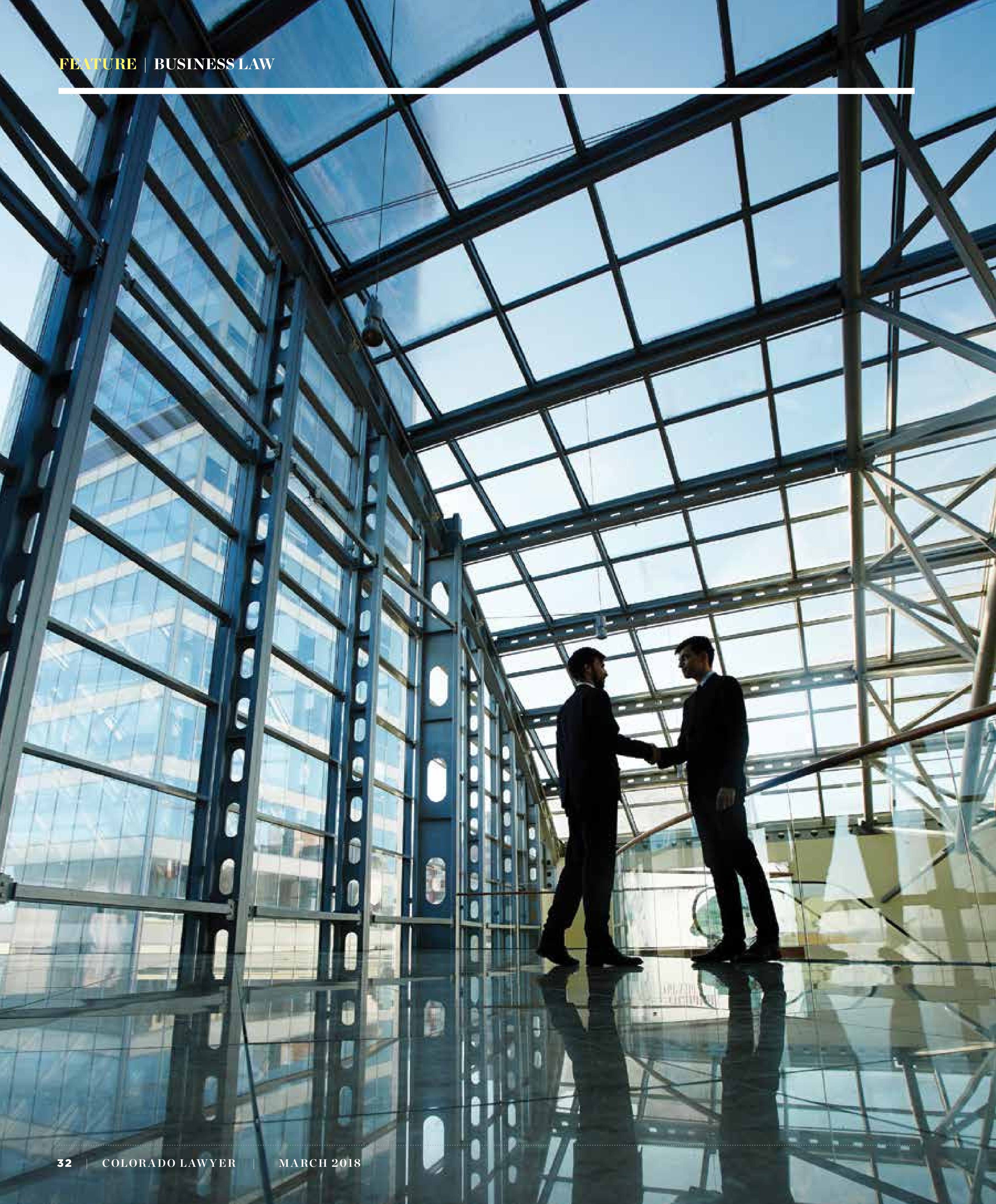


New Fair Debt Collection Practices Act Developments

BY ANNE ZOLTANI

The U.S. Supreme Court recently issued two rulings involving the federal Fair Debt Collection Practices Act. This article discusses these rulings and their impact on consumer protection and consumer bankruptcy practitioners.

