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SHINING A LIGHT ON THE CONSUMER DEBT INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON
FINANCIAL INSTITUTIONS AND CONSUMER PROTECTION

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

SHINING A LIGHT ON THE CONSUMER DEBT INDUSTRY

JULY 17, 2013

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SHINING A LIGHT ON THE CONSUMER DEBT INDUSTRY

WEDNESDAY, JULY 17, 2013

U.S. SENATE,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER PROTECTION,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee met at 10:13 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Sherrod Brown, Chairman of the Subcommittee, presiding.

OPENING STATEMENT OF CHAIRMAN SHERROD BROWN

Chairman BROWN. The Subcommittee will come to order. Thank you to the witnesses for joining us. Thanks for those in the audience who are here in this very warm room today, which I guess is the first Banking hearing since the new Consumer Bureau Director has been confirmed. That is good news in terms of moving forward, good news in terms of setting a precedent in this agency, and good news in expanding the authority that this Committee and this Senate and Federal law gives the Consumer Bureau in terms of the more expansive powers that we vested in him, once confirmed, so that is good news all around.

Senator Toomey is going to try to join us. I apologize for the delay. We had a vote at 10 o'clock, so I had to go vote first. I will make a brief statement. Then we want to hear from the witnesses, and then we will begin the questions.

Two years ago, we learned the Nation's largest banks kept shoddy mortgage records and forged legal documents in the foreclosure process. We know how people, so many homeowners, paid a terrible, terrible price for that.

In response to these issues, the Nation's regulator for national banks began investigating the consumer debt markets to see if there were similar kinds of behaviors, and here is what the OCC said—the OCC not necessarily always in its past a friend of consumers, but increasingly so, and increasingly doing its job as a regulator. And I would thank them for that. But what they said was: "Its current interest debt collection and debt sales activity stems from the OCC's 2010 examination work when mortgage servicing and foreclosure practices that revealed weak governance of third-party vendors, including notaries and affiants, and poor documentation practices more generally. Because of"—this is the important part—"Because of the similarities in processes and heavy reliance on third parties, outside attorneys, notaries, and affiants, the

agency was concerned that similar weaknesses might be present in other retail lending activities."

Just as we saw in the mortgage market, banks and other lenders again are keeping shoddy records and giving them a seal of approval again. Former bank employees have reported that they were instructed to "go ahead and sign" affidavits verifying consumer debts, even when they did not have documentation to back up their claims.

When debt buyers purchased these loans from the biggest banks, they signed as-is contracts, giving banks cover to offload debts for collection that may be inaccurate, they may be incomplete, they may be legally uncollectible, but going forward as is.

When banks and third parties collect debts based on unreliable information, megabanks are again making the rules, and consumers again pay a price for that. And it shows. Last year, the FTC received more complaints about debt collectors than about any other industry. Some 200,000 complaints came in about lenders that collect their own debts, collectors hired by lenders to collect on their behalf, and outside debt buyers that paid just pennies on the dollar for tens of billions of dollars in charged-off debt, hoping to collect even a small fraction of that debt.

In the past year, debt collectors have paid millions to Federal regulators to settle legal action for violating consumer protection laws. Several collectors violated the Fair Debt Collection Practices Act, the law intended to keep collectors from abusing consumers by threatening physical harm, by calling repeatedly at all hours of the day, by divulging consumers' confidential financial information, by attempting to collect debts they know do not exist, and refusing to fully review the validity of a debt even when a consumer says, "I do not owe that."

In 2010, Congress created the Consumer Financial Protection Bureau, the first Federal agency with comprehensive authority over the collection industry. The CFPB is in the process of writing the first rules, as we know, to supervise large creditors and collectors. Collecting on legitimate debts in a safe and sound way can help our Nation's credit system function more efficiently. Banks can make less expensive loans, consumers are better off. But attempting to collect on illegitimate debts using abusive or deceptive tactics hurts consumers and deadlocks our backlogged legal system.

In the 35 years—this bill I believe was signed into law in 1977. In the 35 years since the first debt collection law was passed, the industry has changed, and changed dramatically, but the law has not been updated. I hope to hear from the FTC, the agency that now has authorities over debt collectors, and the CFPB about how we can modernize debt collection oversight to better serve consumers.

I will introduce the panel, and then we will go forward.

Corey Stone is Assistant Director, Credit Information, Collections, and Deposit Markets at the CFPB. He serves as Assistant Director and has extensive experience with electronic payment infrastructures, credit scoring, credit access, and money service businesses. Mr. Stone, thank you for joining us.

Reilly Dolan is Acting Associate Director for the Division of Financial Practices at the FTC's Bureau of Consumer Protection. Mr.

Dolan has a distinguished career in consumer protection at the FTC, has supervised investigations and litigation enforcing the Federal Trade Commission Act and other financial consumer product laws governing nonbank financial service providers.

Mr. Stone, why don't you go first. Thanks for joining us.

STATEMENT OF COREY STONE, ASSISTANT DIRECTOR, OFFICE OF DEPOSITS, CASH, COLLECTIONS, AND REPORTING MARKETS, CONSUMER FINANCIAL PROTECTION BUREAU

Mr. STONE. Thank you, Chairman Brown. It is a pleasure to speak with you today on behalf of the Consumer Financial Protection Bureau on the subject of debt collections.

In the wake of our recent financial crisis, we see far too many people in financial difficulty. By our best estimate, 30 million people have one or more debts in collection. These consumers are likely to hear from one of over 4,000 debt collection and debt purchasing companies. These firms are an essential part of our credit system, and without collection activity, more debts would go unpaid, and lenders would be more reluctant to extend credit and would need to charge more for doing so.

Yet while many debt collectors treat consumers fairly and respectfully, others try to get ahead by flouting the rules. Our job is to root out bad actors and protect consumers against unfair, deceptive, or abusive practices and other violations that harm both consumers and every collector that tries to operate within the law.

In January, the Bureau gained its authority to supervise about 175 of the largest debt collection and debt-buying firms, which represent over 60 percent of consumer collection industry receipts. Through our examinations, we are now in a position to evaluate whether Federal consumer laws are being followed at every stage of the credit-granting process—from credit origination to servicing to debt collection. And through our enforcement authority, we have taken action and we will continue to do so when we see the law being flouted.

Last month, we held a stakeholder roundtable with the Federal Trade Commission to gather insight on the integrity of information used in debt collections and in lawsuits against debtors. We often hear about collectors who pursue payments from the wrong consumers or for the wrong amounts. This can happen when information about a debt gets lost or changed as the debt is assigned or reassigned to a collector or sold off to a debt buyer. Over time, with changing ownership and accumulated interest and fees, the debt may become unrecognizable to the consumer who owes it.

At our roundtable, we heard strong consensus about the need for robust national documentation and accuracy standards pertaining to information used to verify and collect debts, and we will keep that in mind as we consider rulemaking on debt collection issues.

Last week, we announced that we would begin to take consumer complaints about debt collection through our Consumer Response office. As with other complaints we take, these will be forwarded to the collection company, and in some cases to the original creditor, for resolution. We will be able to track responses. The process will aid consumers who may have been subject to potentially improper actions, and it will enable us to identify entities whose prac-

tices generate high levels of complaints and target our supervision and enforcement efforts where they are most needed.

I want to point out two growing challenges in debt collection.

The first is that unsecured debt issued by financial institutions no longer represents the largest focus of debt collection activity in our country. According to one trade group, hospitals and other health care providers now represent both the largest group of customers of collection agencies and their largest amount of recoveries in dollar terms. Unpaid medical bills trouble a large number of Americans, including by adding negative information to their credit reports and hurting their credit scores.

Another fast-growing area of collection is student debt. Nearly $100 billion in Federal and private student loans is currently delinquent or in default. Unpaid medical bills and student debt present some unique challenges to both consumers and collectors and to our overall economy. We will need to be sensitive to these challenges as we seek to improve practices and protections in the overall marketplace for collections.

The second challenge is what you said, Senator: Congress passed the Fair Debt Collection Practices Act many years ago, before many of today's communication technologies were in use. Cell phones, text messaging, email, voicemail, and even faxes did not exist back then, but are now being used by collectors to reach consumers, sometimes in ways that can compromise both dignity and privacy. We intend to engage with our colleagues at the FTC and the FCC, each of which have relevant jurisdictions that pertain to these practices, to establish clearer guidelines for how collectors may use some of these new communication technologies to reach consumers who owe debts, while protecting privacy and dignity.

As our Director, Richard Cordray, pointed out last week, our system of granting credit is based on "an accepted notion that people who owe money to others should in fact repay the money they have borrowed, and that they should feel an obligation to do so." So debt collection activities play an essential role in this system, and without them, credit would be harder to come by and more expensive. Our job is to assure that consumers are not subjected to collection of debts they do not owe or to debts in the wrong amount or that they have already paid. Likewise, Congress has empowered and obligated us to assure that when consumers cannot, or even in the occasion when they will not, repay their debts that they continue to be treated with dignity and respect.

Thank you for having me here today, and I look forward to your questions.

Chairman BROWN. Thank you, Mr. Stone.

Mr. Dolan.

STATEMENT OF JAMES REILLY DOLAN, ACTING ASSOCIATE DIRECTOR, DIVISION OF FINANCIAL PRACTICES, FEDERAL TRADE COMMISSION

Mr. DOLAN. Thank you, Chairman Brown. I am James Reilly Dolan. I am the Acting Associate Director for the Division of Financial Practices in the FTC's Bureau of Consumer Protection. I appreciate the opportunity to present the FTC's testimony on debt collection and the Fair Debt Collection Practices Act. The views ex-

pressed in the written testimony represent the views of the Commission. My oral statement and responses to your questions reflect my own views.

While lawful debt collection serves an important role in making consumer credit more readily available and affordable, unfair, deceptive, and abusive collection practices victimize consumers and undermine fair competition. In some extreme cases, collectors will even threaten to have consumers arrested or jailed, pretend to be law enforcement, or threaten to physically harm consumers or their loved ones.

Accordingly, stopping such unlawful debt collection practices is among the FTC's highest priorities. Since January 1, 2010, the FTC has brought 15 cases against debt collectors and has obtained judgments of more than $56 million and orders that protect hundreds of thousands, if not millions, of consumers from future harm.

Just last week, the FTC announced it reached a settlement with the world's largest debt collector, Expert Global Solutions, commonly known as NCO, to resolve allegations of FDCPA violations. The FTC alleged that NCO annoyed and harassed consumers with repeated phone calls and impermissibly disclosed debt to third parties, especially in answering machine messages. As part of the settlement, NCO agreed to pay a $3.2 million civil penalty, the largest civil penalty the FTC has obtained in cases alleging violations of the FDCPA.

As another example, in 2012, the FTC obtained a civil penalty of $2.5 million as part of a settlement with a leading debt buyer, Asset Acceptance, to resolve alleged violations of the FDCPA. The FTC also obtained strong injunctive relief as part of the settlement, including a requirement that Asset will tell consumers whose debts may be too old to be legally enforceable that it will not sue to collect on that debt. This disclosure requirement already has had a positive impact on industry practices.

In other cases, the FTC has focused on swiftly halting exceptionally egregious debt collection conduct, seeking and obtaining preliminary relief including ex parte temporary restraining orders, assets freezes, and appointments of receivers. The FTC has also obtained strong final relief, including in some cases banning the defendants from engaging in debt collection.

For example, in *FTC v. Forensic Case Management Services,* the Commission stopped a debt collector charged with engaging in a host of egregious conduct, including threatening to physically harm the consumers, desecrate the bodies of dead relatives, and to kill their pets. The defendants ultimately stipulated to a permanent ban on engaging in debt collection.

As another example, the FTC obtained preliminary relief in three recent cases against so-called phantom debt collectors. Phantom debt collectors, in some cases located offshore, attempt to collect on debts, often related to payday loans, that either do not exist or are not owed to the phantom debt collectors. In each case, the FTC alleged that the defendants pretended to be law enforcement or other Government authorities and falsely threatened to arrest or jail consumers immediately if they did not agree to make payment.

While enforcement actions like these are at the heart of the Commission's debt collection work, it also engages in education, public outreach, and research and policy initiatives.

For instance, the FTC held a series of nationwide roundtable discussions and public comments examining debt collection litigation and arbitration proceedings, which culminated in the publication of a report in July 2010. And in January of this year, the FTC released a report on the first empirical study of the debt-buying industry. The report was based on extensive and detailed information that the FTC obtained from nine of the largest first-generation debt-buying companies, and found there is room for improvement in the information and documentation debt buyers have when they contact consumers and try to collect debts.

Most recently, as Mr. Stone referred, as part of the FTC's ongoing coordination with the CFPB on debt collection, the two agencies cohosted a roundtable to examine the flow of consumer data through the debt collection process. The roundtable brought together consumer advocates, credit issuers, collection industry members, State and Federal regulators, academics, and other stakeholders to exchange information on a range of issues related to the consumer information that flows through the life of a debt. All stakeholders agree that better information is better for all.

I thank you for the opportunity to present the Commission's testimony in this critical area, and I am happy to answer your questions.

Chairman BROWN. Thank you very much, Mr. Dolan.

I will start with Mr. Stone. You talked about hospital debt. I will get to that in a second. I understand student loan debt is different because it is the behavior of the debt collectors I assume is different—I want you to walk through that in a moment—because it is not dischargeable in bankruptcy. Is hospital debt any different in terms of the—do you see different trends in hospital debt in terms of how long the hospital tries to collect, the methods that hospitals use, when they sell their debt how those—just the process of selling the debt and collecting, do you see any difference in this growing health care debt from other kinds of debt? Putting aside student loans for a moment.

Mr. STONE. Yes, the biggest difference is there is a huge diversity in medical providers. It is not just hospitals. If you go into the hospital for a medical procedure, you are likely to have consumed the services of a blood testing service and an ambulance service, so a bill typically involves multiple providers and potentially multiple payments by insurers, and the consumer is stuck with the rest if they have insurance. Otherwise, they are getting separate bills.

