

## **NCLC Criticizes States Treating Checking Account Mistakes As Criminal**

Retail merchant trade associations have sought legislation for decades to criminalize consumers' check writing mistakes as way of raising the stakes against their erring customers. Criminalizing checking account mistakes adds the threat of fines and jail time to the plate of civil creditor remedies like wage and bank account garnishment that retailers already have at their disposal. This effort at times runs afoul of the state prohibition against imprisonment for debt in many states' constitutions. By criminalizing dishonored checks, retailers gain the powerful, terrifying threat of jail to hold over check writers' heads and may get access to local prosecutors and criminal courts as their tax subsidized collection agencies.

By going into the check collection business for retailers, some DA offices have augmented their office's revenues, sometimes by millions of dollars with just one large account, such as check collections for WalMart. In recent years check diversion companies have entered this arena. Check diversion companies are debt collectors that work disguised in the name of the district attorney to collect retailers' unpaid checks. They are designed to generate their own profits as well as revenues for county prosecutors.

In August 2007 NCLC filed an amicus brief ([brief on following pages](#)) in the 9<sup>th</sup> Circuit Court of Appeals that argued that check diversion companies target unsophisticated consumers who make check book errors rather than criminals passing bad checks. It argued that retail merchants who take checks have many other ways to collect unpaid checks they receive, and that the federal Fair Debt Collection Practices Act regulates the activities of check diversion companies imposing important safeguards for consumers.

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No. 07-15048

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IN THE UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT

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ELENA M. DEL CAMPO, LOIS ARTZ, MIRIAM CAMPOS,  
LISA JOHNSTON, AND ASHORINA MEDINA, on behalf of  
themselves and all others similarly situated,  
*Plaintiffs-Appellees,*

v.

AMERICAN CORRECTIVE COUNSELING SERVICES, INC.,  
*Defendant-Appellant.*

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On Appeal from the United States District Court  
for the Northern District of California

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**BRIEF FOR AMICUS CURIAE NATIONAL CONSUMER LAW  
CENTER IN SUPPORT OF APPELLEES**

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## **STATEMENT OF INTEREST OF *AMICI CURIAE***

The National Consumer Law Center, Inc. (NCLC) is a non-profit corporation. NCLC was established in 1969 to carry out research, education and litigation to promote consumer justice. The NCLC has as one of its primary objectives providing assistance to attorneys in advancing the interests of their low-income clients in the area of consumer law.

The NCLC has provided research and expertise on consumer law for legal services attorneys, Congress, state legislatures, and state and local offices charged with the enforcement of consumer protection acts. It also has participated as counsel, co-counsel, and Amicus Curiae in litigation throughout the country and has sponsored and participated in conferences designed to provide continuing education for legal services and private attorneys.

The FDCPA has been a major focus of the work of the NCLC. The NCLC publishes Fair Debt Collection (5th ed. 2004 & 2007 Supp.), a comprehensive treatise to assist attorneys who deal with consumer debt collection problems. In addition, the NCLC has directly assisted attorneys in scores of cases arising under the FDCPA. The NCLC was active in the passage of the FDCPA, testifying at hearings and frequently conferring with counsel to the Subcommittee on Consumer Affairs of the Senate Committee

on Banking, Housing and Urban Affairs prior to, and since, the Act's  
passage.

**TABLE OF AUTHORITIES**

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Holtman v. Citifinancial Mortg. Co.,  
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**ARTICLES AND WEBSITES**

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M. Bradford, “*Insufficient Funds, Walmart finds collection agencies efficiently root out hot checks, but prosecutors miss getting the revenue from fines and fees,*” *Arkansas Democrat-Gazette* (Sept. 24, 2006) .....

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M. St. Amand, “*Patience didn’t pay off for victim in bad-check case,*” *St. Louis Post-Dispatch* (Second Edition June 8, 2006).....

Alan M. White , Cathy Lesser Mansfield, “*Literacy And Contract,*” 13 *Stanford Law and Policy Review* 233, 237 (2002).....

The Collector 53 (May 1996).....

[www.midwestcheckrite.com](http://www.midwestcheckrite.com).....

[www.telecheck.com](http://www.telecheck.com).....

[www.usacreditrecovery.com](http://www.usacreditrecovery.com).....