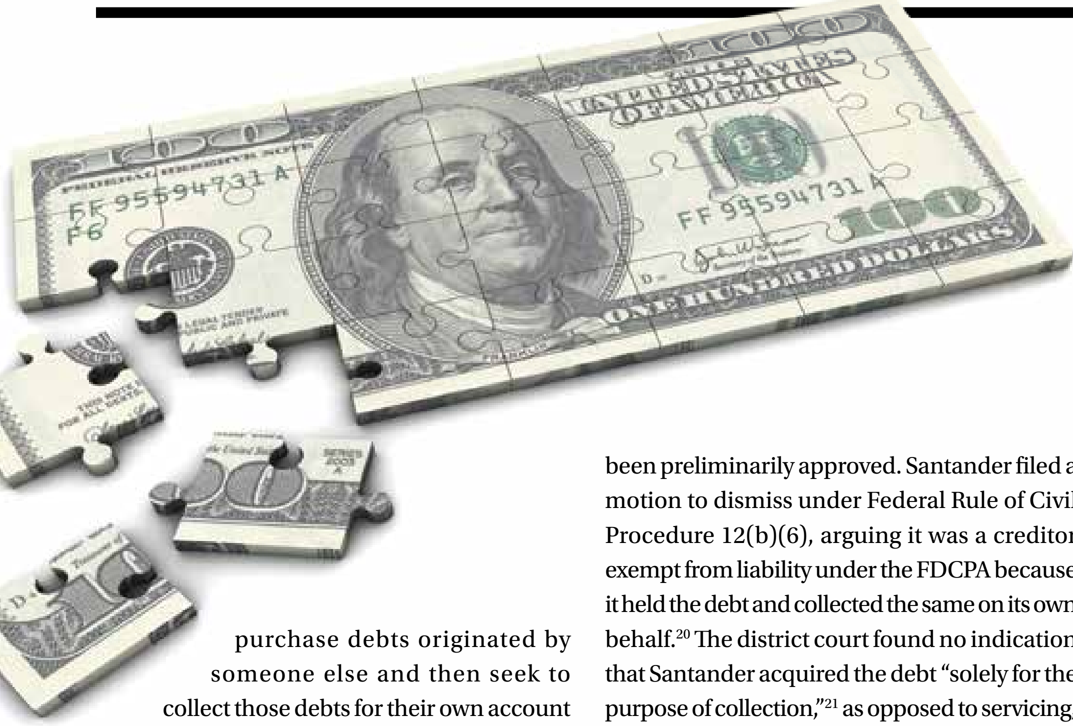
In response to common debt-buying industry practices of "disruptive dinnertime calls, downright deceit,"[1] and other unconscionable conduct, Congress enacted the Fair Debt Collection Practices Act (FDCPA).[2] Two recent U.S. Supreme Court decisions, *Henson v. Santander Consumer USA Inc.*[3] and *Midland Funding, LLC v. Johnson*,[4] address facets of the FDCPA, highlighting issues relevant for debt collection, consumer protection, and consumer bankruptcy practitioners. In *Santander*, the Court considered whether a debt collector that collects purchased debt is a "debt collector" within the meaning of the FDCPA.[5] In *Midland Funding*, the Court examined whether filing a time-barred bankruptcy proof of claim violates the FDCPA.[6]

The FDCPA

The import of these two opinions must be assessed against the FDCPA backdrop. The FDCPA prohibits certain "wayward practices"[7] of the debt collection industry and authorizes causes of action and significant fines to enforce its prohibitions.[8] The FDCPA's purpose is to "eliminate abusive debt collection practices" and to ensure that those who refrain from "abusive debt collection practices are not competitively disadvantaged."[9] Only "debt collectors," however, are subject to the FDCPA.[10]

Henson v. Santander Consumer USA Inc.

In *Santander*, the first opinion authored by Justice Neil Gorsuch, the Court made clear that individuals and entities that regularly