There are no standards yet in terms of when a debt is assigned to a collector or, when it is considered to be charged off. Some collectors in the medical field are essentially outsourced receivables management companies who actually do the billing and take over the calling from day one. They provide the lockbox service to collect the payments while others keep all those collections in-house. There is a great variety in terms of whether hospitals report or do not report items in collection to a consumer reporting agency and when they would report. So we have a little bit of a wild, wild west situation in that——

Chairman BROWN. Thank you. A health care bill where you go to a hospital and you are paying the lab and you owe money to the lab, the doctor, the hospital itself, a number of doctors, and maybe multiple labs or testing facilities or scanning companies or whatever, scanner companies, is there usually—if I am the debtor there, am I usually—am I getting pursued by five or six or eight people for that debt unlike maybe a credit card debt when it is one entity pursuing me? Or is it more likely that there is some coordination among the various medical professionals or companies there in pursuit of that debt? Or is there no rhyme or reason or no trends that you can see?

Mr. STONE. So far we have not been able to see rhyme or reason in that. One of the things that, say, a credit card issuer would have is guidance or accounting rules that are imposed by the prudential regulators when a debt is considered to be charged off, and that typically is a point at which a card issuer would tend to use an outside collection agency. There is no standard like that in the medical field. You have got all these different kinds of providers with different capabilities, different record keeping, and different capabilities to do their own collections. And, in the medical field, they tend to be using different collection agencies, many of whom are small and local, because health care provision tends to be local.

Chairman BROWN. So there is a reasonable chance that I am discharged from a hospital, my insurance was either inadequate or I am fighting with my insurance company, it is not paying what I thought it would, or maybe I do not have insurance, whatever, and I am getting calls then from a number of different collectors, collection agencies, for that hospital bill different—again, very different from running up a debt with one credit card or with one student loan company.

Mr. STONE. Right, and——

Chairman BROWN. Which suggests, if I could interrupt for a moment, which suggests perhaps more protections should be in place for that customer, for that debtor. Go ahead.

Mr. STONE. Yes, standards would be a great starting point. You raise the possibility you might get multiple calls. In fact, many of these debts are very small. I think the statistic from the Fed's initial research on this is that 60 percent of the debts are less than $200 in medical, so in many cases, the consumer will not get a call. In the way our medical system does billing, they may not get a bill from the individual ambulance provider, which may get rolled up in the hospital bill and get lost. However, that does not stop the ambulance service from trying to collect. They need to get paid by somebody. And so the simplest thing for a lot of these providers to do is to report the debt to a credit report company because it is free. Then when the consumer applies for a loan or happens to, perhaps, look at their credit report, they discover the unpaid bill, and that is the time when they first contact the provider.

Chairman BROWN. So the ambulance company to which you owe $180 typically collects that from the hospital where you have been—where the ambulance driver has taken you. And if the hospital does not pay because you have not paid the hospital, all the ambulance driver might—all the ambulance company might do is

put it on your credit report, not go after you directly, I who was riding in the ambulance?

Mr. STONE. We are just beginning to understand this. It is not clear that the hospital is the one who is responsible for paying the ambulance company. It might be the insurance company that is responsible for paying the ambulance company, but the hospital is responsible for billing the insurance company on behalf of the ambulance company, and the insurance company negotiates with each of the billers. It is hard to track exactly what is happening. There is also some question as to whether the insurance company covers the ambulance service or not. If it does, it might pay the hospital, which would pay the ambulance company. The insurance company may also pay the ambulance company directly, bill the consumer, or does not bill the consumer and waits until it has got a response from parking this——

Chairman BROWN. So how do you make rules and standards here? Is it up to the States? Is it up to the Consumer Bureau? What do you see in the next months ahead about this?

Mr. STONE. This is an area where we need to do a lot of further investigation to really understand it. The Affordable Care Act may make a difference. One of the interesting things coming out of the Act is that the first set of standards for collecting of medical debt has been established by the IRS for nonprofit hospitals as part of their retaining a nonprofit status. So, there are growing impetuses for the creation of standards on the record keeping, on the billing, and ultimately for the collections of these debts.

Chairman BROWN. Let me come back to you on student loans, but, Mr. Dolan, the OCC statement for the record quotes Comptroller Curry from a year ago saying he has seen institutions outsourcing such functions as debt collection, but not taking adequate care to ensure that the third-party contracted to perform these functions follows the law and regulations governing them.

You mentioned NCO and the settlement. Does it trouble you that NCO is owned by one of the world's largest banks? Is that troubling, or does that not matter?

Mr. DOLAN. Obviously, we would need to make sure that they deal with conflicts of interest. When we did the debt buyer study, we looked at publicly available data from Nielsen and confirmed that 4 out of the 14 top debt buyers were publicly owned including NCO, and they do have this connection with the bank.

In some ways that could make life easier because they have potentially greater access to the documentation that the original creditor has. I do not know to what extent they had access to that documentation. In most instances, contracts provide limited access to documentation from the original creditor. The debt buyer can only go back so many times, can only go back so many times within a certain timeframe, and then they start being charged for the information.

There could be benefits to having a relationship as long as the arm's-length transactions are maintained.

Chairman BROWN. Let me talk about another one of those, and as you point out—and thank you for that answer—there are a number of examples of large institutions, large banks especially, owning these companies. One collector, Allied Interstate, is owned

by the Canadian Firm iQor in which Citigroup holds a large investment stake. I guess I draw three conclusions from the fact that Citigroup—or another large institution in the case of another one of these collection agencies, these collection firms, I guess I draw three conclusions from Citigroup deciding that Citigroup is not collecting this, that they have created a subsidiary to do this. And let me share the three and get your thoughts about them:

First, that Citigroup and this bank and other banks think that this is a lucrative business to do debt collection;

Second, there is some reputational risk, for want of a better term, in associating with these collection firms. Citigroup does not want, apparently—I mean, my contention perhaps. I think this is the case, that Citigroup probably does not want the imprimatur of Citigroup on their aggressive tactics to pay these debts back, so they have something called iQor or Allied Interstate or something else;

And, third, it should not be that difficult for these banks to share—the banks to whom the debt is owed to share information with iQor or Allied Interstate when they do the collection.

So the problem we cited earlier is that, you know, sometimes the debts are not really owed; other times the debts are—it is more in question; other times the debt has already been paid back, whatever the reason. But the debt collector does not often have that information, so the three points I made, a bit circuitously, the three observations, and I want your comments on each: it must be lucrative, the banks probably do not want their names on it on their aggressive tactics, and, third—and I am not judging their tactics. I am just saying they are aggressive. I think they are. But that does not mean they are good or bad or fair or unfair. And, third, there should be more—there could be more information sharing, which there apparently is not. Would you give me your thoughts on that?

Mr. DOLAN. Happy to. With regard to the reputational risk, you are actually touching on one of the things that we have kind of pulled out through our roundtables and through the debt buyer study, and that is, the identity of the original creditor. Consumers often need that identity in order to be able to assess, Hey, is this a legitimate debt? Did I even deal with this company? That is even, quite frankly, becoming more of an issue with the emergence of phantom debt.

As I said, the contracts often that we were reviewing during the debt buyer study would have provisions in them that actually prohibited the disclosure of the original creditor. While we do not know for sure why, I think the supposition that you put forward is the reputational risk is certainly something that could very well be related to that. Along those lines, the OCC recently issued guidance for safety and soundness concerns when financial institutions are charging off debt to consider who the debt buyer is and to recognize that there will still be reputational harm to them based on the debt buyer's contacts and conduct with regard to the debtors.

So who the original creditor is is very important information. It is not currently required under the FDCPA. The FDCPA simply says that when a consumer requests validation of the debt, the debt collector has to identify who owns the debt. It made sense back in 1977 because debt buying really had not come into the in-

dustry at that time. Things have changed and the Commission has expressed concern that consumers are not getting that information under the current rubric of the FDCPA.

With regard to whether this is lucrative, there is probably a convergence of a number of different issues that play into this. First off, within the last couple of years, the OCC has required financial institutions to charge off debt within a certain period of time. Credit card debt has to be charged off within 180 days. That means it can no longer count toward the bank's assets, and obviously the OCC's concern for banks' safety and soundness, they want to make sure that there is a sufficient asset-to-liability ratio.

So banks have to get rid of the debt within 180 days. One way they are able to still recoup the benefit of what otherwise would be deemed an asset is to sell the debt. Another way is if they have a relationship, they sell it in-house, for lack of a better term, to a debt buyer that they have an ownership interest in. But that allows them to continue to gain benefit of the assets while not affecting the OCC guidelines as to having to charge the debt off and not being able to count that as an asset for their asset-liability ratio.

Information sharing was your third point, and the Commission is very concerned about the level of information that does get passed on, especially generation to generation, from a debt buyer. One of the things that we learned from the debt buyer study—I think we were a little surprised—is that all of the information that currently is required by the FDCPA to be provided in that validation notice is included in the data sheets that the debt buyers get. The biggest issue is the documentation. That is where currently the limitations are. Most sellers, as you noted in your opening remarks, sell it as is. They do not make the warranties, and they currently put restrictions on how many times a debt buyer may come back to get documents both in terms of time and in terms of frequency. So that is definitely one of the concerns the Commission has raised and wants to continue to look at, and we want to work with the CFPB as they are addressing some of these issues in rulemaking, and we will be continuing to look at it from the law enforcement lens.

Chairman BROWN. Thank you.

Mr. Stone, I want your comments on Mr. Dolan's comments, but one question first to Mr. Dolan. Do these large banks that have these subsidiaries or have ownership of these companies, do they sell their debts exclusively to them? Or do they sell some portion of their debt collections to their subsidiaries? So, in other words, does Citigroup sell all of its debt collections to iQor, or do they spread them around to other institutions typically? Or don't you know that?

Mr. DOLAN. I actually do not know the answer to that question.

Chairman BROWN. OK. Mr. Stone, your comments on Mr. Dolan's.

Mr. STONE. Just to answer the question you had, I know that in some cases these are actually in an auction environment, which makes it difficult for the buyer to negotiate better terms in terms of data continuity and data availability with the creditor who is selling the debt and who is trying to get as many dollars for that debt as they possibly can.

The roundtable that we had together really focused on the importance of the need for standards and particularly on the need for the availability and retention of documents that can be used to validate and verify a debt down the line, including when it potentially goes to court.

Interestingly, the Truth in Lending Act data retention requirements are 2 years. The statute of limitations tends to be longer in many States, and the period over which debt is reported to consumer reporting agencies as being in collection can be 7 years. The ability to conduct a proper investigation or to provide proper documentation to a court can be very much limited by the data retention policies of the original creditor.

So we are trying to bring a soup-to-nuts, beginning-to-end approach to this, and make sure that we understand the hand-offs, have standards for how those happen, and what is included in them.

Chairman BROWN. Thank you.

Mr. Stone, tell me how you look at or how you assess the difference between student debt, which, as of course you know, cannot be charged off the bankruptcy—is not dischargeable in bankruptcy as other debt is. That is a whole other judgment call, but how that affects the debt collector's behavior over time versus a debt which is dischargeable with bankruptcy?

Mr. STONE. Yes, well, in some ways, it does not. The largest debt collectors who collect on Federal student debt qualify under contracts with the Department of Education to collect those debts. They are all subject to the Fair Debt Collection Practices Act, and because they are virtually all larger participants in the collection market, they will be subject to our supervision. So we will be looking at their practices just like we do others.

The differences have to do with an area where I do not by any means have the most expertise, and I know my colleague Rohit Chopra, who is our student ombudsman——

Chairman BROWN. He has been here.

Mr. STONE. ——was in front of the full Committee several weeks ago to talk about student debt. The differences are, in addition to the nondischargeability, the youth and lack of sophistication of the population of students who owe student debt. Many of them are coming right out of school and are trying to get their first job to be able to create earnings to begin to pay off their debt; sometimes a mixture of public and private loans, which have different rules and may be a source of confusion. Public Federal debt has a set of rules about ability to pay and payments commensurate with earnings and forbearance that does not apply necessarily to the private student loans, and likewise, the powers that come with collecting student debt are, to some extent, accorded through the Department of Education and the Higher Education Act.

The amount of student debt is a big number. It is a specialized population. We have to pay attention to maximizing the prospects of these people's earnings and ability to move along with their lives in order to maximize their possibility of repaying the debt. I think that this is a particular set of concerns of this population.

Chairman BROWN. Debt collectors recognize what you said and recognize the issue of discharging in bankruptcy. They also know

that the Department of Education and private student lenders like Sallie Mae will pay a premium to collectors, will pay more than other kinds of debt. My understanding is they pay a commission. They give the collector a bonus for getting customers to make large payments. Incentives are not offered to help borrowers, though, enter sustainable income-based repayments. Pioneer Credit Recovery, a collector that contracts with Treasury and with the Education Department, is owned by Sallie Mae. If you would answer this, how do the incentive structures for collectors of student debt, what impact does that have on these consumers? Should these profit-driven practices be part of any lender or collector's business model?

Mr. STONE. Yes. I am by no means the expert on this. The incentives, as you point out, are different. The cost of collection, as I understand it, is rolled into the principal of the loan at the time that it is assigned to collections at default, and that does create a bigger amount of principal. I am not quite sure how the collector gets paid, but my colleague, Rohit, would know much better. But the nature of the incentive, as you point out, is—and this goes back to the servicing as well as in collections, so the servicer of the loan is generally not the collector postdefault—to not necessarily advise the consumer of their options that are available through the rules that pertain to Federal student loans.

Chairman BROWN. Thank you. OK. Mr. Dolan, let me switch over to another issue. The OCC has put out some best practices on this, pretty strong, pretty solid. It seems they have expressed concern that banks' documentation is inadequate, which we had referenced earlier, requiring banks to include relevant information like cease-and-desist requests or whether this person—whether it is a servicemember, include relevant information on accounts that it sells. It questions whether these high-touch accounts should be sold at all.

If banks have spotty documentation, the question to me is whether they should be able to collect or sell any of these accounts. And let me match—that is sort of the question I think we should ask. I just want you to—I want to list a number of policies, potential policies, and ask if you think they would be feasible: to require debt collectors, whether primary creditors or third-party collectors, to have all relevant documentation before issuing their first debt collection notice to the consumer, whether that should be a requirement; whether we should require that information on prior collection attempts travel with the debt, so if the original creditor tried to collect, then sold it to a collection agency, if that information should be available. Should we prohibit the sale of unverifiable debts, implicitly—or suggesting that we need to know—or they should have to—there should be some evidence and proof that they have, in fact, had verifiable debts, and disclosing that a credit collector is selling or collecting time-barred debt. If you would answer those.

Mr. DOLAN. Answering your first question, requiring debt collectors to have all relevant documentation, clearly, as I have noted, we have concerns about the availability of such documentation that collectors have, and the ability to provide that to consumers when they are disputing the debt or requesting validation.

