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**SENATE COMMITTEE ON  
BANKING AND FINANCIAL INSTITUTIONS**  
**Senator Monique Limón, Chair**  
**2021 - 2022 Regular**

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**Bill No:** AB 424 **Hearing Date:** June 23, 2021  
**Author:** Stone  
**Version:** June 14, 2021 Amended  
**Urgency:** No **Fiscal:** No  
**Consultant:** Michael Burdick

**Subject:** Private Student Loan Collections Reform Act: collection actions

**SUMMARY**

This bill establishes documentation and evidentiary standards related to the collection of private student loans.

**EXISTING LAW**

- 1) Provides the Student Borrower Bill of Rights (Civil Code Section 1788.100 et seq.), which imposes requirements and prohibitions on student loan servicers intended to promote meaningful access to affordable repayment and loan forgiveness benefits and to ensure that California borrowers are protected from predatory student loan industry practices.
- 2) Provides the Student Loan Servicing Act (Financial Code Section 28100 et seq.), which requires student loan servicers to obtain a license, unless the entity meets specified exemptions.
- 3) Provides the Fair Debt Buying Practices Act (Civil Code Section 1788.50 et seq.), which regulates the buying of charged-off consumer debt, including requirements for debt buyers to have specified evidence of the origin, balance, payment history, and ownership history of a charged-off consumer debt and to provide this evidence to a debtor upon request.

**THIS BILL**

- 1) Establishes the Private Student Loan Collections Reform Act as a new title in the Civil Code.
- 2) Defines “private education loan” as an express extension of credit to a consumer, in whole or in part, for postsecondary educational expenses, regardless of whether the student’s educational institution provided the loan. Excludes from this definition the following:
  - a) Loans made, insured, or guaranteed by the federal government.
  - b) Open-end credit or any loans secured by real property or a dwelling.
  - c) Short-term extensions of credit by an educational institution to cover gap periods between financial aid installments.
- 3) Prohibits a private education lender or a private education loan collector from making any written statement to a debtor in an attempt to collect a private education loan unless the

private education lender or private education loan collector possesses the following information:

- a) The name of the owner of the private education loan.
- b) The creditor's name at the time of default, if applicable.
- c) The creditor's account number, if any, used to identify the private education loan at the time of default.
- d) The amount due at default.
- e) An itemization of interest and fees, if any, claimed to be owed, and whether those were imposed by the original creditor or any subsequent owners of the private education loan.
- f) The date that the private education loan was incurred.
- g) The date of the first partial payment or the first day that a payment was missed, whichever is earlier.
- h) The date and amount of the last payment, if applicable.
- i) Any payments, settlement, or final remuneration of any kind paid to the creditor by a guarantor, cosigner, or surety, and the amount of payment received.
- j) The names of all persons or entities that owned the private education loan after the time of default, if applicable, and the date of each sale or transfer.
- k) A copy of the self-certification form and any other "needs analysis" conducted by the original creditor prior to origination of the loan.
- l) Documentation establishing that the creditor is the owner of the specific individual private education loan at issue, subject to the following requirements:
  - i) If the loan was assigned more than once, each assignment or other writing evidencing the transfer of ownership of the specific loan, so as to establish an unbroken chain of ownership from the original creditor.
  - ii) Each assignment or other writing evidencing transfer of ownership must contain the original creditor's account number, the date of purchase and assignment, and the borrower's correct name associated with the original account number.
  - iii) Each assignment or other writing evidencing transfer of ownership may not be a document prepared for litigation, but must be the actual document by which the assignee acquired the loan.
- m) A copy of all pages of the contract, application, or other documents evidencing the debtor's liability for the private education loan, stating all terms and conditions applicable to the private education loan.
- n) A log of all collection attempts made in the last 12 months, including the date and time of all calls and letters.

- o) A statement as to whether the creditor is willing to renegotiate the terms of the private student loan.
  - p) Copies of all settlement letters made in the last 12 months, or in the alternative, a statement that the creditor has not attempted to settle or otherwise renegotiate the debt prior to suit.
  - q) A statement as to whether the private education loan is eligible for an income-based repayment plan.
  - r) A statement as to whether the debt arising from the private education loan is dischargeable in bankruptcy.
- 4) Requires a private education lender or a private education loan collector to include in its first written collection communication with a debtor, and any time the debtor requests thereafter, the information described in #3.
  - 5) Requires that all settlement agreements between a debtor and either a private education lender or private education loan collector be documented in open court or otherwise reduced to writing. Further requires that the debtor be provided a copy of the written agreement.
  - 6) Provides that if a private education lender or private education loan collector accepts a payment as a complete settlement of an outstanding private education loan that it shall provide the payor with a final statement with specified information, including that a zero balance is owing. This statement may be provided electronically if the parties agree.
  - 7) Forbids a private education lender or private education loan collection from bringing suit or initiating an arbitration or other legal proceeding to collect a private education loan if the applicable statute of limitations has expired.
  - 8) Requires, in a collection action brought by a private education lender or private education loan collector to collect a private education loan, that the complaint allege all of the following:
    - a) The information set forth in (a) – (j) of #3 above.
    - b) That collection of the debt is not time barred under applicable law.
    - c) That the plaintiff has complied with #3 and #4 above.
  - 9) Requires that the complaint have attached to it the documents set forth in (k) – (m) of #3 above.
  - 10) Clarifies that this bill shall not be deemed to require the disclosure in public records of personal, financial, or medical information if its confidentiality is protected by state or federal law.
  - 11) Prohibits a default or other judgment from being entered against a defendant in an action initiated by a private education lender or private loan collector unless the plaintiff submits documents to the court establishing the facts described in #8 above. These documents must

