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Receivables Management Association International White Paper

# OUT-OF-STATUTE DEBT:
## WHAT IS A SMART, BALANCED, AND RESPONSIBLE APPROACH?

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## EXECUTIVE SUMMARY

Not since 1977, the year of the Fair Debt Collection Practices Act's enactment, has our nation had an important opportunity to rewrite the rules for debt buying and debt collection. Preserving the ability of companies to collect out-of-statute debt (OSD) with appropriate protections without a lawsuit (referred to as "non-adjudicative collection of OSD") will improve the consumer credit economy and enhance protections for consumers.

**What is out-of-statute debt?**

OSD is a debt which can no longer be collected through the courts because the time period (the statute of limitations) during which that type of legal claim can be litigated has expired. These time periods are set by state, not federal, law. For consumer debt, OSD time limits vary from three to 10 years, depending upon the state and the type of consumer debt (credit card, auto, medical, etc.). The national average statute of limitation period is 5.1 years.

**The OSD Market Benefits Consumers**

The OSD market provides an important opportunity for consumers to pay their debts, especially for consumers who, due to economic hardship, need more time to do so. Additionally, because OSD paper is by definition "older," OSD paper is customarily priced at a discount. This discount gives debt buyers an opportunity to settle the debt with the consumer for an amount that is very attractive to the consumer.

RMA estimates that annually, tens of billions of dollars are collected on OSD. That substantial return helps to keep the price of credit affordable for consumers. It also promotes the availability of credit to lower-income consumers.

**Proposals to ban OSD have unintended consequences impacting consumers**

Some states have adopted OSD statute-of-limitation periods that are limited to three years or fewer. However, an outright ban on OSD collection would have the following unintended and adverse consequences for consumers.

- Prohibition of non-litigation-related collection on OSD increases the number of lawsuits brought against consumers resulting in a judgment rather than working out a payment plan.
- An outright OSD collection ban would increase the interest rate offered to most consumers, even those who pay their bills on time.
- Consumers who have defaulted and passed the applicable statutory period would no longer be able to repair their credit score by making voluntary payments on their obligations because the creditor's right to receive payments cease to exist.
- Low-income consumers would be disproportionally harmed as lenders would almost inevitably restrict the availability of consumer credit for those consumers who pose the highest default risk.
- Consumers would face potential tax increases. Debt buyers and lenders are required to issue 1099-c statements to consumers, arising from the cancellation of the OSD. Consumers will, in many circumstances, owe taxes on the difference between the amount of the now uncollectable debt and the minimum amount for which the 1099-c must be provided ($600.00).

**Appropriate OSD Reforms**

RMA International supports appropriate and reasonable CFPB reforms to implement both an effective OSD notice regime and a prohibition on re-tolling OSD.

- RMA supports a policy that once a consumer debt is OSD, it is always OSD.
- RMA supports providing consumers with effective notices about all material elements of their loan or debt.
- RMA also strongly advocates that a valid debt should continue to be collectible after the running of a statute of limitations, although not collectible through litigation.

**What is not needed**

RMA is also clear about what is not needed. The law is explicit and comprehensive that out-of-statute debt cannot be sued upon. The CFPB, the FTC, and various State Attorneys General conclude that attempting to sue on OSD is a violation of existing law. RMA's self-regulatory certification standards prohibit suing on out-of-statute debt.

## INTRODUCTION

Recently, out-of-statute debt (OSD) has received considerable attention. In particular, that attention has raised a key question – should the Consumer Financial Protection Bureau (CFPB) impose new restrictions on the collection of valid but out-of-statute debt?

This report provides an analysis of the debt buying and collection industry and looks, in particular, at three aspects of the out-of-statute debt issue: (1) the law related to OSD; (2) the adverse public policy consequences of a ban on the collection OSD; and (3) RMA's recommendations for OSD collection reform.[1]

OSD is a debt which can no longer be collected through the courts because the time period (the statute of limitations) during which that type of legal claim can be litigated has expired. These time periods are not set by federal law and, rather, are set by state law. For consumer debt, OSD time limits vary from three years to ten years, depending upon the state and the type of consumer debt (credit card, auto, medical, etc.). The national average statute of limitation period is 5.1 years.[2]

OSD is not a debt forgiveness benefit. OSD does not make a valid debt invalid. OSD does not mean that the debtor no longer owes the debt. And, OSD does not mean that the debt can no longer be collected – the debt simply can no longer be collected through litigation.

