

February 12, 2016

Federal Trade Commission
Office of the Secretary
600 Pennsylvania Avenue, NW
Ste. CC-5610 (Annex B)
Washington, DC 20580

Re: Holder Rule Review, FTC File No. P164800

Ladies and Gentlemen:

The American Financial Services Association (“AFSA”)¹ welcomes the opportunity to comment on the Federal Trade Commission’s Request² for public comments on the overall costs and benefits, and regulatory and economic impact, of its Rules and Regulations under the Trade Regulation Rule Concerning Preservation of Consumers’ Claims and Defenses, commonly known as the “Holder Rule.” Since the Commission promulgated the Holder Rule in 1975, AFSA members’ consumer credit contracts regulated by the Commission’s Rule have included the Holder Rule’s language and Notice. Accordingly, AFSA members are uniquely qualified to comment on the application and impact of the Holder Rule.

AFSA is concerned about recent attempts to expand assignee liability well beyond the limits of any fair reading of the Holder Rule’s plain language. In AFSA’s view, the Commission should not amend or alter the text of the Holder Rule, but should clarify and confirm its position in the four respects mentioned below.

AFSA sets forth its comments in four points below because each of these points permeate AFSA’s responses to many of the fifteen questions on which the Commission’s Request seeks comment. AFSA addresses each of the Commission’s questions individually in Attachment A to this Letter.

I. The Commission Should Not Amend or Alter the Text of the Holder Rule, but Should Clarify and Confirm the Meaning of the Rule’s Plain Language

A. The Holder Rule and Summary of AFSA’s Comments

The Commission promulgated the Holder Rule largely to abrogate the Holder-in-Due-Course doctrine in consumer credit transactions, and to prevent a seller from “separat[ing] the buyer’s duty to pay for the goods or services from the seller’s reciprocal duty to perform as promised.”³ The

¹ Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including traditional installment loans, mortgages, direct and indirect vehicle financing, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans. AFSA is based in Washington, D.C.

² 80 Fed. Reg. 230 at pp. 75018-20.

³ See FTC, Promulgation of Trade Regulation Rule and Statement of Basis and Purpose 40 Fed.Reg. 53506, 53507-53508, 5352 (Nov. 15, 1975) (“The definition of “Holder in Due Course” which appears in Article 3 of the Uniform Commercial Code is a recapitulation of principles which were first articulated in *Miller v. Race*, 97 Eng. Rep. 398 (KB

Commission's goal in this regard has been successful. Since its promulgation, the Holder Rule has, in fact, prevented sellers from separating the buyer's duty to pay for the goods or services from the seller's reciprocal duty to perform as promised. The Holder Rule and its required Notice, give consumers a practical means of redress in their purchase of consumer goods and services, and give creditors an incentive to supervise their sellers to prevent losses.

The Commission has noted repeatedly that the language of the Holder Rule is clear and that its plain language should be applied.⁴ It has noted that courts have not always followed the clear and plain language of Rule.⁵ And, it affirmed the "plain language" approach when it opined in 2012 that "no additional limitations on a consumer's right to an affirmative recovery should be read into the Rule, especially since a consumer would not have notice of those limitations because they are not included in the credit contract."⁶

But there is more to the Holder Rule than preserving the claims and defenses which debtors can assert against sellers, and there are many other persistent assaults upon the "plain language" of the Rule also deserving of the Commission's scrutiny. For example, courts, commentators, and the plaintiffs' bar have attempted to apply the Holder Rule to transactions that are not "consumer credit contracts," to transactions that otherwise would be exempt from Truth-in-Lending, or to transactions that are non-executory, have been rescinded by the Holder, or have been paid-in-full by the consumer.

Of particular concern are attempts to expand assignee liability well beyond any fair reading of the Holder Rule's purposed and plain limits. The Rule conditions even an innocent Holder's right to payment on the original seller's duty to perform. But balanced for fairness' sake against this imposition on an innocent party is an "important limitation on the creditor's liability"⁷ that is: "[r]ecoveries hereunder by the debtor shall be limited to amounts paid by the debtor hereunder." Efforts abound, however, to ignore this plain language of the Holder Rule and allow excess recoveries from Holders of consumer credit contracts.

All these attempts to expand the Holder Rule contradict both the Rule's plain language and the

1758). To protect the burgeoning commercial paper market, the Court in *Miller* decided that a bona fide purchaser of an instrument which was negotiable on its face should not be required to look behind the face of obligation").

⁴ Clark, Letter to National Consumer Law Center, pp. 3 (May 3, 2012) ("The Commission affirms that the Rule is unambiguous, and its plain language should be applied"); Keller, FTC Letter to National Consumer Law Center, (May 13, 1999).

⁵ Clark, Letter to National Consumer Law Center, pp. 1 (May 3, 2012) (contrary to the first clause of the Holder Rule - the so-called "claims and defenses" clause - "some courts continue to bar consumers from affirmative recoveries unless rescission is warranted").