As you go down the generations of debt buyers, I am a little more concerned about kind of unintended consequences that may come out of a small debt buyer having a lot of information and they would, therefore, need to make sure that they have data security procedures in place because the last thing we would want is to find all that consumer file sitting in a dumpster. So we would have to make sure we are thinking of all of the unintended consequences as we go down that road.

With regard to prior collection history, one of the things that our debt buyer study noted is that is one of the pieces of information that was not readily available in the data spread sheets that debt buyers would get from the creditors or from prior generations of the debt buyers. Clearly that is very relevant information. If a consumer has already disputed a debt, whether it is the full debt, amount of debt, "I already paid that," "It is not me," whatever the dispute is, that is information that a collector should have so that they are not reinventing the wheel with that particular debtor or purported debtor. So that definitely is something that we would like to work with the CFPB on how to best address that issue.

On prohibiting the sale of unverifiable debt, I think the industry would reply they do not know it until they try it. The way that the Commission has addressed this issue in the past is, in addition to the requirements of the FDCPA, we have applied the FTC Act, and one of the doctrines of the FTC Act is that when an entity makes a claim, they have to have a reasonable basis for that claim. They have to have the substantiation to support that claim. In the debt collection context, what that means is if I am going to call you up and say you owe me money, I have to have a reasonable basis to make that claim.

The creditor's data spread sheet may be a starting point, at least for the initial contact, for me to have a reasonable basis. But if you then say, "Mr. Dolan, it is not me, it is Mr. Brown who lives down the street," I then have to take that information into consideration with the other information that I have in order to say I still have a reasonable basis or, gee, maybe I better go back and get more.

So we have addressed that issue of unverifiable debt through the FTC Act. Trying to prohibit the sale of unverifiable debt we have not really looked at. We did not verify the accuracy of the data in our debt buyer study. There was really no easy way to do that given the volume of aggregate data that we had. So we do not know how accurate the as-is data really is. Clearly we hear plenty of anecdotes, and we receive a lot of complaints saying, hey, wait a minute, they did not get it right. But we just do not know if we are talking 3-, 4-percent error rate, which still may affect a million consumers, or whether we are talking a much larger error rate.

And then, I am sorry, I wrote down "time" for your fourth point, and I do not know what that reference is.

Chairman BROWN. The last is selling or collecting time-barred——

Mr. DOLAN. Time-barred debt, thank you. It is not illegal under the FDCPA to attempt to collect on a time-barred debt. With that being said, it is a violation of the FDCPA to state or to imply that you could be sued in order to collect on that debt. So basically there is nothing wrong with saying, in the cleanest version, you owe this

debt, it is old, I cannot sue you on it, but wouldn't you like to clear your name? That is probably not problematic. Any kind of implied representation, either through silence or through affirmative representations, that imply that I can or would sue you, violates the FDCPA. So right now the way the law is, collecting on time-barred debt, as long as the debt collector does not cross that line, is not a violation of the FDCPA.

Chairman BROWN. Do agencies—and then I will turn to Senator Toomey. Do agencies inform consumers that they can sue? Is this—that they cannot sue? Is that something that they do?

Mr. DOLAN. Most recently in our Asset Acceptance settlement, there is an order provision that if it is likely that the debt is at or near the statute of limitations, Asset has agreed under the order that it will inform the consumer that it will not sue on the debt. There are a couple of State laws that require that disclosure or in some cases a more complicated disclosure. More and more States are considering that type of disclosure. Absent either an order or in a State where disclosure is currently required, the debt collectors usually do not affirmatively say, "I cannot sue you on this debt," or, "I will not sue you on this debt." That is where the implied representation can arise, especially in a situation where, if it has gotten to the point that it is time-barred debt, most likely that consumer has been contacted on that debt multiple times. Prior collectors, who were not facing the time-bar issue, probably were threatening lawsuit. There is a provision in the FDCPA that says you cannot threaten action you do not intend to take. So the threat is sometimes a little more subtle than that. But many of these consumers may have heard the message that they could be sued on these debts. So by the time that a debt buyer is a couple generations into it, has the time-barred debt, and does not say anything but does say, you know, "You have to pay this debt or else," that could be enough to create that implied misrepresentation.

Chairman BROWN. OK. Senator Toomey, thank you for joining us, and take as much time as you would like, of course.

Senator TOOMEY. Thank you very much, Mr. Chairman. I appreciate it. I am sorry I got here a little bit late, and I will not be able to stay long, but I did want to ask Mr. Stone a couple of questions, so I welcome our witnesses and thank them for being here.

My questions, Mr. Stone, are about the process that the Bureau was using to establish the criteria for determining unlawful, inappropriate, unfair, deceptive, abusive practices. And my understanding is that the CFPB has done this by releasing guidance documents in the form of bulletins. There are a couple of bulletins that do this. And my first question is: Why is the CFPB doing this in the form of bulletins instead of in the ordinary rule-making process?

Mr. STONE. Thank you, Senator. I am glad you asked that question, and there are many areas where we do feel that it is important to use a rule to clarify areas of law that are uncertain.

I think one of the things that led up to the bulletin that you are probably referring to that we issued last week, which, essentially, listed practices that are defined in the Fair Debt Collection Practices Act as unfair, deceptive, or abusive, as being potential UDAAPs under our Title X authority, was that these are areas of

established law where the Fair Debt Collection Practices Act is defining what is unfair, deceptive, and abusive. There are court cases that support those findings and add further definition to them. There are also many first-party collectors that are already using the Fair Debt Collection Practices Act as guidance for how to conduct their own collection activities. So we felt we were on pretty conservative ground here in issuing that bulletin.

Senator TOOMEY. But as you point out, you add further definition to existing law, and if there is a need to do a bulletin, there is obviously a perception that there is some need to provide this precision. My reading of Dodd-Frank Title X grants the CFPB authority to use rulemaking for this purpose, and one of the reasons, of course, is that rulemaking is a defined process that requires things like public input and review and opportunity for a real robust public discussion.

In creating the bulletin, did you leave it open for public comment? Was there a comment period? How many comments did you get? Were they incorporated in a revised bulletin? Did any of that process occur?

Mr. STONE. No, Senator. When we issue bulletins, we do not go through a comment process. I thought what I said was that we do issue rules when we need to add further definition, but in this case of unfair, deceptive, or abusive practices in the collections market, we did not think we were adding further definition to the law and, therefore, a rulemaking was not required.

Senator TOOMEY. So what does the bulletin do then? What is the purpose of the bulletin if it is not to provide any additional definition or clarification?

Mr. STONE. The bulletin simply says that the practices that have been deemed over many years to be unfair and deceptive or abusive in the debt collection practices as it applies to third-party collectors may be unfair, deceptive, and abusive practices as practiced by first-party collectors.

Senator TOOMEY. So are you saying the bulletin just says that which is illegal is illegal?

Mr. STONE. I guess I would have to agree with you, Senator.

Senator TOOMEY. Well, that is peculiar. All right. But this is not something for which—I mean, there was some decision made here as to least apply to some parties that which was historically applied to other parties. That is determined, that is the decision that is embodied in the bulletin, right?

Mr. STONE. Well, I think the history behind this includes not just FDCPA actions but actions under the FTC Act. So there are many, many actions that have been taken, including the actions that my colleague from the FTC just described as well as our recent action against American Express that we shared with the OCC and with the FDIC, which referred to the FTC Act in their case, and in our case under our Title X authorities where those practices were deemed to be unfair and deceptive, under the FTC Act and under Title X.

Senator TOOMEY. OK. No further questions. Thanks.

Chairman BROWN. Thank you.

I have one other question. I just want to make a comment. I appreciate Senator Toomey being here. I think that if it is a sugges-

tion of CFPB overreach, I think that looking at what the OCC put out in terms of best practices is a similar kind of regulatory—financial regulatory body looking at suggestions that can make the system perhaps work a bit better.

Mr. Dolan, let me just kind of conclude with a series of questions about the FTC. The FTC recommended that collectors systematically break out for consumers the principal balance of these accounts, the interest, and the fees. Both of you can answer this. These sorts of itemized—do you agree these—and make these answers short. They are pretty easy. Do you both agree these sorts of itemized statements should be provided to consumers? Any reason that you would not say yes to that?

Mr. DOLAN. We have consistently said that consumers should be provided the breakdown of principal, interest, and fees. I will note that one of the things we learned during the joint workshop was that it is easy to calculate postjudgment. It is not quite as easy to calculate prejudgment. But we still take the position that this type of information helps consumers understand the nature of the debt and it is consistent with what the FDCPA wants debt collectors to provide to consumers when they validate the debts.

Chairman BROWN. Mr. Stone, briefly.

Mr. STONE. I think I can make my answer shorter: Yes.

Chairman BROWN. OK. Thanks.

You both described and referred to a couple of times the FTC held a workshop on debt collection—this was 2009—and concluded that debt collectors have inadequate information when they seek to collect from consumers. The FTC then recommended changes in the information that debt collectors and buyers receive and advocated for improved validation notice for consumers.

Last month, at the Debt Collection Roundtable—that one you referred to—we heard over and over again there is just not enough quality information available—well, at least provided to debt collectors or to consumers.

With the technologies available today, why 4 years later are we still waiting on banks to improve their own information and the information they send on to collectors?

Mr. DOLAN. I think at this stage it is what the market bears between the creditors and the debt collectors. Most of the creditors are financial institutions outside of our jurisdiction, so we really are looking at it from just one part of the prism. I think the CFPB has a more global view, so this is one of those areas that we definitely want to continue to work closely with the CFPB as they are able to look at it from both sides.

Mr. STONE. So if I can jump in, there are a couple of promising developments in this area. One is, as part of their due diligence and oversight of their collection agencies, a number of larger banks are requiring the collectors to actually transact their business on the bank's system, so there actually is no transfer of information. The system that is used by an individual representative is a screen that goes back to record keeping that is maintained by the banks, so there is not a hand-off of information. That also has some security benefits.

A second development, that a few companies have proposed and developed the capability to provide, is a debt registry. So when debt

is moved to collection by an institution, a clear set of data, to a standard that is yet to be developed and vetted by us, could be placed in a central repository. Rather than moving records around with ownership of the debt, one moves around access to the records, including access to any kind of documentation. Original statements, for example, and contracts that might travel with the debt, could be made available through the registry and would have a particular advantage for allowing smaller collectors to have access to the records without worrying about compromising data security. It could also serve as a place for consumers to go on a self-service basis, look up the debt with a secure ID, and determine whether it is theirs or not, and whether it actually represents what they think they owe.

Chairman BROWN. Is it particularly costly or burdensome for the creditors to provide documentation to the collectors? That is the argument that, of course, we hear. What is your thought on that?

Mr. STONE. We have not gone and measured it. The companies who are developing these registry systems are saying it is quite inexpensive for them to provide, based on a one-time fee of a couple dollars, that creates a permanent record that could support all the players in the marketplace downstream. So the question really is: How much does it take to load up the original data by the original creditor? And in that regard, technology is moving in favor of that becoming increasingly cheap.

Chairman BROWN. And before you answer that, Mr. Dolan, it is pretty clear that if debt collectors—I mean, there are examples of this, more than anecdotal evidence, that when debt collectors misrepresent information or just get it flat out wrong, that consumers can lose access to credit; they can have a terrible credit report follow them around for the next decade. They spent time unnecessarily fighting the debt and all that comes—all that they are victimized by.

The OCC has suggested that debt losses—that debt buyers would be willing to pay more for better information because they will collect more on these accounts. So when you think about the additional cost, there is a suggestion of additional payoff, that banks will get more money, consumers will benefit. Do you agree with that?

Mr. DOLAN. I was just writing down in my own notes, supply and demand curve. Currently, to kind of follow up on Mr. Stone's comments and then use that as a segue into your question, we have not looked at how much the increase in the cost of debt would be to the debt buyer for this information. What we have heard in the past is that debt buyers have said the creditor wants to charge us more for this, and obviously the incentives of the supply and demand currently have it at, on average, 4 cents—approximately 8 cents for what I will call the cleanest debt. Having the creditor maintain the documentation or provide it to the debt buyer will shift that curve. It is just I do not have a good answer of how far.

With that being said, to the extent that they have more documentation, it is easier to collect on debts that otherwise might be disputed. So I do agree that the better data will allow better collection efforts as well.

Chairman BROWN. Thank you, and thank you both for being here. This was a very helpful discussion. Good luck to you, Mr. Stone, with the new and improved agency and as you work on these rules.

I want to ask unanimous consent that the statement of the Office of the Comptroller of the Currency be included in the hearing record, too. And since nobody else is here to object to the unanimous consent, I guess it is agreed to.

Thank you. If any Members of the Subcommittee have questions in writing to you, we will submit them to you within a week. I hope you can turn around the answers to those questions quickly.

Thanks to both of you for your public service, and the Subcommittee is adjourned.

[Whereupon, at 11:17 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF COREY STONE

ASSISTANT DIRECTOR, OFFICE OF DEPOSITS, CASH, COLLECTIONS, AND REPORTING MARKETS, CONSUMER FINANCIAL PROTECTION BUREAU

JULY 17, 2013

Good morning, Chairman Brown, Ranking Member Toomey, and Members of the Subcommittee, it is a pleasure to be here again, and I am grateful for the opportunity to speak with you today on behalf of the Consumer Financial Protection Bureau on the subject of debt collections.

The topic of today's hearing was also the focus of a field hearing the Bureau held last week in Portland, Maine. Many of my remarks today draw from those given by Director Richard Cordray at that event. Debt collection has long been a source of frustration for many consumers, generating a heavy volume of consumer complaints. It is the focus of considerable enforcement activity by the Federal Trade Commission, by State attorneys general, and most recently by the Bureau. We are all determined to make steady progress, together, to protect consumers in this area.

Debt collection also has more salience today than perhaps at any time in our country's history. In the wake of the recent financial crisis, we see far too many people who have fallen into financial difficulties. Many lost their jobs, much of their savings, and even their homes. Bills piled up and sat unpaid. Many consumers fell behind, either because of bad decisions they made or because they were victims of tough economic conditions during the recession. The best estimates are that 30 million people—nearly one out of every ten Americans—came out of the financial crisis with one or more debts in collection, for amounts that average about $1,400 per person.

While many debt collectors play by the rules and treat consumers fairly and respectfully, others try to get ahead by flouting the rules. Our job is to root out bad actors and protect consumers against unfair, deceptive, or abusive practices and other legal violations, which damage both consumers and every other debt collector that tries to operate within the law.

