January 15, 2024

Department of Financial Protection and Innovation
Legal Division
Attn: DeEtte Phelps, Regulations Coordinator
2101 Arena Blvd.
Sacramento, CA 95834

Re: PRO 05-21 — Proposed Regulations Under the Debt Collection Licensing Act

Dear Ms. Phelps:

On behalf of the American Financial Services Association ("AFSA") and California Financial Services Association ("CFSA"), [1] thank you for the opportunity to provide comments on the Department's November 8 second draft text for the Proposed Scope Rulemaking Under the Debt Collection Licensing Act (PRO 05-21). AFSA and CFSA represent financial institutions of all sizes across many of the industries DFPI oversees, including institutions that may be required to apply for licensure under the Debt Collection Licensing Act (DCLA) and institutions that hold other license types from DFPI. We believe clear rules benefit consumers and financial institutions alike. We appreciate the Department's consideration of our previous comments related to the DCLA and changes made in response to some of those comments. We also appreciate the steps DFPI has taken to clarify definitions and narrow the scope of the rules throughout this process.

§ 1850. Definitions.

(i) "Employee"

We appreciate DFPI exempting employees from the licensing requirements in Section 1850.1(a), similar to the federal Fair Debt Collection Practices Act's (FDCPA) exemption for employees. However, we believe additional clarification is necessary to protect the ability of debt collectors to utilize the services of non-W2 workers, including 1099 workers, temporary help from a staffing agency, or a collection agency employee who works for a creditor to collect in the creditor's name at the creditor's office under the creditor's supervision. Including these additional workers would be consistent with how the FDCPA has historically been applied (e.g., considering workers collecting in the name of an original creditor to be "de facto" employees of

[1] Founded in 1916, the American Financial Services Association (AFSA), based in Washington, D.C., is the primary trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including direct and indirect vehicle financing, traditional installment loans, mortgages, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans.

such creditor). Accordingly, we respectfully reiterate our previous request that the proposed definition be updated. [2]

We also appreciate DFPI exempting employees of subsidiaries and parent companies working for a licensed debt collector on a temporary basis. For internal consistency across provisions in the rule, and to avoid unprincipled distinctions, DFPI should clarify two points: (1) that the exemption of § 1850.1(a) applies to employees of parent entities, subsidiaries, or affiliates; (2) that the exemption of § 1850.1(b) applies to employees of parent entities, subsidiaries, or affiliates working for an exempt entity on a temporary basis. In more complex organizations, corporate shared services such as temporary staffing may be provided by an affiliate that is not a direct parent or subsidiary. There is no principled reason to draw a distinction among entities that are under common ownership and control. Furthermore, if temporary employees assigned by an affiliate to a licensed debt collector are exempt, then there is no reason not to give the same benefit to temporary employees assigned by an affiliate to an exempt bank or exempt licensed lender.

(j) "Engage in the business of debt collection"

We also reiterate our previous request that the DFPI clarify that any debt collection performed by creditors in connection with existing customer obligations is not for the profit and gain from engaging in debt collection. Creditors already have a mutually beneficial contract with the consumer for the profit they intend to make. Requesting their customer to continue to follow the contract and pay by collecting on that contract is not engaging in debt collection for profit and should not be treated as such. When the debt is in default, creditors risk losing their profit, and consumers risk losing their benefits under their contracts. This is a crucial difference between third-party debt collectors and creditors. Third-party debt collectors are performing the collection function for profit and gain solely based on their efforts to collect, whereas the creditor is just attempting to service an existing contract with no extra profit and gain beyond the existing obligation. Accordingly, we recommend the following revision to §1850 (j) to focus the definition on entities whose businesses are solely debt collection from consumers rather than creditors collecting on existing obligations:

> (j) "Engage in the business of debt collection": A person engages in the business of debt collection and is required to be licensed pursuant to section 100001, subdivision (a) of the Financial Code if the person (A) engages in debt collection for a profit or gain that is earned solely from the act of collecting past due amounts, when the person began collecting when the credit obligation was in default, and (B) the activity is of a regular, frequent, or continuous nature. Advertising or otherwise offering the service of debt collection for remuneration constitutes engaging in the business of debt collection.