⁶ Clark, Letter to National Consumer Law Center, pp. 3 (May 3, 2012).

⁷ FTC, Staff Guidelines on Trade Regulation Rule Concerning Preservation of Consumers' Claims and Defenses (Holder in Due Course Rule), Bureau of Consumer Protection, pp. 6 (May 4, 1976) ("There is an important limitation on the creditor's liability, however. The wording of the Notice includes the sentence, "Recovery hereunder by the debtor shall be limited to amounts paid by the debtor hereunder." This limits the consumer to a refund of moneys paid under the contract, in the event that an affirmative money recovery is sought. In other words, the consumer may assert, by way of claim or defense the right not to pay all or part of the outstanding balance owed the creditor under the contract; but the consumer will not be entitled to receive from the creditor an affirmative recovery which exceeds the amounts of money the consumer has paid in.")

Commission's stated purpose for promulgating the Rule.

The Commission need not, and should not, amend or alter the text of the Holder Rule. The Commission should, however, clarify and confirm its position in four important ways:

1. The Commission should confirm that the Holder Rule applies only to "consumer credit contracts." The Commission should not amend or expand the Holder Rule to apply it to consumer vehicle leases.
2. The Commission should confirm that the Holder Rule applies only to "consumer credit contracts" for the sale of consumer goods or services that are not exempt from Truth-in-Lending⁸ and Regulation Z.⁹
3. The Commission should confirm that the Holder Rule applies only to the "holder" of an executory¹⁰ "consumer credit contract." The Holder Rule does not apply to rescinded, re-financed, or paid-in-full consumer credit contracts.
4. The Commission should confirm that under the Holder Rule's plain language, any court-awarded sum, under the Rule, must be "limited to amounts paid by the debtor hereunder." This limitation includes interest, costs and attorney fees. This limitation also precludes a derivative injunction under the Rule,¹¹ since an injunction is not "an amount paid hereunder" by the debtor.

⁸ 15 U.S.C. § 1603(3) ("This subchapter does not apply to the following: (1) Credit transactions involving extensions of credit primarily for business, commercial, or agricultural purposes, or to government or governmental agencies or instrumentalities, or to organizations. . . (3) Credit transactions, other than those in which a security interest is or will be acquired in real property, or in personal property used or expected to be used as the principal dwelling of the consumer and other than private education loans (as that term is defined in section 1650(a) of this title), in which the total amount financed exceeds \$50,000.")

⁹ 12 C.F.R. § 1026.3 ("This regulation does not apply to the following: (a) Business, commercial, agricultural, or organizational credit. (1) An extension of credit primarily for a business, commercial or agricultural purpose. (2) An extension of credit to other than a natural person, including credit to government agencies or instrumentalities. (b) Credit over applicable threshold amount (1) Exemption (i) Requirements. An extension of credit in which the amount of credit extended exceeds the applicable threshold amount or in which there is an express written commitment to extend credit in excess of the applicable threshold amount, unless the extension of credit is: (A) Secured by any real property, or by personal property used or expected to be used as the principal dwelling of the consumer; or (B) A private education loan as defined in § 226.46(b)(5). (ii) Annual adjustments. The threshold amount in paragraph (b)(1)(i) of this section is adjusted annually to reflect increases in the Consumer Price Index for Urban Wage Earners and Clerical Workers, as applicable. See the official staff commentary to this paragraph (b) for the threshold amount applicable to a specific extension of credit or express written commitment to extend credit.")

¹⁰ Black's Law Dict. (9th ed. 2009) ("Executory contract": "Contractual obligation fulfillment actively being done. Some contractual expectations are yet to be done by one or more parties"); Black's Law Dict. (9th ed. 2009) ("Executed and Executory": "Contracts are also distinguished into executed and executory: executed, where nothing remains to be done by either party, and where the transaction is completed at the moment that the arrangement is made, as where an article is sold and delivered, and payment therefor is made on the spot; executory, where some future act is to be done, as where an agreement is made to build a house in six months, or to do an act on or before some future day, or to lend money upon a certain interest, payable at a future time.")

¹¹ Nothing in the Rule prevents a Court from issuing an injunction against a Holder for the Holder's own conduct independent of the Holder Rule.

AFSA explains in greater detail below why its concerns are crucial to the Commission's Request.

B. The Commission Should Confirm and Clarify the Meaning of the Rule's Plain Language

1. The Holder Rule Does Not Apply to Consumer Vehicle Leases.

The plain language of the Rule does not apply to consumer vehicle leases because the Rule applies only to "consumer credit contracts." The Rule defines "consumer credit contract" as "[a]ny instrument which evidences or embodies a debt arising from a 'Purchase Money Loan' transaction or a 'financed sale.'"¹² Neither of these can possibly include a consumer lease.