purchase debts originated by someone else and then seek to collect those debts for their own account are not "debt collectors" within the meaning of the FDCPA.[11] In *Santander*, Ricky Henson, Ian Glover, Karen Pacouloute, and Paulette House (borrowers) borrowed money from CitiFinancial Auto (lender) to purchase cars.[12] When the borrowers failed to make their car payments, the lender repossessed their vehicles and informed them that they each owed a deficiency.[13] Subsequently, the borrowers became part of a class action suit against the lender that was based on violations of state repossession laws.[14] While the class action was pending, Santander Consumer USA Inc. (Santander) purchased the borrowers' delinquent accounts from the lender.[15] Santander was aware that the delinquent accounts were the subject of a class action lawsuit and a preliminarily approved settlement, in which the lender agreed to waive the deficiency balances against the borrowers.[16] Subsequently, the settlement agreement was approved by the district court.[17] In an attempt to "collect more than the few cents on the dollar that it paid for defaulted loans,"[18] Santander contacted the borrowers, misrepresenting the amount of debt owed and its authority to collect such debt.[19] The borrowers filed a lawsuit in the U.S. District Court of Maryland based on FDCPA violations, alleging that Santander was aware the delinquent accounts were the subject of a class action lawsuit and settlement, which had been preliminarily approved. Santander filed a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), arguing it was a creditor exempt from liability under the FDCPA because it held the debt and collected the same on its own behalf.[20] The district court found no indication that Santander acquired the debt "solely for the purpose of collection,"[21] as opposed to servicing, and concluded the borrowers failed to allege Santander was "attempting to improperly shield itself"[22] under the 15 USC § 1692a(4) creditor exemption.[23] The district court rejected the borrowers' contention that Santander was a "debt collector" because it purchased debts in default to collect them.[24] The Fourth Circuit agreed. It noted, however, that "some circuits faced with the same question have ruled otherwise."[25] Accordingly, the U.S. Supreme Court took the case to resolve this conflict.[26]

The Court began its analysis with a faithful adherence to the statutory text. First, the Court focused on the plain language definition of the term "debt collector" in 15 USC § 1692a.[27] Next, it noted as determinative that the plain language does not suggest "how a debt owner came to be a debt owner."[28] The Court recognized that "[a]ll that matters is whether the target of the lawsuit regularly seeks to collect debts for its own account or does so for 'another.'"[29] With these tenets in mind, the Court held that Santander may collect purchased debts for its own account without falling under the statutory definition of "debt collector."[30]

The Court rejected the borrowers' argument that one becomes a "debt collector" when it obtains a debt that was previously owed (the "*past* participle of the verb 'to owe'"[31]) another.[32] The borrowers contended that if Congress intended to exempt "all present debt owners" from being "debt collectors" it would have used the present participle "owing," meaning that "debt collectors" must collect debts *currently* owing another. The Court found the borrowers' argument unconvincing as "even a matter of good grammar, let alone ordinary meaning."[33] The Court further posed an explanatory hypothetical, inviting the reader to "[j]ust imagine if you told a friend that you were seeking to 'collect a debt owed to Steve.' Doesn't it seem likely your friend would understand you as speaking about a debt *currently* owed to Steve, not a debt Steve *used* to own and that's now actually yours?"[34]

Finally, the Court dismissed the borrowers' policy arguments that delinquent debt buyers are more like "debt collectors" than loan originators and should be treated as such to be consistent with the underlying purpose of the FDCPA. In the end, Justice Gorsuch concluded it was "not the proper role of the judiciary" to amend "the work of the People's representatives."[35]

*Post-*Santander *Implications*

Following *Santander*, debt-buying companies that purchase delinquent debts to collect on their own account as opposed to servicing rights now have a strong defense against FDCPA claims brought against them for engaging in any "wayward collection practices."[36] Amid the definitive resolution on this issue, some questions remain unanswered. Foremost, whether Santander was a "debt collector" because "it regularly act[ed] as a third party collection agent for debts owed to others"[37] was not decided. In leaving this question unanswered, *Santander* offers little guidance on the broader issue of whether the term "debt collector" encompasses those "engaged 'in any business the principal purpose of which is the collection of any debts.'"[38] Given the scope of these unanswered questions, practitioners should advise business clients that collect purchased debt for their own account to continue careful compliance with the FDCPA.

Midland Funding LLC v. Johnson

In *Midland Funding*, Aleida Johnson filed a personal chapter 13 bankruptcy case, in which creditor Midland Funding, LLC (Midland) filed a proof of claim.[39] Midland's claim accurately reflected that the last time any charge appeared on the debtor's account had been more than 10 years prior—well after the applicable six-year statute of limitations had expired.[40] The debtor objected, and the bankruptcy court disallowed the claim.[41] The debtor then sued Midland in the District Court for the Southern District of Alabama, alleging that filing a claim "on an obviously time-barred debt was 'deceptive,' 'misleading,' 'unconscionable,' and 'unfair'" under the FDCPA.[42] The district court dismissed the suit, holding that "the [Bankruptcy] Code authorizes filing a proof of claim on a debt known to be stale . . . [and] the [FDCPA] must give way to the [Bankruptcy] Code."[43] The Eleventh Circuit reversed.[44] Midland filed a petition for certiorari, noting a division of opinion among the circuits as to whether Midland's conduct violated the FDCPA.[45] The U.S. Supreme Court granted certiorari and reversed the Eleventh Circuit.[46]