There are over 4,000 debt collection and debt purchasing companies and they represent a wide spectrum of firms. They are an essential part of the credit system, which operates under the accepted notion that people who owe money to others should in fact repay the money they have borrowed, and they should feel their obligation and responsibility to do so. Without collection activity, more debts would go unpaid, and lenders would both be more reluctant to extend credit and would need to charge more for doing so.

In January, the Bureau gained its authority to supervise firms that have more than $10 million in annual receipts from consumer debt collection activities. Our supervision authority extends to about 175 debt collectors and debt buyers, which account for over 60 percent of the consumer debt collection industry as measured by annual receipts. Through our examinations, we are now in a position to evaluate whether Federal consumer laws are being followed at every stage of the process—from credit origination to debt collection. And through our enforcement authority, we have taken action and we will continue to do so when we see the law being violated.

Last month, we held a joint roundtable with our partners at the Federal Trade Commission to gather information and solicit input from a wide range of stakeholders on the integrity of information used in debt collections and in lawsuits against debtors. We often hear about collectors who pursue payments from the wrong consumers or for the wrong amounts. This can happen when information about a debt gets lost or changed when the debt is assigned to a collector or sold off. Over time, when this information is presented to the consumer, the debt may become unrecognizable. At our joint roundtable, we heard strong consensus about the need for robust national documentation standards and the need to maintain the accuracy of information used to collect debts. We will keep that in mind as we move toward a rule-making process on debt collection issues.

Last week we also announced that we would begin to take consumer complaints about debt collection through our Office of Consumer Response. As with other complaints we take, these will be forwarded to the collection company (which in some cases means the original creditor) for resolution and we will be able to track responses to those complaints. In a market composed of over 4,000 collection firms and where consumers are also subjected to scams by illegitimate actors, providing consumers with the opportunity to submit these complaints will serve as an important early warning function, as well as serving to aid consumers who may have been subject to potentially improper actions by companies. We will be able to identify entities whose practices generate high levels of complaints and target our supervision

and enforcement efforts where they are most needed. Likewise, we will be able to identify criminals who are posing as collectors and report them to the proper law enforcement authorities.

I want to point three important challenges in debt collection:

- First, when one excludes mortgages and auto loans, debt issued by financial institutions no longer represents the largest focus of debt collection activity in our country, either by dollar amount or number of consumers affected. This has been surpassed by medical debt. According to ACA International, the largest trade group of debt collection companies, hospitals and other health care providers now represent both the largest group of customers of collection agencies and their largest amount of recoveries in dollar terms.[1] As Senator Merkley pointed out in this Subcommittee's hearing last December on credit reporting, medical debt is affecting a large number of Americans, including adding negative information to their credit reports and exerting a negative impact on their credit scores. Third party collectors of medical debt are subject to the same Federal statute as collectors of financial debt when it comes to protecting consumers, and we will be working with our partners at the FTC to better understand collection practices in this market and work to improve them.

  Close behind, and perhaps the fastest growing area of debt collection is student debt. With nearly $100 billion in Federal and private student loans currently delinquent or in default, this area of debt collection deserves particular scrutiny. As my colleague Rohit Chopra, who is our Student Loan Ombudsman, indicated in testimony before your full Committee three weeks ago,[2] we are working to help young Americans who are having difficulty paying off their student loans to better understand their options under the law either to restructure loan repayments in ways that are affordable, or if their circumstances require it, to obtain forbearance.

  Both medical and student debt have unique characteristics. And when borrowers are delinquent or in default, both types of debt present some unique challenges to both consumers and collectors. We will need to be sensitive to these challenges as we seek to improve practices and protections in the overall marketplace for collections.
- A second point is that there is a surprising amount of consensus across all market participants—from debt collectors, creditors, and collection attorneys, to consumer advocates, legal services providers, and State attorneys general—that we must develop clear standards for data integrity and record-keeping in the debt collection market. This is a finding from our joint roundtable and one that Director Cordray made last week. Too often, important information about a debt, including whether a consumer has disputed the debt, does not travel with the debt when it gets assigned to third party collectors or purchased by a debt buyer. And it is often either not present or available as part of the required notice to consumers when companies initiate collection activity or when owners of debt file claims or seek judgments in court. If we can address this problem, we will be providing consumers with tools they need to engage more confidently in the collection process, set requirements for disclosure and verification of debts that will discourage illegitimate actors, and enable collectors who play by the rules to more often avoid litigation. There is the potential for all legitimate players to benefit.

  This will not be easy. When it comes to standards for the fundamental task of maintaining records and disclosing information, the devil is in the details. It means answering the question: which specific pieces of information about a debt need to be maintained, by whom, and disclosed when? If we get this right, the result will be a more trustworthy collections system that is more likely to treat consumers with dignity and respect, while better meeting the needs of creditors.
- A final point: Congress passed the Fair Debt Collection Practices Act when I was in high school. The Act is significantly about proscribing certain practices that have to do with how a collector communicates with a consumer who owes a debt, and about making sure these communications are conducted in ways that protect that consumer's dignity and privacy. But the act was written before many of today's communication technologies were in use, including cell phones, text messaging, email, voicemail, and even faxes. These communication methods

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[1] ACA statistics on hospital and other health care providers' share of debt collector customers were presented in Bob Hunt's (Philadelphia Fed) presentation at the joint roundtable, available at *http://www.acainternational.org/economicimpact.aspx*.

[2] Testimony of Mr. Rohit Chopra, available at *http://www.consumerfinance.gov/testimonies/the-cfpb-before-the-senate-committee-on-banking-housing-and-urban-affairs/*.

are being used today by some collectors to reach consumers in ways that can compromise both dignity and privacy. We intend to engage with our colleagues at the FTC and the FCC, each of which have relevant and unique jurisdictions that pertain to these practices, to establish clearer guidelines for how collectors may use some of these new communication technologies to reach consumers who owe debts, while protecting consumers' privacy and dignity.

As Director Cordray pointed out last week, our system of granting credit is based on "an accepted notion that people who owe money to others should in fact repay the money they have borrowed, and that they should feel an obligation to do so." Debt collection activities play an essential role in this system. Without them, credit would be harder to come by and more expensive. Our job is to assure that consumers are not subjected to collection of debts they do not owe or to debts in the wrong amount or that have already been paid. Likewise, Congress has empowered and obligated us to assure that when a consumer cannot, or even in the occasion where they will not, repay their debts that they continue to be treated with dignity and respect.

Again, thank you for the opportunity to join you today and I look forward to discussing these matters further with you and to answering your questions.

PREPARED STATEMENT OF JAMES REILLY DOLAN

ACTING ASSOCIATE DIRECTOR, DIVISION OF FINANCIAL PRACTICES, FEDERAL TRADE COMMISSION

JULY 17, 2013

Chairman Brown, Ranking Member Toomey, and distinguished Members of the Subcommittee, I am James Reilly Dolan, the Acting Associate Director for the Division of Financial Practices at the Federal Trade Commission ("Commission" or "FTC").[1] I appreciate the opportunity to appear before you today to discuss the Commission's efforts to protect consumers from unfair, deceptive, and abusive debt collection practices.

Consumer credit is a critical component of today's economy, allowing consumers to purchase goods and services for which they are unable or unwilling to pay the entire cost at the time of purchase. If consumers do not pay their debts, creditors may be less willing to extend credit or may increase the cost of borrowing money. Lawful debt collection thus helps keep credit more readily available and affordable.

Unlawful debt collection practices, however, cause serious harm to consumers—both those in financial distress as well as others who do not owe the debt they are being contacted about—and place law-abiding debt collectors at a competitive disadvantage. Accordingly, challenging unlawful debt collection practices continues to be one of the Commission's highest priorities. The Commission receives more complaints about debt collection than any other specific industry, and these complaints have constituted around 25 percent of the total number of complaints received by the FTC over the past 3 years.[2] In 2012, consumers filed 125,136 complaints about third-party debt collectors and in-house collectors.[3] The consumer complaints most frequently reported are that collectors falsely represented the character, amount, or status of a debt (38.9 percent); made repeated or continuous calls (36.5 percent); falsely threatened to sue consumers or take other unintended actions (29.6 percent); failed to send a written notice of the debt to the debtor (25.4 percent); and falsely threatened to arrest a consumer or seize a consumer's property (23.4 percent).[4]

To stop these illegal practices, the Commission maintains an active program of vigorous law enforcement, education and public outreach, and research and policy initiatives. This testimony will describe the Commission's actions in each of these

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[1] While the views expressed in this statement represent the views of the Commission, my oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission or any individual Commissioner.

[2] *See,* Consumer Financial Protection Bureau, Fair Debt Collection Practices Act: CFPB Annual Report 2013, at 14 (24.1 percent of all complaints the FTC received); Consumer Financial Protection Bureau, Fair Debt Collection Practices Act: CFPB Annual Report 2012, at 14 (27.16 percent of all complaints the FTC received); FTC, Annual Report 2011: Fair Debt Collection Practices Act, at 5 (27 percent of all complaints the FTC received).

[3] Id. These numbers only include complaints filed directly with the FTC, which are coded and categorized in a consistent manner. These numbers also do not include identify theft or Do Not Call Registry complaints that may involve debt collection.

[4] Because consumer complaints frequently address more than one debt collection practice, a single complaint may count towards multiple violation categories. Hence, the sum of these percentages will be more than 100 percent.

areas, as well as the Commission's coordination and cooperation with the Consumer Financial Protection Bureau (CFPB) in addressing unlawful debt collection practices.

I. Enforcement

The Commission is primarily a law enforcement agency, and law enforcement investigations and litigation are at the heart of our recent debt collection work. The Commission has the authority to investigate and take law enforcement action against debt collectors who engage in unfair, deceptive, abusive, or other practices that violate the Fair Debt Collection Practices Act (FDCPA).[5] The Commission also has the power to investigate and take enforcement action against entities that, in connection with collecting on debts, engage in unfair or deceptive acts or practices in violation of Section 5 of the FTC Act.[6] These law enforcement actions supplement what Congress intended to be a significant part of FDCPA enforcement—private individual and class action lawsuits.[7]

The Commission generally carries out these powers in two ways.[8] First, the Commission may refer cases alleging violations of the FDCPA to the Department of Justice (DOJ) in instances where preliminary injunctive relief to halt unlawful conduct is not needed and where civil penalties are appropriate monetary relief. Second, the Commission has the authority under Section 13(b) of the FTC Act to file actions in Federal district court to obtain injunctions and disgorgement of ill-gotten gains or restitution against those who violate the FDCPA or the FTC Act.[9] The Commission generally files actions under Section 13(b) where the unlawful conduct of collectors is so egregious that a court order is needed to bring an immediate halt to the conduct or where equitable monetary relief, such as restitution and disgorgement of ill-gotten gains, are more appropriate forms of monetary relief than civil penalties.

In recent years, to improve deterrence, the Commission has focused on bringing a greater number of cases and obtaining stronger monetary and injunctive remedies against debt collectors that violate the law. Since January 1, 2010, the Commission has brought fifteen debt collection cases[10] and has obtained judgments of more than $56.2 million—including civil penalties, disgorgement of ill-gotten gains, and restitution—against a variety of debt collectors.[11] These cases include three civil penalty actions—*United States v. Expert Global Solutions, Inc.*, *United States v. West Asset Management, Inc.,* and *United States v. Asset Acceptance, LLC*—that resulted in settlements in which the debt collectors paid $3.2 million, $2.8 million, and $2.5 million, respectively, the three largest civil penalties obtained by the agency in cases alleging violations of the FDCPA.

In each of these cases, the FTC charged debt collectors with engaging in a host of unlawful practices. For example, in the most recent case, announced last week, the Commission filed a complaint against, and obtained a settlement with, the largest third-party debt collector in the world, Expert Global Solutions Inc. The FTC alleged that the defendants—commonly known as NCO—annoyed and harassed consumers for years with repeated phone calls, despite being told that the consumer does not owe the debt, does not know the whereabouts of the alleged debtor, or does

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[5] 15 U.S.C. §1692-1692p.

[6] 15 U.S.C. §45.

[7] *See,* S. Rep. No. 95-382.

[8] Section 814 of the FDCPA, 15 U.S.C. §1692l(a), authorizes the FTC to use all of its functions and powers under the FTC Act to enforce the FDCPA, including but not limited to the power to address a violation of the FDCPA in the same manner as if the violation had been a violation of a FTC trade regulation rule. Accordingly, the FTC can either seek civil penalties through a referral to the Department of Justice or seek equitable relief through its own attorneys.

[9] 15 U.S.C. §53(b).

[10] *FTC v. Expert Global Solutions, Inc.,* No. 3-13 CV 26 2611-M (N.D. Tex. filed July 8, 2013); *FTC v. Security Credit Services, LLC,* No. 1:13-cv-00799-CC (N.D. Ga. filed March 13, 2013); *FTC v. Goldman Schwartz, Inc.,* No. 4:13-cv-00106 (S.D. Tex. filed Jan. 14, 2013); *FTC v. Pro Credit Group, LLC,* No. 8:12cv586 (M.D. Fla. filed Mar. 19, 2013); *United States v. Luebke Baker & Assocs., Inc.,* Civ. A. No. 1:12-cv-1145 (C.D. Ill. filed May 11, 2012); *FTC v. Broadway Global Master Inc.,* 2:12-cv-00855-JAM-GGH (E.D. Cal. filed Apr. 3, 2012); *FTC v. AMG Servs.,* Inc., 2:12-cv-00536 (D. Nev. filed Apr. 2, 2012); *FTC v. Am. Credit Crunchers,* No. 12cv1028 (N.D. Ill. filed Feb. 13, 2012); *United States v. Asset Acceptance,* 8:12-cv-182-T-27EAJ (M.D. Fla. filed Jan. 30, 2012); *FTC v. Rincon Mgmt. Servs., LLC,* 5:11-cv-01623-VAP-SP (C.D. Cal. filed Oct. 11, 2011); *FTC v. Forensic Case Mgmt. Servs., Inc.,* LACV11-7484 RGK (C.D. Cal. filed Sept. 12, 2011); *FTC v. Payday Fin., LLC,* 3:11-cv-3017-RAL (D.S.D. filed Sept. 6, 2011); *United States v. West Asset Mgmt., Inc.,* 1:11-cv-0746 (N.D. Ga. filed Mar. 10, 2011); *FTC v. LoanPointe, LLC,* 2:10-cv-00225-DAK (D. Utah filed Mar. 15, 2010); *United States v. Credit Bureau Collection Servs.,* 2:10-cv-169 (S.D. Ohio filed Feb. 24, 2010).