Nor should the Commission revise the Holder Rule's definition of "consumer credit contract" to include consumer leases. Congress enacted the Consumer Leasing Act¹³ ("CLA") in 1976 as an amendment to TILA in part "to provide consumers with meaningful information about the component and aggregate costs of consumer leases, so that they can make better informed choices between leases, *and between leases and credit sales.*"¹⁴

Requiring that both consumer credit contracts and consumer vehicle leases contain identical terms - including the Notice - blurs the line between consumer credit contracts and consumer vehicle leases and gives consumers less informed choices in choosing whether to purchase or to lease a new vehicle. Narrowing the distinction between these two very different types of financial instruments by extending liability to a lease assignee beyond TILA's "face-of-the-document" assignee liability rule does not further the purpose of the CLA or its state law equivalents; namely, to assist the consumer in making informed choices between leases and credit sales, or understanding all the ramifications.

Congress enacted the CLA in 1976 as an amendment to TILA because consumer leases were increasingly being used as an alternative to credit purchases.¹⁵ Vehicle lessors and consumers leasing vehicles have acted under TILA's assignee liability rules for the last 40 years. Despite leasing accounting for approximately 27% of new vehicle transactions,¹⁶ there is no demonstrable

¹² 16 C.F.R. § 433.1, subd. (i) (italics supplied). A "purchase money loan" transaction involves a cash advance received by the customer "which is applied, in whole or substantial part, to a purchase of goods or services from a seller." 16 C.F.R. § 433.1, subd. (d). "Financing a sale" refers to "[e]xtending credit to a consumer in connection with a 'Credit Sale' within the meaning of the Truth in Lending Act and Regulation Z." 16 C.F.R. § 433.1, subd. (e). Regulation Z, in turn, defines a "credit sale" as a sale in which (1) the seller is the creditor, and the consumer agrees to pay an amount substantially equivalent to or in excess of the total value of the property involved, and (2) either will become, or has the option of becoming, the owner of the property upon compliance with the agreement for no additional consideration or for nominal consideration. Accordingly, consumer leases are not "consumer credit contracts" under the Holder Rule, and do not need to include the Holder Rule's Notice. See *LaChapelle v. Toyota Motor Credit Corp.*, 102 Cal.App.4th 977, 987 (Cal.App. 2002) ("The lease agreement therefore does meet the definition of a consumer credit contract, and that the FTC Holder Rule, therefore, does not apply to it"); *Bescos v. Bank of America*, 105 Cal.App.4th 378, 393 (Cal.App. 2003) ("Furthermore, the lease agreement does not qualify as a "consumer credit contract. . . Thus, the FTC Holder Rule does not apply to the facts of this case.")

¹³ 15 U.S.C. § 1667 et seq.

¹⁴ Sen. Rep. No. 94-590 (1976), reprinted in 1976 U.S.Code Cong. & Admin. News, pp. 431, 432 (emphasis added).

¹⁵ Sen. Rep. No. 94-590 (1976), reprinted in 1976 U.S.Code Cong. & Admin. News, pp. 431, 432.

¹⁶ <http://www.edmunds.com/car-news/car-shoppers-lease-vehicles-at-record-pace-study-says.html>; <https://www.>

need for expanding the Holder Rule to include automobile leases by expanding lease-holder assignee liability beyond TILA's more limited facial-defect liability rule. Many financial institutions create an application and leasing forms and provide them to vehicle dealers who are in the best position to ensure compliance with related CLA-requirements.¹⁷

Consumer vehicle lessors have priced their products based on proper functioning liability rules in place since 1976. "It would place a significant burden on a financial institution to be required to ascertain that the lessee and the dealer actually had "agreed upon" a particular value in order to shield itself from liability in every lease transaction. When the cost of monitoring and investigation is added to that of the litigation that often results from the acts of allegedly errant dealers, ... it can be expected to increase interest rates and, ultimately, to shrink the availability of credit. Such a result does not ultimately assist the consumer."¹⁸ Moreover, consumer lease assignees, unlike holders of consumer credit contracts, already are exposed to additional risks such as depreciation beyond the residual value disclosed on the closed-end lease, and they are able to offer more attractive residual values to consumer lessees when not allocating for assignee liability beyond TILA's assignee liability rules.

The Commission should not upset these adequately functioning liability and pricing rules by amending or altering the Holder Rule to include consumer vehicle leases.

2. The Holder Rule applies only to "consumer credit contracts" that are not exempt from Truth-in-Lending and Regulation Z

The Commission has confirmed that the Holder Rule is tethered to limitations set forth in TILA and Reg. Z.¹⁹ This is because "financing a sale" refers to "[e]xtending credit to a consumer in connection with a 'Credit Sale' within the meaning of the Truth in Lending Act and Regulation Z,"²⁰ but "[c]redit transactions ... in which the total amount financed exceeds \$50,000"²¹ are exempt from TILA. There is no need to extend the Holder Rule to protect the wealthiest Americans purchasing luxury goods and services, such as a \$1,000,000 Recreational Vehicle or a \$100,000+ luxury automobile. And, the category of consumer credit contracts subject to the Holder Rule will expand in correlation to adjustments to Regulation Z without tinkering with the Holder Rule's plain language.

experianplc.com/media/news/2015/q3-2015-safm-part-2/ ("leasing accounted for nearly 27 percent of all new vehicle transactions").