## ARGUMENT

### AMERICAN CORRECTIVE COUNSELING SERVICES, IS A PRIVATE DEBT COLLECTION AGENCY PERFORMING DEBT COLLECTION FOR RETAIL MERCHANTS, NOT PERFORMING A STATE FUNCTION FOR CALIFORNIA

Retail merchant trade associations over the years have sought legislation to criminalize check writing mistakes as way of raising the stakes against their erring customers, adding the threat of fines and jail time to their platter of civil creditor remedies like wage and bank account garnishment. This effort at times runs afoul of the prohibition against imprisonment for debt in many states' constitutions.<sup>1</sup> By criminalizing dishonored checks, retailers gain the powerful, in terrorem threat of jail to hold over check writers' heads and may get access to local prosecutors and criminal courts as their subsidized collection agencies. By going into the check collection business for retailers, some DA offices have augmented their office's revenues, sometimes by millions of dollars with just one large account, such as check

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<sup>1</sup> See, Comment, *Imprisonment for Debt and the Constitution*, 1970 Law & Social Order 658; Anno., *Constitutionality of 'Bad Check Statute,'* 16 A.L.R.4<sup>th</sup> 631 (1982).

collections for WalMart.<sup>2</sup> The use of threats of jail time for civil check collections has been criticized in the academic community as violating the prohibition against imprisonment for debt and the unseemly intrusion of prosecutors into the ordinary business of debt collectors.<sup>3</sup> Ordinary debt collectors do not welcome the competition from the prosecutors.<sup>4</sup>

This brief describes how check diversion companies like Appellant American Corrective Counseling Services (“ACCS”) have built on this check collection business by offering prosecutors turnkey systems to increase the prosecutor’s revenues and the check diversion companies’ profits. Millions of dollars in revenues and profits are siphoned from low-income households in the process. The brief then describes federal Fair Debt Collection Practices Act’s approach to protecting the unsophisticated consumers caught up by this business.

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<sup>2</sup> Michelle Bradford, “Insufficient Funds, Walmart finds collection agencies efficiently root out hot checks, but prosecutors miss getting the revenue from fines and fees,” *Arkansas Democrat-Gazette* (Sept. 24, 2006) (“In Oklahoma, district attorneys estimated they’ll lose \$2.8 million a year without Wal-Mart’s business...”).

<sup>3</sup> See J. Potuto, *And Mussolini Had the Trains Running on Time: A Review of the Bad Check Offense and the Law Enforcement Debt Collector*, 64 *Neb. L. Rev.* 242 (1986).

<sup>4</sup> E. Lisser, “DAs Give Debt Collectors Competition,” *Wall St. J. B1* (June 13, 1994).

## **A. Check Diversion Companies Target Unsophisticated Consumers Who Make Check Book Errors, Not Criminals Passing Bad Checks**

A tremendous number of checks are written every day, but only a fraction of a percent of those checks is mistakenly written against insufficient funds. A Federal Reserve study estimates there were 36.6 billion checks that flowed between banks in 2003.<sup>5</sup> An estimated 99.5% of the checks clear and are not returned.<sup>6</sup> Then about a half of small portion of returned checks are paid on a second presentment.<sup>7</sup> This prompt payment of dishonored checks on representment reflects the data showing that most Americans are *not* adept at reconciling their check books with their bank statements. A major national assessment of mathematical skills of American adults found that only 16% could correctly reconcile a test check book with a monthly bank statement.<sup>8</sup>

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<sup>5</sup> Geoffrey R. Gerdes, et al., “Trends in the Use of Payment Instruments in the United States,” Fed. Res. Bull. 180, 191 (May 2005), available at [www.federalreserve.gov/pubs/bulletin/2005/spring05\\_payment.pdf](http://www.federalreserve.gov/pubs/bulletin/2005/spring05_payment.pdf)

<sup>6</sup> *Id.* at 194.

<sup>7</sup> Barkley Clark, *The Law of Bank Deposits, Collections and Credit Cards* ¶6.02[2] n.5 (3d ed. 1990) (Of items dishonored, about 50 percent are paid on second presentment, and nearly two-thirds of returns are for checks of less than \$100. Of all returns, the vast majority (72 percent) are NSF; about 3 percent of checks are returned due to a stop payment order; 4 percent for closed accounts; 5 percent for missing indorsements; and something less than 3 percent for uncollected funds, the category that reflects holds.”).