Filing a Time-Barred Claim Does Not Violate the FDCPA

The *Midland* Court held that filing a proof of claim that on its face indicates the statute of limitations for the underlying debt has expired does not violate the FDCPA.[47] The Court reasoned that Midland's conduct was not "false, deceptive, or misleading"[48] because a creditor has a right to payment of a debt even after the statute of limitations period has expired. The Court began its opinion by noting that Midland's proof of claim fell within the Bankruptcy Code's (Code) definition of the term claim.[49] First, the Court acknowledged that state law determines whether a person has a right to payment, and the relevant state law was that of Alabama.[50] Next, the Court reviewed Alabama's law and determined that a creditor's right to payment is not extinguished by the statute of limitations.[51] Rather, only the creditor's right to collect is extinguished, and the expiration of the statute of limitations can be raised as a defense in the event of a collection effort.[52]

The Court rejected Johnson's argument that "claim" means "enforceable claim," which was based on a previous opinion where the Court referred to a claim as an "enforceable obligation."[53] The Court reasoned that "the word 'enforceable' does not appear in the Code's definition of 'claim'"[54] and that its previous use of the word "enforceable" was likely descriptive, as the debt in that case was an enforceable debt.[55] Further, the Court could not square Johnson's interpretation with 11 USC §§ 502(b)(1)[56] and 101(5)(A).[57] Having determined that an unenforceable claim was nonetheless a claim, the Court turned to consider 15 USC §§ 1692e[58] and 1692f.[59]

> "Following *Santander*, debt-buying companies that purchase delinquent debts to collect on their own account as opposed to servicing rights now have a strong defense against FDCPA claims brought against them for engaging in any 'wayward collection practices.' "

First, the Court concluded there was nothing false, misleading, or deceptive within the meaning of 15 USC § 1692e in filing an unenforceable claim. The Court noted that determining whether a statement is misleading requires consideration of the legal sophistication of its audience and the audience in a Chapter 13 bankruptcy case includes a Chapter 13 trustee.[60] Whether filing a claim for a time-barred debt is unfair or unconscionable within the meaning of 15 USC § 1692f presented a closer question for the Court.[61] Johnson underscored that lower courts across the board have determined a civil lawsuit to collect a time-barred debt to be unfair.[62] Ultimately, the Court was not convinced by the standard adopted by the lower courts, differentiating a civil lawsuit from a Chapter 13 bankruptcy proceeding.[63] The Court highlighted that lower courts established that standard based on the concern that a consumer might unwittingly repay a time-barred debt.[64] But in a Chapter 13 proceeding, a "knowledgeable trustee is available,"[65] and "the claims resolution process is 'generally a more streamlined and less unnerving prospect for a debtor than [ ] a collection lawsuit.'"[66] In a Chapter 13 bankruptcy proceeding, an effort to collect a time-barred claim would be met with "resistance, objection, and disallowance."[67]

Next, Johnson contended that allowing creditors to file time-barred claims creates a high risk of harm to debtors for no legitimate reason.[68] Johnson argued it would be unfair for a debt collector to adopt a practice of buying time-barred claims and asserting them in a bankruptcy proceeding, hoping for a careless trustee.[69] The Court rejected this argument, observing that untimeliness is "an affirmative defense" and stressing that a change in the affirmative defense approach would require "defining the boundaries of the exception."[70] The Court posed questions with hypothetical boundaries: Would it apply, as in Johnson's case, only when the claim is time-barred on its face? Would it apply to other affirmative defenses or time-barred claims that don't identify their time-barred nature?[71]

The Court was also concerned with the interplay between the Code and the FDCPA, determining that Congress did not intend an "ordinary civil court"[72] to be applying the FDCPA and ruling on these bankruptcy-related questions.[73] In support, the Court noted that the FDCPA and the Code have "different purposes and structural features."[74] The FDCPA seeks to help consumers "by preventing consumer bankruptcies in the first place."[75] The Code, however, "creates and maintains . . . 'the delicate balance of a debtor's protections and obligations.'"[76] The Court concluded that applying the FDCPA here would upset this "delicate balance"[77] because

