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VIA E-MAIL (regulations@dfpi.ca.gov)

Ms. Sandra Sandoval
Legal Analyst
California Department of Financial Protection & Innovation Division
300 S. Spring Street, Suite 15513
Los Angeles, CA 90013

Re: PRO 05-21 - Comments on California's Debt Collection Licensing Act

Dear Ms. Sandoval:

Please accept this comment letter in response to the California Department of Financial Protection and Innovation's ("DFPI") second request for comment regarding the Debt Collection Licensing Act ("DCLA"). The Acting Commissioner is considering a second rulemaking regarding various provisions of the DCLA, including its scope, and the DFPI has invited commenters to submit example language for potential regulations interpreting the DCLA. We write to comment on the proposed scope of the DCLA under topic I.D.: "**Financial Code section 100001, subdivisions (b)(1) and (c) provide exemptions from the DCLA. Is further clarification needed regarding which entities or transactions are exempt**?"

In our view, DFPI's final regulations should establish the depository institution exemption referenced in Section 10001(b)(1) of the DCLA applies to subsidiaries and affiliates of depository institutions in addition to the institutions themselves. These wholly-owned subsidiaries and affiliates, like their parents, are subject to extensive regulation from prudential regulators including the affiliates of California banks, which are regulated by the DFPI itself, and large national banks, which are regulated by the Office of the Comptroller of the Currency ("OCC") and the Consumer Financial Protection Bureau ("CFPB"). Requiring these entities to also comply with the new requirements imposed by the DCLA would be unnecessarily duplicative and burdensome both for the entities themselves and the DFPI, which can better use its resources to focus on heretofore-unlicensed debt buyers and collectors.

Analysis

Effective January 1, 2022, California's new debt collection licensing law will require debt collectors to apply for and obtain a license from the DFPI.[1] The DCLA provides a licensing exemption for "depository institutions,"[2] defined to include FDIC-insured banks, NCUA-insured credit unions, and members of the Federal Home Loan Bank system.[3] The definition of "depository institution" does not extend to affiliates and subsidiaries of depository institutions.

As a result, while an FDIC-insured bank does not need to obtain a debt collector license, if that bank uses a wholly-owned affiliate or subsidiary to perform collection activities, the affiliate or subsidiary would be required to obtain a license and subject itself to DFPI oversight, including audits, periodic reporting requirements, examinations, investigations, fines and penalties.[4] Given the non-DFPI oversight of the FDIC-insured bank includes oversight of its affiliates, inclusion in this licensing regime is unnecessary.

Existing Oversight of Bank Affiliates is Comprehensive and Substantial

Affiliates and subsidiaries of depository institutions are already subject to expansive oversight. Federal and state-chartered banks are subject to oversight from a prudential regulator[5] and, for large banks, the CFPB. This oversight extends to the bank's affiliates and subsidiaries.

For example, DFPI has the ability to examine subsidiaries of state-chartered banks in California.[6] As for national banks, the OCC supervises and examines them conducting on-site reviews for compliance with applicable statutes and regulations, providing ongoing supervision of each bank's operations, and regularly meeting with a bank's management and its board of directors.[7] The OCC also brings enforcement actions against banks and their affiliates that engage in risky practices or do not comply with their rules and regulations. The OCC's guideline for examinations—the Comptroller's Handbook—emphasizes this review must include oversight of a bank's affiliates. The Handbook explains the risks to a bank may be increased by the activities of its affiliates and examiners must include affiliates in their examinations:

> While the OCC's supervision focuses on individual banks, the risks to these banks may be mitigated or increased by the activities of affiliates and other related

[1] Senate Bill No. 908.

[2] CAL. FIN. CODE § 10001(b)(1).

[3] CAL. FIN. CODE § 1420(a).

[4] Senate Bill No. 908 Floor Analysis at 1.

