face-to-face transactions, but increasingly may only be memorialized by electronic transactions effected by telephone or internet, that may not be readily accessible. Attempting to produce every document bearing the signature of the debtor with regard to the many individual transactions that make up a current open-end account balance and are reflected in whole or in part in a past due installment would create a tremendous burden. Also, if a consumer has agreed to receive documents electronically, we feel a creditor should be able to send this communication electronically. As written, the Regulations would seem to foreclose that option.

[4] 174 F.3d 394, 405-07 (4th Cir. 1999).

[5] *Id.* (citations omitted).

Neither "problem" addressed by verification (whether dunning the wrong person or attempting to collect debts which the consumer has already paid) is so common an occurrence in the context of creditors as to justify the considerable expense of notice and document production, but, understandably, can arise with some anticipated frequency with regard to traditional debt buyers and third party debt collectors. The *Chaudhry* court found that the debt collector adequately verified the debt by confirming the amount owed with the creditor and then sending a verification of the indebtedness to the debtors' attorney along with a computerized summary of the debtors' loan transactions, which included a running account of the debt amount, a description of every transaction and the date on which the transaction occurred.[6]

The Federal Trade Commission staff has been asked whether a debt collector for a medical provider could satisfy the validation requirement of the FDCPA by producing "an itemized statement of services rendered to a patient on its own computer from information provided by the medical institution."[7] The FTC staff responded that:

> Because one of the principal purposes of this Section is to help consumers who have been misidentified by the debt collector or who dispute the amount of the debt, it is important that the verification of the identity of the consumer and the amount of the debt be obtained directly from the creditor. Mere itemization of what the debt collector already has does not accomplish this purpose.[8]

When passed by the House of Representatives, the legislation creating the FDCPA contained language requiring that debt collectors obtain "certification of validity" of a disputed debt "from the creditor" and mail it to the consumer.[9] The House Report described adequate "certification" as "a statement which includes an itemization of the amount of the debt, and the name of the consumer, a statement that the debt has not been paid, and a statement that the creditor (to whom the debt was originally owed,) in consideration of the consumer's debt, had either delivered a merchantable product or properly rendered a service." However, in its final form, the legislation substituted the term "verification" for the previous term "certification" and deleted any reference to the debt collector obtaining this information directly from the creditor. The FTC staff has similarly indicated that detailed verification is sufficient but not necessarily required in order to verify a debt.[10]

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[6] *Id.* at 406. The *Chaudhry* decision has been followed by courts outside of the Fourth Circuit. *See, e.g., Anderson v. Frederick J. Hanna & Assocs.,* 361 F. Supp.2d 1379, 1383 (N.D. Ga. 2005); *Stonehart v. Rosenthal,* No. 01 Civ. 651(SAS), 2001 WL 910771, at *6-7 (S.D.N.Y Aug. 13, 2001); *Clark v. Capital Credit & Collection Servs., Inc.,* No. Civ. 03-340-JE, 2004 WL 1305326, at *9-10 (D. Or. Jan. 23, 2004). Case law from Indiana suggests that in order to verify a debt, a debt collector need only provide the debtor with an itemization of the disputed debt. *See Spears v. Brennan,* 745 N.E.2d 862, 878-79 (Ind. Ct. App. 2001); s*ee also, e.g., Mahon v. Credit Bureau of Placer County Inc.,* 171 F.3d 1197, 1203 (9th Cir. 1999); *Graziano v. Harrison,* 950 F.2d 107, 113 (3rd Cir. 1991); *Ducrest v. ALCO Collections, Inc.,* 931 F. Supp. 459, 461-62 (M.D. La. 1996).

[7] *See* FTC Informal Staff Letter from John F. LeFevre, Att'y, Div. of Cred. Practices, to Jeffrey S. Wollman (Mar. 10, 1993).

[8] *Id.*

[9] H.R. Rep. No. 131, 95th Cong. 1st Sess. 22 (1977).

[10] *See* FTC Informal Staff Letter from Roger J. Fitzpatrick, Att'y, Div. of Cred. Practices, to Betty M. Glover, Paralegal Assistant, Consumer Protection Section of the Office of the Alaska Att'y General (June 23, 1986) (indicating that the FDCPA does not require a debt collector to furnish detailed information regarding payments made

The documents to be provided under Section 7.08(2) far exceed "validation" as historically interpreted under state and federal laws and are not appropriate for the simple collection of a past due installment on a long-standing account with otherwise current balances.