> it would authorize a new significant bankruptcy-related remedy in the absence of language in the Code. . . . [I]t would permit postbankruptcy litigation in an ordinary civil court concerning a creditor's state of mind—a matter often hard to determine. . . .[I]t would require creditors (who assert a claim) to investigate the merits of an affirmative defense (typically the debtor's job to assert and prove) lest the creditor later be found to have known the claim was untimely.[78]

The Midland *Dissent*

The Court's opinion and the debt-buying industry were not without reproach. Justice Sotomayor, joined by Justices Ruth Bader Ginsburg and Elena Kagan, dissented, reasoning that the practice of "debt collectors" in "buying stale debt, filing claims in bankruptcy proceedings to collect it, and hoping that no one notices that the debt is too old to be enforced by the courts" is unfair and unconscionable.[79] The dissent criticized the debt-buying industry, noting that for years "debt buyers have won 'billions of dollars in default judgments' simply by filing suit and betting that consumers will lack the resources to respond."[80] The dissent acknowledged that the FDCPA's prohibition on unfair conduct has "beaten back"[81] this practice and "[e]very court to have considered the question has held that a debt collector that knowingly files suit in court to collect a time-barred debt violates the FDCPA."[82] According to the dissent, there is no reason to depart from this conclusion.[83]

The dissent also noted that in 2015 Midland and its parent company entered into a consent decree with the government prohibiting them from filing suit to collect time-barred debts and ordering them to pay $34 million in restitution.[84] The dissent asserted that, as a result of such progress in enforcement, the same debt-buying industry has now turned to the bankruptcy forum to file time-barred claims, specifically in Chapter 13 cases.[85] Just as occurred previously with ordinary civil cases, this practice of filing time-barred claims has now become "widespread."[86]

The dissent took issue with the majority's suggestion that the "structural features of the bankruptcy process"[87] reduce the risk that time-barred debt will be allowed. The dissent maintained that "everyone with actual experience in the matter insists that" relying on the trustee as gatekeeper to ferret out time-barred claims that should be disallowed is not realistic.[88] Finally, the dissent took comfort in "the knowledge that the Court's decision today need not be the last word on the matter. If Congress wants to amend the FDCPA to make explicit what . . . is already implicit in the law, it need only say so."[89]

*Post-*Midland *Implications*

The division in opinion as to whether filing a time-barred claim in a bankruptcy proceeding violates the FDCPA has likely baffled debtor's counsel, Chapter 13 trustees, and other lawyers with experience in this issue. Especially bewildering is the Court's claim that "the assertion of even a stale claim can benefit a debtor" on occasion because through the filing and disallowance of a time-barred claim the debt will be discharged and will not remain to wreak financial havoc on a credit report.[90] As a matter of law, even if a proof of claim is not filed, a scheduled debt will be discharged as long as the creditor was sent notice of the bankruptcy.[91]

For practitioners on both sides, the opinion fails "to define the boundaries"[92] of its ruling, leaving open whether this holding extends to Chapter 7 cases. The opinion also leaves unanswered the FDCPA's application to a debt collector's conduct in a bankruptcy proceeding. As the dissent noted, the Court "does not hold that the Bankruptcy Code altogether displaces the FDCPA."[93]

Conclusion

Santander and *Midland* both provide a needed resolution to the issues at hand. Yet it is no surprise that both cases also leave questions unanswered. While consumer protection and debtor's counsel had likely hoped for different results, both cases conclude with a hopeful call to Congress to address the "evolution of the debt collection business"[94] through various clarifying amendments to the FDCPA.[95] Practitioners should remain watchful to see whether Congress answers this call. CL