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[2] [2] See our prior August 29, 2022 comment letter, available at https://dfpi.ca.gov/wp-content/uploads/sites/337/2022/10/PRO-05-21-American-and-California-Financial-Services-Association-8.29.22_Redacted.pdf.

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§ 1850.1 Scope of Licensing requirement.

Subsidiaries and Affiliates

We again urge the DFPI to reconsider Section 1850.1(b), which given the extensive requirements under state and federal law with which existing licensees and other federally chartered financial institutions already comply, additional requirements under the DCLA would be duplicative, with limited consumer benefit and will only serve to distract the DFPI from the main target of the law and licensing requirements— California debt collectors with no existing state or federal oversight. As such, we respectfully request the DFPI revise the last sentence proposed in Section 1850.1(b) to the following:

> The exemption also applies to parent entities, subsidiaries, and affiliates (and their employees) seeking repayment of consumer debt in the name of the listed entity so long as the principal business of the parent, subsidiary or affiliate is not the collection of debt.

This revision would be consistent with the FDCPA.

A bank's structure should not be the factor that ultimately determines whether its activities subject it to state debt collector licensing. Under the rule as written, a bank insured by the Federal Deposit Insurance Corporation (FDIC) does not need to be licensed as a debt collector. But, if the bank has certain servicing activities performed by an affiliate or subsidiary, it must be licensed as a debt collector, even though these affiliates and subsidiaries are also regulated by the FDIC, Office of the Comptroller of the Currency (OCC), Consumer Financial Protection Bureau (CFPB), and others, just like the parent bank, and are subject to federal examinations and oversight. DFPI oversight would be duplicative.

The OCC, for example, supervises and examines national banks by conducting on-site reviews, providing ongoing supervision of the bank's operations, and regularly meets with bank management and the board of directors. [3] The OCC also takes enforcement action against banks that engage in risky practices or do not comply with their rules and regulations.

Unlike other debt collectors, national banks have examiners that are assigned and solely dedicated to the examination of their operations, and even may reside on site in pre-pandemic environments. A credentialed national bank examiner has the following responsibilities:

- maintains an up-to-date understanding of the condition and risk profile of the bank;
- identifies risks and responds in an appropriate and timely manner;
- considers the risks posed by significant activities or affiliates, including affiliates or lines of business subject to the primary supervision of another regulator, in determining the bank's ratings and risk assessment;

[3] Comptroller's Handbook Examination Process, Bank Supervision Process, Version 1.0, June 2018 https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/bank-supervision-process/pub-ch-bank-supervision-process.pdf

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- maintains responsibility for ongoing supervision of the bank and oversees the execution of examination plans;
- updates the OCC's supervisory information systems to reflect the bank's current risk profile and condition;
- maintains ongoing and effective communication with bank management and the board;
- keeps the supervisory office informed about the status of each assigned bank;
- establishes and maintains points of contact with domestic and foreign banking supervisors and other regulatory agencies, as appropriate;
- implements OCC and supervisory office directives;
- takes actions to require banks to address deficiencies, or recommends such actions to the supervisory office; and
- follows up on bank management's actions to address deficiencies and outstanding enforcement actions.

DFPI's proposed rule would also require the sharing of significant personal information of licensee principal officers and others, including their social security numbers and fingerprints. National banks already follow an in-depth application process to be chartered as an OCC-supervised bank, that includes character requirements as well as comprehensive background checks of the bank's organizers, senior executive officers, senior officers, directors, principal bank shareholders, and general managers of federal branches or agencies. [4] In this application, the OCC must consider experience, competence, and integrity, and may also consider a person's character, financial ability, or willingness to direct or lead a bank's business in a safe, sound, and legal manner. The OCC also closely examines the backgrounds of filers whose previous experience contributed to a failed or "troubled" financial institution or when other facts may raise questions about competence, character, or personal or fiduciary integrity. These background checks include information from:

- Credit Bureaus;
- Federal Bureau of Investigation;
- Federal and state regulators of banks and other entities;
- IRS;
- Publicly available online resources, including the "Interagency Biographical and Financial Report";
- FinCEN; and
- Enforcement Action Report System, an OCC database of historical criminal referral information.