¹⁷ *Bescos v. Bank of America*, 105 Cal.App.4th 378, 391 (Cal.App. 2003)

¹⁸ *Id.*

¹⁹ FTC, Staff Guidelines on Trade Regulation Rule Concerning Preservation of Consumers' Claims and Defenses (Holder in Due Course Rule), Bureau of Consumer Protection, pp. 9 (May 4, 1976) ("Additional limitations on affected transactions are present because the definitions of "Financing a Sale" and "Purchase Money Loan" expressly refer to the Truth-in-Lending Act and Regulation Z, and thus incorporate the limitations contained in these laws. As a result, even with respect to transactions involving a sale of consumer goods or services, a purchase involving an expenditure of more than \$25,000 is not affected by the Rule.")

²⁰ 16 C.F.R. § 433.1, subd. (e); FTC, Promulgation of Trade Regulation Rule and Statement of Basis and Purpose 40 Fed. Reg. 53506, 53506 (Nov. 15, 1975)

²¹ 15 U.S.C. § 1603(3) ("Exempted transactions"). When the Commission originally promulgated the Holder Rule, credit transactions in which the total amount financed exceeded \$25,000 were exempt from TILA's reach. Congress later amended TILA to extend TILA's applicability to transactions that do not exceed \$50,000, which is and has been subject to annual adjustment under Regulation Z. (12 C.F.R. § 226.3)

Because “. . .the Notice must appear without qualification,”²² the Commission should clarify that creditors do not run afoul of the Holder Rule by including qualifying language that the Notice and Holder Rule do not apply if the consumer credit contract is exempt from TILA and Regulation Z. The Commission need not modify the Holder Rule to do so, however, so long as the Commission confirms its purpose and intent.²³

3. A “Holder” under the Holder Rule is only the person who holds an executory consumer credit contract

The Commission should clarify that the “Holder” under the Holder Rule means only the current Holder of an executory consumer credit contract, not every entity that previously held the contract.

Though the Holder Rule does not define the term “Holder,” its meaning is readily apparent from the fact that the Commission adopted the rule largely to abrogate the Holder-in-Due-Course doctrine in consumer credit transactions.²⁴ As the Commission noted, the Holder-in-Due-Course doctrine has been codified in Article 3 of the Uniform Commercial Code (“UCC”).²⁵ Although the Commission’s promulgation of the Holder Rule altered the “Holder in due course” doctrine, it did not alter what a “Holder” is, but instead kept the term “Holder” tethered to the UCC’s definition.

The UCC defines “Holder” to mean (A) the person in possession of a negotiable instrument that is payable either to bearer or, to an identified person that is the person in possession.²⁶ Thus, “Holder” under the Uniform Commercial Code turns on (1) physical possession of the negotiable instrument, and (2) entitlement to receive payment under it. “Holder,” means: (A) the person in possession of a negotiable instrument that is payable either to bearer or, to an identified person that is the person in possession.”

A person who has rescinded assignment of a consumer credit transaction, or who has been paid in full by the consumer or by the consumer’s re-finance of the consumer credit contract with a new

²² FTC, Staff Guidelines on Trade Regulation Rule Concerning Preservation of Consumers’ Claims and Defenses (Holder in Due Course Rule), Bureau of Consumer Protection, pp. 6 (May 4, 1976)

²³ “[E]ven though contained within the contract, [the clause] was not the subject of bargaining between the parties, and indeed could not have been. It is part of the contract by force of law . . .” *Taylor v. Quality Hyundai, Inc.* 150 F.3d 689, 693 (7th Cir. 1998). Legally required contractual language is interpreted in accordance with the intent of the Legislature or agency that prescribed it, rather than according to otherwise applicable rules of contract interpretation. *E.g. Feaz v. Wells Fargo Bank, N.A.*, 745 F.3d 1098, 1104-06 (11th Cir. 2014); *United States Elevator Corp. v. Associated Internat. Ins. Co.* 215 Cal.App.3d 636, 647 (1989).

²⁴ FTC, Promulgation of Trade Regulation Rule and Statement of Basis and Purpose, 40 Fed.Reg. 53506, 53507-53508 (Nov. 15, 1975); *Lafferty v. Wells Fargo Bank*, 213 Cal.App.4th 545, 559 (2013)

²⁵ See, e.g., Cal. Com. Code, § 3305(b).