Indeed, the concept of out-of-statute debt was never intended to provide consumers who owe a legitimate debt with a lottery type windfall that turns a valid loan into a gift. OSD is an evidentiary rule, intended to promote the use, in litigation, of fresh documentation; the reliance in court upon recent memory; and the avoidance in court of older claims clogging the judicial system.[3]

The OSD market provides an important opportunity for consumers to pay their valid debts, especially for consumers who, due to economic hardship, need more time to repay. In order to improve the consumer credit economy and enhance protections for consumers, RMA believes that federal regulators should, as discussed below: (1) confirm the need for all OSD collections to contain clear and reasonable OSD notices; and (2) ban retolling. Adding these two best practices to the current prohibited practices will enhance the consumer safeguards without crippling the ability of the debt industry to assist consumers in paying their legitimate debts.

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[1] Receivables Management Association International (RMA) is the nonprofit trade association that represents the interests of more than 575 companies that purchase or support the purchase of performing and nonperforming receivables on the secondary market. RMA continually sets the standard in the receivables management industry through its grassroots advocacy, conferences, committees, taskforces, publications, webinars, teleconferences, and breaking news alerts. RMA provides its members with extensive networking, educational, and business development opportunities in asset classes that span numerous industries. Founded in 1997, RMA is headquartered in Sacramento, California.

RMAs Receivables Management Certification Program and its Code of Ethics set the "gold standard" within the receivables industry due to its rigorous uniform industry standards of best practice which focus on the protection of the consumer. RMA launched its Certification Program in March of 2013. The program certifies both debt buying companies and debt buying professionals. The goal of the program is to provide additional consumer protections through the adoption of uniform industry best practice standards and to maintain high levels of educational awareness.

Under the Certification Program, certified debt buyers must comply with all applicable law including the law as it relates to the collection of out-of-statute debt. This includes Standard 12 which prohibits the use of litigation to attempt to collect out-of-statute debt.

[2] RMA has reviewed statutes of limitation as they apply to the majority of the population in the 50 states.

[3] See, Tyler T. Ochoa and Andrew J. Wistrich, "The Puzzling Purpose of Statutes of Limitation", 28 Pacific Law J, 453 at pp. 500-509 (1997).

## THE DEBT BUYING INDUSTRY

**Who are Debt Buyers and What Do They Do?**

Debt buyers are companies that purchase consumer debt from originating creditors or from other debt buyers. The types of consumer debt that are purchased can differ dramatically, based upon the contractual agreement—revolving credit card debt, auto debt, medical debt, etc.—not to mention other factors, such as whether the debt is performing or nonperforming; whether payment guarantees have been made by third parties; or whether collateral has been provided.

When a debt buying company purchases an account from a creditor, the debt buyer purchases essentially all rights, benefits and liabilities associated with the debt. Debt buyers are debt collectors under the Fair Debt Collection Practices Act 15 U.S.C. §§ 1692-1692p (FDCPA) when they purchase consumer debts that are in default.

Debt buyers employ thousands of people nationwide and operate in all 50 states. While most debt buying companies are privately held small businesses that operate on a state or regional basis, there are also a number of larger privately held companies, as well as publicly traded companies. The largest debt buying companies each employ over 1,000 people.[4]

**Debt Buying and Debt Collecting Provide Important Benefits to the Economy and to Consumers**

In July, 2014, ACA International, a national trade association representing third party collection agencies, released the E&Y Report.[5] The report found that the collections industry returned about $44.9 billion to creditors in 2013.[6] This cumulative economic return was equal to 1.9 percent of all US corporate profits before tax and

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[4] Debt collectors (unless they are also debt buyers) do not own the debts which they collect. Collectors are retained by originating creditors and/or debt buyers. Third party collectors are fully regulated under the FDCPA. According to a report by the Federal Reserve Bank of Philadelphia, debt collection agencies employ more than 140,000 people and recover more than $50 billion each year. Fedaseyeu and Hunt, "The Economics of Debt Collection: Enforcement of Consumer Credit Contracts" Federal Reserve Bank of Philadelphia (March, 2014) at pp. 9-10 ("Philadelphia Fed Report"). Other estimates are corroborative. An Ernst & Young Report done for the American Collectors Association International (ACA) found direct employment in the range of 148,000 and the total direct and indirect employment in the range of 302,000 jobs. See, *The Impact of Third-Party Debt Collection on the National and State Economies,* July 2014, at p. 2 ("E&Y Report").

