Debt Buyer Lawsuits And Inaccurate Data

Advocates for lower-income families need to be aware that many debt buyers are suing the wrong people, and for the wrong amounts.

Over the past decade, banks have increasingly moved away from collecting defaulted credit card accounts in-house to a model of selling off bad accounts for pennies on the dollar to debt buyers. The accounts are sold “as is,” pursuant to contracts in which the banks state that the debts may not be owed, the amounts claimed may not be accurate, and documentation may be missing.

Despite the broad disclaimers, debt buyers then pursue these accounts and seek to collect 100 percent of the face value of debts for which they paid only 3 percent or 4 percent of face value sometimes much less.

The people pursued are often the elderly, the poor, and low-income families with limited resources to hire a lawyer or take a day off from work to go to court and challenge dubious claims. Instead, they tend to either enter into a settlement or fail to appear in court. They are then subjected to a default judgment and subsequent wage garnishment (money taken out of their paychecks). The ripple effects of a court judgment and garnishment cannot be overstated: bounced checks, family stress, impaired credit scores, and potential obstacles to the victim’s ability to get a job or an apartment.

Selling Off Debt

Debt is sold at low prices when banks have little or no documentation to provide the buyer often just an electronic Excel spreadsheet and a few monthly statements. The contracts of sale between bank and debt buyer (also known as *forward-flow agreements*) typically contain broad disclaimers of warranty, including warranty of title, legality, validity, documentation, or accuracy. Further, the contracts usually provide that “ineligible accounts” may be included in the bulk sales, even accounts where the debt has been paid, settled, discharged in bankruptcy, or was never owed to begin with because of identity theft or other fraud committed against the consumer. One widely publicized forward-flow agreement states that the account balances are only “approximate.” The sale of unverified, inaccurate, and incomplete accounts has led to consumers getting sued twice on the same debt and to reports of abuse by debt collectors, some with criminal backgrounds.

These and other issues resulting from the sale and subsequent attempts to collect on junk debt have drawn increasing attention from regulators, courts, and the media. In one instance, the Office of the Comptroller of the Currency (OCC) found that a bank’s collection lawsuits involved the following behaviors:

- Filing affidavits which the bank falsely represented as based on personal knowledge;

- Filing inaccurate sworn documents that resulted in "judgments with financial errors in favor of the bank";
- Filing "numerous affidavits that were not properly notarized";
- Failing to have proper procedures in place to ensure compliance with the Service members civil relief act;
- Failing to devote sufficient resources to properly administer its collections litigation processes;
- Failing to devote adequate controls, policies, and training to its collection litigation processes; and
- Failing to sufficiently oversee outside counsel and other third-party providers handling collection-litigation services.

The OCC also found data-integrity problems in the bank's sale of charged-off accounts to debt buyers.

Ineligible accounts may be included in the bulk sales, even accounts where the debt has been paid, settled, discharged in bankruptcy, or was never owed.

Hidden Agreements

The problems inherent to the business model are most starkly exposed in the context of lawsuits filed by debt buyers. On the one hand, the debt buyer acknowledges in the forward-flow agreement that the data it received from the bank is limited and potentially inaccurate, with frequent specific disclaimers of warranty of title, validity, accuracy, and documentation.

On the other hand, despite explicit knowledge that the specific accounts are highly suspect, debt buyers argue in court that the allegations about ownership, liability, and amount are "inherently reliable" because the data came from a highly regulated national bank, which has a duty to keep accurate records. All the while, the debt buyers fail to disclose to the courts or to the defendants the terms of the forward-flow agreements, and typically fight any efforts under-taken by consumers to obtain them.

The OCC recently issued a "best practices" memorandum to deal with some of the issues.11 However, no reform to date has called for the disclosure of the forward-flow agreements generally or the disclaimers of warranty specifically.

Regulators and courts are at a crossroads. Will there be national standards on data integrity? Will there be a ban on the sale of certain accounts? Will disclosure of the terms of the forward-flow agreements be mandated?

These are important questions to those who are concerned with the economic viability of lower-income people, because in the zero-sum game of their monthly expenses, every dollar paid to someone with a dubious claim impairs the ability of consumers to pay legitimate creditors for car loans, mortgages, rent, and health insurance premiums. Successfully challenging bogus debt-buyer claims can keep low-income consumers out of bankruptcy and can preserve precious assets for paying legitimate debts and helping to ensure family and community stability.

Sometime this year, there will very likely be broad agreement on national standards and best practices for data integrity and for banning the sale of certain types of accounts. But any reforms will probably have little effect unless banks and debt buyers are required to disclose the terms, conditions, and specific warranties and disclaimers contained in the forward-flow agreements. Shining a light on the red flags identified in those agreements should help preserve low-income community resources by reducing the number of lawsuits and judgments against the wrong people for the wrong amounts.

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