²⁶ See, e.g., Com. Code, §§ 1201(b)(21)(A) (emphasis added); see also Black’s Law Dict. (9th ed. 2009) (“Holder, def. 1: “The Holder of a bill of exchange, promissory note, or check is the person who has legally acquired the possession of the same, from a person capable of transferring it, by endorsement or delivery, and who is entitled to receive payment of the instrument from the party or parties liable to meet it.”). The converse also is true. “Person entitled to enforce” an instrument means (a) the Holder of the instrument, (b) a nonHolder in possession of the instrument who has the rights of a Holder, or (c) a person not in possession of the instrument who is entitled to enforce the instrument pursuant to Section 3309 or subdivision (d) of Section 3418.” (Cal. Comm. Code § 3301)

creditor, is no longer the “Holder” subject to liability under the Holder Rule. Whether rescinded or paid-in-full, a former creditor no longer has possession of the credit contract and, quite literally, does not “hold” it. Thus, the person does not have possession of the credit contract nor is the person entitled to receive payment under it. Yet, debtors have attempted to foist liability on former Holders of consumer credit contracts under a “once-a-Holder/always-a-Holder” theory.²⁷ In other words, these debtors contend that a former Holder is subject to liability under the Holder Rule even after it no longer possesses, or retains any rights under, the consumer credit contract.

In context, “any Holder” has a simple, plain meaning, which is what the Commission repeatedly has stated. The term “any” protects consumers whatever the nature of the Holder and no matter how many times the consumer credit contract is assigned or purchased. In other words, a third “Holder” down the line of multiply-sold debt is still subject to the Notice contained in the contract – so long as the contract is still executory. But, the third “Holder” would be the only “Holder;” intermediary, non-holder creditors to whom payments are not being made should not be vicariously liable for the seller’s conduct.

This interpretation also fulfills the principal purpose of the FTC Holder Rule which, according to the Commission, was intended primarily to prevent a seller from “separat[ing] the buyer’s duty to pay for the goods or services from the seller’s reciprocal duty to perform as promised.”²⁸ That objective is fully satisfied if the party currently possessing the contract and holding the right to payment under it is subject to claims and defenses against the seller. The seller’s and buyer’s obligations are fully reunited. The buyer can stop paying on the contract if the seller has breached or committed fraud, thus exercising the buyer’s most powerful self-help remedy—“his most effective weapon.”²⁹

By contrast, a contrary interpretation would revive—albeit in the consumer’s favor—the very evil that the Commission sought to correct; namely, separation of the right to payment under the consumer credit contract from the seller’s obligation to perform it. A former Holder no longer has the right to payment under the contract, yet the former Holder would remain liable for the seller’s breach of its obligations under the contract.

4. The plain language of the Holder Rule’s limitation of liability to “amounts paid by the debtor hereunder” caps the Holders’ liability

- (a) Interest, costs, and attorneys’ fees are included in, and capped by, the Holder Rule’s limitation of liability to “amounts paid by the debtor hereunder”

The Holder Rule’s second sentence states: “Recovery hereunder by the debtor shall not exceed amounts paid by the debtor hereunder.” By its plain language,³⁰ the Holder Rule limits the debtor’s “recovery” under the Rule to the amount the debtor paid under the contract. The debtor cannot “recover” any additional sum from the Holder, whatever the added sum’s label—whether it be damages, interest, costs, attorney fees or otherwise. “It would be antithetical to the language and

²⁷ *E.g. Tun v. Plus West LA Corp.*, (Cal. Sup. No. 30-2011-00510433)

²⁸ 50 Fed. Reg. at p. 53522.

²⁹ *Id.*, at p. 53509.

³⁰ FTC Advisory Opinion Letter (May 3, 2012) p. 3); *Lafferty v. Wells Fargo Bank*, 213 Cal.App.4th 545, 560-561 (2013).

its typographic emphasis to hold that the Holder Rule language does not mean what it says.”³¹ The Holder Rule’s plain meaning should govern its second sentence’s limitation on recovery just as it governs the Rule’s first sentence’s imposition of liability on the Holder for all claims and defenses the consumer has against the dealer.

Fairly read, the Rule’s limit on the consumer’s “recovery” should extend beyond merely capping damages or restitution. “Recovery” means “[a]n amount awarded in or collected from a judgment or decree.”³² As an award of interest, costs, or attorney fees constitutes an amount awarded in or collected from a judgment, it is a “recovery” and hence falls with the literal, plain meaning of the Holder Rule’s second sentence.

Not surprisingly, courts applying the Commission’s plain language repeatedly have held that if attorneys’ fees are awardable against the Holder under the Notice, they are part of the debtor’s “recovery” under the Holder Rule and thus cannot exceed the amounts the debtor paid under the contract.³³ The Commission cited a number of these decisions with approval in the footnote appended to this sentence: “It remains the Commission’s intent that the plain language of the Rule be applied, which many courts have done.”³⁴ The Commission should affirm the plain language of the Rule that the Holder Rule’s limitation on recovery applies to all recovery under the under the Notice - including interest, costs and attorney fees.