[5] It is important to emphasize that the elimination of the sale and collection of OSD would make a great deal of the existing consumer debt, either held by first party creditors or sold on the secondary market, worthless. This would have a material adverse impact on the entire debt industry which employs hundreds of thousands of people and would eliminate the positive aspects that can come from the secondary market's increased flexibility to provide consumer's lower interest rates, smaller monthly payments over a longer period of time, and discounted settlements to resolve their legal obligations and repair their credit..

[6] RMA has worked hard but has not succeeded in developing a reliable methodology for determining an exact number for the out-of-statute debt collected each year. RMA is not alone. Neither the CFPB nor the FTC, nor other industry and academic sources, have been able to develop such a methodology.

The FTC Structure Report (pp. 14-15) estimates that, in 2008, debt buyers purchased $72.3 billion in consumer debt. Much more consumer debt was not purchased by debt buyers because it was held and worked by first party issuers and/or their collectors; or because it was already in the hands of debt buyers; or because it was health care or student loan debt, as opposed to debt buyers' preferred type of debt – credit card debt (about 75 percent of debt purchased by debt buyers is credit card debt (FTC Structure Report, p. 15).

Using the FTC purchase number, it would not take very many years before debt buyers owned and were collecting upon hundreds of billions of dollars in consumer debt. According to the E&Y Report, about $45 billion is collected on and returned to creditors (and, indirectly, to consumers and the economy) each year (E&Y Report at Executive Summary (i)). Given the amount of OSD in the pipeline and an average statute of limitations of five years, it would hardly be surprising if at least half of the debt collected each year was OSD. It may be much more and informal estimates by RMA members of their own experience place it at much more.

3.1 percent of before tax profits of all US domestic, nonfinancial corporations.

The OSD market is important and beneficial to the consumer credit economy and, indeed, beneficial to consumers. First, RMA estimates that tens of billions of dollars are collected on out-of-statute debt every year. That very substantial return helps to keep the price of credit affordable for consumers. This return also promotes the availability of credit to lower income consumers.[7]

Second, because OSD paper is, by definition, "older", OSD paper is customarily priced at a discount. This gives debt buyers an opportunity to settle the debt with the consumer for an amount that is very attractive to the consumer.

Third, it is no longer correct—if it ever was—that there are systemic consumer protection abuses associated with OSD.[8] The FTC Structure Report suggests that there are abuses, but that report is based upon data collected in 2009—six years ago. Today, information is available to debt buyers so that OSD can be validated and the amount owed can be broken down by principle, interest and fees and communicated to the consumer. Further, the name of the originating creditor is far less likely today to be missing or unavailable than was the case years ago.[9]

Three factors support the conclusion that debt buyers are obtaining more relevant information today than was previously the case. First, legal changes, including new state statutes (see, the California Fair Debt Buying Practices Act), require sellers to provide enhanced information. Second, CFPB regulatory oversight, including both enforcement and supervision, is changing the expectation regarding the documentation that must be obtained. Third, industry reform including, in particular, RMA's Certification Program (see Standard 18), is requiring debt buyers to seek and obtain more information and documentation.

Finally, it is a truism in the debt industry that the vast majority of consumers want to pay their valid debts. For example, a 2010 study and consumer survey of debtors who received an OSD notice found that "knowing that the debt was out-of-statute influenced the debt repayment plan chosen by the consumer, but knowing that the debt was out-of-statute did not otherwise impact consumer behavior."[10] In other words, consumers still wanted to pay their debt.

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[7] Zywicki, *The Role of Debt Collection in the Ecosystem of Consumer Credit,* 2015 (unpublished manuscript) ("Zywicki"). The FTC debt buyer report, based on 2009 data, does not provide definitive data about the prevalence of OSD. The FTC Report does suggest, however, that a significant percentage of debt purchased by debt buyers from originating creditors is OSD (perhaps 20 percent) and a higher percentage of debt purchased from other debt buyers is also OSD (perhaps 40 percent). Of course, as the debt is worked, a higher percentage of the debt subsequently becomes OSD. (See, F*ederal Trade Commission: The Structure and Practices of the Debt Buying Industry,* January 2013("FTC Structure Report"), at pp. 42-44).

[8] RMA member firms are debt buyers who are engaged in complying with standards at or above the requirements of the state and federal laws impacting their business. While there are bad actors in the debt industry, they are the minority and are consistently being weeded out by self-regulatory initiatives and by state and federal agencies. Those bad actors are not RMA members or, when bad actors are discovered, they do not remain RMA members for very long. RMA is also working with, and has been very supportive of, the FTC's very successful efforts to identify and prosecute rogue collectors and unlawful collection activity.

