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DIVISION OF ECONOMIC JUSTICE
CONSUMER FRAUDS & PROTECTION BUREAU

February 12, 2016

Edith Ramirez
Chairwoman
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, DC 20580

Re: Holder Rule Review, FTC File No. P164800

Dear Commissioner Ramirez:

The Office of the New York Attorney General (“NYAG”) along with the Attorneys General of Idaho, Iowa, Kentucky, Louisiana, Maine, Maryland, Minnesota, Virginia and Washington welcome the opportunity to submit comments in response to the Federal Trade Commission’s review of its Holder Rule Regulation, 16 CFR Part 433.

(1) Is there a continuing need for the Holder Rule as currently promulgated?

The underlying policy considerations that prompted the Federal Trade Commission (“the Commission”) to promulgate the Holder Rule are as relevant and pressing today as they were in 1975 when the rule was adopted. Consumers continue to rely on seller-offered or arranged financing for a vast array of consumer goods and services. Further, the NYAG is regularly confronted with examples of unscrupulous sellers who defraud consumers into financing goods or services using deceptive marketing and sales practices. These sellers often work closely with lenders who finance and/or accept assignment of the consumer credit agreements and who know, or have reason to know, of the seller’s fraudulent or illegal conduct. In many cases, the lender provides the financing that permits a seller to continue defrauding consumers. The rule affords individual consumers a powerful tool by enabling them to assert the same claims and defenses against the lender that they could raise against the original seller.

Although the NYAG and other state law enforcement officials can bring suit and seek monetary relief under their respective consumer protection statutes against the sellers, all too often the wrongdoer has gone out of business or lacks funds to provide consumers with the refunds to which they are entitled. Where the victims of those practices have financed their purchases, the Holder Rule also enables law enforcement agencies to obtain relief for consumers who otherwise would be left without an adequate remedy.

(2) What benefits has the Holder Rule provided to consumers? What evidence supports the asserted benefits?

One recent lawsuit filed by the NYAG demonstrates the continuing importance and relevance of

the Holder Rule. The NYAG amassed extensive evidence that consumers were induced by The College Network, a nationwide seller of certain alleged educational goods and services, to sign Purchase Agreements through high pressure, one-on-one sales pitches during which sales associates materially misrepresented nearly every aspect of the seller's so-called "program." In many cases, the contract amounts exceeded \$10,000. Because most consumers were of modest means, the seller offered, and the vast majority of consumers accepted, financing that was provided by third party lenders with whom the seller had contracted. As required by the Holder Rule, the consumer promissory notes, which typically had 5 year terms, contained the Holder Rule notice.

Our lawsuit alleged, among other things, that The College Network engaged in a variety of deceptive acts and practices and sought restitution for consumers pursuant to New York's consumer protection statutes.¹ The lawsuit also named one lender that, by its own admission, provided the financing to the bulk of the seller's customers. Relying on the Holder Rule language in the promissory notes, the NYAG has sought both to prohibit the lender from collecting on the promissory notes and to require the lender to refund the amounts paid by the consumers whose notes the lender holds. The availability of such injunctive and monetary relief against the lender may be the only viable means of providing consumers with meaningful relief. The Holder Rule ensures that injured consumers who received little, if any, benefit from the seller, will not be left without recourse and forced to continue making payments totaling thousands of dollars for a program they do not use.

(3) What modifications, if any, should the Commission make to the Holder Rule to increase its benefits to consumers? (a) what evidence supports the proposed modifications? (b) How would these modifications affect the costs and benefits to consumers?

Based on our discussions with consumers, we have found that even where contracts contain the Holder Rule language, consumers are generally unaware of their right to assert claims and defenses against the lender.

The Commission has recognized that consumers often simply fail to read the terms of their contracts. SBP, 40 Fed. Reg. 53506, 53525. As is typically the case with a retail installment contract or promissory note, the Holder Rule notice is often embedded among numerous densely worded paragraphs and/or inserted on the reverse side of the document, where consumers are unlikely to notice it. Additionally, consumers are often pressured to sign numerous documents during a sales pitch and have inadequate opportunity to read through them. But, even if consumers do read the Holder Rule provision, its "legalistic" wording may make it difficult for consumers to understand their rights. SBP, 40 Fed. Reg. 53506, 53526. Those who understand the provision are unlikely to retain the information, which, at that time, is likely not to be of relevance.