[5] The OCC, Federal Deposit Insurance Corporation ("FDIC"), or the Federal Reserve. In addition, federally-chartered credit unions are subject to oversight by the National Credit Union Administration ("NCUA").

[6] CAL. FIN. CODE § 500(a)(7) ("The commissioner may examine subsidiaries of every California state bank, state trust company, and foreign (other nation) bank licensed under Article 3….").

[7] Comptroller's Handbook Examination Process, Bank Supervision Process, Version 1.0, June 2018 https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/bank-supervision-process/pub-ch-bank-supervision-process.pdf.

> organizations (e.g., financial subsidiaries). Therefore, examiners must determine the risk profile of OCC supervised banks, regardless of how activities are structured within the bank's overall company. Examiners' assessments should consider the OCC-supervised bank's risks from *affiliates* and other related organizations, and the effectiveness of the OCC-supervised bank's risk management systems in controlling those risks. To do this, examiners obtain information from the bank, the bank's affiliates, and other regulatory agencies, as necessary.[8]

OCC examiners are also tasked with "[c]onsider[ing] the risks posed by significant activities or affiliates in determining the bank's ratings and risk assessment."[9]

The other federal prudential banking regulators also emphasize the importance of including affiliates in examinations:

- Federal Reserve: "To understand an organization's compliance risks, examiners must understand the types of business it conducts within the institution, *its affiliates, and subsidiaries*."[10]
- FDIC: The FDIC's Consumer Compliance Exam Manual has an entire chapter explaining the importance of examining affiliates and subsidiaries and proscribing the process to do so.[11]

Substantively, these regulators examine banks and their affiliates for compliance with debt collection rules.[12] That affiliates must be included in these exams is not surprising; were they excluded, all banks would move their riskiest activities to affiliates outside the reach of federal examiners. To add the additional burden of potential DFPI examinations would be duplicative, and will only serve to distract the DFPI from the main target of the law and licensing requirements—California debt collectors and debt buyers with no prudential oversight.

Prudential regulators are not the only entities that examine banks for compliance with debt collection laws. The CFPB, which examines banks with more than $10 billion in assets, is

[8] *See* Comptroller's Handbook ch. 1 at 30; *id.* at 35.
[9] *Id.* at 5.
[10] Consumer Compliance Handbook, at 1 (emphasis added), available at https://www.federalreserve.gov/boarddocs/supmanual/cch/cch.pdf.
[11] *See* FDIC, Consumer Compliance Exam Manual, "Bank Affiliates and Subsidiaries" ch. X-5.1 (Jan. 2014), at https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/10/x-5-1.pdf.
[12] *See* FDIC, Consumer Compliance Exam Manual chs. V-VIII (Aug. 16, 2021), available at https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/index.html; Comptroller's Handbook, "Other Consumer Protection Laws and Regulations" (August 2009), at 16, available at https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/other-consumer-protection-laws-regs/pub-ch-other-consumer-protect-laws-regs.pdf.

expressly authorized by the Dodd-Frank Act to include bank affiliates in its exams.[13] These exams include review of compliance with the FDCPA and the Dodd-Frank Act's prohibition on unfair, deceptive, and abusive acts and practices.[14]

As the examples cited in the margin illustrate, bank oversight has been an effective tool in curbing concerning practices engaged in by debt collectors.[15]

Process for Vetting Affiliates would be Duplicative of Existing Processes

The DCLA, if applied to affiliates and subsidiaries, would require their parent banks to produce significant personal information of licensees' principal officers and others already obtained in greater detail by the prudential regulators.[16] For example, national banks follow an in-depth application process to be chartered as an OCC-supervised bank and in this process the OCC conducts background checks of key personnel.[17] This may include leadership of an affiliate if those individuals are "[s]enior executive officers," defined to include "any … individual … who exercises significant influence over, or participates in, major policy making decisions of the national bank."[18]

These background checks evaluate the experience, competence, and integrity of the individual and may also consider a person’s character, financial ability, or willingness to direct or lead in a safe, sound, and legal manner.[19] The OCC also closely examines the backgrounds of filers whose previous experience contributed to a failed or "troubled" financial institution or when other facts may raise questions about competence, character, or personal or fiduciary integrity. These

[13] 12 U.S.C. § 5515 (authorizing CFPB to examine "an insured depository institution with total assets of more than $10,000,000,000 and any **affiliate** thereof") (emphasis added).

