What Schools Need to Know About Debt Collection Laws

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This presentation is not legal advice regarding any specific situation, product, or service. Consult an attorney for specific legal guidance. Due to time constraints, this webinar will not cover the entire range of potentially applicable laws, which can vary significantly between states.

Overview

1. Federal debt collection law
   a. Definitions
   b. "First party" v. "Third-party" debt collection
   c. Debt Collectors' compliance obligations
   d. What to do?
2. State debt collection law
3. Student loan related debt collection law
4. Best practices for postsecondary schools

Intro and Definitions

- Students are sometimes obligated to make payments to postsecondary schools.
  - These payment obligations may be "debts"
  - Attempts to obtain payment of these "debts" from the student may constitute "debt collection."
  - In some instances, a postsecondary school engaging in debt collection activity may legally be considered a "debt collector."
  - In some instances, those payment obligations may also be "student loans" or "private education loans," in which case the postsecondary school may me deemed "a student loan servicer."
- Each of these terms are legally defined under both federal and many states' laws, and the definitions are often very different.
- My goal with this webinar is to describe how these laws may apply to postsecondary schools and to explain the ramifications to a school if these laws do apply.
- I will also talk briefly about how schools can minimize their regulatory risk when working with external debt collection agencies.

Fair Debt Collection Practices Act

- The Fair Debt Collection Practices Act ("FDCPA") is the Federal law regulating debt collection practices. See, 15 USC §1692.

> It is the purpose of this subchapter to eliminate abusive debt collection practices by debt collectors, to insure that those debt collectors who refrain from using abusive debt collection practices are not competitively disadvantaged, and to promote consistent State action to protect consumers against debt collection abuses.

Fair Debt Collection Practices Act

- "Debt":

  "[A]ny obligation or alleged obligation of a consumer to pay money arising out of a transaction in which the money, property, insurance, or services which are the subject of the transaction are primarily for personal, family, or household purposes, whether or not such obligation has been reduced to judgment."

- "*Any obligation to pay money* arising out of a transaction."
  - "arising out of a transaction" means not just formal loans or extensions of credit.
- Courts have applied this definition expansively:
  - Parking tickets.
  - Rent and utility obligations.
  - Recovery of amount due because of the dishonor of check.

Fair Debt Collection Practices Act

Definitions

- Creditor:
  > "any person who offers or extends credit creating a debt or to whom a debt is owed, but such term does not include any person to the extent that he receives an assignment or transfer of a debt in default solely for the purpose of facilitating collection of such debt for another."
- Any person offering credit.
- Any person to whom a debt is owed.
- Excludes any person who receives an assignment or transfer of a debt *in default* to collect such debt for another.
  - We'll come back to the definition of "in default"

Fair Debt Collection Practices Act

- Debt Collector:

  "any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another. Notwithstanding the exclusion provided by clause (F) of the last sentence of this paragraph, the term includes any creditor who, in the process of collecting his own debts, uses any name other than his own which would indicate that a third person is collecting or attempting to collect such debts.

- Under Federal Law, a debt collector is:
  - A business whose principal purpose is the collection of debt;
  - A person who regularly collects debts owed to another; OR
  - A creditor who uses a "false name" to imply that anyone else is attempting to collect a debt.
- Note that there's not definition of "collection" with respect to the definition of a debt collector.
  - For example, courts have held that filing a lawsuit is "debt collection"

Fair Debt Collection Practices Act

- The FDCPA excludes the following from the definition of a debt collector:
  - "any officer or employee of a creditor while, in the name of the creditor, collecting debts for such creditor"
  - "any person while acting as a debt collector for another person, both of whom are related by common ownership or affiliated by corporate control, if the person acting as a debt collector does so only for persons to whom it is so related or affiliated and if the principal business of such person is not the collection of debts"
  - **"**any person collecting or attempting to collect any debt owed or due or asserted to be owed or due another to the extent such activity . . . (ii) concerns a debt which was originated by such person; (iii) concerns a debt which was not in default at the time it was obtained by such person . . ."

Fair Debt Collection Practices Act

First Party v. Third Party Debt Collection

- "Owed to another" but "originated by such person."
  - If an institution offers payments plans managed by a third-party, that third-party can collect on it without being deemed a debt collector if it also originated the debt.
- "Concerns a debt which was not in default at the time it was obtained by such person"
  - A collector or servicer that obtains a debt for collection prior to "default" is not a debt collector, even if the debt goes into default afterwards.

