

Department of Legislative Services
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FISCAL AND POLICY NOTE
First Reader

Senate Bill 773

(The President)(By Request - Office of the Attorney
 General)

Finance

Consumer Protection - Debt Buyers and Collectors - Restrictions

This bill prohibits a debt buyer or collector acting on behalf of a debt buyer from (1) collecting or attempting to collect an alleged debt under specified circumstances; (2) filing a civil action or initiating an arbitration or other legal proceeding under specified circumstances; and (3) collecting or attempting to collect attorney’s fees or interest under specified circumstances. The bill requires a debt buyer or collector to include a notice in its first written communication with a debtor, and to provide copies of certain records to the debtor. If the debtor fails to request copies of the records described under the bill, it is not an admission of liability on the part of the debtor. Finally, the bill alters the damages for which a debt buyer or collector may be liable.

Fiscal Summary

State Effect: General fund expenditures increase by \$404,100 in FY 2017 for the Commissioner of Financial Regulation in the Department of Labor, Licensing, and Regulation (DLLR) to hire additional examiners and two assistant Attorneys General to implement the bill. Future years reflect annualization and inflation. The Judiciary can handle the bill’s changes with existing resources. The Consumer Protection Division of the Office of the Attorney General advises it can handle any additional workload with existing resources. The bill’s imposition of existing penalty provisions does not have a material impact on State finances or operations.

(in dollars)	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	404,100	506,100	525,500	545,800	567,000
Net Effect	(\$404,100)	(\$506,100)	(\$525,500)	(\$545,800)	(\$567,000)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: The circuit courts can handle the bill's changes with existing resources. The bill's imposition of existing penalty provisions does not have a material impact on local government finances or operations.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The bill defines several terms related to consumer debt collection.

- A “debt buyer” is a person that purchases or otherwise acquires debt from an original creditor (or from a subsequent owner of the debt). A “debt buyer” does not include a check services company that acquires the right to collect on a paper or electronic check instrument, including an automated clearinghouse item that has been returned unpaid to a merchant.
- An “original creditor” is the lender, provider, or other person originally owed or alleged to be owed money by a consumer in a consumer transaction.
- “Principal” is the unpaid balance of a debt or an obligation arising from a consumer transaction that is owed or alleged to be owed to the original creditor. “Principal” does not include interest, fees, or charges added to the debt or obligation by the original creditor or any subsequent owners of a consumer debt.

The bill establishes that a debt buyer (or a collector acting on behalf of a debt buyer) may not collect or attempt to collect an alleged debt if the applicable statute of limitations would prohibit a civil action to collect the debt, unless the debt buyer first provides a notice specified by the bill. In addition, a debt buyer or collector must be able to authenticate the debt, with specified statements and documents, and must have a reasonable basis to believe that the debtor actually owes the debt and the amount being collected is accurate. A debt buyer or collector must also provide the debtor, in the first communication between the debtor and the debt buyer or collector, written notice of the status of the debt that includes specified information about the debt buyer and the debt.

A debt buyer or a collector acting on behalf of a debt buyer may not file a civil action or initiate an arbitration or any other legal proceeding to collect a debt if the applicable statute of limitations on the debt buyer's claim has expired. In addition, a debt buyer or a collector acting on behalf of a debt buyer may not collect or attempt to collect any attorney's fees *unless* the debt buyer has a certified or otherwise properly authenticated copy of the terms and conditions of the agreement between the original creditor and the debtor that (1) are

specifically applicable to the debt being collected; (2) expressly authorize the collection of the attorney's fees; and (3) include all applicable amendments to the agreement.

A debt buyer or collector acting on behalf of a debt buyer may not collect or attempt to collect any prejudgment interest or interest specified in the agreement between the original creditor and the debtor that is *in excess* of (1) the original creditor's charge-off amount or (2) if there has been no charge-off, the amount allegedly owed to the original creditor at the time of the sale of the debt by the original creditor.

A debt buyer or a collector acting on behalf of a debt buyer may, however, collect or attempt to collect any amount of prejudgment interest or interest specified in the agreement between the original creditor and the debtor if:

- the debt buyer has a certified or otherwise properly authenticated copy of the terms and conditions of the agreement that are specifically applicable to the debt being collected and include specified information;
- the original creditor did not stop collecting interest on the debt before the sale of the debt;
- the debt buyer or collector has a breakdown of (1) the original creditor's charge-off amount or (2) the amount allegedly owed to the original creditor at the time the original creditor sold the debt, including principal, interest, and other fees; and
- the debt buyer or collector does not seek an amount that is more than a simple annual interest rate of 6% of (1) the principal of the original creditor's charge-off amount or (2) the amount allegedly owed to the original creditor at the time of the sale of the debt by the original creditor.