[14] *See* CFPB Examination Procedures - Debt Collection, available at https://files.consumerfinance.gov/f/documents/201210_cfpb_debt-collection-examination-procedures.pdf.

[15] *See, e.g.*, *In re Cornerstone Mortgage Co., Houston, Tex.*, OCC Enforcement Action Case No. 2006-85 (enforcement action involving Cornerstone Mortgage Company, Houston, Texas, an operating subsidiary of First National Bank of Omaha, for violations of the Home Mortgage Disclosure Act); *In re Financial Management Consulting Group, LLC* f/k/a Financial Management Consulting Group, OCC Enforcement Action Case No. 2005-91 (fining Financial Management Consulting Group, LLC as an “institution-affiliated party” of the First National Bank of Northern Kentucky); *In re Citibank, N.A.; Department Stores National Bank; and Citicorp Credit Services, Inc. (USA)*, CFPB Admin Pro. No. 2015-CFPB-0015 (ordering bank subsidiaries to provide an estimated $700 million in relief to eligible consumers harmed by illegal practices related to credit card add-on products and services); *In re Chase Bank, USA N.A. and Chase Bankcard Services, Inc.*, CFPB Admin Pro. No. 2015-CFPB-0013 (ordering bank and its subsidiary to pay $30,000,000 to the CFPB for selling bad credit card debt and illegally “robo-signing” court documents).

[16] *See* CAL. FIN. CODE § 100004(a); § 1284 ("Each bank holding company and its subsidiaries shall be subject to examination by the commissioner").

[17] Comptroller’s Licensing Manual: Background Investigations, https://www.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/background-investigations-licensing-manual.pdf.

[18] 12 C.F.R. § 5.51(c)(4).

[19] Comptroller’s Licensing Manual: Background Investigations, at 4, https://www.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/background-investigations-licensing-manual.pdf.

background checks include information from credit bureaus, the FBI, other federal and state regulators, the IRS, various databases, FinCEN, and the OCC's Enforcement Action Report System, a database of historical criminal referral information.

The FDIC likewise requires background checks for state-chartered banks to obtain deposit insurance.[20] Each bank organizer, proposed director, senior executive officer, and 10-percent-or-more shareholder must provide fingerprints, authorize a background check, and file a disclosure report.[21] The FDIC or OCC may also perform additional background checks when they deem it appropriate, including making a request for background information from other agencies such as law enforcement, the courts, and other federal and state regulators. It is important to note these background check requirements extend beyond the bank's initial review—when a bank experiences a change in management or institutional control, the bank is required to notify its regulator of the change to ensure the new individuals are vetted and approved by the regulator. These requirements help ensure bank management transparency, which is a critical component to maintaining a safe and sound banking system.

These background checks, and those performed by the other prudential regulators, appear more comprehensive than those mandated by the DCLA. This is not surprising because the Legislature likely intended this new process to vet previously-unvetted debt collectors, debt buyers, and related entities not otherwise known to regulators.

Exempting Banks' Affiliates Allows DFPI to Focus on Bad, Unlicensed Actors

The goal of the DCLA is for the DFPI to have oversight of debt buyers and debt collectors who have heretofore escaped substantial scrutiny. In explaining its reasoning, "the author’s office observe[d] that the debt collection and debt buying industries are notoriously unscrupulous in their practices."[22] Prior to the DCLA, consumers could complain to the Attorney General or the CFPB, or file their own lawsuits, but DFPI (and its predecessor) had no proactive means of maintaining oversight over these unlicensed actors. Given that many collection entities are smaller and that debtors may be unwilling or unable to raise a complaint, the Legislature's focus on these entities makes sense.