Fair Debt Collection Practices Act

First Party v. Third Party Debt Collection

- What does "default" mean?
  - It depends on who you ask!
  - Courts often look at any applicable state laws.
  - In the absence of state laws, Courts often look at the definition of "default" in the contract creating the debt.
  - Per a 2002 FTC opinion letter (the "DeMayo Letter"):

> We believe that, in the absence of a contractual definition or conclusive state or federal law, a creditor's reasonable, written guidelines may be used to determine when an account is "in default."

Fair Debt Collection Practices Act

First Party v. Third Party Debt Collection

- The FTC's DeMayo Letter also provided an alternative basis for first party debt collection, where the collectors are "*de facto*" employees of the creditor.
- The letter cites the FTC's Staff Commentary to the FDCPA, that the exception from the definition of a debt collector for employees of the creditor

> "includes a collection agency employee who works for a creditor to collect in the creditor's name at the creditor's office under the creditor's supervision because he has become the de facto employee of the creditor."

- The FTC continues:

> The more that agency employees are treated like creditor employees, the more likely it is that we would deem them de facto employees. Whether agency employees -- working on the creditor's premises or on the agency's premises -- are treated enough like creditor employees to become de facto employees of the creditor will depend on the degree of control and supervision exercised by the creditor over the agency employees' collection activity, and how similar that control and supervision is to that exercised by the creditor over its own employees. Relevant facts will include, for example, whether the creditor directly supervises and monitors the collection activities of the agency employees and, if so, how that supervision and monitoring is carried out; whether the creditor trains the agency employees; and whether the agency employees are subject to the same rules, procedures, and disciplinary actions that govern the collection activities of creditor employees.

Fair Debt Collection Practices Act

First Party v. Third Party Debt Collection

- The "debt not in default" exception underlies the so-called "first party" debt collection industry, in which collectors of delinquent but not defaulted debts collect the debt as the creditor, i.e., acting as the "first party" creditor.
  - Because first party debt collectors obtain debts prior to default, they are not a debt collectors subject to the FDCPA.
  - First party debt collectors often communicate with consumers using the creditors name, because, at least in part, the FDCPA's prohibitions against false or misleading representations don't apply..
  - Of course, other legal requirements may still apply.

Fair Debt Collection Practices Act

What if the FDCPA applies?

- The FDCPA imposes numerous obligations on debt collectors. Failure to comply can lead to regulatory action and private litigation. Obligations include:
  - Debt "Validation."
    - Debt collectors must notify debtors of their right to dispute the validity of the debt within 5 days of their initial communication with the consumer.
    - If validation is requested within the 30-day validation period, cannot continue collecting the debt until after it provides validation.
  - Must disclose the "mini-miranda" in communications.
    - "This is an attempt to collect a debt. Any information you provide will be used for this purpose."
  - False or misleading representations and harassment prohibited. Harassment includes making telephone calls:

    "at any unusual time or place or a time or place known or which should be known to be inconvenient to the consumer. In the absence of knowledge of circumstances to the contrary, a debt collector shall assume that the convenient time for communicating with a consumer is after 8 o'clock antemeridian and before 9 o'clock postmeridian, local time at the consumer's location"
  - Cannot disclose the debt to any third party (other than the creditor, a credit reporting agency, or the debtor's or debt collector's attorney).
  - Must comply with debtor's requests to "cease and desist" communications upon request or upon refusal to pay the debt.
  - Cannot communicate with the consumer if the debt collector knows that the consumer is represented by an attorney.

Fair Debt Collection Practices Act

What does all this mean for postsecondary institutions?

- The term "debt" can be interpreted broadly, and may include all kinds of payment obligations, not just formal extensions of credit.
  - Do you know what debts are being collected?
- "Debt Collection" can include more than just communications that demand a payment.
  - Do you know what activities might be deemed debt collection? Transcript withholding? Credit reporting? Sending collection letters? Refusing to provide alumni benefits? Refusing to allow re-enrollment?
- The entity to whom a debt is originally owed is generally not a debt collector under the FDCPA (unless it uses a false name).
  - Do you have affiliates or subsidiaries that may collect on debts for another entity? What is that entity's principal purpose? Make sure that the exemption for affiliates applies.
- A collector that obtains a debt "not in default" is generally not a debt collector.
  - Is the term "default" defined in the applicable contract? Is it legally defined?
  - Do you treat debts differently based on age or other criteria such that a court could infer that you consider the debt to be in default?
- Do you utilize first-party collectors?
  - Are the debts in default when assigned to the first-party agency?
  - Do the collectors qualify as "de facto" employees?