[9] The FTC's 2013 Structure Report states, "the Commission's analysis reveals that the debt buyers usually had all the information that the FDCPA currently requires debt buyers to provide consumers in validation notices at the beginning of the collections process…" at p. 36.

[10] T. Goldsmith and N. Martin, "Testing Materiality …What Information Matters When Collecting Time Barred Debt", Consumer Finance Law Quarterly Report 64(4), Winter 2011 at p. 373.

Of course, consumers may sometimes need additional time and forbearance because of economic hardship, medical problems or other personal problems. Out-of-statute debt gives consumers the time that they need. Simply stated, OSD allows consumers to pay off the debt that they acknowledge and very much wish to pay off. Consumers do not want to turn a valid debt into a gift. United States public policy should not want to do that, either. Rather, our public policy should respect the integrity of the bargain between consumers and their lenders.

**Consumer Complaints about Debt Buying and Collecting**

The total raw number of consumer complaints against debt buyers and debt collectors is frequently cited as evidence of a systemic problem within the debt collection industry. The raw number of complaints, however, is deceiving. A recent RMA analysis of Federal Trade Commission (FTC) data, for example, indicates that an actual majority of the complaints received by the FTC are against unknown or fictitious entities – often a sign of fraudulent criminal activity.[11]

Furthermore, the following statistics demonstrate that very few consumers ever experience a default status on their credit card or loan (which usually occurs when an account is 180 days past due) and rarely have any experience with the collections process.

- Approximately 95 percent of all consumer debt is paid off on time.
- According to the Fair Isaac Corporation, less than half of all consumers have been reported as 30 or more days late on a payment.
- Only three out of ten consumers have ever been 60 or more days late on a payment.
- Only two out of ten consumers have ever been 90 or more days late on a payment.[12]

As these statistics suggest, only a small percentage of consumer accounts ever wind up in collection. There is too much complexity, however, for RMA to provide a specific number or percentage for the amount of debt in collections. What kind of consumer debt? How is the debt owned? How is it being collected? The CFPB estimates that, in 2013, about 30 million Americans had debts in collection. It is not clear what the CFPB means by "debts in collection". The FTC has recently stated publicly that about 15 percent of the public has debt in collections with an average balance of about $5,000.00.[13]

It is important to recognize, however, that the collections process is not only a recognized and regulated activity, but, when conducted properly, represents a fair and reasonable process for consumers. As an example, of all the contacts that debt buyers and debt collectors have with consumers each year, only 0.002 percent of those consumers complain to the FTC.[14]

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[11] RMA member firms are complying with standards at or above the requirements of state and federal law impacting their business. While there are bad actors in the debt industry, they are the minority and are consistently being weeded out by self-regulatory initiatives and by state and federal agencies.

[12] RMA, "The Debt Buying Industry – A White Paper", January 8, 2015, p. 4, relying on data provided in the FTC Annual Report 2010: Fair Debt Collection Practices Act, April 2010. Inasmuch as the vast majority of consumer debt purchased by debt buyers is credit card debt, we have included here only statistics for credit card debt. The statistics for health care debt, student debt, and even auto debt are different but less relevant for debt buying.

[13] See, transcript of remarks by Jessica Rich, Director of the FTC's Bureau of Consumer Protection, at an FTC, New York State Department of Financial Services, and CFPB debt collection dialogue in Buffalo, NY on June 15, 2015.

[14] Federal Trade Commission, Annual Report 2010: Fair Debt Collection Practices Act.

## WHAT IS THE LAW GOVERNING OUT OF STATUTE DEBT?

A statute of limitations is an affirmative defense to a judicial claim for enforcement of a debt. It is sometimes said that it is designed as a shield for litigants, not a sword.[15] Thus, a statute of limitations only becomes relevant in the event that litigation has been commenced by a creditor against a consumer. Like any affirmative defense, if the statute of limitations is not raised by the consumer, it is waived.[16]

**Judicial Collections and Determining When a Debt is OSD**

It is important to put litigation into context as a collection tool for consumer debt. Debt buyers almost always purchase consumer debt for a discounted amount.[17] The FTC, for example, estimates that, on average, debt buyers pay four cents on the dollar for credit card debt.[18] As should be expected, the amount of the discount varies depending upon the type of consumer debt; its age; the extent to which collection efforts have already been made; and, sometimes, other factors such as the consumer's location. Because the debt buyer's investment is discounted, debt buyers have an ability, and an incentive, to settle with the consumer for an amount that represents only a small percentage of what the consumer owes. This is, by far, the debt buyer's preferred method to collect and settle on consumer debt.