Further, the NYAG has found that, in some instances, after consumers discover that they have been defrauded and attempt to cancel their financing contracts or have stopped making

¹ The lawsuit, which was filed in June 2015 is still pending. See <http://www.ag.ny.gov/press-release/ag-schneiderman-sues-company-allegedly-duping-prospective-nursing-students-across-nys>.

payments, the creditor misrepresents the consumer's obligations under the contract. Consumers are often falsely led to believe that the debts are valid and/or that the misconduct of the seller has no bearing on their obligation to make payments under their loans. Thus, for example in our investigation of The College Network, the majority of consumers who felt they had been defrauded, and in many cases, had stopped using the seller's materials, nonetheless continued to make payments to the lender. Many consumers felt compelled to do so for fear of harming their credit or by representations of the lender that they were obligated to continue making payments. This evidence highlights the need to modify the regulation to increase the likelihood that consumers are aware of their rights under the Holder Rule. The NYAG offers the following suggestions.

a. Require the Holder Rule language to be included in collection notices.

The Commission should amend the regulation to require that collection notices sent either by the lender or a third party debt collector include a notice advising consumers of their right to assert seller-related claims and defenses against the creditor. Such a modification will greatly increase the likelihood that consumers will be aware of their rights. First, collection letters generally are not lengthy and therefore consumers would be more likely to notice the Holder Rule language. Second, if the consumer's default is related to the non-performance or misconduct of the seller, the notice would be more effective at this juncture, when it is presented at a time when it has more relevance to the consumer. Further, including the notice in the letter would decrease the likelihood that consumers would be misled by debt collectors who may assert that the debt is owed, notwithstanding the debtor's claim of seller misconduct.

We note that the Commission, when initially seeking public comment on the proposed rule, rejected suggestions by consumer groups to require a separate notice annexed to the financing contract advising consumers of their rights, citing the expense to sellers and creditors. SBP, 40 Fed. Reg. 53506, 53526. The NYAG does not anticipate that the amendment urged here--requiring the notice in collection letters--would involve considerable expense or otherwise unduly burden sellers or creditors. As a practical matter, it is likely that such consumer debts are sold or assigned to debt collectors in bulk, rather than on a piecemeal basis. Thus, it should not be difficult for either creditors or third party debt collectors to identify the accounts where such notices must be included in collection letters. Nor should the added notice result in any significant expense because the proposed amendment would not require debt collectors to send a separate notice, but rather, would simply require the notice to be included in any collection letters it does send.

b. Modify the Holder Rule language to make it more readily understandable.

We think the Holder Rule notice, as written, may not be readily understood by consumers and urge the Commission to amend it using less "legalistic" language. 40 Fed. Reg. 53506, 53526. In its SBP, the Commission recognized this potential shortcoming of the notice, but suggested that the FTC's subsequent consumer education efforts and periodic lawsuits testing the rule would result in "increasing knowledge and use on the part of all consumers." *Id.* However, the NYAG's experience suggests that, despite the rule's 40 year existence, consumers do not have a general awareness of their rights, highlighting the importance of ensuring that consumers are advised of their rights in language that is easily understood by a layperson. We therefore, urge

the Commission to revise the notice language.

c. Modify the regulation to explicitly state that consumers' right to assert claims is unconditional and cannot be waived.

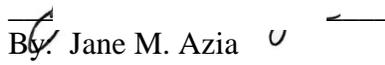
We note that the Commission issued an advisory opinion in May 2012 affirming that the Holder Rule does not limit a consumer's right to an affirmative recovery to circumstances where the consumer can legally rescind the transaction or where the goods or services sold to the consumer are worthless. The letter cited a number of state and federal decisions reading such a limitation into the rule. FTC Holder Rule Advisory Op., May 3, 2012 (FTC File No. P124802). While the NYAG agrees that the plain language of the rule places no such limit on the consumer's right to an affirmative recovery and the advisory opinion removes any perceived ambiguity, it nonetheless makes sense to amend the rule to explicitly state that the consumer's right to an affirmative recovery is unqualified.

The FTC should also clarify that the holder rule cannot be waived.

d. Amend the rule to make clear that any holder of a consumer credit contract is subject to all claims and defenses regardless of whether the underlying contract contains the required notice.

We also note one additional significant limitation of the Holder Rule. Because the rule only regulates the conduct of "sellers," consumers are potentially left without remedy against the creditor if the notice is omitted from the lender's promissory note. Thus, we urge the Commission to require that such a notice be read into any consumer credit contract to ensure that even if the absence of such an express notice, lenders who are assigned the underlying contract or other holders of consumer credit contracts are subject to all claims and defenses that could be asserted against the seller of such goods or services. There is clear precedent under the UCC for reading the notice into such contracts. Article 9 of the UCC, adopted in all fifty states, makes an omitted Holder notice part of a credit-sale agreement as a matter of law. UCC §§ 9-403(d), 9-404(d). Article 3 includes a similar provision for promissory notes. UCC § 3-305(e). The Holder Rule should also expressly provide that a holder who misrepresents a consumer's liability under the credit agreement by, for example, misrepresenting that the consumer can only assert claims and defenses against the seller and must continue paying the holder, is engaged in an unfair and deceptive practice.

Respectfully submitted,
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