[11] This includes approximately $42.5 million in equitable monetary relief and approximately $13.2 million in civil penalties. In some settlement orders, the monetary judgment is suspended in part or in whole based on the defendants' ability to pay.

not wish to receive any more communications.[12] The FTC also alleged that the debt collector disclosed consumers' debts to third parties through voicemail messages, even when the outgoing answering machine greeting either did not give the name of the person or announced that the answering machine was for a person other than the consumer that the collector was trying to reach.

In *West Asset Management, Inc.,* the Commission alleged that a leading debt collector misrepresented that the collector was a law firm or that its collectors were attorneys; falsely claimed that debtors would be arrested or have property seized if they did not pay, among other false statements; revealed to third parties that a consumer owed a debt; and committed other violations of the FDCPA and the FTC Act.[13]

In *Asset Acceptance, LLC,* the Commission alleged that one of the Nation's largest debt buyers had failed to disclose that debts were too old to be legally enforceable or that a partial payment would extend the time a debt could be legally enforceable; misrepresented that consumers owed a debt when it could not substantiate its representations; provided information to credit reporting agencies, while knowing or having reasonable cause to believe that the information was inaccurate; repeatedly called third parties who did not owe a debt; and committed other violations of the FDCPA, the FTC Act, and the Fair Credit Reporting Act.[14]

In addition to its civil penalty cases, which must be referred to the Department of Justice for filing, the Commission has brought a number of court actions, filed under Section 13(b) of the FTC Act, against debt collectors in which it sought injunctions and restitution or disgorgement of ill-gotten gains.[15] In these cases, the Commission has focused on swiftly halting exceptionally egregious debt collection conduct. Accordingly, in many of these cases the Commission has sought and obtained preliminary relief, including ex parte temporary restraining orders with asset freezes, immediate access to business premises, and appointment of receivers to run the debt collection business. The Commission also has sought and obtained strong permanent relief to ensure that defendants do not engage in unlawful debt collection practices in the future. In certain cases, this relief includes banning individuals or entities from engaging in debt collection. Since January 1, 2010, the FTC has obtained such bans against 12 entities and individuals.

For example, in *FTC v. Forensic Case Management Services, Inc.,* the Commission obtained a wide array of relief against a debt collector charged with engaging in a host of egregious conduct, such as threatening to physically harm consumers and desecrate the bodies of their dead relatives; threatening to kill consumers' pets; using obscene and profane language; revealing consumers' debts to third parties; and falsely threatening consumers with lawsuits, arrest, and wage garnishment.[16] In addition to obtaining the strong preliminary relief discussed above, the Commission ultimately secured substantial monetary judgments against the defendant debt collection enterprise and a complete ban on future debt collection activity, along with other permanent injunctive relief.[17]

The Commission has also used its Section 13(b) authority to halt debt collectors from employing unfair and deceptive tactics to recover on payday loans. In a typical payday loan, consumers receive cash in exchange for their personal checks or authorization to debit their bank accounts, and the lenders agree that consumers' checks will not be cashed or consumers' accounts will not be debited until a designated future date. Payday loans have high fees and short repayment periods, which translate to high annual rates, and they often are due on the borrower's next payday.

In two recent cases, the FTC alleged that a payday loan operation violated the law by attempting to garnish consumers' wages without first obtaining a State court order. Although Federal law allows Federal agencies to require employers to garnish employees' wages without a State court order if the employees owe money to the

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[12] *United States v. Expert Global Solutions, Inc.,* No. 3-13 CV 26 2611-M (N.D. Tex. July 8, 2013).

[13] *United States v. West Asset Mgmt., Inc.,* No. 1-11-cv-0746 (N.D. Ga. Mar. 14, 2011); *see also,* FTC, "Leading Debt Collector Agrees To Pay Record $2.8 Million To Settle FTC Charges", Mar. 16, 2011, available at *http://www.ftc.gov/opa/2011/03/wam.shtm.*

[14] *United States v. Asset Acceptance LLC,* No. 8:12-cv-182-T-27EAJ (M.D. Fla. Jan. 31, 2012); *see also,* FTC, "Under FTC Settlement, Debt Buyer Agrees To Pay $2.5 Million for Alleged Consumer Deception", Jan. 30, 2012, available at *http://www.ftc.gov/opa/2012/01/asset.shtm.*

[15] Under the FTC Act, the Commission must refer to DOJ all cases in which it seeks civil penalties. DOJ then has 45 days to decide whether to file the case in its own name or return it to the FTC to file. Section 16(a) of the FTC Act, 15 U.S.C. §56.

[16] *FTC v. Forensic Case Mgmt. Servs., Inc.,* No. LACV11-7484 RGK (C.D. Cal. Jan. 4, 2013).

[17] *See,* FTC, "FTC Settlement Obtains Permanent Ban Against Abusive Debt Collection Operation", Jan. 17, 2013, available at *http://www.ftc.gov/opa/2013/01/rumson.shtm.*

Federal Government, private parties must obtain a court order to garnish wages. In the first case—*FTC v. LoanPointe, LLC*—the FTC alleged that defendants sent documents to the employers of consumers that mimicked the documents that the Federal Government sends in collecting on its own debts, thereby falsely representing that the defendants (like the Federal Government) were entitled to garnish wages without obtaining a court order.[18] The FTC won a preliminary injunction and summary judgment against the defendants. In awarding summary judgment to the FTC, the United States District Court for the District of Utah observed that wage assignment clauses like the ones used by the defendants may cause "substantial harm to consumers" by imposing administrative costs on employers, pressuring consumers into forgoing valid defenses against the debt collection attempt, jeopardizing consumers' job stability, and obtaining wage earnings that may otherwise go to basic necessities.[19]

In the second case—*FTC v. Payday Financial LLC*—the FTC alleged that a payday loan operation that purportedly has an association with a Native American tribe employed similar wage garnishment tactics.[20] The FTC specifically alleged that the defendants were sending documents to consumers' employers that falsely represented that, under tribal laws, they were entitled to garnish wages without obtaining a State court order. The case is currently in litigation.

Recently, the FTC also has used its Section 13(b) authority to shut down so-called "phantom" debt collectors. Phantom debt collectors engage in wholesale fraud by attempting to collect on debts (often related to payday loans) that either do not exist or are not owed to the phantom debt collectors. In 2012, the Commission filed three cases against alleged phantom debt collectors, and obtained strong preliminary injunctive relief in each case.[21] In these three cases, the Commission alleged that the callers carrying out the phantom debt collection schemes pretended to be law enforcement or other Government authorities, and falsely threatened to arrest and jail consumers immediately if they did not agree to make payments. One of the cases ended with the Commission obtaining a permanent injunction—including bans prohibiting the defendants from working in debt collection—and a substantial monetary judgment.[22] The FTC continues to litigate the other two cases.

As a supplement to its Section 13(b) and civil penalty cases, the FTC also files amicus briefs to offer the Commission's views on important questions of law. For example, in December 2011, the Commission, in a joint brief with the United States and the CFPB, urged the Supreme Court to deny certiorari in *Fein, Such, Kahn and Shepard, PC v. Allen*,[23] a consumer class action against several entities involved in a mortgage foreclosure action. The putative consumer class alleged that the law firm that brought the foreclosure action violated the FDCPA by sending a letter to the consumer's attorney that demanded payment for fees that were much higher than the amounts allowed under State law. The district court and court of appeals rejected the law firm's motion to dismiss the FDCPA claims, which argued that communications to a consumer's attorney are categorically excluded from the FDCPA.

Among other things, the joint brief advocated that the Supreme Court deny certiorari in Fein because the decision of the Third Circuit is consistent with the plain language of the FDCPA, the structure of the FDCPA, and the underlying purposes of the FDCPA. In January 2012, the Supreme Court denied the petition for certiorari.[24]

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[18] *FTC v. LoanPointe, LLC,* No. 2:10-CV-00225-DAK (D. Utah Dec. 9, 2011); *see also,* FTC, "Court Rules in Favor of FTC; Orders Defendants in Payday Lending Case To Pay More Than $294,000 for Illegal Garnishment of Consumers' Paychecks", Dec. 19, 2011, available at *http://www.ftc.gov/opa/2011/12/getecash.shtm.*

[19] *FTC v. LoanPointe, LLC,* No: 2:10-CV-00225-DAK (D. Utah Sept. 16, 2011) (decision and order) (relying in part on *Am. Fin. Servs. Assoc. v. FTC,* 767 F.2d 957, 974 (D.C. Cir. 1985)).

[20] *FTC v. Payday Fin., LLC,* No. 3:11-cv-03017-RAL (D.S.D. filed Sept. 6, 2011); *see also,* FTC, "FTC Action Halts Allegedly Illegal Tactics of Payday Lending Operation That Attempted To Garnish Consumers' Paychecks", Sept. 12, 2011, available at *http://www.ftc.gov/opa/2011/09/payday.shtm.*

[21] *FTC v. American Credit Crunchers, LLC,* No. 12cv1028 (N.D. Ill. Oct. 10, 2012); *FTC v. Broadway Global Master Inc.,* No. 2:12-cv-00855-JAM-GGH, (E.D. Cal. filed Apr. 3, 2012); *FTC v. ProCredit Group LLC,* No. 8:12cv586 (MD. Fla. filed Mar. 19, 2012).

[22] *See,* FTC, "U.S. Defendants Who Allegedly Abetted Fake Debt Collector Calls From India Agree To Settle FTC Charges", Oct. 23, 2012, available at *http://www.ftc.gov/opa/2012/10/americancredit.shtm.*

[23] Brief for the United States as Amicus Curiae, *Fein, Such, Kahn and Shepard, PC v. Allen,* No. 10-1417 (U.S. Dec. 23, 2011).

[24] *Fein, Such, Kahn and Shepard, PC v. Allen*, No. 10-1417, 2012 WL 171347 (U.S. Jan. 23, 2012) (mem.) (order denying cert.).

II. Education and Public Outreach

The FTC works to educate consumers and businesses about their rights and obligations under the FDCPA. The FTC's consumer education efforts include English and Spanish written materials, one-on-one guidance, and speeches and presentations. In 2012, the Commission supplemented its distribution of this information by launching two consumer-oriented Web sites: consumer.ftc.gov and consumer.gov. Consumer.ftc.gov offers straightforward articles about a variety of consumer protection topics, as well as videos, educational games, and a blog that invites consumer comments. The site addresses debt collection topics such as how to spot a fake or "phantom" debt collector, the rights consumers have when debt collectors are seeking to recover on time-barred debts, and the rights and responsibilities related to the debts of a deceased relative. Consumer.gov is the product of extensive work in coordination with the Center for Applied Linguistics to write and design the site for audiences with low literacy levels. Features include short videos, infographics, and read-along audio. The site includes basic material on a variety of consumer protection topics, including a section about dealing with debt collectors.

Business education is also a priority for the FTC. Over the past 3 years, the Commission's business outreach activities have included developing and distributing business education materials, delivering speeches, participating in panel discussions at industry conferences, and providing interviews to general media and trade publications. These efforts help to ensure that debt collectors understand their responsibilities under the FDCPA.

Finally, as part of the FTC's Legal Services Collaboration project, FTC staff regularly meets with legal services providers to discuss various consumer protection issues, including the FTC's work in the debt collection arena. These discussions allow staff to better identify debt collection practices that are causing serious consumer harm and to improve the development and direction of our educational resources. Recent legal services outreach efforts have included providing information in a webinar hosted by the National Association for Consumer Advocates and convening legal services providers and Government agencies for a Washington, DC, conference that had a strong focus on debt collection issues. The FTC also organizes "Common Ground" conferences that bring together legal services providers and law enforcement agencies to discuss a wide variety of consumer protection issues, including debt collection.

III. Research and Policy Development Activities

The third prong of the FTC's debt collection program is research and policy initiatives. Since 2010, the FTC has continued to monitor and examine the debt collection industry and its practices through workshops, reports, and policy statements.

As part of these initiatives, the FTC hosts roundtables and conferences on topics ranging from the use of new debt collection technologies to the flow of information in the debt collection process. For example, the FTC held a series of nationwide roundtable discussions and public comments examining debt collection litigation and arbitration proceedings, which culminated in the publication of a 72-page report in July 2010.[25] Drawing from the roundtables and comments, the report concluded that the system for resolving consumer debt collection disputes is broken and recommended that States consider significant reforms to improve efficiency and fairness to consumers. These reforms included measures to increase consumer participation in debt collection lawsuits, requiring collectors to include more debt-related information in legal complaints against consumers, and assigning the burden of proving that debts are not time-barred to collectors.

In April 2011, the FTC hosted a workshop on the use of new technologies in the debt collection process.[26] The workshop brought together industry representatives, consumer advocates, regulators, researchers, and other stakeholders to discuss issues related to a variety of debt collection technologies. For example, participants discussed the use of mobile telephones, email, social media, text message services, information gathering tools, dialers, databases, and payment portals. Topics included: how technologies have evolved in recent years; how technologies may affect the accuracy of underlying debt information or in correctly identifying debtors; the costs and benefits to consumers and collectors of employing newer technologies for

[25] FTC, "Repairing a Broken System: Protecting Consumers in Debt Collection Litigation and Arbitration", July 2010, available at *http://www.ftc.gov/os/2010/07/debtcollectionreport.pdf*.

[26] "Debt Collection 2.0: Protecting Consumers as Technologies Change" (April 2011). A transcript and related materials are available at *http://www.ftc.gov/bcp/workshops/debtcollectiontech/index.shtml*.

information collection and storage, communication, and payment; and whether any related legal or policy reforms might enhance consumer protection.