<sup>8</sup> National Assessment of Educational Progress: Consumer Math 5-6 (June 1975) (GPO) (“There were a number of factors to be considered in

Only 1% of the tested high school students correctly reconciled the check book, deflating hope for future improvements in that skill as those students enter into the workforce.<sup>9</sup>

The great bulk of the Americans who cannot quickly cover their mistaken overdrafts are low income families who live hand to mouth and do not have the savings to immediately cover their mathematical check book mistakes. Many of these low income families also have lower literacy, computer, and mathematical skills that prevent them from understanding or explaining their mistake. If these families are criminals for mistakenly writing dishonored checks, their crime is more a result of their poverty than their intentions.

Their financial plight is dramatically deepened by the high fees, \$100 to

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reconciling the statements; a subtraction error and a deposit error had to be corrected, and service charges and an outstanding check had to be included.”). *See also* Alan M. White , Cathy Lesser Mansfield, “Literacy And Contract, ”13 *Stanford Law and Policy Review* 233, 237 (2002) describing another national assessment of consumer’s quantitative skills: “Similarly, large numbers of adults have limited quantitative literacy skills. Surprisingly, basic quantitative tasks are classified at Levels IV and V. For example, comparing price per pound of one product to price per ounce of a similar product is considered to be a Level IV task. The task requires comparison of dissimilar quantities from multiple documents, and requires a consumer to combine printed numerical information with his or her own knowledge and therefore is considered a relatively high-level task. Of the adult population, 79% cannot reliably perform quantitative tasks classified at Levels IV and V.” (footnotes omitted).

<sup>9</sup> *See* National Assessment of Educational Progress: Consumer Math 5-6 (June 1975) (GPO).

\$170, that ACCS requires of them before they can cover their mistake. They may be able to cover the check, particularly if it was a typical small check,<sup>10</sup> but the high fee may be insurmountable.

Their plight is further compounded by the ripple effect associated with a dishonored check. Thus a mistaken overdraft often results in multiple fees from ACCS because the mistake caused multiple dishonored checks. A small mistake causing four small dishonored checks could result in fees from ACCS alone of \$400 to \$680! In addition to the fees of ACCS, the consumers often incur additional \$25 to \$40 fees per check from the retailer who received the check as well as similar fees from the check writer's bank.

It should be noted that mistakes are not the only reason for dishonored checks. Banks dishonor consumers' checks for myriad reasons, such as a check hold policy for deposits from distant banks, set-off of a debt owed to the bank, to an intervening garnishment, bank error, stop payment orders, missing or questioned signatures, and honoring third-party checks written against the consumer's account.

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<sup>10</sup> About a third of dishonored checks are for less than \$42.00. Board of Governors of the Federal Reserve System, "The Use of Checks and Other Noncash Payment Instruments in the United States," 88 Federal Reserve Bulletin 360, 368 (2002).

Likewise, consumers issue insufficient funds checks for many innocent reasons, including forgetting to enter a check in the ledger, spouses writing contemporaneous checks without alerting each other, ignorance of hold periods on deposited checks, failure of an obligor to electronically transfer funds (such as wages, public benefits, or investment proceeds) into a checking account in a timely manner, and theft of the checkbook resulting in the thief passing forged checks.

### **B. Retail Merchants Who Take Checks Have Many Other Ways to Collect Dishonored Checks They Receive**

There are many ways for merchants to collect dishonored checks. The collection of dishonored checks written to retailers is often undertaken by the retailers themselves to preserve their customer relationships. The retailer may also hire one of the many collection agencies and collection lawyers that handle check collections, often on a contingent fee basis.<sup>11</sup> A large check debt collector, TeleCheck, offers a variety of check collection

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<sup>11</sup> The collection industry's trade association magazine identified check collections as one of the industry's largest markets. *See* The Collector 53 (May 1996).

programs, including an online databank of checking account numbers for merchants not to accept at the point of sale.<sup>12</sup> Merchants may use a combination of these methods.

Check diversion companies are a specialized type of private debt collector that enters into contracts with District Attorneys to collect dishonored checks for local merchants, including some of the largest retailers in the world like Walmart and CVS. Last year WalMart, for a time, changed from using ACCS's for its primary check collections and sent most of its dishonored customer checks to another private debt collector, Telecheck, using ACCS only for the residual collections that involved fraud or forgery. The resulting press account suggests that most of the check collections that had been previously handled by ACCS did not involve fraud in the view of Walmart's spokesman.<sup>13</sup> Check diversion companies regularly send letters

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<sup>12</sup> See [www.telecheck.com](http://www.telecheck.com) ("From the checkout line to the phone line to online, TeleCheck makes it possible to turn check payments into safe, secure sales through traditional, and now, digital processes.").