be properly authenticated and in a form admissible as a business record under the Evidence Code.

- 12) Prohibits a court from entering a default judgment in an action on a private education loan unless the plaintiff has complied with the requirements of this bill, and grants the court discretion to dismiss the action if the plaintiff has failed to do so.
- 13) Permits a person to set aside a default or default judgment in an action brought by a private education lender or private education loan collector using the procedures established by the Fair Debt Buying Practices Act if service of the summons resulted in the person not receiving actual notice of the action.
- 14) Provides a cause of action against a creditor, private education lender, or private education loan collector that violates any provision of this bill. Available remedies include:
  - a) Actual damages sustained as a result of the violation.
  - b) Statutory damages of not less than \$500 per violation.
  - c) Exemplary damages under an existing Civil Code provision.
  - d) An order vacating any default judgment taken against the plaintiff.
  - e) Restitution of all moneys taken from or paid by the plaintiff after its default judgment was taken.
  - f) An order directing the private education lender or private education loan collector to either furnish correct information to a credit reporting agency or request that the credit reporting agency correct its report.
  - g) Costs and reasonable attorney's fees, unless the defendant can show that the plaintiff's suit was not brought in good faith.
- 15) Provides that, in a class action, defendants shall be liable for statutory damages of not less than \$500 per violation to each named plaintiff. Additional damages of up to the lesser of \$500,000 or one percent of the net worth of the defendant are available if the court finds that the defendant engaged in a pattern and practice of violating a provision of this bill.
- 16) Exempts private education lenders and private education loan collectors from liability for damages if they show by a preponderance of the evidence that a violation was not intentional and resulted from a bona fide error, and occurred notwithstanding the maintenance of procedures reasonably adopted to avoid error.

## COMMENTS

### 1) PURPOSE

According to the author:

As of June 2020, more than 650,000 Californians owed \$10.3 billion in private student loan debt. Private student loans often have higher interest rates and offer fewer consumer protections than federally-backed student loans. Low-income and

students of color are more likely to take out private loans and are often subjected to predatory practices that increase their debt burden and decrease their likelihood of pay-off.

When borrowers fall behind on loan payments, student loan lenders and debt collectors pursue aggressive litigation, characterized as an “assembly line of lawsuits” against the borrower. Yet, trusts, servicers, and collectors routinely fail to prove that they own the loan, file lawsuits within the statute of limitations, and comply with court requests for additional information. Nevertheless, lenders and collectors automatically win many of these lawsuits because borrowers are unfamiliar with the judicial system, or are unable to afford legal representation. Court rulings in favor of debt collectors result in garnished wages or seizure of federal benefits deposited in bank accounts.

AB 424 will protect private student loan borrowers from unsubstantiated lawsuits and collection on illegitimate debts. The bill requires private student loan lenders and debt collectors to comply with common sense evidentiary standards when bringing debt collection lawsuits against borrowers.

## 2) BACKGROUND

Californians owe more than \$10 billion in private student loan debt, according to statistics provided by the author’s office from the Federal Reserve Bank of New York and the US Department of Education. Using the same data sources, the author’s office estimates that more than 650,000 Californians owe this debt. The California Department of Financial Protection and Innovation stated in a recent press release that more than 1.1 million Californians owe private student loan debt.<sup>1</sup> While there is no authoritative, publicly available data source to provide a more precise estimate, the available evidence suggests that the problem is sufficiently large to warrant closer scrutiny from the Legislature.

Relative to federal loans, private student loans typically charge higher interest rates, contain fewer consumer protections, and are targeted at the most vulnerable borrowers, like those attending for-profit schools.<sup>2</sup> Similar to federal loans, private student loans are difficult to discharge in bankruptcy, which reduces the incentive for private lenders to carefully underwrite loans or to offer modified payment plans. Many private student loans are bundled and sold off after origination to investors who pay third-parties modest fees to service the loans and pursue delinquent debts. This market structure – a risky product with creditor-friendly collections terms serviced by austere third parties – creates incentives that lead to outcomes harmful to vulnerable borrowers.