By contrast, litigation is an expensive and time consuming way to collect a consumer debt. Most consumer credit card debts are for relatively small amounts. Lawyers are expensive, and, if a debt buyer is not careful, legal fees and court costs may frequently exceed the amount which the consumer owes. As a result, it is estimated that perhaps less than five percent of consumer debt is collected through litigation.[19]

In a recent poll of all RMA debt buyer members, not a single member responded that they knowingly or intentionally file lawsuits after the expiration of the applicable statutes of limitation. Although, as noted, the statute of limitations is an affirmative defense that, in almost all states, must be raised by the defendant or it is waived, it is improper to knowingly file OSD suits and wait to see if the defense is pled. RMA members have adopted rigorous policies and procedures to assure that a suit is filed only before the expiration of the applicable statutes of limitation.

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[15] See, Norgart v. Upjohn Co., 21 Cal. 4th 583, 603 (1995).

[16] See, Minton v. Cavaney, 56 Cal. 2nd 576, 581 (1961).

[17] FTC, Reporting a Broken System: Protecting Consumers in Debt Collection Litigation and Arbitration.

[18] CFPB Annual Report 2014 at p. 7 ("CFPB Report").

[19] This is very much an estimate and needs further qualification. RMA surveyed its members regarding judicial collections. One of the largest debt buyers reported that their judgment balances represent 7.75 percent of their total collected balances. Further, this buyer reported that its judgment balances represent 3.35 percent of its total accounts. Finally, they reported that as to "fresher paper" (acquired in the last three years), court judgments represented 18.25 percent of total collected balances and 12.6 percent of total accounts.

With this debt buyer's experience in mind, it may well be that a five percent number is right only when comparing legal judgments with the number of accounts owned. If the revenue generated by legal collections is compared with total revenue from all collections, the correct percentage of legal collections may be higher. One of the large, publicly traded debt buyers, Encore, reports "legal collections" in the range of 49 percent. They define "legal collections", however, as any collections by a law firm. This includes collections arising from a validation letter; from calling; and from correspondence and other communications. Only a portion of "legal collections" are attributable to an actual judgment.

Regardless of the exact percentages, the CFPB has expressed the view that the percentage of judicial collections has grown (CFPB ANPR Statement, 78 Fed. Reg. 67848, Nov. 12, 2013).

When litigation is used, attorneys representing debt buyers know that a debt which is older than the applicable statute of limitations does not constitute a valid claim. Attorneys are officers of the court, and by bringing an invalid claim, the attorney is violating the canons of ethics.[20] Attorneys simply are not going to risk their license, livelihood, credibility and reputation by intentionally suing on OSD debts. Combine this with the RMA's prohibition on knowingly suing on an out-of-statue debt, and the reality is that an extraordinarily small percentage of out-of-statute debts find their way to court.[21]

RMA and the debt buying industry recognize that state law controls whether a debt is OSD. A debt owner's attorney must know that the debt is, in fact, out-of-statute under the applicable state law. This can be a complex determination. In many instances, multiple causes of action are pled with multiple statutes of limitation. Moreover, the majority of suits involving debt buyers or debt collectors that are sued on OSD concern intricate legal issues upon which there is relatively little guidance from the courts.

For instance, the application of choice of law provisions, both contractually and statutorily, to determine which statute of limitation applies, has been heavily litigated for years. Choice of law conflicts could implicate the statutes of limitation in the states where the consumer resides, where the transaction occurred, where payment is due, where the consumer made the decision not to pay, or where the creditor is based, assuming yet another jurisdiction is not designated in the contract. Moreover, the standards for starting the out-of-statute clock vary from state to state; the circumstances under which a statute of limitations clock may be suspended (tolled) vary from state to state; and the actual amount of time allowed under a state statute varies among states.[22]

**OSD Legal Protections**

Recently, both the FTC and the CFPB, along with legislatures in several states, have acted to enhance consumer protections associated with attempts to collect on out-of-statute debt. In 2012, for example, the FTC's Consent Decree in Asset Acceptance asserted that it can be an unfair and deceptive practice for a party collecting an out-of-statute debt not to inform the consumer, in writing, that the debt is, in fact, out-of-statute and can no longer be collected through litigation.[23]

In August of 2013, the 7th Circuit, in Delgado v. Capital Management Services, endorsed a FTC and CFPB position articulated in their amicus brief, holding that a time limited settlement offer to a consumer debtor on an out-of-statute debt could imply that once the time limit is exceeded, the debt owner could sue, even if the letter did not include a threat of litigation.[24] (But, the 7th Circuit did endorse the ability of a debt collector to seek repayment of time-barred debt but, of course, not through litigation.)

