

*Finding New Ways to Motivate Them: Debt
Collection Laws and Alternative Communication
Strategies*

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Types of State Collection Agency Laws

- 29 states mandate licensure or registration of collection agencies and impose practice restrictions.
- 3 states impose more minimal notification requirements before operating a collection agency
- 5 states have no licensing/notification requirement but impose practice restrictions.
- 13 states require neither licensure/notification nor impose collection agency-specific practice restrictions.
- 3 municipalities also have collection agency laws of note: the District of Columbia, Buffalo and New York City (the latter two also require licensure).

Scope of State Collection Agency Laws

- Many states follow the federal FDCPA for practice restrictions.
- But important differences exist.
- These differences can result in a company satisfying the federal FDCPA but nonetheless running afoul of state law.

Broader Application of State Collection Agency Laws than Federal FDCPA

- Some states apply their collection agency laws to companies that service performing debts. For example:
 - Idaho: if a company collects performing debts for another, and does not use the other company's name in its collection efforts, a license is required.
 - Massachusetts: collecting performing debts for another triggers licensing requirement.
 - Maryland, North Dakota, Wisconsin: state regulators have informally advised that a license is required to collect performing accounts for another company.

Broader Application (cont'd)

- Trend toward application of state law to passive debt buyers.
- NYC, NC, MD, IO
- Commerce Clause: recent case law (*MidWest Title Loans, Inc. v. Mills*, 2010 U.S. App. LEXIS 1929 (7th Cir. Jan. 28, 2010)) suggests that courts may be willing to accept constitutional challenges to application of a state law to an out-of-state entity that purchases delinquent debt via an out-of-state transaction and that does not directly service the purchased debt.

Broader Application (cont'd)

- “De facto” employee exemption based upon FTC interpretation of federal FDCPA.
- Application to states uncertain. In most states, there is no guidance suggesting the exemption does or does not apply to state law.
 - Some states most likely would adopt the FTC’s interpretation, based on statutory language that state law should be interpreted in accordance with the federal FDCPA.
 - Other states are silent on the matter and have indicated through informal conversations that it would be wrong to assume that the FTC’s “de facto” employee exemption applied to state law.

Broader Application (cont'd)

- Some state collection agency practice restrictions apply to original creditors collecting in their own name.
- Usually not an issue because the prohibitions that would generally apply to original creditors encompass conduct that is unfair and deceptive and, therefore, arguably would also be prohibited under the state's UDAP law.

More Extensive Disclosure Obligations Under State Law

- Some states impose disclosure requirements beyond those found under the federal FDCPA. For example:
 - Arizona: regulations provide that “[w]ithin five days after the initial communication with the debtor, a collection agency shall obtain, and be able to inform the debtor of: 1. The name of the creditor; 2. The time and place of the creation of the debt; 3. The merchandise, services, or other value provided in exchange for the debt; and 4. The date when the account was turned over to the collection agency by the creditor.” Ariz. Admin. Code R20-4-1514(A) (emphasis added).
 - Arkansas: requires that in every communication, a collection agency disclose, among other things, the name of the creditor to whom the debt is owed. 031-00 Ark. Code R. §§ 001(XIV).
 - California: mandates a specific notice with the first written communication. Cal. Civ. Code § 1812.700(a).
 - District of Columbia: mandates that every communication contain the same disclosures that are required for the first communication under the federal FDCPA. D.C. Code § 28-3814(f)(2).
 - New York City: provides that “[i]n any permitted communication with the consumer, [a debt collection agency must] provide: i. a call-back number to a phone that is answered by a natural person, ii. the name of the agency, iii. the originating creditor of the debt, iv. the name of the person to call back, and v. the amount of the debt at the time of the communication.” New York City, New York, Code § 20-493.1.

More Restrictive Communication Requirements Under State Law

- Some states restrict communications beyond that required by the federal FDCPA.
 - For example, some states impose a limit on the number of calls that can be made.
 - Massachusetts: no more than two calls per week at the borrower's residence and no more than two calls per month at any other place. 209 Mass. Code Regs. § 18.14(1).
 - Washington: no more than three calls per week. Wash. Rev. Code § 19.16.250(12).
 - Other states impose greater restrictions on calls to a borrower's place of employment.
 - Arizona: no contacting borrower at place of employment unless "a reasonable attempt to contact the debtor at the debtor's residence has failed." Ariz. Admin. Code R20-4-1512(A).
 - New Hampshire: unlawful to contact a borrower at his place of employment unless efforts to reach the borrower at his residence have been unsuccessful and, even then, may only send a single letter to the place of employment or make no more than one call per month. N.H. Rev. Stat. § 358-C:3.