## 3) LOAN SERVICING AND DEBT COLLECTION ISSUES

Originating lenders often sell or outsource the servicing of private student loans to a third party. After funding the loan, the originator bundles and sells the loan, which may pass through multiple entities before landing in a trust that pays a separate entity to service the loan. The servicer receives payments from borrowers and sends money back to the trust. In the case of delinquent loans, the servicer may assign the loan to a different servicer that

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<sup>1</sup> <https://dfpi.ca.gov/2020/04/23/california-provides-expansion-of-student-loan-relief-most-private-loan-servicers-agree-to-help/>

<sup>2</sup> <https://www.nytimes.com/2017/07/17/business/dealbook/student-loan-debt-collection.html>

specializes in overdue accounts. These servicers may engage in debt collection practices directly or may outsource collection activities to debt collectors. In order to eke out a profit, servicers seek to restrict or streamline activities in order to keep their costs low.

Collections practices related to private student debt have come under legal scrutiny in recent years. In 2017 the Consumer Financial Protection Bureau (CFPB) took action against the National Collegiate Student Loan Trusts and their debt collector, Transworld Systems, Inc., for illegal student loan debt collection lawsuits. These companies sued consumers for private student loan debt that the companies couldn't prove was owed or was too old to sue over, and the lawsuits relied on the filing of false or misleading legal documents.<sup>3</sup> The prevalent factor that caused these failures was a business model that relied on mass production of lawsuits by unqualified paralegals and clerks who were forced to make false attestations of their knowledge of individual cases.<sup>4</sup>

In private litigation, consumers have been sued for debts they no longer owed, by companies they never borrowed from, and by creditors that lacked the legal standing to sue in the first place.<sup>5</sup> Judges across the country have quashed hundreds of lawsuits due to the poor evidentiary merits of cases brought by private student lenders and collectors. The probability of a borrower prevailing in such a case, however, is dependent on whether the borrower is represented by an attorney.

#### 4) DEFAULT JUDGMENTS

Borrowers who ignore a summons related to their private student loans will likely be hit with a default judgment. While some borrowers may intentionally avoid court, others may not be aware of their rights or are unable to afford legal representation. Regardless of the reason, a default judgment authorizes the private student lender or collector to garnish wages and seize certain assets – legal tools with serious consequences that may significantly disrupt a family's life. With default judgments for private student loan debt often exceeding \$10,000, this debt can weigh significantly on a low- to moderate-income family's budget for years.

Cases resulting in default judgments may have concluded differently had the defendants retained legal representation. According to an in-depth report from the National Consumer Law Center in 2014, a review of more than 200 cases in California and Ohio showed that approximately half of cases resulted in a default judgment; however, *every single one* of those cases relied on robo-signed affidavits that did not meet basic evidentiary standards.<sup>6</sup> Defendants in these cases had valid defenses, but their lack of awareness or ability to seek legal counsel left them with substantial debt.

#### 5) THIS BILL PROTECTS CONSUMERS WHO CANNOT AFFORD TO HIRE LAWYERS

Although state law provides consumer protections related to student loan servicing and debt collection, the law fails to establish commonsense evidentiary standards before collection activities commence against consumers who allegedly owe debts related to private student

<sup>3</sup> <https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-national-collegiate-student-loan-trusts-transworld-systems-illegal-student-loan-debt-collection-lawsuits/>

<sup>4</sup> <https://www.nytimes.com/2017/11/13/business/dealbook/student-debt-lawsuits.html>

<sup>5</sup> Ibid.

<sup>6</sup> <https://www.studentloanborrowerassistance.org/wp-content/uploads/2013/05/robo-signing-2014.pdf>

loans. As discussed above, the private student loan market requires heightened scrutiny due to several factors:

- Private student loans carry higher costs, contain fewer consumer protections, and are targeted to a riskier population of borrowers, compared to federal loans.
- Private student loans are rarely held by the originator, often transferring to multiple parties with potentially different servicers that ultimately work on behalf of investors.
- Many defendants who have low awareness of legal procedure and/or lack the financial resources to retain legal counsel are burdened by default judgments that would not have held if collectors were required to show proof of ownership and proof of amount owed.

The author and sponsors approached this bill with the goal of providing similar protections to a consumer who does not have legal representation as the protections provided to a consumer represented by a competent attorney. Both supporters and opponents seemingly agree that the documentation required by this bill would be requested by a consumer's attorney pursuant to a lawsuit filed against the borrower. Instead of waiting for a consumer's attorney to request the documentation after a lawsuit is filed, this bill requires the documentation to be possessed by a collector prior to engaging in written communication with the consumer and establishes minimum evidentiary standards when a collector files a lawsuit.