<sup>13</sup> Michelle Bradford, "Insufficient Funds, Walmart finds collection agencies efficiently root out hot checks, but prosecutors miss getting the revenue from fines and fees," *Arkansas Democrat-Gazette* (Sept. 24, 2006) ("...Wal-Mart hired Telecheck Services Inc. as its primary check collection provider. Telecheck..collects bounced checks that don't appear to involve criminal intent, [Wal-Mart spokesman] Simley said...The harder-to collect checks, such as those involving fraud or forgery, go to American Corrective Counseling Services, a "check diversion" vendor, he said...').

on the DA's letterhead threatening criminal prosecution and jail time if the consumer does not pay their extra high fees for a "financial responsibility" class. However, regardless of the involvement of the for-profit check diversion program, the majority of dishonored check cases are not criminally prosecuted because there is no intent to defraud, a required element of the crime, and most DA's do not have the resources to screen every dishonored check to determine whether criminality was involved.

Many consumers have been deceived by ACCS's letters into believing that if they did not pay these extra fees they would be criminally prosecuted, even when no prosecutor had ever determined that a crime had been committed, and the local prosecutor would never actually prosecute.<sup>14</sup> Indeed, there is no reason to believe that the check diversion companies have any effectiveness when it comes to real criminal check schemes.<sup>15</sup> The check diversion companies split their high fees with DA offices providing another source of revenue for these resource starved public offices so long as the DA's are willing to enter into this sideline of deceptive civil debt collection.

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<sup>14</sup> See e.g. M. St. Amand, "*Patience didn't pay off for victim in bad-check case,*" St. Louis Post-Dispatch (Second Edition June 8, 2006).

<sup>15</sup> C.f. Keith Slotter, *Check Fraud: A Sophisticated Criminal Enterprise*, <http://www.fbi.gov/publications/leb/1996/aug961.txt> .

**C. The Federal Fair Debt Collection Practices Act Regulates the  
Activities of Check Diversion Companies Imposing Important  
Safeguards For Consumers**

The federal Fair Debt Collection Practices Act (FDCPA)<sup>16</sup> generally regulates the consumer debt collection practices of debt collection agencies and collection lawyers. It shares<sup>17</sup> this area of regulation with numerous other federal laws<sup>18</sup> and state tort<sup>19</sup> and statutory laws.<sup>20</sup> The FDCPA protects consumers' privacy and prohibits debt collection that is abusive, deceptive, or unfair.

Check diversion companies vigorously disputed the suggestion that they were debt collectors subject to the FDCPA but the courts have disagreed with them.<sup>21</sup> So the diversion companies went to Congress, hoping to get a

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<sup>16</sup> 15 U.S.C. § 1692 et seq.

<sup>17</sup> 15 U.S.C. § 1692n.

<sup>18</sup> For example 26 U.S.C. § 6304 applies the FDCPA to certain federal tax collections by private debt collectors.

<sup>19</sup> See e.g. *Holtman v. Citifinancial Mortg. Co.*, 2006 WL 1699589 (D.Conn. June 19, 2006); *Zito v. Leascomm Corp.*, 2004 WL 22251352 (S.D.N.Y. Sept. 30, 2004).

<sup>20</sup> See e.g. Cal. Civ. Code §§ 1788 to 1788.33, 1812.700 to .702. See generally National Consumer Law Center, *Fair Debt Collection* (5th Ed. 2004 & 2007 Supp).

<sup>21</sup> See e.g. *Liles v. American Corrective Counseling Servs., Inc.*, 231 F.R.D. 565 (S.D. Iowa 2005); *Gradisher v. Check Enforcement Unit, Inc.*, 210 F. Supp. 2d 107 (W.D. Mich. 2002). See also, *Liles v. Del Campo*, 350 F.3d 742 (8th Cir. 2003).

blanket exemption from the statute. But consumer groups and the debt collection industry itself opposed the exemption and the result was a provision that places strict limits on what check diversion companies can do and if they don't do those things, they are subject to full panoply of the FDCPA's protections.