The OCC may also perform additional background checks when deemed appropriate, including making a request for background information from:

- U.S. Commodity Futures Trading Commission;
- State and local law enforcement agencies;

[4] Comptroller's Licensing Manual: Background Investigations, https://www.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/background-investigations-licensing-manual.pdf

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- Federal Trade Commission;
- Local courts;
- National Association of Securities Dealers; and
- U.S. Securities and Exchange Commission.

Most investigations also include fingerprint checks and "IRS Tax Check Waiver" forms. Indeed, changes in directors and senior officers of a national bank or federal savings association require notice that includes fingerprinting of any individual that hasn't been fingerprinted within the prior three years. [5] For all these reasons, we respectfully urge DFPI to reconsider Section 1850.1(b), and instead apply the depository institution exemption referenced in Section 10001(b)(1) of the DCLA to subsidiaries and affiliates of depository institutions.

In addition, we recommend a "common or affiliated corporate ownership" exemption for non-depository institutions similar to that of the Fair Debt Collection Practices Act (FDCPA).

Original Creditors

We applaud the DFPI refining its licensing requirement to more closely follow the federal FDCPA by recognizing that creditors are not engaged in the business of debt collection simply to recover a profit by collecting debts. We also appreciate the changes made to the definition of original creditor to more broadly cover finance companies that provided the financing to the customer through the seller of the goods or services (e.g. a retail installment sales contract financing the purchase of a vehicle) and not lenders that directly contracted with the customer. We would like to request an additional revision (underlined below), also consistent with the FDCPA [6], to clarify that "original creditors" includes assignees of consumer credit transactions:

> Original creditors: A creditor, including a provider of non-financial services, seeking, in its own name, repayment of consumer debt arising from a consumer credit transaction between itself, in its own name, and a customer <u>(including assignees of consumer credit transactions so long as the assignment was not solely for the purpose of facilitating collection of a debt in default)</u>, is not engaged in the business of debt collection, for purposes of licensure under the Debt Collection Licensing Act, unless it meets one or more of the following criteria…

We also appreciate the DFPI accepting our previous recommendation for edits to parts (c)(1)-(3) by changing the "within the last 12 months" language of each part to reflect the previous calendar year. This change to the timing requirement ensures a clearer scope for the licensing requirement. We also appreciate the clarity that parts (c)(1)-(3) are limited to California consumer accounts. However, we request additional clarity for part (c)(2). What does

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[5] 12 CFR § 5.51

[6] The FDCPA defines "creditor" as: "any person who offers or extends credit creating a debt or to whom a debt is owed, but such term does not include any person to the extent that he receives an assignment or transfer of a debt in default solely for the purpose of facilitating collection of such debt for another." 15 U.S. Code § 1692a (4).

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"inventory" mean? Is this referring to the creditor's portfolio of debt? If so, is it limited to the portfolio of debt secured by a motor vehicle?

Servicers

We support the DFPI's inclusion of a servicer exception, recognizing that servicers are the creditors under many contracts and often the only creditor with whom a consumer has a direct relationship. Consumer obligations being managed by servicers is very common in financial markets, and a clear exception would be consistent with the federal FDCPA. In most cases, a servicer either obtains an account immediately after it is originated and works with the consumer throughout the contract, or, the servicer was the original creditor who has securitized the obligation but retained the servicing rights to be performed in the servicer's name. The account is not in default when acquired and the servicer will only need to exercise remedies available under the contract if the consumer does not pay. As with creditors, the servicers are not in the business to make a profit on debt collection. They manage the contract through completion, including communicating with the consumer to address any concerns and helping the consumer to stay current so the consumer can comply with the contract.