(b) The Holder Rule’s plain language limiting any court-awarded sum “to amounts paid by the debtor hereunder” prevents using the Rule to impose an injunction on Holders

³¹ *Id.*, at p. 560; see also FTC Letter, at p. 3.

³² Black’s Law Dict. (9th ed. 2009) “recovery,” def. 3; see also *Goodman v. Lozano*, 47 Cal.4th 1327, 1333 (2010).

³³ *Houser v. Diamond Corp.*, 125 Wash.App. 1009, 2005 WL 94452, at *6 (Wn. App. 2005) (“Treble damages and attorney fees which would be available remedies against Designer Homes are available against AHF, subject to the limitation on total recovery contained in 16 C.F.R. sec. 433.2”); *Alduridi v. Community Trust Bank*, 1999 WL 969644, at *12 (Tn. App. 1999) (“The Plaintiffs’ claim for attorney’s fees against NationsBank is based in part on the Holder Rule. In this case, the attorney’s fees are not an amount ‘paid by the debtor hereunder’ and thus are not recoverable under the Holder Rule”); *Riggs v. Anthony Auto Sales, Inc.*, 32 F.Supp.2d 411, 417 (W.D. La. 1998) (“Accordingly, this court holds that a creditor’s derivative liability for seller misconduct under the FTC rule is limited to the amount paid by the consumer under the credit contract. Therefore, with respect to each plaintiff, each lender’s liability is limited to the amount paid to it by that plaintiff. In other words, each plaintiff may recover from their lender their actual damages times three or \$1,500, whichever is greater, the costs of the action, and their lender’s pro rata share of reasonable attorney’s fees, provided that the maximum recovery by any plaintiff may not exceed the amount paid the lender by that plaintiff”); *Simpson v. Anthony Auto Sales, Inc.*, 32 F.Supp.2d 405, 410-411 (W.D. La. 1998) (same); *Patton v. McHone*, 1993 WL 82405, at *4-5 (Tenn. App. 1993) (“The Chancellor wrongfully assessed attorney’s fees against FMCC.”); *Reagans v. Mountainhigh Coach Works, Inc.*, 881 N.E.2d 245, 253-254 (Ohio 2008) (“We conclude that the bank is not derivatively liable under the FTC rule for treble damages and attorney fees imposed against the seller under the Ohio Consumer Sales Practices Act.”); *Scott v. Mayflower Home Improvement Corp.*, 831 A.2d 564, 576 (N.J. Super. 2001) (“The court holds that plaintiffs may not recover from the defendants treble damages or counsel fees if that would result in a recovery in excess of the amount paid by the consumer”), *over’d on other g’nds*, *Psensky v. Am. Honda Fin. Co.*, 875 A.2d 290, 296 (N.J. Super. A.D. 2005).

³⁴ FTC Advisory Opinion Letter (May 3, 2012) p. 3 & n. 7. The three cases are *Simpson v. Anthony Auto Sales, Inc.*, 32 F.Supp.2d 405, 409 n. 10 (W.D. La. 1998); *Riggs v. Anthony Auto Sales, Inc.*, 32 F.Supp.2d 411, 416 n. 13 (W.D. La. 1998); and *Scott v. Mayflower Home Improvement Corp.*, 831 A.2d 564, 573-574 (N.J. Super. Ct. Law Div. 2001). Another of the cases cited in the same footnote affirmed an attorney fee award without considering whether the Holder Rule’s cap on “recovery” against the Holder applied to the fee award. See *Jaramillo v. Gonzalez*, 50 P.3d 554, 563-564 (N.M. Ct. App. 2002).

Nothing in the Holder Rule prevents a court from issuing an injunction against a Holder for the Holder's own independent conduct against a debtor. Debtors, however, have attempted to use the Holder Rule to obtain vicarious injunctions against Holders for *seller* misconduct. Nothing in the plain language of the Holder Rule, however, allows for such derivative injunctions. Rather, the plain language of the Holder Rule limits relief against Holders *through the Holder Rule* to monetary relief.

The Commission's 2012 letter affirmed the "plain language" of Rule does not limit the claims and defenses that can be asserted against the Holder under the Holder Rule's first clause.³⁵ An injunction, however, is neither a "claim" nor a "defense,"³⁶ subject to the plain language of Holder Rule's first clause. Rather, an injunction is a remedy, subject to the limited remedies afforded by the plain language of the Holder Rule's second clause.

Since the Holder Rule limits the remedies afforded to debtors under the Holder Rule to "amounts paid by the debtor hereunder," the Commission should affirm that the plain language of the Holder Rule does not afford *through the Rule* a derivative, non-monetary injunction against Holders arising from sellers' conduct.

³⁵ Clark, Letter to National Consumer Law Center, pp. 3 (May 3, 2012).