The same cannot be said for affiliates of banks. A wholly-owned subsidiary or affiliate of a regulated banking institution that engages in notorious and unscrupulous practices will not last long because it cannot persist under the radar. These institutions invest heavily in compliance, training, and oversight with the understanding that they are subject to ongoing supervision by examiners. Prior to the DCLA, many unlicensed debt collectors and buyers in California had no such oversight.

[20] 12 U.S.C. §§ 1815; 1829; 12 C.F.R. part 303.
[21] Interagency Biographical and Financial Report—FR 2081c.
[22] SB 908 Senate Floor Analysis, page 5.

The purpose of the law is not to impose new substantive restrictions on debt collectors and debt buyers beyond those imposed through the licensing process.[23] But in the case of affiliates and subsidiaries of depository institutions, the licensing process *would* impose new and duplicative requirements, in exchange for no discernible benefit because these entities are already subject to comprehensive oversight. Including banks' subsidiaries in this process only adds to the administrative burden on the DFPI and diverts the DFPI's limited resources from the otherwise-unlicensed actors onto whom the Legislature seeks to focus the DFPI's attention.

DFPI Can Exempt Affiliates and Subsidiaries.

The California Consumer Financial Protection Law provides rule-writing authority to the DFPI commissioner allowing the commissioner to "issue rules and regulations consistent with law as the commissioner may deem necessary or advisable in executing the powers, duties, and responsibilities of the department."[24] Using this authority to remove oversight of affiliates and subsidiaries already subject to extensive oversight would be "advisable" because it would allow DFPI to focus its efforts on other, unregulated debt buyers and collectors.

In signing the DCLA legislation, Governor Newsom stated it would give "Californians a department to enforce our consumer laws rather than relying on individuals to sue the debt collectors."[25] Californians whose debts are being collected by affiliates or subsidiaries of banks, already have a "department"—the prudential regulator and, in many cases, the CFPB, enforcing applicable consumer laws. While California does maintain the Rosenthal Act, it largely "mimics" the requirements of the FDCPA.[26] Broadening the depository institution exemption to the DCLA would allow DFPI to focus its efforts and limited resources on the entities that most concerned the Legislature. And doing so would not result in less consumer protection for California because of the extensive oversight of banks.

[23] "With only minor exceptions, this bill does not add any new requirements on debt collectors or debt buyers; instead, it adds a layer of regulatory oversight over debt collectors and debt buyers already subject to state law, but not currently subject to licensure." SB 908 Senate Floor Analysis, page 6.

[24] CAL. FIN. CODE. § 326; *see also* Cal. Assembly Bill 1864 § 1 (DFPI can "promulgate regulations").

[25] "Governor Newsom signs Wieckowski bill to license debt collectors in California," California Senate (Sept. 25, 2020), at https://sd10.senate.ca.gov/news/2020-09-25-governor-newsom-signs-wieckowski-bill-license-debt-collectors-california.

[26] *See, e.g., Riggs. v. Prober & Raphael*, 681 F.3d 1097, 1099 (9th Cir. 2012) ("The Rosenthal Act mimics or incorporates by reference the FDCPA's requirements … and makes available the FDCPA's remedies for violations. Thus, for purposes of this case, whether a validation notice violates the Rosenthal Act turns on whether it violates the FDCPA.").

Conclusion

The DFPI's final regulations should clearly state that the depository institution exemption referenced in Section 10001(b)(1) of the Debt Collection Licensing Act also applies to subsidiaries and affiliates of depository institutions.

If you have any questions or would like to discuss this comment in further detail, I can be reached at [redacted] or eric.goldberg@akerman.com.

Sincerely,

[redacted]

Eric I. Goldberg