Exemptions Available

- Banks
 - Twenty-six states, plus the City of Buffalo, exempt banks, including out-of-state, state-chartered banks
 - Six of these states include subsidiaries of the bank within the exemption: FL, ID (subject to some limiting language), IL, MA, NC, RI
 - Thirteen states, plus NYC, do not exempt banks (or their subsidiaries)
- Mortgage Lenders/Brokers/Serviceicers
 - Some states exempt licensed mortgage lenders, brokers, or serviceicers (e.g., Arizona, Idaho, Maryland, North Carolina, North Dakota, Oregon, Washington, Wyoming).
- Interstate Communications/Reciprocity
 - Some states will exempt certain collection agencies licensed in another state if their activities in the subject state are only performed through means of interstate communications and the home state reciprocates such exemption (e.g., Colorado, Hawaii, Illinois, Indiana, Michigan, Nebraska, New Mexico, North Dakota, Oregon). In some states, the debt must have been incurred outside of the subject state in order to qualify for the exemption.

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Component Servicers

- Other state licensing laws may apply if component servicer engages in certain activities:
 - contacts consumers to advise them of workout options?
 - takes income or other personal information from the borrower?
 - assists in offering or negotiating terms of a loan modification?
 - calls borrowers to retrieve loan documentation related to a modification?
 - represents that it can help borrowers improve their credit or reduce their debt?
 - accepts fees or payments from consumers?
 - offers credit counseling?

Types of State Licensing Laws

- Collection agency
- Credit services organization
- Credit report organization
- Debt adjustor/manager
- Money transmitter/escrow agent
- Foreclosure consultant/rescue agency
- Loan broker/lender/servicer
- Mortgage loan originator
- Real estate broker

Credit Services/Credit Repair Organization Laws

- Approximately 35 states regulate credit services/credit repair organizations.
- A credit services/credit repair organization typically is defined as a person or entity that, with respect to the extension of credit to others, represents that it can improve a buyer's credit record, history, or rating in exchange for compensation, or obtain an extension of credit for a buyer or provide advice or assistance to a buyer regarding the above.
- Most definitions of "buyer" require that the buyer purchase or be solicited to purchase the services of a credit services/repair organization. Some, however, may not contain this limitation.

Laws That Involve the Receipt or Delivery of Money

- **Debt adjuster or debt management laws** typically define the licensable activity as the planning and management of the financial affairs of a debtor and receiving money to distribute to the debtor's creditors in payment or partial payment of the debtor's obligation for a fee.
- **Money service or transmitter laws** typically apply when a person engages in the business of receiving currency or payment instruments for the purpose of transmission, either domestically or to or from international locations, or both, by wire, facsimile, electronic transfer, courier or otherwise.
- **Escrow agent acts** typically apply to a person or entity who administers escrow for compensation by receiving, holding, and delivering money, other consideration, or instruments affecting title to real property.

Foreclosure Consultant/Rescue Laws

- A handful of states have begun to regulate – and some license – foreclosure consultants
- These laws have defined foreclosure consultant based on activities that may include: (i) promising assistance in connection with avoiding or delaying actual or anticipated foreclosure proceedings or curing or otherwise addressing a default or failure to timely pay with respect to residential mortgage loans (Mass.); (ii) performing, for compensation, acts that adjust the terms of a mortgage loan in a manner not provided for in the original or previously modified mortgage loans (Nevada).

Mortgage Servicer Laws

- Approximately 36 states license entities that service first- or subordinate-lien residential mortgage loans, either in their own portfolios or for others for a fee.
- Many of these laws define servicing narrowly to collecting or receiving payments directly from borrowers to remit to others.
- But there are outliers – see, e.g., Illinois Residential Mortgage License Act.