Other Federal Laws

- While outside of the scope of this webinar, note:
  - Unfair, Deceptive, or Abusive Acts or Practices ("UDAAP")
    - CFPB under prior administration tried to apply UDAAP to creditors collection conduct
    - FTC remains aggressive in enforcing UDAP laws (no abusiveness jurisdiction).
  - Bankruptcy code.
    - May prohibit debt collection efforts if a consumer is involved in a bankruptcy proceeding. This may be the case even where the debt is a non-dischargeable student loan.
  - Telephone Consumer Protection Act.
    - Prohibits calls made using an "automated dialing and announcing device" to a consumer's cellular telephone without the prior express consent of the called party.
    - May apply to text messages.
    - May have greater impact you if you "skip trace" or obtain telephone numbers from third-parties.
    - Consumers may revoke consent for texting/automated calls.
    - There are also state versions of the TCPA with different requirements.
  - IRS Code.
    - May require filing a form 1099C if you "forgive" a debt of $600 or more, including upon "a discharge of indebtedness pursuant to a decision by the creditor or the application of a defined policy of the creditor to discontinue collection activity and discharge debt."

State Laws

State Debt Collection Laws

- **Many states' debt collection laws apply to creditors.**
- States use all sorts of different definitions.
- States often apply their debt collection laws to their residents *regardless of where the creditor is located or where the debt was incurred*.
- I can't cover all applicable requirements in this webinar. I'll try to provide a high-level overview of some states' requirements.

State Debt Collection Laws

Some states' definitions of "debt collector":

- California: "debt collector" means any person who, in the ordinary course of business, regularly, on behalf of that person or others, engages in debt collection.
  - Note that the definition doesn't say that the collection is "for another"
  - CA imposes substantive compliance obligations on creditors and on non-creditor debt collectors.
- Illinois: "Collection agency' means any person who, in the ordinary course of business, regularly, on behalf of himself or herself or others, engages in the collection of a debt."
  - There are some potentially applicable exceptions, including for "persons whose collection activities are confined to and are directly related to the operation of a business other than that of a collection agency" and "any person or business under contract with a creditor to notify the creditor's debtors of a debt using only the creditor's name."

State Debt Collection Laws

State Definitions:

- District of Columbia:
  - "Consumer debt" means money or its equivalent, or a loan or advance of money, which is, or is alleged to be, more than 30 days past due and owing, unless a different period is agreed to by the consumer, as a result of a purchase, lease, or loan of goods, services, or real or personal property for personal, family, medical, or household purposes.
  - "Debt collector' means a person, including an original creditor or debt buyer engaging directly or indirectly in debt collection . . .."
  - "Original creditor' means the person that owned a consumer debt at the date of default, or the date of charge-off for credit cards or revolving credit accounts, giving rise to a cause of action for its collection."

State Debt Collection Laws

State Requirements

- State requirements can vary significantly from each other and from the FDCPA. These requirements can include:
  - Restrictions on collecting debts after the end of the applicable statute of limitations.
  - Validation requirements.
  - "Mini-miranda" disclosure requirements.
  - ID Theft investigation requirements.
  - Charging collection or other fees in connection with the collection of a debt.
  - Third-party communications.
  - Communicating with the debtor via email or using social media to collect a debt.
  - Etc.
- There's a lot and we don't have time to fully cover every states' requirements.

Student Loan Laws That May Impact Debt Collection Activities

Federal Student Loan Laws

Federal Student Loan Laws

- If the debt being collected meets the definition of a private education loan, then that debt may also be subject to added federal regulatory requirements.
  - A closed-end loan
  - That is extended to a consumer expressly, in whole or in part, for postsecondary educational expenses, regardless of whether the loan is provided by the educational institution that the student attends.
  - Does not include extensions of credit where the school is the creditor, if:
    - The term of the extension of credit is 90 days or less; or
    - The term of the extension of credit is one-year or less AND no interest rate is applied to the credit balance.
- The Truth In Lending Act imposes various disclosure obligations when a private education loan is originated, which is beyond the scope of this webinar.
- With respect to collecting on a private education loan with a non-student cosigner, note that the Truth In Lending Act requires that:

  > [T]he creditor shall not declare a default or accelerate the debt against the student obligor on the sole basis of a bankruptcy or death of a cosigner.