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[20] American Bar Association, Canons of Professional Ethics, Canon 22.

[21] RMA's Debt Buyer Certification Program states, "A Certified Company shall not knowingly bring a lawsuit on a debt that is beyond the applicable statute of limitations; however, a Certified Company may continue to attempt collection beyond the expiration of the statute provided there are no laws and regulations to the contrary."

[22] Critics also claim that suits have been filed after the applicable statute of limitations has run based on an oral contract, even though the suit was, or should have been, in fact, based upon a written contract/credit card agreement. The issue of whether credit card debt is subject to a written or oral contract statute of limitations (to the extent a state has such separate statutes of limitation) has been decided in some, but not all, jurisdictions.

[23] United States v. Asset Acceptance, LLC, No. 8:1d-cv-00182-T-27EAJ (M.D. Fla., Jan. 31, 2012) ("Asset Acceptance").

[24] Delgado v. Capital Management Services, LP, Number 13-20130 (7th Cir. August 4, 2013).

More recently, in Buchanan v. Northland Group Inc., No. 13-2523 (6th Cir. March 5, 2014), the 6th Circuit ultimately agreed with Delgado that a collection letter that does not explicitly notify the consumer that the debt is out-of-statute could be misleading. The opinions in Delgado and Buchanan by the 6th and 7th Circuits, however, are at odds with holdings in the 3rd and 8th Circuits. Nevertheless, there appears to be an emerging trend that debt collectors should affirmatively disclose to consumer debtors that a debt is out-of-statute.[25]

Another complexity associated with collecting out-of-statute debt arises when a consumer takes an action, such as making a partial payment, that has the effect of "tolling" the running of the statute of limitations so that a new statute of limitations clock begins. A consumer's reaffirmation of a debt or a consumer using an account to make a new charge may also retoll the statute.

RMA supports providing consumers with effective notices about all material elements of their loan or debt.[26] RMA also opposes the retolling of OSD. RMA, however, very much believes that a valid debt should continue to be collectible after the running of a statute of limitations but, of course, not collectible through litigation.

## THE ADVERSE CONSEQUENCES OF BANNING THE COLLECTION OF OSD

Senator Sherrod Brown (D-OH), the Ranking Member of the Senate Banking Committee, has called for a ban on the collection of OSD.[27] The CFPB, to its credit, has never suggested, through its ANPR or otherwise, that they would or should consider such a ban. In fact, in the CFPB's ANPR, they posed eleven questions about out-of-statute debt. Not one of those questions addressed or related to an outright ban.

There can be little doubt that an outright ban on the collection of OSD would have unintended but, nevertheless profoundly adverse, consequences for consumers. As noted earlier, some states have adopted statute of limitation periods that are limited to three years or less. Thus, any prohibition on the non-adjudicated collection of OSD would almost certainly create a rush to the courthouse and substantially increase the number of lawsuits brought against consumers.

Professor Todd J. Zywicki, an expert on consumer debt, has emphasized that the CFPB should, under no circumstances, ban the collection of OSD. Zywicki points out that a change in law to forbid the collection of out-of-statute debt would be, "likely to have one major unintended consequence that would be heavily harmful to consumers: it would be likely to increase the number of lawsuits against debtors to enforce debts. Although there appear to be no empirical studies on whether the propensity to file lawsuits increases immediately before the expiration of the statute of limitations, common sense suggests that is the case. Thus...one unintended consequence would likely be more lawsuits against consumers that could otherwise be avoided."[28] Certainly, debt buyers' current flexibility to work through a consumer's difficult financial circumstances would be eviscerated.

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[25] See, Donald Maurice, "Appeals Decision Supports CFPB-FTC View on Out-of-Statute Debt Collection" at Inside Arm, March 17, 2014 and, see, "West Virginia to Require New Disclosure for Out-of-Statute Debt", ACA International News, June 6, 2014.

[26] RMA does not, however, support a requirement that debt buyers provide a "warning notice" as a debt approaches OSD status.

[27] Letter to Richard Cordray from Sherrod Brown dated June 4, 2013. The National Consumer Law Center (NCLC) has also called upon the CFPB to adopt an outright ban on the collection of out-of-statute debt. See, NCLC, "Zombie Debt: What the CFPB Should Do About Attempts to Collect Old Debt", January 2015 at p. 5 ("NCLC Paper").