A debt buyer or a collector acting on behalf of a debt buyer must include in its first written communication with a debtor a separate, prominent notice stating that the debtor may request copies of specified records about the debt. The notice must include contact information for the debt buyer or collector. It has to specify that the records must be provided at no cost to the debtor.

- For collection of a debt that is past the applicable statute of limitations for a civil action to collect the debt but *not* past the date of obsolescence specified in the Fair Credit Reporting Act, the notice must state that the debt buyer or collector cannot sue the debtor for the debt, but may continue to report it to credit reporting agencies as unpaid for as long as permitted by law.

- For collection of a debt that is past the applicable statute of limitations for a civil action to collect the debt *and* past the date of obsolescence specified in the Fair Credit Reporting Act, the notice must state that the debt buyer or collector cannot sue the debtor for the debt, and will not report it to any credit reporting agency.

In either case, the notice must also state that, if the debtor makes a payment on the debt, admits to owing the debt, promises to pay the debt, or waives the statute of limitations on the debt, the time period in which the debt is enforceable in court may start again.

If the debtor requests any records specified in the required notice, the debt buyer or collector must provide the records to the debtor (at no cost to the debtor) within 10 days after the date of the request. The failure of a debtor to request the records described in the required notice may not be considered an admission of liability on the part of the debtor in any lawsuit or arbitration proceeding.

A collector in violation of the Maryland Consumer Debt Collection Act is liable for the greater of (1) any damages proximately caused by the violation, including damages for emotional distress or mental anguish suffered with or without accompanying physical injury, or (2) statutory damages in the amount of \$1,000.

Current Law: In collecting or attempting to collect an alleged debt, under the Maryland Consumer Debt Collection Act, a collector may not:

- use or threaten force or violence;
- threaten criminal prosecution, unless the transaction involved criminal action;
- disclose or threaten to disclose information that affects the debtor's reputation for credit worthiness with knowledge that the information is false;
- unlawfully contact a person's employer with respect to a delinquent indebtedness before obtaining a final judgment against the debtor;
- unlawfully disclose or threaten to disclose to a person other than the debtor, his or her spouse, or, if the debtor is a minor, his or her parent, information that affects the debtor's reputation with knowledge that the other person does not have a legitimate business need for the information;
- communicate with the debtor or a person related to him in a manner that can be reasonably expected to abuse or harass the debtor;
- use obscene or grossly abusive language in communicating with the debtor or a person related to him;
- claim, attempt, or threaten to enforce a right with knowledge that the right does not exist; or

- use a communication that simulates legal or judicial process or gives the appearance of being authorized, issued, or approved by a government, governmental agency, or lawyer when it is not.

A collector in violation of the Act is liable for any damages proximately caused by the violation, including damages for emotional distress or mental anguish suffered with or without accompanying physical injury.

Violation of the Maryland Consumer Debt Collection Act is also an unfair or deceptive trade practice under the Maryland Consumer Protection Act (MCPA), subject to MCPA's civil and criminal penalty provisions.

An unfair or deceptive trade practice under MCPA includes, among other acts, any false, falsely disparaging, or misleading oral or written statement, visual description, or other representation of any kind that has the capacity, tendency, or effect of deceiving or misleading consumers. The prohibition against engaging in any unfair or deceptive trade practice encompasses the offer for or actual sale, lease, rental, loan, or bailment of any consumer goods, consumer realty, or consumer services; the extension of consumer credit; the collection of consumer debt; or the offer for or actual purchase of consumer goods or consumer realty from a consumer by a merchant whose business includes paying off consumer debt in connection with the purchase of any consumer goods or consumer realty from a consumer.

The Consumer Protection Division within the Office of the Attorney General is responsible for enforcing MCPA and investigating the complaints of aggrieved consumers. The division may attempt to conciliate the matter, issue a cease and desist order, or file a civil action in court. A merchant who violates MCPA is subject to a fine of up to \$1,000 for the first violation and up to \$5,000 for each subsequent violation. In addition to any civil penalties that may be imposed, any person who violates MCPA is guilty of a misdemeanor and, on conviction, is subject to a fine of up to \$1,000 and/or imprisonment for up to one year.

Background: The State Collection Agency Licensing Board, under the Office of the Commissioner of Financial Regulation, licenses and regulates debt collection agencies. In fiscal 2015, the commissioner received a total of 1,579 complaints regarding collection agencies, of which 375 were written complaints.

As reported by the Department of Legislative Services in its full evaluation of the State Collection Agency Licensing Board in 2010, according to a September 2009 report by the U.S. Government Accountability Office, approximately 50% of all retail credit accounts purchased directly from original creditors are eventually resold. The sale of consumer debt (primarily credit card debt) is an increasingly common industry practice, and it is not

uncommon for a consumer's debt to be resold repeatedly over time. Debt buyers typically purchase unpaid consumer debts for cents on the dollar and pursue multiple collection tactics in the hopes of collecting enough unpaid debts to recoup their costs and ultimately turn a profit.