If the validation requirement is retained, a number of issues arise in attempting to implement Section 7.08 in a creditor context, for which clarification is needed. The term "debt" is specifically defined in the Rules, but is also subject to alternative definition by agreement with the debtor. Whether the 30-day reference in the definition of "debt" is intended to establish a baseline concept of "default" in the absence of alternative agreement, such that a credit agreement defining "default" as "any failure to pay" would render an installment that is even one day past due a "debt" for Section 7.08 purposes, (requiring immediate notice) is unclear. While the information required to validate the debt is being gathered, the provision may require the cessation of normal account servicing documents, such as invoices. This could have the unintended consequence of confusing consumers. It is similarly unclear whether a creditor can simply reference the "additional materials described in 940 CMR 7.08(2)" or must actually list such materials in summary or detail in the notice. Clarification would also be appreciated with regard to providing copies of judgments. Although not explicit, it appears reasonable to limit the production of judgments to those concerning the debt, and not literally "any" judgment against the debtor in the public record.

Section 708 (1) supports the argument that the intention of the Rules was not to truly impact creditors who have been servicing and communicating with customers throughout the term of the finance transaction. The requirement that the creditor provide the debtor certain documentation within five business days after *initial* communication in connection with the collection of a debt implies that the customer did not have previous communications with the creditor. However, debtors in a financial transaction would have normally already been communicating with the creditor regarding the finance transaction throughout the term of the relationship or account. The applicability of the validation provisions to creditors is almost unworkable and as a creditor would mean providing a disclaimer at the time of origination that does not make sense.

Additional Concerns

In addition to the issues raised above with respect to the impact of Section 7.08, our members have also raised the following concerns:

Potentially inconsistent standards and unreasonable limitations on the ability to exercise enforceable security interests in property, set forth in Sections 7.07(18) and 7.07(19)

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and the balance due between interest and principal); FTC Informal Staff Letter from Alan D. Reffkin, Att'y, Div. of Cred. Practices, to Jan L. Kodner, Esq. (Mar. 7, 1979) (indicating that in order to verify a debt, the debt collector must furnish a statement showing the amount of the debt, the name and address of the creditor to whom the debt was originally owed [as it appeared in the original sales contract or bill of sale], and, where applicable, the name of the creditor to whom the debt is currently owed).

Section 7.07(18) provides that the following shall constitute an unfair or deceptive act or practice:

> (18) Taking or threatening to take any non-judicial action to effect dispossession or disablement of property if:
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> (a) there is no present right to possession of the property claimed as collateral through a court order or an enforceable security interest;
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> (b) there is no present intention to take possession of the property;
>
> (c) the creditor knows or has reason to know that demands for payment and/or legal notices were not directed to the debtor's current address; or
>
> (d) the property is exempt from seizure on execution because its value does not exceed the value for exemption set forth in M.G.L. c. 235, §34, or the property is otherwise exempt by law from such dispossession or disablement; this provision shall not apply to first mortgage foreclosures properly conducted in accordance with Massachusetts law.

Section 7.07(19) provides that the following shall constitute an unfair or deceptive act or practice:

> (19) Taking possession of or selling upon execution property that is exempt from seizure on execution because its value does not exceed the value for exemption set forth in M.G.L. c 235, §34, or the property is otherwise exempt by law from such dispossession or disablement; this provision shall not apply to first mortgage foreclosures properly conducted in accordance with Massachusetts law.

Both of these sections appear to impose significant limitations on the ability of creditors to exercise self-help remedies and repossession of collateral in which they hold a perfected security interest. The language could be interpreted to preclude self-help repossession of any collateral where its value does not exceed the value of property exempt from seizure on execution under Mass. Gen. Laws ch. 235, § 34, as well as limiting the ability to exercise self-help remedies with respect to any consumer that has failed to provide current address information to a creditor resulting in returned billing statement or other correspondence from the creditor.

We strongly urge clarification of these provisions to specify that they are not intended to limit the exercise of rights of secured creditors under Article 9 of the Uniform Commercial Code.