At the end of 2006 Congress passed alternative FDCPA regulation for check diversion companies that can meet the high threshold that it sets.<sup>22</sup> Notably, the new law requires that the prosecutor, not the check diversion company, decide that probable cause under the applicable penal statutes applies. The check diversion company must operate under the control and supervision of the prosecutor, and the program must have a system for the check writer to dispute the charges. Further the prosecutor's program must establish a system to exclude from prosecution postdated checks, checks subject to a good faith stop payment order, checks dishonored as a result of certain bank adjustments to the account, checks written for certain partial payments of preexisting debts, checks written by an incompetent person or minor, and checks written for certain illegal transactions.

When check diversion companies do not qualify for the new regulation, the rest of the Fair Debt Collection Practices Act applies. The FDCPA does not

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<sup>22</sup> Pub. L. No. 109-351 § 818, 120 Stat. 2004 (Oct. 13, 2006), adding 15 U.S.C. § 1692p to the Fair Debt Collection Practices Act.

stop or inhibit the legal activities of check collection companies. In fact, most collectors of dishonored checks operate fruitful businesses while routinely complying with the FDCPA.<sup>23</sup> When check diversion companies are not sufficiently supervised by the DA's office to operate under the new FDCPA regulation, the FDCPA's most important limits on the activities of check diversion companies are in its requirements that no deception be committed,<sup>24</sup> that consumers be advised of their right to request validation of the debt,<sup>25</sup> and that only authorized fees be collected.<sup>26</sup> These are requirements that all debt collectors collecting dishonored checks are able to comply with and still successfully collect. Check diversion companies subject to the FDCPA's requirements have been found liable by the courts, or have settled cases, involving three types of illegal conduct:

-Deceptive Behavior.

The check diversion companies' letters to consumers are deceptive because they look like they actually came from the District Attorney and imply that

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<sup>23</sup> See e.g. [www.telecheck.com](http://www.telecheck.com);  
[www.midwestcheckrite.com](http://www.midwestcheckrite.com); [www.usacreditrecovery.com](http://www.usacreditrecovery.com).

<sup>24</sup> 15 U.S.C. § 1692e.

<sup>25</sup> 15 U.S.C. § 1692g.

<sup>26</sup> 15 U.S.C. §§ 1692e(2)(A) and 1692f(1).

the DA had determined the consumer had committed a crime.<sup>27</sup> It is rare for a DA to review cases before the letter threatening criminal prosecution is mailed. In many situations, if the DA had reviewed the case, no intent to defraud would have been found, and no criminal prosecution would have been threatened.

-Failure to Provide Notice of the Right To Verify the Debt.

Unlike all other private debt collectors collecting debts, including dishonored checks, the check diversion companies refuse to provide notice to consumers that they have the right to request verification of the debt or dispute the debt. In many situations this right would allow consumers to explain that they have already paid off the check, or do not believe they owe it.

-Attempted Collection of Illegal Fees.

Generally, state laws specifically provide the extra fees that consumers owe when they write a check that is dishonored. Often the courts can impose monetary penalties after a conviction for writing a dishonored check (which must include a finding of intent to defraud). Yet the check diversion

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<sup>27</sup> Gradisher v. Check Enforcement Unit, Inc., 210 F. Supp. 2d 107 (W.D. Mich. 2002).

programs insist upon the payment of large fees even when no court has found – or could find – the consumer guilty of the criminal offense. For consumers, this large fee often turns a mistake of a \$10 or \$20 dishonored check into a cost approaching \$200.

The majority of District Attorneys in the nation do not use check diversion companies, leaving it up to retailers to do their own check collections using ordinary debt collection agencies and lawyers and the civil court system. Some DAs use dispute settlement programs to resolve dishonored check issues between merchants and consumers. Other DAs simply write their own letters explaining the process to consumers. These letters do not require the payment of the exorbitant additional fees charged by the check diversion companies, they simply outline the process involved when a payee of a check which has bounced brings the case to the criminal court. These DAs find that even without employing private companies which make millions of dollars in profit from mostly poverty stricken households, who have inadvertently written a dishonored check, only a very few cases require criminal prosecution.

## **CONCLUSION**

ACCS is a private company engaged in debt collection for merchants. It should not be considered the equivalent of a state agency when it is engaging in that business and not be granted sovereign immunity.

Dated: August 10, 2007

Respectfully Submitted,

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