On January 30, 2013, the FTC released a report based on the first empirical study of the debt buying industry.[27] The report was based on extensive and detailed information that the FTC had obtained from nine of the Nation's largest debt buying companies, and analyzed more than 5,000 portfolios of consumer debt containing nearly 90 million accounts with a face value of $143 billion. The report noted significant consumer protection concerns in the debt buying industry and concluded that there is room for improvement in the information debt buyers possess when they contact consumers and try to collect debts. The report explained that debt buyers typically receive some information from creditors at the time a debt is purchased, but seldom receive certain key information and documentation about the debt, such as the dispute history or outstanding balances broken down by principal, interest, and fees. The report also found that consumers disputed an estimated one million or more debts that debt buyers attempted to collect.[28] In addition, the report found that debt buyers only verified about half of the debts that consumers disputed.[29]

Most recently, building on these reports and the related source material, on June 6, 2013, the FTC cohosted a roundtable with the CFPB to examine the flow of consumer data throughout the debt collection process.[30] The roundtable brought together consumer advocates, credit issuers, collection industry members, State and Federal regulators, academics, and other stakeholders to exchange information on a range of issues. The topics discussed included the amount of documentation currently available to different types of collectors, the costs and benefits of providing consumers with additional disclosures about their debts and debt-related rights, and information issues related to debt collection litigation.

In addition to its workshops and reports, the FTC also issues statements clarifying the FTC's debt collection enforcement policy. For example on July 27, 2011, the FTC published a statement of enforcement policy regarding the collection of the debts of deceased persons. In general, debts survive the death of the debtor for a period of time, and a debt collector may seek payment of the debt from the estate of the deceased.[31] Pursuant to Section 805 of the FDCPA, however, debt collectors in this situation may only communicate with the deceased's spouse, parent (if the deceased was a minor), guardian, executor, or administrator.

State probate laws, however, have evolved considerably since the passage of the FDCPA, and now, in many cases, confer authority on individuals other than those set forth in Section 805 to wind up the estate, including the payment of the decedent's debts. For this reason, the FTC's policy statement clarifies that the agency will not take enforcement action under the FDCPA or the FTC Act against companies solely for communicating with someone who is authorized to pay debts from the estate of the deceased, regardless of whether that person has been appointed as an "executor" or "administrator". The statement also emphasizes that debt collectors may not mislead relatives to believe that they are personally liable for a deceased consumer's debts, or use other deceptive or abusive tactics.

IV. Coordination With the Consumer Financial Protection Bureau

The Dodd-Frank Wall Street Reform and Consumer Protection Act, which created the CFPB, directs the FTC and the CFPB to coordinate their law enforcement activities and promote consistent regulatory treatment of consumer financial products and services, including debt collection.[32] The Commission has done so by working closely with our partners at the CFPB to coordinate efforts to protect consumers from unfair, deceptive, and abusive debt collection practices. In addition, in January 2012, the FTC and CFPB entered into a memorandum of understanding that supplements the requirements of the Dodd-Frank Act and creates a strong and comprehensive framework for coordination and cooperation.[33]

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[27] FTC, "The Structure and Practices of the Debt Buying Industry", Jan. 2013, available at *http://www.ftc.gov/os/2013/01/debtbuyingreport.pdf.*

[28] Id. at 38.

[29] Id. at 39.

[30] A recorded Web cast of the event and related materials are available at *http://www.ftc.gov/bcp/workshops/lifeofadebt/*.

[31] *See,* FTC, "Statement of Policy Regarding Communications in Connection With the Collection of Decedents' Debts", 76 Fed. Reg. 44915 (July 27, 2011).

[32] *See,* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 §1024(c)(3) (July 21, 2010).

[33] Memorandum of Understanding Between the Consumer Financial Protection Bureau and the Federal Trade Commission, January 2012, available at *http://ftc.gov/os/2012/01/120123ftc-cfpb-mou.pdf.*

As reflected in the memorandum of understanding, FTC and CFPB staff have worked with one another to coordinate their debt collection programs. These efforts include regular staff meetings to discuss ongoing and upcoming law enforcement, rulemaking, and other activities; sharing debt collection complaints; cooperation on consumer education efforts in the debt collection arena; and consulting on debt collection rulemaking and guidance initiatives. For example, as discussed above, the two agencies recently hosted a joint workshop on issues related to the life cycle of consumer information as it flows through the debt collection process.

V. Conclusion

Thank you for the opportunity to discuss the Commission's debt collection program. We look forward to continuing to work with Congress and this Subcommittee on this important area.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR TOOMEY FROM COREY STONE

Q.1. Director Cordray recently announced that the CFPB will soon be engaging in FDCPA rulemaking. What key areas of the FDCPA will this rulemaking address? Are there any areas of the FDCPA that the CFPB considers off the table? Because the FDCPA is over 35 years old, should comprehensive FDCPA reform be left to the Congress rather than the CFPB?

A.1. In the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Congress amended the Fair Debt Collection Practices Act (FDCPA) to give the Consumer Financial Protection Bureau (Bureau) the authority to prescribe rules with respect to the collection of debts by debt collectors to implement that law. The Dodd-Frank Act also empowered the Bureau to issue rules applicable to covered persons and service providers (including debt collectors and creditors collecting their own debts) identifying unlawful unfair, deceptive, and abusive acts and practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service, including requirements for the purpose of preventing such acts or practices. The Dodd-Frank Act also authorized the Bureau to prescribe rules to ensure that the features of any consumer financial product or service, both initially and over the term of the product or service, are fully, accurately, and effectively disclosed to consumers in a manner that permits consumers to understand the costs, benefits, and risks associated with the product or service, in light of the facts and circumstances.

The Bureau is in the early stages of a debt collection rulemaking. Specifically, the Bureau is planning to publish an Advance Notice of Proposed Rulemaking (ANPR). The ANPR would elicit information about the nature and extent of consumer protection problems in debt collection as well as the advantages and disadvantages of various solutions to those problems. A broad focus in an ANPR is prudent in light of the many consumer protection concerns that have been raised relating to debt collection and the limited legislative changes and absence of regulation of debt collection practices since the FDCPA was enacted in 1977.

The information that the Bureau receives from consumer groups, industry, and others in response to the ANPR will help identify topics that the Bureau might include in a proposed rule. At this time, the Bureau has not made a determination about which topics to cover in a proposed rule, although improving data integrity in the debt collection system and updating debt collection law to reflect technological advances are among the topics addressed.

Q.2. My office is aware of a number of industry self-regulatory initiatives, such as the certification program established by the Debt Buyers Association earlier this year. Are you aware of these efforts? Have you considered the impact of these industry-based solutions instead of pursuing a Government solution through FDCPA rulemaking?

A.2. The Bureau is aware of the Debt Buyers Association's (DBA) certification process, and during its development we provided infor-

mal comments on the program jointly with the Federal Trade Commission staff. The Bureau applauds the DBA's efforts.

As we move forward, the Bureau will be taking consideration of the DBA's certification program as it evaluates what rulemaking activity to undertake in this area.

Q.3. What consumer cost-benefit analysis is the CFPB doing with respect to the proposed debt collection rulemaking? When evaluating what is best for consumers, is the CFPB taking into account the costs that will be passed onto the consumers who are current on their obligations in order to benefit late consumer debtors?

A.3. The Bureau's goal in the debt collection rulemaking will be to develop rules that protect consumers without imposing unnecessary or undue burdens on those who must comply with those rules. The Bureau will consider the costs, benefits, and impacts of any rules it issues on consumers and businesses, including creditors, debt buyers, and debt collectors. As part of that evaluation, the Bureau will assess whether the cost of complying with proposed debt collection rules could ultimately be reflected in higher prices and decreased availability of consumer credit and other consumer financial products and services.

To obtain information about the costs and benefits of proposed rules, the Bureau anticipates requesting public comment on these issues in the ANPR and any Notice of Proposed Rulemaking it may issue.

Q.4. The CFPB has stated that attorneys who collect debts on behalf of their clients can be subject to the CFPB's rulemaking and supervision.

Does the CFPB intend to examine, supervise or regulate the conduct of attorneys who are litigating matters before a court if they are defined as a "covered person" or "service provider"?

A.4. As the Bureau explained in its rule defining larger participants in the consumer debt collection market that are subject to the Bureau's supervision, the Bureau has authority "regarding the offering or provision of a consumer financial product or service . . . that is . . . offered or provided by [an] attorney . . . with respect to any consumer who is not receiving legal advice or services from the attorney in connection with that product or service." 12 U.S.C. §5517(e)(2)(B). Consumer debt collection is a consumer financial service that is provided "with respect to" the consumers who owe, or are claimed to owe, the debts subject to collection. An attorney engaged in consumer debt collection, as defined by the Bureau's larger-participant rule, does not provide "legal advice or services" to those consumers; to the contrary, the attorney represents clients with interests that may be or are likely to be adverse to those consumers. Such an attorney can therefore be properly subject to the Bureau's authority.

As the larger-participant rule further explained, though, not every occasion on which an attorney seeks money from a consumer, including in the course of litigation, constitutes consumer debt collection. Consumer debt collection, under the Bureau's larger-participant rule, includes only the activities of persons whose principal business activity is debt collection or that regularly engage in debt collection.

With respect to rulemaking, the Bureau notes that the Supreme Court has held that an attorney can be a debt collector subject to the FDCPA, and that the FDCPA does regulate to a certain degree the litigation activities of such an attorney. A rulemaking under the FDCPA could properly regulate the debt collection activities of an attorney subject to the FDCPA.

Q.5. The CFPB has stated that it "continues to adhere to the position that it can compel privileged information pursuant to its supervisory authority" and has noted that submission of privileged information to the CFPB will not be construed as a waiver of the privilege, even when the CFPB shares, for example, attorney–client privileged information with other Federal and State regulators. Does the CFPB have any concern that attorney's clients may have significantly less sense of security when sharing sensitive information with their counsel, knowing that it may be demanded by the CFPB and disclosed to other regulators? Does the CFPB feel that demanding such information may have the effect of limiting advice sought from attorneys relating to compliance questions?

A.5. The Bureau believes that the submission of privileged information to the Bureau does not constitute a waiver of privilege and will not have any significant adverse impact on supervised entities' willingness to share sensitive information with counsel. Congress has provided for this nonwaiver of privilege by statute, see 12 U.S.C. §1828(x), as it has for other agencies—and other agencies have been mandating the production of privileged information from their supervised entities for decades. The production of privileged information to the Bureau does not change the nature or status of the information shared between an institution and its counsel.

Q.6. The CFPB has issued "Action Letters" designed for use by consumers in responding to collection attempts by collection agencies or attorneys.

One of the Action Letters may request that the collector provide more information to the consumer than is required by law. If a collector provides only the information that is required by law, and the consumer subsequently files a complaint with the CFPB because all the information requested was not provided, how will the CFPB respond? What will the CFPB do if the collector still refuses to provide more information than lawfully required?

A.6. The Bureau has received feedback on this point from one industry association, and has solicited feedback from others, as well as from consumer advocacy groups, and will review these comments to better understand any concerns and take appropriate action if necessary.

It is important to note that in the background to the letter, the Bureau highlights that the debt collector is not legally required to provide all the information that a consumer may request, and that this would not necessarily mean that the collector has violated the law. However, prudent use of the letter may facilitate communication between the collector and the consumer by providing the consumer with information that would allow them to recognize the debt and verify that the balance is correct.

Q.7. Another Action Letter allows consumers to demand that the debt collector or collection attorney cease communicating with them. Is the CFPB concerned that the act of providing this letter to consumer may be construed as encouragement to use the letter even though circumstances may not warrant its use?

A.7. The Bureau has also received feedback on this point, and it is also considering whether to revise this letter. It is important to note that the Bureau does advise consumers of the potential consequences of using this letter, and suggests it may be prudent for them to request more information prior to using it.

Q.8. Can the CFPB state how much of its budget, in dollars and as a percentage, are directed toward consumer debt collection issues?

A.8. The Bureau's activities related to debt collection involve a variety of personnel and support services across multiple divisions. Bureau staff take complaints from consumers about debt collection issues; examine debt collection firms for compliance with consumer financial protection laws; research trends in the debt collection industry; and help educate consumers about the their rights related to debt collection. While we don't have a specific amount budgeted for debt collection activities, the budget for each of the Bureau's divisions, including staffing levels and key investments, is available on consumerfinance.gov. The Bureau has made and will continue to make investments to support ongoing work related to debt collection.

Q.9. The CFPB opened a portal to accept consumer debt collection complaints. The identity of the companies being complained of, and the nature of the complaints, is publicly available on the CFPB's Web site.

Will the CFPB take any reasonable steps to ensure the validity of the complaints before posting the complaint, and the company's identity, on its Web site?

If a company can show that a complaint was invalid, will the complaint be removed from the CFPB's Web site?

A.9. The Bureau began handling debt collection complaints on July 10, 2013. In addition to debt collection complaints, the Bureau also handles complaints on credit cards, mortgages, bank account and services, private student loans, consumer loans, credit reporting, and money transfers.

Information about consumer complaints is available to the public through the Bureau's public Consumer Complaint Database. The database currently contains consumer complaints on credit cards, mortgages, bank accounts and services, private student loans, consumer loans, credit reporting, and money transfers.

While the Bureau now accepts debt collection complaints, these complaints are not currently posted on the Consumer Complaint Database. When the Bureau accepts complaints about a specific product or service, it first evaluates the initial data about the complaints to consider whether any specific policy changes are warranted regarding what information gets published on complaints about that product or service before beginning to publish those complaints. The Bureau will evaluate debt collection complaint data in anticipation of publishing those complaints accordingly.

The Bureau maintains significant controls to authenticate complaints. Each complaint is checked to ensure that it is submitted by the identified consumer or from his or her specifically authorized representative. Each submission is also reviewed to determine if it is a complaint, an inquiry, or feedback (submissions in the latter two categories are not forwarded to companies for handling). Further, each complaint is checked to identify duplicate submissions by a consumer who has already submitted a complaint on the same issue to the Bureau. Finally, complaints are only routed to companies when they contain all the required fields, including the complaint narrative, the consumer's narrative statement of his or her request, and the consumer's contact information. Companies view and respond to complaints using their secure web portals, which they also use to notify the Bureau if a complaint has been routed incorrectly. As we work to continually improve our complaint routing accuracy, such notifications from companies are key to routing complaints to the correct companies and increasing routing accuracy over time.

Complaints will only be posted on the Consumer Complaint Database after the company responds confirming a commercial relationship with the consumer or after they have had the complaint for 15 calendar days, whichever comes first. Complaints can be removed if they do not meet all publication criteria. Additionally, the database does not include information about consumers' identities.