Loan Broker Laws

- Negotiating, soliciting, arranging, finding (or offering to do so) loan modifications with consumers on behalf of third party noteholders may impose broker licensing obligations.
- Many states have issued guidance indicating that providing loan modification services is subject to these laws:
 - Alabama - any person providing consumer mortgage loan modification services for compensation must be licensed either under the Consumer Credit Act or the Mortgage Brokers Licensing Act. Ala. Emergency Regulation 2009-1A.
 - Florida - to act as a mortgage broker is defined under the Florida Mortgage Brokerage and Mortgage Lending Act to include “for compensation or gain, or in the expectation of compensation or gain, directly or indirectly, accepting or offering to accept an application for a mortgage loan, soliciting or offering to solicit a mortgage loan on behalf of a borrower, negotiating or offering to negotiate the terms or conditions of a new or existing mortgage loan on behalf of a borrower or lender . . .”
 - Massachusetts - negotiating or assisting in the process of obtaining a loan modification by an unlicensed person will trigger mortgage broker (and/or mortgage loan originator) licensing requirements. Industry Letter (April 27, 2009). State regulators have informally confirmed that an entity does not need to be licensed as a mortgage broker if the entity contracts with a servicer to engage in loan modification activities and only gets compensated by the servicer and receives no fee from the consumer.

Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) – Background

- Enacted July 30, 2008.
- Establishes federal minimal standards for licensing and registration for individual “loan originators.”
- State licensing and registration of state loan originators; registration of financial institution/subsidiary loan originators through the Nationwide Mortgage Licensing System & Registry (NMLSR).
- HUD determines whether state system of licensing complies with SAFE Act.
- Model State Law Loan Originator – Individual who takes a residential mortgage loan application or offers or negotiates terms of a residential mortgage loan for compensation/gain (definition used by nearly all states; SAFE Act – uses “and”).

SAFE Act and Modifications

- HUD proposed to include in its definition of a “loan originator” an individual who performs a residential mortgage loan modification that involves offering or negotiating loan terms that are materially different from the original loan.
- The proposal would (if finalized) permit states to extend the deadline for licensing individuals who perform or facilitate only modifications or refinancings under the federal government’s Making Home Affordable mortgage program.
- Without firm HUD guidance, states have taken various approaches:
 - Approximately half the states have asserted a position on the licensing of loss mitigation employees.
 - Approximately 14 jurisdictions have attempted to exclude/exempt from licensing individuals performing loan modification or other loan servicing related activities.
 - Approximately 10 jurisdictions implicitly require those loss mitigation individuals to be licensed but have provided a delayed deadline for that licensing.

Federal Banking Agency Implementation of SAFE Act

- Registered Loan Originator = Individual who meets the definition of loan originator (SAFE Act definition), and is an employee of:
 - A depository institution;
 - A subsidiary that is owned and controlled by a depository institution and regulated by a federal banking agency; or
 - An institution regulated by the Farm Credit Administration
- Must be registered with and maintain a unique identifier through the NMLSR
- Model State Laws/Actual State Laws exempt registered loan originators

Gaps Between Federal Registration Rules and State MLO Licensing Rules

- **Definitional Gap**
- **Timing Transition Gap**
- **De Minimis Gap**

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State UDAP Statutes – An Introduction

- Most states have statutes that protect consumers from unfair and deceptive acts and practices (UDAP) in the course of trade or commerce.
- While the exact requirements vary from state to state, common elements of a UDAP violation generally include: (1) an unfair or deceptive act or practice, (2) occurring in trade or commerce or a consumer transaction, (3) injury to a person's business or property, (4) as a result of the alleged unfair or deceptive conduct (causation).
- Other requirements that states may impose include:
 - unfair or deceptive conduct that affects the public interest (e.g., Washington)
 - justifiable reliance by the consumer (e.g., Texas and Pennsylvania)
- Another variant is the California Unfair Competition Law, which permits a cause of action for the violation of any other law.
- UDAP statutes may provide an additional cause of action for debtors, in addition to FDCPA and state debt collection practice act claims.

State UDAP Statutes – Potential Advantages from Debtor Perspective

- Longer statutes of limitations: many UDAP statutes provide for three- or four-year statutes of limitations, whereas the FDCPA and some state debt collection statutes provide for a one-year statute of limitations period.
 - While courts generally do not allow plaintiffs to pursue UDAP claims based solely on time-barred FDCPA claims, plaintiffs may otherwise be able to assert an independent basis for a UDAP claim. *See Harrington v. CACV of Colorado, LLC*, 508 F. Supp. 2d 128 (D. Mass. 2007) (Massachusetts UDAP provides a separate basis of liability for debt collection practices).
- Several UDAP statutes provide additional remedies that are generally not available under the FDCPA or under certain state debt collection practices statutes: treble/punitive damages and injunctive relief.
- UDAP statutes are generally broadly drafted and may cover creditors collecting their own debt (as well as debt collectors), which the FDCPA does not.
- Where certain state debt collection practice statutes do not provide debtors with a private right of action (see, e.g., New York), plaintiffs may nonetheless argue that they are entitled to relief under state UDAP statutes.