The Committee may see that the current system is not designed to create equitable outcomes. If two consumers are sued for debts that they do not legally owe, but one consumer can hire legal representation while the other cannot, the deck is stacked against the unrepresented consumer. This bill would bring the effective requirements related to documentation that applies in a court setting upstream in the collections process. By requiring adequate documentation before a collector engages in written communication with the borrower, this bill aims to stop unfair collections practices before they commence, rather than relying on a consumer's attorney to sort out the mess in court, assuming the consumer can afford an attorney in the first place.

#### 6) THIS BILL IS MODELED AFTER THE FAIR DEBT BUYERS PRACTICES ACT

Amendments made by the Assembly Judiciary Committee brought this bill into closer resemblance of the Fair Debt Buyers Practices Act (FDBPA). The FDBPA was enacted in 2013 after an extensive stakeholder process between consumer advocates, creditors, debt buyers, collectors, and then-Attorney General Kamala Harris. The FDBPA addresses similar underlying problems found in the market for charged-off consumer debt (often credit card debt) as this bill seeks to address in the private student loan market: poor recordkeeping related to amounts owed and a lack of documentation showing who has legal rights to collect on debts. These deficiencies led to consumers being sued on debts they did not owe, and unrepresented consumers would often receive default judgments because they failed to appear in court.

The FDBPA has not put an end to all lawsuits filed against debtors. An analysis of court filings in the ten most populous California counties finds that case filings by large debt buyers declined after enactment of the FDBPA, but debt buyers still filed over 50,000 suits in 2017.<sup>7</sup> The analysis also finds that nearly all borrowers – 98 percent – were not represented

<sup>7</sup> <https://www.responsiblelending.org/research-publication/court-system-overload-state-debt-collection-california-after-fair-debt-buyer>

by an attorney. For those who had legal representation, all of their cases were dismissed. For those who represented themselves, 70% of cases were dismissed. The analysis did not show whether or to what extent those borrowers relied on specific provisions of the FDBPA in their defense, but it is reasonable to assume that the FDBPA has provided benefits to consumers by reducing the number of poorly-documented lawsuits filed in the first place and by giving borrowers a better chance of defending themselves if they end up in court. The author and sponsors of this bill hope to see similar, if not stronger, benefits for people who allegedly owe private student loan debt.

#### 7) DOUBLE REFERRAL

This bill is double referred to the Committee on Judiciary.

#### 8) ARGUMENTS IN SUPPORT

A coalition of consumer advocates and community organizations writes in support:

Trusts, loan servicers and debt collectors, or creditors, often lack documentation to prove they have the legal right to pursue private student loan debt by seeking wage garnishment orders in court. Despite this, creditors are dragging borrowers into court across the country, including in California, to try and collect on these debts. This involves misrepresenting to the courts along the way by claiming they have the right to collect on these debts. Many times, debt collectors win these frivolous lawsuits because borrowers are unfamiliar with the judicial system and usually are unable to afford legal representation...

[AB 424] bans the use of mass-produced documentation, also known as “robo-signing,” by prohibiting creditors from obtaining judgements against borrowers without accurate, personalized loan records and documentation. This protection will prevent creditors from obtaining court orders to garnish wages and seize assets to repay defaulted student loans that creditors cannot prove borrowers owe.

#### 9) ARGUMENTS IN OPPOSITION

The Consumer Bankers Association argues that this bill would create regulatory requirements that differ from requirements at the federal level and requests an exemption for federally regulated banks. The association proceeds to argue that while 98% of private student loans are repaid successfully due to careful underwriting, this bill’s requirements related to collection of unpaid debts will “dramatically reduce availability” of private education loans.

### **LIST OF REGISTERED SUPPORT/OPPOSITION**

#### Support

California Association for Micro Enterprise Opportunity  
 California Association of Nonprofits  
 California Association of Realtors  
 California Dental Association  
 California Federation of Teachers  
 California Low-income Consumer Coalition



California Optometric Association  
California Student Aid Commission  
Californians for Economic Justice  
CAMEO - California Association for Micro Enterprise Opportunity  
Center for Public Interest Law University of San Diego School of Law  
Consumer Federation of California  
Consumer Reports  
Friends Committee on Legislation of California  
Housing and Economic Rights Advocates  
Legal Aid Association of California  
Legal Aid Foundation of Los Angeles  
Neighborhood Legal Services of Los Angeles County  
Nextgen California  
Public Counsel  
Public Law Center  
SEIU California  
Student Borrower Protection Center  
Student Debt Crisis  
Student Senate for California Community Colleges  
The Century Foundation  
The Institute for College Access & Success  
University of California Student Association  
University of California, Irvine School of Law Consumer Law Clinic  
Western Center on Law and Poverty  
Young Invincibles

Opposition

California Association of Collectors, INC  
California Bankers Association  
California Credit Union League  
Consumer Bankers Association

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