- The lender must allow the student to designate an individual to have the legal authority to act on behalf of the student obligor with respect to the loan in the event of the student's death.

State Student Loan Laws

State Requirements

- If the debt being collected meets a state's definition of a student loan, then collecting on that debt may also be subject to added restrictions.
- States do NOT use the federal definition, so you may want to check to see if you are a student loan creditor under any applicable state laws.
  - Student Loan creditors must register in some states.
  - Student loan servicers may need a license in some states.
  - State student loan servicing laws may apply.
  - Many states require forgiveness of a student loan upon the death or total and permanent disability of the borrower.
    - Total and permanent disability is sometimes defined as any disability that is expected to last for more than one year.
  - Some states require student loan creditors to have certain documents about a loan before they can refer the debt to a debt collector or have a collection lawsuit brought against the debtor.
  - States may also impose more restrictive debt validation requirements on student loan creditors, servicers, and collectors, including the right to appeal adverse determinations to more senior employees.

What Schools Should Do

Dealing With Collection Agencies

Dealing with collection agencies

- Always have a written contract.
  - Fees. How and when earned, require that funds are deposited into a trust or FBO account in case the collection agency files for BK.
  - If doing first party collections, make sure that the contract is clear about the fact that the accounts are not in default and/or that you're exercised sufficient control over staff that they qualify as de facto employees.
  - Make sure you provide the required documentation of any debt you outsource.
- Compliance audits.
  - Have the right to review the agency's activities for compliance. Use it.
- Insurance.
  - Make sure that the agency's coverage is in-line with your potential risk.
- Termination.
  - Make sure you can terminate for failure to comply with applicable law.
- Privacy and data security.
  - I assume this goes without saying, but, if not, make sure that any collection agency agreement provides for appropriate privacy and data security provisions.
  - If you're subject to FERPA, ensure that you've covered this, too.
  - GLBA's privacy and information security provisions may apply.

Dealing with collection agencies

- A contractual promise to follow the law is a good start.
- They should also promise to maintain internal compliance management systems that are reasonably designed to prevent, detect, and mitigate compliance issues, including:
  - Legal review of collection letters.
  - Employee training and oversight
    - listening to phone calls, escalation, and remedial actions (additional training, bonus clawbacks, or even termination)
  - Effective dispute, debt validation, and ID Theft resolution procedures.
  - Non-discrimination.
    - It is illegal to discriminate on a prohibited-class basis in connection with "any aspect" of a credit transactions, including collection of the debt.
    - Although the federal government has ceased bring so-called "disparate impact" theory cases, states continue to do so.
  - Process for continual updates – some jurisdictions update their laws frequently.
  - Notice to you of regulatory inquiries or investigations or lawsuits that may impact you.
  - If credit reporting, ensure compliance with "Metro 2" guidelines.

What Schools Should Do

- Follow the law.
  - State AGs often act aggressively against perceived debt collection violations.
  - Liability for debt collection violations can be significant in individual and class action lawsuits and can also require payment of attorneys' fees to a plaintiff.
- Build or buy expertise:
  - Compliance isn't easy, but its not rocket science.
  - The requirements aren't always intuitive – "technical" violations are still violations, even if you were "unfair" to your students.
- Don't collect debts if you don't have a good grasp of the technical requirements.
  - Hire a servicer or collection agency.
  - They may be expensive, but not nearly as expensive as a defense attorney.
  - Avoids reputational damage, too.

About me

- Senior regulatory counsel, Sallie Mae and Citizens Bank re private student loan origination, servicing and collection.
- 2x fintech general counsel.
- Special Counsel in the consumer financial services groups at Manatt, Phelps & Phillips, LLP.
- Founder of Joshua Law Firm LLC to provide cost-effective regulatory compliance guidance to schools, student loan servicers, and fintechs.
- Legislative Co-Chair, Board of Directors of the Council of Higher Education Assistance Organizations ("COHEAO").

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For information about state laws relating to student loan creditors, servicers, and collections, see: www.studentloancompliance.com.