State UDAP Statutes – Basis of Liability

- In a number of states, courts have not yet addressed whether their respective UDAP statute covers debt collection practices.
- *Per se* liability – a number of decisions have found *per se* unfair or deceptive act/conduct under state UDAP statutes for violations of the FDCPA and/or state debt collection laws. Examples include:
 - *Gathuru v. Credit Control Servs., Inc.*, 623 F. Supp. 2d 113 (D. Mass. 2009) (“[a] violation of the FDCPA constitutes a *per se* violation” of the Massachusetts UDAP statute); and
 - *Robinson v. Managed Accounts Receivables Corp.*, 654 F. Supp. 2d 1051 (C.D. Cal. 2009) (because plaintiff stated a claim under the FDCPA and the California FDCPA, complaint also stated a claim under the California UDAP statute).
- Regardless of whether the FDCPA and/or state debt collection practices acts apply, courts may allow plaintiffs to use UDAP statutes to seek recovery for debt collection practices that are not covered by the FDCPA and/or state debt collection laws, but which practices are allegedly unfair, deceptive or fraudulent. Examples include:
 - *Panag v. Farmers Insurance Company of Washington*, 204 P.3d 885 (Wash. 2009) (Washington Consumer Protection Act covers the collection of insurance subrogation claims even where the FDCPA and the Washington state debt collection statute do not); and
 - *Williams v. Edelman*, 408 F. Supp. 2d 1261 (S.D. Fla. 2005) (plaintiff stated Florida UDAP claim for debt collection conduct not actionable under the FDCPA).

State UDAP Statutes – Potential Defenses

- Some UDAP statutes have been interpreted to limit recovery against debt collectors. Examples include:
 - *Walker v. Gallegos*, 167 F. Supp. 2d 1105 (D. Ariz. 2001) (dismissing claim under Arizona Consumer Fraud Act based on alleged misrepresentations in repossession petition; collector's actions were not "in connection with the sale or advertisement of any merchandise" as required by the Act); and
 - *Thinesen v. JBC Legal Group, P.C.*, 2005 WL 2346991 (D. Minn. 2005) (dismissing claim against debt collector under Minnesota Deceptive Trade Practices Act for alleged misrepresentations of amount due; alleged misrepresentations did not concern goods or services).

State UDAP Statutes – Potential Defenses (cont.)

- UDAP statutes often require actual damages and/or “ascertainable loss” as a prerequisite to recovery. Examples include:
 - *Veach v. Sheeks*, 316 F.3d 690 (7th Cir. 2003) (dismissing Indiana UDAP claim as plaintiff suffered no monetary loss); and
 - *Gervais v. Riddle & Associates, P.C.*, 479 F. Supp. 2d 270 (D. Conn. 2007) (“false communications from a debt collector alone, without further damage to a plaintiff, are insufficient to constitute ascertainable loss [under Connecticut UDAP]”).

State UDAP Statutes – Class Actions

- Most states permit consumers to pursue class actions under their respective UDAP statutes.
 - For example, the Massachusetts UDAP statute specifically provides that a party may maintain a class action when (1) the use or employment of the unfair or deceptive act or practice caused similar injury to numerous other persons similarly situated and (2) the putative class representative “adequately and fairly represents such other persons.” Mass. Gen. Laws ch. 93A, § 9(2).
- Some UDAP statutes require consumers to demonstrate reliance on deceptive conduct to recover – such a requirement may be an impediment to certification of a class under Rule 23(b)(3), which requires that common issues predominate over individual issues.
- Additional information regarding class action practice and procedure in each of the 50 states and the District of Columbia can be found in the newly published treatise *State Class Actions: Practice and Procedure*, Aspen Publishers, edited by Matthew G. Ball, Todd L. Nunn, Irene C. Freidel, 2009. This treatise, which includes contributions from over 65 K&L Gates partners and associates across the firm, guides users through each step of class action litigation in the state courts.

State UDAP Statutes – Enforcement Actions

- Many UDAP statutes empower states' Attorneys General to bring enforcement actions.
 - Civil penalties can be significant: e.g., Tex. Bus. & Com. Code § 17.47(c) (up to \$20,000 per violation); N.Y. Gen. Bus. Law § 350-d (up to \$5,000 per violation); Ariz. Rev. Stat. § 44-1531(A) (\$10,000 per willful violation); 815 Ill. Comp. Stat. Ann. § 505/7(b) (up to \$50,000 per violation with intent to defraud); Iowa Code § 714.16(7) (up to \$40,000 per violation).
 - States' AGs can also pursue injunctive relief and restitution for consumers.

