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Department of Financial Protection and Innovation *By e-mail to regulations@dfpi.ca.gov*
Legal Division
Attn: DeEtte Phelps, Regulations Coordinator
2101 Arena Blvd.
Sacramento, CA 95834

Re: **Second Draft Text of Proposed Regulations: Debt Collection Licensing Act PRO 01-23**

Dear Ms. Phelps,

This letter is written on behalf of my client base. I am a California attorney who has been practicing in the area of consumer finance since 1982. My clients include approximately 60 banks, savings banks, California Finance Lenders, California Deferred Deposit Transaction Law lenders, retail installment sellers and retail installment sales financing entities, fintechs, residential solar system providers and financiers, servicers of performing portfolios of consumer obligations, and various other entities engaged in offering financial services to consumers and businesses.

I do not represent any collection agencies, debt buyers, or other third-party collectors of delinquent debt portfolios. Nonetheless, many of my clients' activities are, *ipse dixit*, subject to regulation under the Debt Collection License Act (the "Act" or the "DCLA"). As I have previously stated to the Department, the consumer finance ecosystem is more nuanced than a noncontextual reading of the Act would indicate; this has led to significant misunderstandings, inefficiencies, and the fitting of round pegs into square holes in the implementation of the Act. As will be discussed below, this complexity is directly applicable to this Proposal.

**Procedural Objection**

First, I must reiterate that the short time provided for submitting comments precludes a full review of the proposal by my client base. It just takes longer than 15 days to disseminate, explain, discuss, fully staff, digest, analyze, and conform responses from the loan servicing community, and then to draft a workmanlike comment letter. The business entities that are affected by such proposals generally do not have the luxury of having full-time compliance staffs to monitor such

developments; accordingly, it takes some time for their employees and management to receive and absorb such proposals.

Speaking harshly but frankly, this inappropriately short comment period is symptomatic of the Department's lack of understanding or consideration of the complexity and scope of the compliance burdens upon its regulated business entities. DCLA compliance is far from the only compliance structure with which those entities must contend. In this regard, I believe it is fair to note that the Department – not just the DCLA Section - regularly takes months and months to conduct its internal review of all of its tasks: regulatory initiatives, license applications, responses to regulated entities responses to inquiries, etc. Yet, in these situations, no one at the Department runs any risk of adverse financial consequences. By contrast, if a regulated entity misses an opportunity to provide a comment, or provides an inadequate content, the effect on the business entity can be devastating, and people can lose their jobs or their investments. As President Joe Biden stated during one of the Presidential debates in 2016, quoting his father, "I don't expect government to solve my problems for me, but I do expect government to understand them." Therefore, all government agencies, including the Department, owes the business community the respect and understanding of that consideration. At some point, this practice of inappropriately short comment period will rise to the level of an actionable due process issue.

**Substantive Issues**

My substantive comments are limited to the issue of how "net proceeds generated by California debtor accounts" are calculated for purposes of exceptions:

I have no comment as to proposed Section 1850(p)(1), applicable as to debt buyers, none of whom I represent and for whom I do not speak.

Proposed Section 1850(p)(2) seems appropriate and reasonable as to owners of debt.

I express no objection as to proposed Section 1850(p)(3) as that subsection is applicable to true third party, non-servicer debt collectors who are collecting *delinquent* debt on behalf "of another." However, that assessment level is completely inappropriate as to servicers of portfolios of *performing* obligations, to which it also seems to apply. Indeed, since the servicing of nondelinquent debt is beyond the Department's jurisdiction to supervise, it follows that assessments on such debt would similarly be beyond the Department's regulatory reach. Specifically, the description of "net proceeds generated by California debtor accounts" applies to servicers of performing obligations. Those entities, referred to herein and generally in the consumer credit industry as "Loan Servicers," are entities that manage and process the payment process for original obligors and other holders of consumer payment obligations. As described in the basic search tool, Investopedia, "Loan servicers are compensated by retaining a relatively small percentage of the outstanding balance, known as the servicing fee or servicing strip. This fee usually amounts to 0.25 to 0.5 percentage points of each periodic loan payment"

(https://www.investopedia.com/terms/l/loan_servicing.asp#:~:text=Loan%20servicers%20are%20compensated%20by,of%20each%20periodic%20loan%20payment).