The Bureau's entire Policy Statement on the Disclosure of Consumer Complaint Data (78 Fed. Reg. 21218 (April 10, 2013)) is available at *http://files.consumerfinance.gov/f/201303_cfpb_Final-Policy-Statement-Disclosure-of-Consumer-Complaint-Data.pdf.*

Q.10. States play an active role in regulating the consumer debt industry. The States' licensing system, the Nationwide Mortgage Licensing System (NMLS), allows the States to track licensees of all types from State-to-State on a nationwide basis. State regulators have begun using NMLS as the licensing platform for all types of nondepository financial service providers, including the Pennsylvania Department of Banking and Securities, which uses NMLS for licensing debt management companies.

I have cosponsored legislation to enhance confidentiality and privilege for information shared among regulators in this system. Would it be beneficial to extend the privilege and confidentiality protections for mortgage-related information contained in the NMLS and which is shared by State and Federal regulators to information in the NMLS relating to all types of nonbanks?

A.10. The Bureau is committed to establishing and maintaining productive working relationships with State bank and nonbank regulators, and understands the importance of protecting the confidentiality of information that may be shared through such coordination efforts. To this end, the Bureau has entered into information-sharing and cooperation Memorandums of Understanding (MOU), requiring the safeguarding of confidential information, with most State bank and nonbank regulators that participate in the Nationwide Mortgage Licensing System (NMLS). Moreover, the Bureau recently entered into a State Coordination Framework to es-

tablish a process for coordinated Federal/State consumer protection supervision and enforcement of entities providing consumer financial products or services that are subject to concurrent jurisdiction of the Bureau and one or more State regulators.

The Bureau believes that steps to better facilitate the sharing of information among regulators by extending the confidentiality safeguards and privilege protections applicable to information placed in the NMLS to additional nonbank activities could potentially be beneficial.

Q.11. I understand that the CFPB and the FTC have formed a debt collection working group to coordinate the respective activities between your agencies. Can you tell me more about this working group? Is this group considering how to pursue the bad actors without burdening legitimate businesses with undue regulatory requirements?

A.11. The Bureau and the Federal Trade Commission (Commission) formed a debt collection working group to pool resources, experiences, and ideas in our efforts to protect consumers in debt collection. The working group convenes periodically to discuss ongoing investigations, recent legal developments, and trends in the debt collection industry. This is part of a sustained effort by the Bureau and the Commission, as partners in consumer protection, to advance a united front against unlawful practices in debt collection.

As stated during the hearing, the Bureau recognizes that debt collectors are an essential part of the credit system. With that in mind, the working group coordinates activities to prevent duplicative and burdensome regulatory action against businesses in the debt collection industry. By working together, the agencies can harmonize their regulatory efforts in a way that is effective for consumers and efficient for businesses.

The coordination between the Bureau and the Commission is in accordance with the January 20, 2012, MOU between the two agencies. A copy of that MOU is available at *http://files.consumerfinance.gov/f/2012/01/FTC.MOUwSig.1.20.pdf.*

RESPONSES TO WRITTEN QUESTIONS OF SENATOR TOOMEY FROM JAMES REILLY DOLAN

Q.1. States play an active role in regulating the consumer debt industry. The States' licensing system, the Nationwide Mortgage Licensing System (NMLS), allows the States to track licensees of all types from State-to-State on a nationwide basis. State regulators have begun using NMLS as the licensing platform for all types of nondepository financial service providers, including the Pennsylvania Department of Banking and Securities, which uses NMLS for licensing debt management companies.

I have cosponsored legislation to enhance confidentiality and privilege for information shared among regulators in this system. Would it be beneficial to extend the privilege and confidentiality protections for mortgage-related information contained in the NMLS and which is shared by State and Federal regulators to information in the NMLS relating to all types of nonbanks?

A.1. I am not familiar with the specific confidentiality provisions in the NMLS or how State regulators are using the information. I agree, however, that regulators generally should properly safeguard any confidential information they receive, thereby promoting confidence by industry and ensuring public trust. With respect to the FTC's practices in that regard, as a general matter, when the FTC requests and obtains information from targets and third parties pursuant to Civil Investigative Demands, it handles the information consistent with its published policies and procedures for handling nonpublic information. Disclosure is permitted only pursuant to procedures for use set forth in the Commission's Rules of Practice or as set forth by statute. *See,* 15 U.S.C. §§46 and 57b-2, and 16 CFR §§4.9–4.11. The Commission generally does not require targets to produce privileged information. *See,* 16 CFR §2.11.

Q.2. I understand that the CFPB and the FTC have formed a debt collection working group to coordinate the respective activities between your agencies. Can you tell me more about this working group? Is this group considering how to pursue the bad actors without burdening legitimate businesses with undue regulatory requirements?

A.2. The FTC is primarily a law enforcement agency that takes legal action when the Commission has reason to believe that an entity has been engaging in deceptive or unfair acts or practices.

To coordinate such law enforcement efforts against debt collectors with the CFPB, which has concurrent law enforcement jurisdiction, staff-level FTC and CFPB attorneys have formed an informal working group. Staffs from the two agencies meet regularly to discuss matters related to the agencies' debt collection enforcement actions and the CFPB's examination authority, including current or upcoming investigations and examinations, enforcement actions, and enforcement or examination-related activities. These discussions generally are confined to ensuring the agencies do not engage in unduly duplicate investigations and examinations and to ensuring the staffs are consistent in how we interpret existing laws. The working group generally does not discuss new regulatory requirements.

Apart from the two agencies' efforts to coordinate our law enforcement and supervision missions through the working group, the CFPB recently announced it intends to issue an Advance Notice of Proposed Rulemaking to implement the Fair Debt Collection Practices Act (FDCPA). Although the FTC has not had rulemaking authority to implement the FDCPA since its enactment in 1977, the FTC has a long history of enforcing the FDCPA and hosting informative workshops discussing hot debt collection topics. The FTC is likely to share its FDCPA enforcement experiences with the CFPB during the rulemaking process and comment on any regulatory proposals. In doing so, the FTC is likely to consider whether the proposals address problematic conduct without imposing undue regulatory burdens by considering whether they target unfair or deceptive acts or practices. It is well established that an act or practice is unfair if it causes or is likely to cause substantial consumer injury that is not reasonably avoidable by consumers and that is not outweighed by countervailing benefits to consumers or

to competition. Likewise, an act or practice is deceptive if it is likely to mislead a consumer acting reasonably under the circumstances and the act or practice is material.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

STATEMENT OF THE OFFICE OF COMPTROLLER OF THE CURRENCY

Introduction

Chairman Brown and Ranking Member Toomey, please find below a statement for the Subcommittee hearing record regarding the Office of the Comptroller of the Currency's (OCC) supervision of debt collection and debt sales practices of national banks and Federal savings associations (collectively, banks). Lending is a central part of the business of banking. It is the means by which banks and savings associations meet the credit needs of the customers and communities they serve. With lending comes the risk of some of that debt going unpaid. While banks have a responsibility to their shareholders to minimize and recover losses on their unpaid debts, they must do so in a safe and sound manner that complies with applicable laws and consumer protections.

Since the beginning of his term, Comptroller Curry has stressed the importance of banks effectively managing the operational risks associated with their activities. Debt collection and the sale of charged-off debt raises operational and reputational risks that the agency expects institutions to manage effectively and in a manner that ensures customers are treated fairly.

The process of debt collection actually begins with the issuance of the loan. When current, that debt is collected through the routine payment and servicing of the loan. When delinquent, collection involves additional efforts that can involve internal collections by the bank, collection on behalf of the bank by a third party (referred to as debt placement), or the sale of the debt to a third party debt collector, where the bank no longer retains a legal interest in the debt. Improving debt collection practices and establishing effective controls reduce risks facing banks but also provide important consumer protections by ensuring debt collectors (banks or third parties) seek the right amounts of repayment from the right borrowers in the appropriate manner. This statement provides an overview of the OCC's supervision of consumer debt collection and debt sales activities of banks. It provides a brief description of the scope of debt collection and debt sales activity within the Federal banking system, a description of ongoing supervisory concerns and actions, and a discussion of policy implications.

Scope of Debt Collection and Debt Sales Activity Within the Federal Banking System

As providers of consumer credit, banks are in the business of lending money to be repaid with interest. They underwrite the loans and price them according to the risk associated with that lending and the customers' creditworthiness. A certain percentage of the loans that banks make go unpaid. Under the Interagency Uniform Retail Classification and Account Management Policy guidelines, banks must charge off open-ended retail credit loans, such as credit cards, once they have become 180 days past due.[1] When a bank charges off a debt, it realizes a loss, but the borrower generally continues to have an obligation to repay the loan. At that point, the bank faces a business decision on how to recover that loss or not to pursue collection of the debt. Debt collection may take several forms, including continued efforts by the bank to collect it on its own, the hiring of a third party to collect the debt on its behalf, or the sale of the debt to an unaffiliated third party, which generates a partial recovery. While banks are expressly authorized to conduct debt collection activities,[2] that decision must involve a consideration of all of the legal, reputational, and operational risks associated with the debt and the collection activity. The remainder of this statement focuses on one aspect of banks' debt collection activities, debt sales.

The majority of bank debt sales activity is concentrated among the 19 largest banking organizations, with the five largest making up about 82 percent of the annual total average sales of debt. On average, the 19 largest banking organizations have sold about $37 billion in charged-off debt sales in each of the past few years.

To provide some context to this number, the total retail credit portfolio for these 19 banks averaged $2.5 trillion each of the last 5 years. During that period, their combined annual charge-offs on these portfolios averaged $93.2 billion. The amount of retail debt charged off in recent years has fallen significantly as the economy has

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[1] *See,* OCC Bulletin 2000-20, "Uniform Retail Credit Classification and Account Management Policy", *http://www.occ.gov/news-issuances/bulletins/2000/bulletin-2000-20.html.*

[2] *See,* "Activities Permissible for a National Bank, Cumulative", *http://www.occ.gov/publications/publications-by-type/other-publications-reports/bankact.pdf.*

improved, with charge-offs declining from $130 billion in 2010 to $67.8 billion in 2012, a decline of more than 48 percent.

The vast majority of debt charged off by these large financial institutions and sold to third party debt collectors involves delinquent debt related to credit cards, but also includes other types of consumer credit such as auto, home equity, mortgage, and student loans.

The value of debt sold to third party debt collectors likewise varies significantly based on the age of the debt, the completeness and quality of records related to the debt, previous work done to collect the debt, and the amount of debt being sold overall (supply). Recently, charged-off debt has sold for between $.05 and $.10 for every dollar of most types of debt. That price has increased lately as the overall supply of debt sold has declined.

The volume of charged-off debt sold by the largest banks has decreased over the past few years. The drop reflects both the improvement in portfolio quality and a decision by some banks to limit or curtail their debt sales due to the heightened reputation and legal risks such activity can pose.[3]

Ongoing Supervisory Concerns and Actions

The OCC expects all national banks and Federal savings associations to have policies and procedures in place to manage their debt collection activities effectively. This includes managing the operational and reputational risks, and complying with all relevant consumer protection laws. When banks sell debt, the agency expects them to have policies, procedures, and practices that result in the third party treating customers fairly and consistently with the expectations of the banks and regulators. Even though a bank may have sold a consumer's debt to a third party, consumers often continue to view themselves as the bank's customers and may have other relationships with that bank. As a result, the debt collector's behavior affects the bank's reputation. Failure to implement proper controls and governance that effectively manage these activities represent safety and soundness and compliance concerns for the OCC. The Comptroller's Handbook on "Other Consumer Protection Laws and Regulations" describes a bank's obligations under the Fair Debt Collection Act when conducting debt collection activities.[4] The OCC has also published guidance to banks that provides principles for effectively managing risks associated with vendors and third-party service providers, which also applies to third-party vendors collecting debt on behalf of the banks (debt placement relationships) and is also relevant to their relationships with buyers of their debt (debt sales relationships).[5]

The OCC has expressed concern about operational risk at banks on a number of occasions.[6] While operational risk includes a range of activities, the Comptroller specifically raised concerns with debt collection in May 2012 when he noted that the OCC has "seen institutions outsourcing such functions as debt collection but not taking adequate care to ensure that the third-party contracted to perform those functions follows the laws and regulations governing them."[7]

The OCC's current interest in debt collection and debt sales activities stems from our 2010 examination work on mortgage servicing and foreclosure practices that revealed weak governance of third-party vendors, including notaries and affiants, and poor documentation practices more generally. Because of the similarities in processes and heavy reliance on third parties, outside attorneys, notaries, and affiants, the agency was concerned that similar weaknesses might be present in other retail lending activities. As a result, the OCC commenced a review of debt collection and sales activities across the large banks it regulates in April 2011, focusing primarily on notary and affiant practices. The review sought assurance that bank management had implemented necessary governance and control processes in this area. Throughout the summer of 2011, additional work continued in this area stressing the agency's concerns and communicating them to large bank management.

Through its more recent work on debt sales, the OCC identified a number of best practices that OCC large bank examiners are incorporating into their supervision of debt sales activities. A copy of these best practices is included in the appendix to this statement. The OCC uses such best practices and insights gained from its

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[3] *See,* "Chase Halts Card Debt Sales of Crackdown", *American Banker,* July 1, 2013. *http://www.americanbanker.com/issues/178__126/chase-halts-card-debt-sales-ahead-of-crackdown-1060326-1.html*

[4] *See,* "Comptroller's Handbook on Other Consumer Protection Laws and Regulations", August 2009. *http://www.occ.gov/publications/publications-by-type/comptrollers-handbook/other.pdf*

[5] *See,* OCC 2001-47, "Risk Management of Third Party Relationships", *See, http://www.occ.gov/news-issuances/bulletins/2001/bulletin-2001-47.html.*

[6] *See,* Remarks by Deputy Comptroller for Operational Risk Carolyn DuChene, *http://www.occ.gov/news-issuances/speeches/2013/index-2013-speeches.html.*

[7] *See, http://www.occ.gov/news-issuances/speeches/2012/pub-speech-2012-77.pdf.*

on-site supervisory activities to inform the development of policy rules and guidance that may be more applicable to a broader range of financial institutions. As described later in this statement, efforts are currently underway to develop such guidance.