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He has also helped new entrants into the financial services arena—such as wireless carriers—navigate federal and state financial laws.

- FDCPA provides clear rules on the use of the following:
 - Collect Telephone Calls
 - Telegram
 - Post Card

- FDCPA doesn't mention:
 - Voice mail
 - Mobile phones
 - SMS (text messages)
 - E-mail
 - Social Networking Sites

Voice Mail

- Do you leave the mini-Miranda?
- Do you identify the company calling, even if it would reveal itself to be a debt collector?

Mini-Miranda Requirement

- *First Communication:* Must disclose that the communication is an attempt to collect a debt and that any information will be used for that purpose.
- *Each Subsequent Communication:* Must disclose that the communication is from a debt collector.
- Many debt collectors use a combined disclosure in all communications. *E.g.:* **“This communication is from a debt collector and is an attempt to collect a debt. Any information will be used for that purpose.”**

Third-Party Communication Rules

- FDCPA restricts disclosures of information about debts to third parties.
- Courts held that a debt collector might violate these restrictions if it left information about a debt on a voice mail.
- Industry Solution: Don't mention debt on the voice mail—which includes omitting the mini-Miranda.

- Beginning in 2005, a series of court decisions held that this violates the FDCPA.
 - *Edwards v. Niagara Credit Solutions, Inc.*, 584 F.3d 1350, 1351 (11th Cir. 2009)
 - *Masciarelli v. Richard J. Boudreau & Assoc.*, 529 F. Supp. 2d 183, 185 (D. Mass. 2007)
 - *Foti v. NCO Fin. Sys., Inc.*, 424 F. Supp. 2d 643, 669 (S.D.N.Y. 2006)
 - *Hosseinzadeh v. M.R.S. Assocs.*, 387 F. Supp. 2d 1104, 1112, 1116 (C.D. Cal. 2005)

So how can a debt collector leave a voice mail message?

- Courts might not be sympathetic to the dilemma:

“Niagara complains that if it is not permitted to leave out of its answering machine messages the disclosure required by § 1692e(11), the result will be that it cannot leave any messages on answering machines. . . . [E]ven if Niagara’s assumption is correct, the answer is that the [FDCPA] does not guarantee a debt collector the right to leave answering machine messages.”
- *Edwards v. Niagara Credit Solutions, Inc.*, 584 F.3d 1350, 1351 (11th Cir. 2009)

SMS and E-mail

- Same issue as voice mail. Some people share accounts, so there is risk of disclosure to third parties.
 - No real “overhearing” risk, which especially concerned some courts with answering machine messages.
- SMS might result in consumer incurring charges. Some state debt collection laws prohibit debt collectors from contacting consumer via a method that will result in the consumer incurring a charge.
 - Arguably limited to situations where a debt collector deliberately causes the consumer to incur a charge.

Social Networking Sites

- Debt collectors/servicers have started to use them
- Good for skip-tracing debtors
- Another way to communicate with debtors
- Likely to become more common as the Facebook generation grows older

Risks of Using Social Networking Sites

- Virtually no authorities on subject.
- It might not be obvious to collectors and other employees what they can and can't do.
- Debt collectors could kill the goose that laid the golden egg: If site operators don't like what debt collectors are doing, they might ban debt collectors.

Which of These Actions Violate the FDCPA?

- Searching for a debtor on Facebook, and then gathering public information.
 - Surprising how much information some people make public.

- Friending a debtor using a bogus account.
 - See, e.g., Ben Popken, “Debt Collectors Using Cute Chicks On Facebook As Bait,” *The Consumerist* (May 5, 2009) (online publication) (available at <http://consumerist.com/2009/05/debt-collectors-using-cute-chicks-on-facebook-as-bait.html>) (last accessed March 2, 2010).

- Friending a debtor using an account in the real name of the collector or other employee.
 - Does the notification of the friend request, which Facebook e-mails to the consumer, a “communication” that needs to include the mini-Miranda?

- Friending friends of the debtor.
 - Being friends with someone’s friend may allow you to access more information about the person.

Other Considerations

- Be sure that your collectors know the difference between private and public communications on Facebook, etc.
- Don't do anything that might be harassing.
 - No inviting consumers to join the "I'm a Deadbeat Loser Group."
 - Remember that for many people a Facebook page is their virtual home.