[28] Zywicki at p. 74.

A further unintended, but very likely adverse, consequence for consumers arising from an outright ban on the collection of OSD would be an increase in the price (the interest rate) of credit offered to most consumers, even those who pay their bills on time. Collection costs would go up in order to manage distressed debt in a shortened time period. In addition, lenders would recoup less money from charged-off and defaulted debt through negotiated settlements or the sale of debt. This would recalculate the cost benefit equation arising from consumer lending and, inevitably, raise costs and reduce availability. This increased price would help to compensate credit card issuers and other lenders for the cost that would occur once a debt became OSD if the debt could no longer be collected in any manner.

A third unintended adverse consequence for consumers who have defaulted on their credit obligations and who have passed the applicable statutory period is that they would no longer be able to repair their credit score by making voluntary payments on their obligations because the creditor's right to receive payments from the consumer would be "extinguished". The legal "right" to collect voluntary payments beyond the statute of limitations is recognized by the Federal Trade Commission and by over 45 states. The elimination of this legal right would mean that consumers would be left with no way to repair their credit history in the time between the expiration of the statute of limitations and the seven year reporting period on credit reports. The negative mark on a consumer's credit score would remain with no means for the consumer to address the problem. Imagine the hardship for consumers who got their life back together following a financial difficulty but who find out that they would have to wait years for the next realistic opportunity to obtain credit.[29]

A fourth unintended and adverse consequence for consumers, particularly low income consumers, would be that lenders would almost inevitably restrict the availability of consumer credit for those consumers who pose the highest risk of default. Professor Zywicki characterizes this as "regressive distributional effects"—"low-risk and higher-income borrowers who can provide collateral may avoid many of the costs of a less-efficient debt collection regime, whereas higher-risk and low-income borrowers will not".[30] The Philadelphia Fed Report reaches the same conclusion.[31]

Finally, another unintended and adverse consumer consequence would be the potential increase in taxes for consumers who have an out-of-statute debt that can no longer be collected. Debt buyers and lenders will have to issue 1099-c statements to consumers, arising from the cancellation of the OSD. Consumers will, in many circumstances, owe taxes on the difference between the amount of the now uncollectable debt and the minimum amount for which the 1099-c must be provided ($600.00). Thus, a consumer who owed an OSD amount of $5,000.00 would have taxable income, potentially, of $4,400.00 but would not have received the commensurate revenue with which to pay any resulting tax. This would particularly harm lower income consumers.[32]

[29] Most large debt buyers report a payoff or a settlement of consumer debt to the national credit bureaus. Most small debt buyers do not. Those debt buyers that do report do so presumably on the theory that reporting encourages repayment and is, therefore, worthwhile, notwithstanding the reporting burdens and risks.

Although common sense suggests that paying off or settling an outstanding collection account helps to improve credit reports and scores, there is little research or granularity associated with this proposition. The association between resolving a collection account and improving a credit score is further blurred by the fact that most consumers have dozens of credit scores. These scores track differing criteria. Thus, the best that can be said is that satisfying an outstanding collection item is usually good for a consumer's credit report and credit score.

[30] Zywicki at p. 75.

[31] See, Philadelphia Fed Report at p. 27.

[32] It is also important to note that elimination of right and remedy to collect OSD undercuts the provisions of the United States Bankruptcy Code which are designed to provide the type of relief needed by consumers who find themselves in extreme financial circumstances.

Therefore, it is not unusual under current practice for consumers to receive 1099-cs from debt buyers. If, however, OSD was deemed uncollectible, literally millions of consumers would abruptly receive 1099-cs with, in most cases, resulting tax liability.

Furthermore, consumers who owe money to the Internal Revenue Service (IRS) frequently find that the IRS is a harsh creditor. The IRS charges very high interest rates. The IRS does not have to comply with the FDCPA; there is a long statute of limitations on taxes owed to the IRS; and the IRS has the ability to place tax liens on property. Plus, unpaid taxes are not dischargeable in bankruptcy.

## APPROPRIATE OSD REFORMS

First, we should be clear about what is not needed. The law is explicit and comprehensive that out-of-statute debt cannot be sued upon. Both the CFPB and the FTC (not to mention various State Attorneys General) conclude that attempting to sue on OSD is a violation of the FDCPA and of UDAAP. The CFPB and the FTC have demonstrated a willingness and a capacity to vigorously enforce this prohibition.[33] RMA's self-regulatory certification standards prohibit suing on out-of-statute debt. Custom and usage throughout the debt industry establishes that suing on OSD has all but disappeared.