The best practices document provides a practical description of effective risk management practices examiners should expect to see in large banks with debt sales activities. Such practices should include the establishment of detailed policies and procedures to govern debt sales practices consistently across the organization. Those policies and procedures should:

- require financial analysis of why selling the debt is a better option than collecting debt internally;
- identify types of accounts that should not be sold and specify quality standards and quality control for debt that is sold, emphasizing the accuracy of the account balances;
- ensure the purchase and sale agreements clearly delineate roles and responsibilities of all parties for fair debt collection;
- require detailed documentation to ensure accurate and reliable information is provided to the debt buyer at the time of purchase;
- specify internal bank documentation retention practices; and
- address due diligence requirements of third parties to ensure compliance with the bank's own policies and procedures. [8]

Due diligence reviews and ongoing monitoring of potential debt buyers are particularly important in managing the reputational risk associated with debt sales activities. Appropriate due diligence reviews should occur before the sale. The reviews should answer questions such as whether debt buyers have appropriate licenses; whether there are existing regulatory and legal actions against the debt buyer or its owners; and whether they are in good standing. In addition to these general governance activities characteristic of sound risk management, the document also includes a variety of specific actions that reflect best practices seen by examiners across large banks:

- *Establish oversight committee*—an oversight body to monitor third party debt buyers and provide a corresponding single, consistent control structure for overall consumer debt sales within an institution.
- *Use debt buyer scorecards*—enhanced controls to assess legal and reputation risk of the debt buyer that takes into consideration consumer complaints, repurchases, legal actions filed against the company, and other regulatory compliance issues.
- *Maintain account accuracy and documentation*—confirm the accuracy of account balances, confirm marketable title that is free and clear from all liens, and confirm the completeness and accuracy of account documentation prior to debt sales.
- *Use clear, consistent contract terminology*—use boilerplate contract language across lines of businesses when appropriate.
- *Provide sufficient documentation*—sufficient documentation will allow fair and informed collection of debts including relevant customer account codes and explanation of codes that should alert a debt buyer to special handling of certain accounts (e.g., attorney handling, etc.).
- *Limit the resale of debt*—contractually limiting the ability of the third party to resell the debt to another entity allows the bank to control who ultimately will pursue collection from "their" customers and helps prevent legal validity and ownership questions later.
- *Limit the litigation strategy*—banks should evaluate the litigation strategies of debt buyers, consider selecting debt buyers who limit their use of litigation, or use contractual provisions or other means to limit the use of litigation by buyers of their debt.
- *Maintain quality Management Information Systems*—establish appropriate management reporting that tracks debt sales, sales price, and repurchase causes and volume.

[8] We recognize that debt buyers generally are not third-party vendors subject to OCC jurisdiction. Nonetheless, many of the principles enunciated in connection with risk management of third party vendors are relevant to ensuring that a bank has adequate policies and procedures in place to manage risks associated with debt sales.

- *Conduct periodic reviews*—depending on past practices and controls, a look-back review may be required to determine if prior practices resulted in consumer harm.

Specific debt sales practices vary from bank to bank as does the degree to which banks have implemented controls and procedures consistent with those in the best practices document. Weaknesses in debt sales activities stem from several sources. Many of the largest institutions have acquired other institutions, resulting in data quality and integrity issues and a collection of acquired systems that have been difficult to integrate. In some cases, customer account history in these legacy portfolios is not complete.

Consistent with the OCC's heightened expectations for large banks overall, the agency is raising its expectations with regard to the banks' oversight and management of their debt sales activities. For example, while banks continue to work through integration issues, the OCC has emphasized the need for rigorous quality control processes and strong audit programs. The OCC has planned supervisory activities in the largest banks to assess policies, internal monitoring, and oversight of debt sale programs. Where OCC has been informed of planned Consumer Financial Protection Bureau (CFPB) reviews, resident OCC teams will collaborate with CFPB bringing both a safety and soundness and a consumer protection focus to these reviews. Where examiners find unsafe and unsound practices, practices that fail to comply with applicable laws or regulations, or practices that fail to meet our heightened expectations; the OCC will take appropriate supervisory action, including enforcement actions when warranted. Where the agency becomes aware of concerns with nonbank, third party debt collectors, it will refer those issues to the CFPB, which has jurisdiction over those types of entities.

Policy Implications

While supervisory action continues, the OCC recognizes the need for clear, actionable, and effective policy regarding debt sales among all national banks and Federal savings associations that engage in this activity. The OCC is in the process of developing supervisory guidance that outlines safe and sound banking principles that should be followed in connection with sales of charged-off consumer debt. The guidance will outline risk management expectations for banks so they can appropriately assess and prudently manage the operational, compliance, and reputational risks associated with this activity and implement appropriate practices to address and mitigate those risks.

The OCC expects a bank's sale of charged-off consumer debt to be structured and operated in a prudent and safe and sound manner that continues to ensure fair treatment of the affected customers. The OCC's guidance will detail the principles that OCC-supervised institutions will be expected to apply in their risk management processes, policies, and procedures regarding disposing of charged-off consumer debts. The principles articulated in the guidance will provide banks with appropriate flexibility in their business decisions regarding nonperforming consumer debts, while ensuring that their practices do not enable third party debt buyers to create unnecessary hardships for consumers through their actions after the acquisition of these charged-off debts.

Conclusion

Debt collection is a fundamental part of the business of lending. While banks must carefully underwrite the loans they make by considering the ability and willingness of the borrower to repay that debt, lending retains the inherent risk of borrowers failing to repay their debt. When that occurs, banks have the responsibility to attempt to collect that debt and to recover losses associated with that bad debt. They must do this in a manner that is not only safe and sound, but fair to their customers and in compliance with applicable laws and regulations.

In seeking to recover their losses, banks should exercise particular care when they choose to sell that debt to third party debt collectors. Selling debt to third party debt collectors carries particular compliance, reputational, and operational risks. The OCC has highlighted these risks on a number of occasions and while the industry continues to heal from the credit and capital market challenges of the financial crisis, it is evident that these risks are gaining increasing prominence. For this reason, the OCC has raised its expectations for banks to provide effective risk management over all facets of their operations and activities. Meeting those expectations will require additional effort and investment on the part of the banks, but we are confident that they can meet those expectations, and we will insist that they do.

Appendix 1 -- Debt Sales / Best Practices

Topics

I. Background
II. Policies and Procedures
III. Third Party Due Diligence—Vendor Management
    - Initial and Ongoing
IV. Quality Control and Audit—Internal Controls
V. Contract Terminology
    - Account accuracy
    - Initial and subsequent documentation requests
    - Repurchase risk
    - Litigation limits
VI. Accounting and Reserves
VII. Best Practices
VIII. Debt Placements

I. Background

Banks have used debt sales (i.e., charged-off assets) as a management tool to control problem credit resolutions and improve recovery numbers in a timely and cost effective manner. In a debt sale, accounts are sold outright to a third party with the sales price generally based on a small percentage of the outstanding balances and the third party retaining 100 percent of the collected amount. Debt sales are generally arranged through an individual bulk sale or contractual forward-flow agreements. Debt sales require increased due diligence and enhanced controls to limit the bank's reputation and legal risks.

II. Policies and Procedures

A sound management control structure includes detailed policies and procedures to promote a consistent process across the organization. Items to consider within an effective policy or procedures include:

- The policy should describe who is responsible for debt sales across the organization (e.g., Corporate Credit, Ops Risk, Steering Committee, etc.).
- Require the involvement of various bank risk personnel in the debt sale approval process to ensure all risks are considered (i.e. compliance, information technology, credit, legal, collections, finance, recovery, information security, etc.). Each debt sale should go through a formal approval process that is similar to a product approval process.
- Require a financial analysis of why selling the debt is better than collecting the debt internally.
- Detail documentation requirements to ensure accurate and reliable information is provided to the debt buyer at time of purchase. In addition, the policy should outline internal bank documentation retention standards.
- The policy should address initial third party due diligence requirements and ongoing due diligence monitoring requirements.

- Require affirmative sign-off by a quality control review function that the debt sale assets meet the characteristics of the purchase and sale agreement and account balances are accurate.
- Outline accounts that should not be sold. Items for consideration include: SCRA; minors (date of birth); settled; deceased with no remaining responsible party; accounts in disaster areas; pending bankruptcy; fraud; accounts close to statute of limitations; accounts lacking clear title; accounts lacking proof of right-to-cure or notice of intent-to-sell letters; balances comprised largely of interest and fees; cease and desist accounts; debts where payments were recently received; and, accounts in ongoing loss mitigation programs (short sales, deed in lieu; etc.).

III. Third Party Due Diligence—Vendor Management

Strong debt sale oversight includes an established initial and ongoing due diligence process of third party debt buyers to help control and limit legal and reputation risk. Management should establish minimum criteria for approving debt buyers and should consider the following:

- Do debt buyers have appropriate licenses to operate across various state jurisdictions?
- Is the debt buyer an established business? What is the length of time the debt buyer is required to be in business by bank standards?
- Does the debt buying entity have audited financial statements? Are they financially sound and not under undue financial distress?
- Are any regulatory or legal actions currently taken against the debt buyer or its owners/principals raising concerns or issues? Are the debt buyers and owners/principals in good standing (e.g., National Association of Retail Collection Attorneys (NARCA))?
- Are collection activities primarily performed in-house or are they outsourced? What activities can be outsourced—bankruptcy filing, repossessions, litigation activities, skip tracing, etc? Does the company off-shore collection processes?
- Determination of how often legal actions are performed by the debt buyer in an effort to collect debt (consider placing litigation limits within the contract)?
- For forward flow agreements, can the debt buyer demonstrate the needed liquidity to purchase future debt sales?
- Does the debt buyer carry sufficient insurance (i.e. commercial liability and errors and omissions policy)?
- Are debt buyers prohibited from reselling accounts? If they are not prohibited, what additional controls are required within the original purchase and sales agreement?
- Management should maintain a file on approved debt buyer with supporting documentation to meet OCC vendor management expectations. See *OCC Bulletin 2001-47 Third Party Relationships: Risk Management Principles* for additional information.

Management should consider the following items when performing an onsite inspection of the debt buying entity:

- Business culture;
- Management and business structure;

- Regulatory and compliance—FDCPA, SCRA, FCRA, Telephone Consumer Protection Act, BK, Fraud, and Deceased;
- Quality of internal quality control function;
- Qualified legal staff;
- How consumer complaints are handled and tracked;
- Collection training—handbooks, procedures, and job aids;
- Consumer privacy policy;
- Information, data, and physical security;
- Regulatory communication;
- Communications are state compliant (i.e., letters, phone calls); and,
- Call or collection attempt frequency.

Ongoing due diligence should consider:

- Reviewing annual financial statements of the buying entity to ensure ongoing financial strength.
- The buying entity and its principal/owners remain in good standing.
- If there are any significant changes in processes, operations, or personnel.
- The volume and type of consumer complaints, as well as applicable remediation.
- The volume and reason of repurchases.

IV. Quality Control and Audit—Internal Controls

A strong risk structure includes a quality control function that evaluates debt sales prior to the sale. This function should evaluate "data scrubs" to validate and ensure account data is complete and accurate and the account data is updated from the system of record. A transaction sample at an account level should be completed prior to the debt sale. In addition, quality control should ensured account characteristics are maintained as specified in the purchase and sales agreement. Finally, quality control should assess the reason accounts are repurchased after a debt sale is completed, and determine if additional controls are required.

Audit should evaluate compliance with debt sale policy or procedures and evaluate vendor management compliance. Audit or quality control should ensure the credit bureau reporting is updated and accurate reflecting the sale or transfer of the debt.

V. Contract Terminology

Management should consider having a standard (i.e., boilerplate) debt sales contract for bulk and forward flow debt sales for use across business lines to ensure consistent debt sales treatment. Contract language should confirm the accuracy of account balances, confirm marketable title that is free and clear from all liens, and confirm the completeness and accuracy of account documentation. Account documentation should be sufficient to allow the debt buyer to collect accounts in the normal course of business without having to request additional documentation; however, the contract should address when additional documentation requests are required (e.g., litigation). Best practice would provide subsequent information requests for no charge, or a minimal charge once a certain threshold is reached. The bank needs to avoid the appearance of

not providing the debt buyer with sufficient and appropriate information to collect debt in compliance with federal and state regulations. In this regard, bank management must supply relevant codes and an explanation of the codes (e.g., codes that indicate special handling—don't call at work, attorney handling, etc.).

The contract should spell out the debt buyer must comply with the various consumer laws and standards, such as: FDCPA; FCRA; UDAP, TCPA (Telephone Consumer Protection Act); SCRA; cease and desist—no calls at work; etc. The contract should spell out when and under what circumstances the bank will repurchase accounts. In addition, it should allow the bank the ability to conduct ongoing, at least annual field visits. Finally, a best practice is to limit the volume of accounts the debt buyer can litigate and spell this out within the contract.

VI. Accounting and Reserves

Management should determine if reserves are required given the size and type of debt sales and expected repurchase risk or losses. Reserves should be established in accordance with GAAP. In addition, maintaining standard contract language would assist in the reserve process helping to eliminate the need to review each debt sale individually for different terms and conditions.

VII. Best Practices

- *Debt buyer scorecards*—enhanced controls to assess legal and reputation risk of the debt buyer that takes into consideration consumer complaints, repurchases, legal actions filed against the company, and other regulatory compliance issues.
- *Established oversight committee*—an oversight body to oversee third party debt buyers and corresponding control structure.
- *Contract terminology*—confirm the accuracy of account balances, confirm marketable title that is free and clear from all liens, and confirm the completeness and accuracy of account documentation. Also, the use of boilerplate contract language across lines of businesses when appropriate.
- *Documents*—provide sufficient documentation to the debt buyer that will allow the collection of debts including relevant codes and explanation of codes (e.g., attorney handling, etc.). Some banks are now providing account statements for each account to support account balances.
- *No resale of debt*—limiting the ability of the third party to resell the debt to another entity. By not limiting the resale of debt, the bank does not control who ultimately will collect on "their" customers and the documentary paper trail may become corrupted over time, calling legal validity and ownership into question.
- *Limiting the litigation strategy*—banks should evaluate the litigation strategies of debt buyers and determine when and how often this strategy is used. Does it take into consideration the borrower's ability to pay, is it a model based approach, or is the initial action to litigate all accounts at the very beginning?
- *MIS*—establish appropriate management reporting tracking debt sales by LOB, sales price, and repurchases risk - along with the reason for repurchases.
- *Look-back*—depending on past practices and controls, a look-back review may be required to determine if prior practices resulted in consumer harm.

Debt Placements

Sometimes debts are placed with a third party in an effort to improve collections prior to selling the debt. These debts placements are collected on the bank's behalf with the third party retaining a percentage of the collected amount. Management should establish appropriate policies, procedures, and controls around these debt placements to demonstrate appropriate oversight and due diligence. Many items in this document are also relevant to debt placements.