We appreciate the DFPI's attempts to further clarify the exception for servicers in this draft, but we recommend that the DFPI adopt a requirement more similar to the FDCPA definition of the servicer exception: if the servicer was the original creditor who securitized the obligation but retained servicing obligations [7] or if the servicer receives the account before it is in default, the servicer is not considered a debt collector. There is no policy rationale for limiting the exemption to only servicers working on behalf of original creditors; the rule leaves an unintended donut hole for servicers working on behalf of securitizations and other secondary market purchasers who purchase performing loans for investment rather than collection. There is also no policy rationale for drawing an additional line when that account later becomes 90 days past or even charged-off. If a servicer was exempt at the time the account was placed, the exemption should continue through the servicer's attempts to avoid default and to provide workout options for newly charged-off accounts. We propose the following edits:

> (d) A person solely servicing debts on behalf of an original creditor, as described in subdivision (c), that are less than 90 days past due and have not been charged off, is not engaged in the business of debt collection for purposes of licensure under the Debt Collection Licensing Act <u>if the debt was not in default at the time it was obtained from the creditor and the person's principal purpose is not the business of debt collection</u>. For purposes of this section, "default" means when at least one payment has not been fully paid within 90 days of the date that the payment was originally scheduled to be paid on the debt.

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[7] Limiting the servicer exemption to servicing debts "on behalf of" the original creditor would not exempt original creditors who securitize debts but retain servicing obligations because such entities would not be servicing the debt "on behalf of an original creditor". Similar, original creditors who securitize debts but retain servicing obligations should not be required to send 15 U.S.C. 1692g "validation" letters if account goes into default as such process would be inherently confusing to consumers who only had debt with the original creditor/servicer from the inception of an account.

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Attorneys or Law Firms

We applaud the proposed amendments to Section 1850.1 related to attorneys and law firms representing a creditor. We appreciate DFPI accepting our suggested change and clarifying in Section 1850.1(j)(1)(A) that an attorney or law firm representing a creditor in an action initiated by a debtor plaintiff is not engaged in the business of debt collection. We seek clarification of our understanding on two issues. First, as we understand the proposed amendment, attorneys engaged in defending actions initiated by consumers would not be required to obtain a license, whether the attorney is defending an action initiated by a consumer even if the attorney initiates a permissive or compulsory counterclaim on the debt in such consumer-initiated litigation. Second, we interpret the term "action" broadly, to include arbitrations or pre-litigation demands made upon attorneys' clients in anticipation of litigation by the consumer.

§ 1850.2 Consumer credit transactions.

We respectfully request that DFPI add consumer vehicle leases to the exclusions under Section 1850.2(a) of types of debt that are not "consumer debt" within the meaning of section 100002, subdivision (f) of the Financial Code. The DFPI's jurisdiction is limited to regulation of "consumer credit transactions." (Fin. Code section 100002(e)). California Courts of Appeal have held that a consumer vehicle lease is not a "consumer credit contract." *LaChapelle v. Toyota Motor Credit Corp.,* 102 Cal. App. 4th 977, 987 (2002) ("The lease agreement therefore does meet the definition of a consumer credit contract, and that the FTC Holder Rule, therefore, does not apply to it."); *Bescos v. Bank of Am.,* 105 Cal. App. 4th 378, 393 (2003) ("Furthermore, the lease agreement does not qualify as a "consumer credit contract."). For the same reason that the DFPI's proposed regulation concludes, as do a host of decisions, that residential rent is not a "consumer credit transaction" and that the Courts of Appeal have concluded that vehicle leases are not "consumer credit transactions," the DFPI should add consumer vehicle leases to the types of debt that do not constitute "consumer credit transactions" (i.e. consumer debt") within the meaning of Fin. Code section 10000(e)-(f) and section 1850.2 of the proposed regulations.

§1850.71 Document Retention.

We applaud the DFPI for accepting our recommendation and limiting the seven-year retention requirement in part 1850.71(d) to three years instead. Similarly, we also recommend that the DFPI adopt a three-year limit for the records required to be maintained in 1850.71(a). As drafted, the records required in part (a) would be held, seemingly, in perpetuity and create a significant compliance burden for licensees, particularly regarding the call recordings in (a)(5). This change would be consistent with the changes to part (d) and with existing California Financing Law, which only requires records be retained "for at least three years after making the final entry on any loan recorded therein." See Cal. Fin. Code 22157.

Thank you in advance for your consideration of our comments. If you have any questions or would like to discuss this further, please do not hesitate to contact us.

Sincerely,

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