As the unpaid consumer debt is typically purchased at a substantially reduced rate, it is highly unlikely, from a business perspective, that debt buyers receive detailed information about the original debts and underlying contracts when these purchases are made. This is primarily because the amount of work needed for a debt seller or creditor to review individual files and provide such information would prohibit the sale at such low prices.

Typically, debt buyers receive spreadsheets or electronic databases with basic information about the underlying consumer debt, such as the individual's name, home address, outstanding balance, and date of default. Collection law firms have turned to specialized computer software that automatically produces collection letters, summonses, and lawsuits using the information contained in the electronic databases. Once a lawsuit has been filed and a debt collector receives a judgment in litigation, the party can utilize wage and property garnishment mechanisms to collect on the judgment. A July 2010 article in the *New York Times* highlighted a New York debt collection law firm of 14 attorneys that filed 80,878 debt collection lawsuits in 2008 using automated computer software (more than 5,700 cases per lawyer).

An industry that once relied on phone calls and collection notices has discovered that collecting on unpaid consumer debts by filing a massive number of lawsuits is a financially sound business model. In a 2009 investor presentation, Encore Capital Group (Encore), one of the nation's largest debt collection companies, reported that litigation-based collections comprised \$232.6 million of its \$487.7 million in gross collection revenue, making it the largest recovery method of consumer debt collections for the company.

Although debt collection lawsuits are legal when conducted in accordance with State and federal law, the huge volume of lawsuits filed that are based on limited details of the alleged debts can ultimately lead to mistakes and abuses of the court system. In September 2009, the State Collection Agency Licensing Board issued a cease and desist order against Encore, Midland Funding (Midland), and associated entities for engaging in collection agency activities, including civil litigation, without a collection agency license. Furthermore, the companies failed to validate certain debts when challenged by consumers, a violation of both State and federal law. In December 2009, the board reached a settlement with Encore and Midland whereby the companies agreed to pay \$1 million in civil penalties, alter their business practices, and become licensed collectors in the State. According to the Commissioner of Financial Regulation's Office, Encore and Midland filed over 10,000 collection-related actions in Maryland courts from 2007 through 2009.

In January 2010, the board also suspended the collection agency licenses and issued a cease and desist order against Mann Bracken, which is headquartered in Maryland and is one of the largest debt collection firms in the nation. This action, combined with the board's previous action against Midland and other issues related to Mann Bracken's solvency, precipitated the District Court's dismissal of approximately 20,000 to 25,000 lawsuits filed by Mann Bracken on behalf of Midland in the State. The board subsequently revoked the collection agency licenses of Mann Bracken pursuant to a Consent Order issued on August 10, 2010.

State Fiscal Effect: DLLR advises it expects an additional 750 complaints under the bill. The department further advises the commissioner's current complaint staff of 6.0 financial examiners would be unable to resolve the additional complaints within 60 days and, thus, the department requires 3.5 additional financial examiners as a result of the bill. DLLR also notes that investigating consumer claims is a time-intensive process that requires additional legal staff to bring cases to court or settlement. With the expected 750 additional complaints against collection agencies, DLLR anticipates many violations will lead to charges against companies, some of which could be appealed through the Office of Administrative Hearings or other courts. Companies often settle for fines, which must be negotiated by attorneys. Thus, DLLR estimates 2.0 assistant Attorneys General are needed to handle the increased number of investigations.

Thus, general fund expenditures increase by \$404,130 in fiscal 2017, which accounts for the bill's October 1, 2016 effective date. This estimate reflects the cost of hiring 3.5 financial examiners to handle additional complaints brought under the bill, as well as 2.0 assistant Attorneys General to bring cases to court or settlement. The estimate includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Positions	5.5
Salaries and Fringe Benefits	\$375,468
Operating Expenses	<u>28,662</u>
Total FY 2017 State Expenditures	\$404,130

Future year expenditures reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses.

The Consumer Protection Division of the Office of the Attorney General advises that it can likely handle *any* additional complaint volume with existing resources. The Department of Legislative Services advises that additional support could be needed within that office as well; however, this analysis assumes most complaints are handled instead by DLLR.

Small Business Effect: The bill may have an impact on collection agencies that qualify as small businesses by limiting their purchases and collection efforts. Such business could also incur increased legal fees as a result of the bill.

Additional Information

Prior Introductions: None.

Cross File: HB 1159 (The Speaker, *et al.*) (By Request - Office of the Attorney General) - Economic Matters.

Information Source(s): Office of the Attorney General (Consumer Protection Division); Judiciary (Administrative Office of the Courts); Department of Labor, Licensing, and Regulation; Department of Legislative Services

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