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January 12, 2024

Re: PRO 05-21

Comments on Second Draft Text of Proposed Regulations Under the Debt Collection Licensing Act (PRO 05-21)

We appreciate the opportunity to provide comments on the Department's proposed rules enacting the Debt Collection Licensing Act.

Our commentary focuses directly on the narrow issue of whether the collection of unpaid rent gives rise to the necessity for applying for, and obtaining, a debt collection license from the Commission of the Department of Financial Protection and Innovation.

It is well-settled law (both statutory law and case law) that the collection of unpaid rent falls outside of the purview of the Rosenthal Fair Debt Collection Practices Act. (Rosenthal.)

In the proposed new law, business entities "engaged in the business of debt collection" are required to be licensed. Under California statutes, debt collection has a specific, technical definition that does not include seeking to collect residential tenancy debt. In order for an activity to fall within the purview of Rosenthal, the activity must relate to a "consumer credit transaction." A "consumer credit transaction" means a transaction between a natural person and another person in which property, services, or money is acquired on credit by that natural person from the other person primarily for personal, family, or household purposes. Cal. Civ. Code 1788.2(c) (emphasis added.)

With respect to residential rental properties, there is no extension of credit. The notion that rent is not a "consumer credit transaction" has been consistently upheld by a significant number of court cases. Even if a party sought unpaid rent in an unlawful detainer action, a tenant could not prevail on a Rosenthal Act claim because "residential rent collection is not a consumer credit transaction protected under the Rosenthal Act." Phillips v. Archstone Simi Valley LLC, 2016 U.S. Dist. LEXIS 186266, 2016 WL 7444550, at *5 (C.D. Cal. Dec. 15, 2016). Residential tenancies that require monthly rent paid in advance do not involve any extension of credit by the landlord. "Renting an apartment is not truly a credit transaction" because the landlord "neither sells property on time nor makes funds available to tenants." Ortiz v. Lyon Management Group, Inc., 157 Cal. App. 4th 604, 619, 69 Cal. Rptr. 3d 66 (2007). Because tenants did not acquire their leasehold on credit, no consumer credit transaction occurred between tenant and landlord, and the rent paid by tenants is not a consumer debt under the Rosenthal Act. See Leasure v. Willmark Communities, Inc., 2013 U.S. Dist. LEXIS

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35795, 2013 WL 6097944, at *4 (S.D. Cal. Mar. 14, 2013) (concluding that residential rent collection does not qualify as a consumer credit transaction.)

The controlling statutes and subsequent case law is of utmost importance with respect to the proposed requirement for landlords, property management companies, and those seeking to collect rent on behalf of landlord-clients.

The authority referred to herein is of utmost importance since the legislative scheme that was enacted by the legislature during COVID was a measure to allow tenants to avoid eviction based upon rents that were accrued between March 1, 2020 through September 30, 2021. It should be noted that a landlord (or a landlord's agent may later pursue the rents which were accrued between March 1, 2020 through September 30, 2021.) These unpaid rents were not forgiven by legislation, the legislation merely created a timeframe for tenants to financially recover from adverse COVID ramifications without facing eviction. Landlords may still seek the unpaid rent incurred during this time period through collection work and through the pursuit of small claims judgments (subject to any more stringent local ordinance.) Landlords are restricted only from evicting for unpaid rent incurred during this time period.

As a general matter, the proposed legislation at hand, takes no narrow treatment of residential tenancy debt. Moreover, the history contains considerable discussion about the need to regulate collectors as defined by the Rosenthal Act. In fact, it contains various terms including "debt collector," "consumer credit transaction," "creditor," "debt," "debt collection," "consumer debt," and "person" -as being defined identically as defined in the Rosenthal Act. See, Cal. Civ. Code 100002, subs (e), (f), (i). (emphasis added.)

Proponents of the changes to Section 1850.2 argue COVID Rental Debt is a "consumer debt." Generally, this argument is based on Assembly Bill 3088 and the prevention of unlawful detainers due to unpaid COVID Rental Debt. They argue, while a residential lease did not create a consumer credit transaction, one was retroactively foisted upon the parties. However, a consumer credit transaction should not be created where the underlying contract mutually agreed to by the parties does not involve any extension of credit Yatooma v. OP Prop. Mgmt. LP 2017 U.S. Dist. LEXIS 114298, at *7-8.

In the proposed law's most recent iteration related to rent collection, new language has been added to treat COVID rental obligations differently than rental obligations incurred otherwise. This additional language found at 1850.2(a)(1) in PRO 05-21 Second Draft Text runs contrary to the plain language and spirit of the Rosenthal Act and case law that has interpreted it for well more than a decade.

While the Second Draft Text is well-meaning, it likely will only create a cavalcade of administrative hoops for the rental industry to navigate, burden government resources, and provide no additional protection to renters. For example, under the recently revised CCP 708.111 which provides certain requirements for judgment debtor exams, rental debt is specifically excluded from some of them. However, by creating inconsistent definitions of what constitutes rental debt there will more than likely be further arguments about which part of the statute applies to which specific debts. Unnecessary litigation, legislation, and expenses for Plaintiffs and Defendants will ensue.

We respectfully comment and request that the most recent draft of the proposed legislature omit the licensing language as it pertains to COVID rent. The pursuit of rent falls outside of the statutory language that was drafted by the California Legislature.

Thank you for your consideration.

Sincerely,

D. Patrick O'Laughlin
Partner