Mortgage Clarification

The prior version excluded first mortgages and loans in excess of $25,000 from the definition of "debt." By removing these exclusions, the regulation now encompasses all mortgage

debt, but does not appear to consider the foreclosure regulations issued by the Division of Banks.[11]

Section 7.08 (2) requires the lender to cease collection of the debt until the creditor verifies the debt. It is not clear how this provision would be implemented in juxtaposition with the Division of Banking regulations applicable to mortgage lenders that requires a 90 or 150 day notice to borrower (*i.e.,* would the notice period be "stayed" or would a new notice have to be sent, thus starting a new notice period.)[12]

Advancement in communication technologies

Some of the provisions in the Rules are outdated given the advancement of communication technologies and increased use of cell phones by consumers.

For example, the amended Section 7.04 (1)(f) of the Rules, limiting the times a creditor can "*initiate"* a communication with the debtor (via telephone, either in person or via text messaging or recorded audio message) is vague. It is not clear whether "initiating" means making an actual connection with the customer or whether and "attempt" at reaching the customer by phone and not an actual completed call would be sufficient to trigger the Rules' limitations.

Though no modification was made to section 7.04 1(h), which prohibits making telephone calls to the debtor's place of employment if the debtor elected to make such restriction, this section needs clarification because it would be extremely difficult for a creditor trying to reach a customer by cell phone to determine whether the debtor is at work or someplace else.

Likewise, though no substantial modification was made to section 7.05 (contact with persons residing in the household of a debtor), it is important to note that a creditor's ability to communicate with its customer regarding a delinquent account is extremely limited under current provisions. These restrictions, which limit communications initiated by creditors to two communications over any seven-day period at the consumer's personal phone number, and two communications over any 30-day period at any other number, go far beyond any limitations provided under the federal FDCPA, as well as under most other state and local fair debt collection laws and regulations. Moreover, such severe restrictions may have the unintended consequence of limiting the ability of creditors in mortgage transactions that were previously exempt from the scope of the regulations to contact delinquent borrowers about home preservation options or other loss mitigation/workout treatments that benefit the borrower and their dependents. At the very least, the contact restrictions should be limited to actual contacts with the borrower during which the debt is discussed, "as opposed to a communication with any debtor via telephone, either in person or text messaging or recorded audio message..." Limiting the scope of the contact restrictions to actual in-person conversations with the debtor will accomplish the consumer protection goals of the Regulations, without limiting the creditor's ability to explore every possible loss mitigation treatment that the debtor may qualify for.

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[11] *See* 209 CMR 56.4: Right to Cure Notice, effective March 2, 2012.
[12] *Id.*

Recommendations

AFSA members recommend a full reconsideration of the Rules in light of the important distinctions between creditors on the one hand and debt buyers (whether active or passive) and debt collectors on the other. For example, AFSA members would recommend, with regard to revised Section 7.08, (i) restoring the original definition of "creditor"; (ii) creating a new definition for "debt buyers" and "third party debt collectors"; (iii) restoring previous Section 7.08 as a provision for supplying documents *upon request*; (iv) renumbering revised Section 7.08 (as a new section or new subsection), narrowing the validation provisions to require validation only of debt buyers and third party debt collectors, and clarifying which other sections apply only to debt buyers and third party debt collectors; (v) clarifying that 7.07(18) and 7.07(19) in no way limit the exercise of rights by secured creditors under Article 9 of the Uniform Commercial Code; and (vi) changing section 7.08 to reflect that additional obligations should attach only when the purchaser obtains past due debt, not when an account becomes delinquent with a creditor. Care should be taken in defining "debt buyers" and "third party debt collectors" not to include creditors with established customer relationships and current balances, including buyers of portfolios of predominantly current accounts and creditors who securitize or sell accounts but retain servicing.

Conclusion

We have serious concerns about the effects of the Rules on the consumer credit industry. We look forward to working with you and your staff to resolve the concerns expressed in this letter, as well as well as other AFSA member concerns regarding the revised debt collection regulations. Please contact me by phone (952-922-6500) or e-mail (dfagre@afsamail.org) at your soonest convenience so that we can discuss these issues. Thank you for your time and consideration.

Sincerely,

Danielle Fagre Arlowe
Senior Vice President
American Financial Services Association