³⁶ *E.g.*, *Miller v. United States Department of the Interior*, 2015 WL 5307578, at *2 (D.Ariz. 2015) ("Declaratory judgment and injunction are remedies, not causes of action. Each violation of a legal right must be pleaded in a separate count"); *Williams v. Bank of America, N.A.*, 2012 WL 2106225, at *4 (S.D.Cal. 2012) ("An injunction is not a cause of action, but rather is a remedy. . . .A cause of action must exist before an injunction may be granted"); *Behdjou v. U.S. Bancorp*, 2009 WL 2048124, at *3 (C.D.Cal. 2009) ("An injunction is not a cause of action"); *Allen v. City of Sacramento*, 234 Cal. App.4th 41, 48 (Cal.App. 2015) ("Regarding the second cause of action for an injunction, the trial court did not err in sustaining the demurrer because an injunction is not a cause of action").

II. Conclusion

In conclusion, AFSA appreciates the opportunity to comment on the Commission's Holder Rule. AFSA requests that the Commission not amend or alter the Holder Rule, but clarify and confirm its position in four meaningful ways:

1. The Commission should confirm that the Holder Rule applies only to "consumer credit contracts." The Commission should not amend or expand the Holder Rule to apply it to consumer vehicle leases.
2. The Commission should confirm that the Holder Rule applies only to "consumer credit contracts" for the sale of consumer goods or services that are not exempt from Truth-in-Lending and Regulation Z.
3. The Commission should confirm that the Holder Rule applies only to the "Holder" of an executory consumer credit contract, not to rescinded, re-financed, or paid-in-full consumer credit contracts.
4. The Commission should confirm that under the Holder Rule's plain language, any court-awarded sum, under the Rule, must be "limited to amounts paid by the debtor hereunder." This limitation caps interest, costs, and attorney fees. This limitation also precludes a derivative injunction for seller-based conduct.

Please contact me by phone, 202-466-8616, or e-mail, bhimpler@afsamail.org, with any questions.

Sincerely,



Bill Himpler
Executive Vice President
American Financial Services Association

Attachment A

AFSA'S Response to the Commission's Request's Specific Questions

(1) Is there a continuing need for the Holder Rule as currently promulgated? Why or why not?

The Commission promulgated the Holder Rule largely to abrogate the Holder-in-due-course doctrine in consumer credit transactions, and to prevent a seller from "separat[ing] the buyer's duty to pay for the goods or services from the seller's reciprocal duty to perform as promised."³⁷ Especially if clarified as recommended in this comment, the Rule would continue to provide a clear path through the otherwise muddied waters resulting from assignment of an obligation. The text of the Holder Rule as promulgated should not be changed, so long as the Commission clarifies the purpose and effect.

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

The Holder Rule has abrogated effectively the Holder-in-due-course doctrine in consumer credit transactions and prevented sellers from separating the buyer's duty to pay for the goods or services from the seller's reciprocal duty to perform as promised.

(3) What modifications, if any, should the Commission make to the Holder Rule to increase its benefits to consumers?

None are necessary to achieve the original aims of the Rule.

(4) What impact has the Holder Rule had on the flow of truthful information to consumers and on the flow of deceptive information to consumers?

The Holder Rule provides a limited remedy for consumers by connecting the buyer's duty to pay for the goods or services to the seller's reciprocal duty to perform as promised – and imposing that condition even on an innocent purchase of the obligation. However, nothing in the Holder Rule itself directly works to encourage the flow of truthful information (or discourage deceptive information) from sellers to consumers.

To be sure, the Commission intends that lenders police sellers³⁸ to ensure that sellers provide truthful information. But the fact is that "[L]enders cannot determine fraud from the face of a contract when the numbers have been manipulated."³⁹ So any discipline will be retrospective

³⁷ FTC, Promulgation of Trade Regulation Rule and Statement of Basis and Purpose (Nov. 15, 1975) 40 Fed.Reg. 53506, 53507-53508, 5352.

³⁸ FTC, Promulgation of Trade Regulation Rule and Statement of Basis and Purpose (Nov. 15, 1975) 40 Fed.Reg. 53506, 53518.

³⁹ *Thompson v. 10,000 RV Sales, Inc.*, 130 Cal.App.4th 950, 978 (Cal.App. 4 Dist. 2005) ("Additionally, this practice negatively impacts lenders who extend credit for sales misrepresented to them based on fictitious values of vehicles being financed. As the evidence at trial showed, lenders cannot determine fraud from the face of a contract when the

- assuming a relationship still exists. Moreover, where there are allegations of fraud - proof is notoriously difficult to come by. This makes the "policing function particularly difficult, if not dangerous. Finally, providing a deep-pocket alternative source of satisfaction for wronged consumers may just as well work to relieve unscrupulous sellers of the consequences of their actions where the Holder must step in to satisfy the customer's loss.

(5) What significant costs, if any, has the Holder Rule imposed on consumers? What evidence supports the asserted costs?