Providing a notice to consumers when OSD is being collected is also an increasingly established practice. Indeed, both the CFPB and the FTC have taken the position that, in many cases, it may be a violation of the FDCPA and an unfair and deceptive practice to fail to provide consumers with an appropriate notice.

Some consumer groups have argued that, regardless of how clear or conspicuous a notice may be, it is impossible to craft a notice regarding a debt's OSD status that can provide consumers with effective information.[34] Putting aside the paternalistic aspects of this argument, there is simply no empirical support for this argument. Consumers are accustomed to receiving notices with respect to all manner of purchases and services, as well as legal communications. There is no reason, whatsoever, to believe that a clear, conspicuous and brief notice would not work effectively to put consumers on notice that a debt is OSD.[35]

Another OSD reform that is rapidly becoming established prohibits retolling a consumer debt based upon a consumer's partial payment of an existing OSD debt. Here, too, a clear, conspicuous and brief notice should work effectively.

RMA supports appropriate and reasonable CFPB reforms to implement both an effective OSD notice regime and a prohibition on retolling OSD. RMA supports a policy that once a consumer debt is OSD, it is always OSD.

Finally, some groups have argued that debt buyers and collectors should be required to disclose to a consumer that their payment of an out-of-statute debt will not improve their credit score. The great majority of debt

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[33] See, CFPB's Amicus Brief, March 2014, in Buchanan v. Northland and August 14, 2013 in Delgado v. Capital Management Services. See, the FTC's August 7, 2014 complaint against CreditSmart, LLC.

[34] NCLC Paper at pp. 9-10.

[35] The FTC's Consent Decree in Asset Acceptance prescribes just such a notice: "The law limits how long you can be sued on a debt. Because of the age of your debt, we will not sue you for it. If you do not pay the debt, we may continue to report it to the credit reporting agencies as unpaid." Consent Decree at p.13. Or, as RMA discusses in RMA's ANPR response, the CFPB could prescribe an OSD notice and post the notice online.

buyers do not, in fact, report to the national credit reporting systems. For those that do, a disclosure that the payment of a debt that is OSD will not improve their credit score may well be, in and of itself, misleading and deceptive. As discussed, the effect that payment on out-of-statute debt may have on a credit score is complex and variable, and depends upon the type of score that is at issue; on the consumer's credit profile; and on numerous other factors. Requiring a disclosure regarding the credit reporting effect of paying off out-of-statute debt may well do more harm than good.

## CONCLUSION

Not since 1977 (the year in which the Fair Debt Collection Practices Act was enacted) has our nation had such an important opportunity to rewrite the rules for debt buying and debt collection. Preserving the non-adjudicative collection of OSD, with appropriate protections (reasonable notices and a ban on revitalization and retolling), will improve the consumer credit economy and enhance protections for consumers.

- This approach will assist consumers in paying off their debts and doing so for an amount that is afford able and attractive.
- This approach will help creditors recoup losses on charged-off debt, thereby promoting the availability of consumer credit.
- This approach will encourage the pricing of consumer credit at attractive rates that will help to support the consumer credit economy.
- This approach will encourage the availability of credit to all segments of consumers, including those who are most in need of credit.[36]

Simply stated, the approach discussed in this paper, for all of the reasons discussed in this paper, would be a smart, balanced and responsible way for the CFPB to rewrite the rules for the collection of out-of-statute debt.

## ABOUT RMA

Receivables Management Association International (RMA) is the nonprofit trade association that represents the interests of more than 575 companies that purchase performing and nonperforming receivables on the secondary market. RMA's Receivables Management Certification Program and its Code of Ethics set the "gold standard" within the receivables industry due to its rigorous uniform industry standards of best practice which focus on the protection of the consumer. RMA provides its members with extensive networking, educational, and business development opportunities in asset classes that span numerous industries. RMA continually sets the standard in the receivables management industry through its highly effective grassroots advocacy, conferences, committees, taskforces, publications, webinars, teleconferences, and breaking news alerts. Founded in 1997, RMA is headquartered in Sacramento, California.

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[36] Of course, with the exception of a few states, non-adjudicative collection of OSD is currently the norm. However, as discussed earlier, adjudicative collections before a debt has reached OSD status may be growing. Perhaps this growth, if any, is a result of concerns that non-adjudicative collection of OSD could be banned or sharply limited. Establishing that non-adjudicative collection of OSD will not be restricted may not only avoid a rush to court and preserve current market practices, but may encourage greater reliance on non-adjudicative collections with all of the resulting consumer benefits.