As I understand proposed Section 1850(p)(3), the "net proceeds" assessment would therefore be equal to the servicing fee: i.e., 0.25% - 0.5% of each outstanding periodic obligation payment on every performing obligation in California. That is a huge sum of money compared to the amounts proposed in Sections (p)(1) and (p)(2). Yet, this is the transaction model that should be subject to the *lowest* level of scrutiny under the DCLA: the servicing of performing obligations incurred in the normal course of business. These Loan Servicers generally represent the top end of the consumer credit pyramid: the obligees who are in the business of either (i) extending direct credit to creditworthy consumers who are shown by appropriate underwriting to have good histories of performing on their credit obligations, or (ii); selling goods or services to credit-worthy consumers who are shown by appropriate underwriting to have good histories of performing on their credit obligations. These Loan Servicers are in the business of making consumer obligors succeed. These Loan Servicers do not earn any money, nor even recover the funds or the costs of goods and/or services that they have already expended, unless these Loan Servicers perform their contractual duties in a manner that is, both short-term and long-term, consumer-friendly, compliant, and replicable. These Loan Servicers have for years been required to comply with the federal Fair Debt Compliance Practices Act, and the Rosenthal Act, and now are required to comply with the DCLA. They should not be unduly and unfairly taxed by virtue of a that fails to distinguish between their activities and those of industry bottom-feeders.

Therefore, I propose that Section 1850(p)(3) be revised to read as follows:

(3) For all other *California debt collection activity debt collectors that are engaged in the collection of debt that was delinquent at the time the collector began its collection efforts*, this is equal to the amount ~~*a*~~ *the debt* collector receives from its clients, regardless of fee structure, before deducting costs and expenses. For purposes of this section, "client" means the company on whose behalf the debt collector has been contracted to collect on an account, and "delinquent" means more than 90 days past due under the terms of the underlying obligation.

(4) For all other *California debt servicers and/or collection activity debt collectors that are engaged in the collection of debt portfolios that are not more than 15% delinquent, by number of obligations, at the time the collector began its collection efforts*, this is equal to the amount ~~*a*~~ *the debt* collector ~~*receives from its clients, regardless of fee structure,*~~ *collects on delinquent debt in for form of late fees, penalty charges, default interest rate differentials over contract interest rate payments, and any other amounts collected in connection with delinquent debt that would not have been collected for non-delinquent debt,* the from before deducting costs and expenses. For purposes of this section, "delinquent" means more than 90 days past due under the terms of the underlying obligation.

**Further Comments on the Department's Authority Under the DCLA**

I will freely admit that I may have missed some other important issues due to the short time frame afforded to me and my clients for review of this proposal. As is noted above, the Department is well aware of the complexities of staffing policy-related matters: that complexity increases when the staffing must be done across various entity, lines, such as the various stakeholders in the business community who stand to be affected by this regulation. Accordingly, the revisions to the proposed regulations proposed above are made solely for the purpose of ameliorating the possible immediate effect of those regulations upon my clients, and should not be interpreted as endorsement of those regulations nor as my final word on what level of assessment would be appropriate. I expressly reserve the right to change my mind or modify these comments as I receive more information.

Further, I believe that there is significant doubt as to whether the DCLA affords the Department has jurisdiction over Loan Servicers, whose activities are limited to collecting performing portfolios. Many of my more learned colleagues and I continue to maintain that the coverage of the DCLA is limited to the governance of the collection of obligations that are "due and owing," as is set forth in the Rosenthal Act. For that reason, I express must question whether the Department has the authority to make assessments on the servicing of performing obligations by Loan Servicers. In this regard, I will note the strongly relevant analogy that exists under the assessment rules of the California Financing Law (the "CF Law"). Assessments under the CF Law are based on the licensee's licensable activity under the CF Law. Thus, if a licensee is a very large entity with numerous business activities throughout the world, and a small CF Law-governed portfolio, the assessment is based only on the CF Law-governed portfolio. Here, however, by seeking to base the assessment on a Loan Servicer's entire portfolio of serviced obligations, whether fully performing or due and owing, the Department appears to be exceeding both reasonableness and its authority under the DCLA. As the Attorney General has noted, the Rosenthal Act applies only to debts said have become delinquent or are the subject to collection. We have heard assertions from the Department to the effect that the coverage of the DCLA differs from the coverage of the Rosenthal Act, but we have not seen any analysis to that effect with regard to the underlying question of the scope of whether Loan Servicers' activities pertaining to obligations that are not due and owing under the Rosenthal Act are nonetheless somehow subject to the DCLA. This is, I believe, a complex issue and one that is not susceptible of resolution without appropriate consideration and comment, which a 15-day time frame does not afford. Therefore, my request is that the Department consider these comments, formulate a position that takes the issues raised herein into account, and reissues its proposed regulation with an appropriate comment period.

Thank you very much for the consideration of these comments.

Sincerely,

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R. Paul Soter, Jr.

cc: Mary Tome *(By e-mail to mary.tome@dfpi.ca.gov)*