When Courts apply the plain language of the Holder Rule to consumer credit contracts to which it was meant to apply, there should be no additional significant costs to consumers. When Courts extend Holder Rule liability beyond its plain language - to rescinded, paid-in-full, or re-financed consumer credit contracts, or imposing liability beyond Rule's balanced limitation, the cost of credit increases irrationally and, correspondingly, imposes additional costs on consumers.

(6) What modifications, if any, should be made to the Holder Rule to reduce any costs imposed on consumers?

None are needed.

(7) What benefits, if any, has the Holder Rule provided to businesses, and in particular to small businesses? What evidence supports the asserted benefits?

When the plain language of the Holder Rule is applied as intended, businesses have predictability in their risk management and in the application of the terms of the consumer credit contracts they use.

(8) What modifications, if any, should be made to the Holder Rule to increase the benefits to businesses, and particularly to small businesses?

The plain language of the Holder Rule should not be modified. As set forth in the accompanying letter with applicable legal authority, the Commission should, however, confirm the purpose of the Holder Rule's plain language that (1) the Holder Rule applies only to "consumer credit contracts," which does not include consumer leases, (2) the Holder Rule applies only to "consumer credit contracts" that are subject to Truth-in-Lending and Regulation Z, (3) the Holder Rule applies only the "Holder" of an executory consumer credit contract, not to rescinded, re-financed, or paid-in-full consumer credit contracts, and (4) the plain language of the Holder Rule's limitation of liability to sums paid by the debtor hereunder caps Holders' liability, including attorneys' fees and costs and does not allow the issuance of an injunction under the Rule.

(a) What evidence supports your proposed modifications?

See above.

(b) How would these modifications affect the costs and benefits of the Holder Rule for consumers?

Consumers have operated under the Holder Rule since its promulgation. The Holder Rule, through application of its plain language, would thus impose no additional costs on consumers.

(c) How would these modifications affect the costs and benefits of the Holder Rule for businesses?

Businesses subject to the Holder Rule similarly have operated under the Holder Rule since its promulgation. It is only when the Holder Rule is applied unpredictably and contrary to its plain language that the cost to businesses and so to consumers expands exponentially.

(9) What significant costs, if any, including costs of compliance, has the Holder Rule imposed on businesses, particularly small businesses? What evidence supports the asserted costs?

Businesses subject to the Holder Rule similarly have operated under the Holder Rule since its promulgation. It is only when the Holder Rule is applied unpredictably and contrary to its plain language that the cost to businesses and so to consumers expands exponentially.

(10) What modifications, if any, should be made to the Holder Rule to reduce the costs imposed on businesses, and particularly on small businesses?

See Response to Question #8.

(11) What evidence is available concerning the degree of industry compliance with the Holder Rule? Does this evidence indicate that the Rule should be modified? If so, why, and how? If not, why not?

There is no evidence that AFSA members have not complied with the Holder Rule's requirements for consumer credit contracts. Accordingly, there is no empirical basis to modify the Rule.

(12) Are any of the Holder Rule's requirements no longer needed? If so, explain. Please provide supporting evidence.

None.

(13) What modifications, if any, should be made to the Holder Rule to account for changes in relevant technology or economic conditions?

None.

(14) Does the Holder Rule overlap or conflict with other federal, state, or local laws or regulations? If so, how?

(a) What evidence supports the asserted conflicts?

The Truth-in-Lending Act's assignee liability provisions limit the liability of an assignee of a consumer credit to violations that are apparent on the face of the disclosure statement.⁴⁰ The Holder Rule, however, imposes liability on the Holder for "all claims" that can be asserted against the seller - without TILA's "face of the disclosure statement" limitation. Courts universally have held that TILA's "face-of-the-disclosure-statement" limitation of liability controls over the Holder Rule's "all claims" unlimited clause.⁴¹

(b) With reference to the asserted conflicts, should the Holder Rule be modified? If so, why, and how? If not, why not?

The Commission cannot promulgate a rule or modify the Holder Rule to supplant a federal statute, and TILA's assignee liability provision controls over the Holder Rule.

(15) Are there foreign or international laws, regulations, or standards with respect to the products or services covered by the Holder Rule that the Commission should consider as it reviews the Holder Rule? If so, what are they?

None that AFSA requests the Commission consider.

⁴⁰ 15 U.S.C. § 1641 ("Liability of assignees").

⁴¹ *E.g. Ramadan v. Chase Manhattan Corp.*, 229 F.3d 194, 200 (3d Cir. 2000); *Taylor v. Quality Hyundai, Inc.*, 150 F.3d 689, 693 (7th Cir.1998), *cert. denied*, 525 U.S. 1141, 119 S.Ct. 1032, 143 L.Ed.2d 41 (1999); *Walker v. Wallace Auto Sales, Inc.*, 155 F.3d 927, 935 (7th Cir.1998).