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NOTES

1. *Henson v. Santander Consumer USA Inc.*, 137 S.Ct. 1718, 1720 (2017).
2. 15 USC §§ 1692 to 1692p.
3. *Santander*, 137 S.Ct. 1718.
4. *Midland Funding, LLC v. Johnson*, 137 S.Ct. 1407 (2017).
5. *Santander*, 137 S.Ct. 1718.
6. *Midland Funding*, 137 S.Ct. 1407 at 1411.
7. *Santander,* 137 S.Ct. at 1719; 15 USC § 1692(e).
8. 15 USC §§ 1692 to 1692p.
9. 15 USC § 1692(e).
10. 15 USC § 1692a. The FDCPA defines "debt collector" as "any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another." *Id.*
11. *Santander*, 137 S.Ct. at 1720.
12. *Henson v. Santander Consumer USA, Inc.*, 817 F.3d 131, 134 (4th Cir. 2016), *aff'd* 137 S.Ct. at 1720.
13. *Id.*
14. *Henson v. Santander Consumer USA, Inc.*, No. RDB-12-3519, 2014 WL 1806915 at *1 (D.Md. May 6, 2014), *aff'd* 817 F.3d at 134, *aff'd* 137 S.Ct. at 1720.
15. *Santander*, 817 F.3d at 134.
16. *Santander*, 2014 WL 1806915 at *1.
17. *Id.*
18. *Santander*, 817 F.3d at 134.
19. *Id.*
20. *Santander*, 2014 WL 1806915 at *3–4.
21. *Id.* at *5.
22. *Id.*
23. *Id.*
24. *Id.*
25. *Santander*, 137 S.Ct. at 1721.

26. *Id.*

27. 11 USC § 1692a.

28. *Santander*, 137 S.Ct. at 1721.

29. *Id.*

30. *Id.*

31. *Id.* at 1719.

32. *Id.* at 1721.

33. *Id.* at 1722.

34. *Id.* (emphasis in original).

35. *Id.* at 1726.

36. *Id.* at 1720.

37. The Court noted that the borrowers did not raise this argument in their petition for certiorari and the Court did not agree to review it. *Id.* at 1721.

38. *Id.*

39. *Midland Funding*, 137 S.Ct. at 1411.

40. *Id.* (citing Ala. Code § 6-2-34 (2014) and stating the applicable statute of limitations under Alabama law is six years).

41. *Id.*

42. *Id.* at 1409.

43. *Johnson v. Midland Funding, LLC*, 528 B.R. 462, 473 (S.D.Ala. 2015), *rev'd* 823 F.3d 1334 (11th Cir. 2016), *vacated sub nom* 137 S.Ct. 1407.

44. *Johnson v. Midland Funding, LLC*, 823 F.3d 1334 (11th Cir. 2016), *vacated sub nom* 137 S.Ct. 1407.

45. *Midland Funding*, 137 S.Ct. at 1411 (citing *In re Dubois*, 834 F.3d 726 (4th Cir. 2016); *Owens v. LVNV Funding, LLC*, 832 F.3d 726 (7th Cir. 2016); *Nelson v. Midland Credit Management, Inc.*, 828 F.3d 749 (8th Cir. 2016)).

46. *Id.*

47. *Id.*

48. *Id.*

49. *Id.* Under 11 USC § 101(5)(A), a claim is a right to payment.

50. *Id.*

51. *Id.*

52. *Id.*

53. *Id.* at 1412.

54. *Id.*

55. *Id.*

56. *Id.* 11 USC § 502(b)(1) directs that if a claim is unenforceable, it will be disallowed. There is no Code provision indicating that an unenforceable claim is not a claim.

57. 11 USC § 101(5)(A) directed that a claim is a right to payment "whether or not such right is . . . fixed, contingent . . . [or] disputed." "[I]f a claimant loses a dispute, then the claim is unenforceable. Yet this section makes clear that the unenforceable claim is nonetheless a 'right to payment' . . . ." *Midland Funding,* 137 S.Ct. at 1412.

58. 15 USC § 1692e prohibits false, deceptive, or misleading representations or means in the collection of a debt.

59. 15 USC § 1692f prohibits unfair and unconscionable collection practices.

60. *Midland Funding,* 137 S.Ct. at 1413. The Court submitted that a Chapter 13 trustee is likely to understand that a proof of claim is a statement by the creditor that they have a right to payment subject to disallowance. *Id.*

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.*

67. *Id.* at 1414.

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. *Id.*

76. *Id.* at 1415.

77. *Id.*

78. *Id.* (internal citations omitted).

79. *Id.* at 1416. The dissent did not take issue with the majority's conclusion that the practice of filing a time-barred claim was not false, deceptive, or misleading.

80. *Id.*

81. *Id.*

82. *Id.*

83. *Id.* at 1418.

84. *Id.* at 1417.

85. *Id.* The dissent asserts this practice is especially common in Chapter 13 cases, which require "consumers earning regular incomes to restructure their debts and repay as many as they can over a period of several years." *Id.*

86. *Id.* at 1418.

87. *Id.* at 1420.

88. *Id.*

89. *Id.* at 1421.

90. *Id.* at 1414.

91. In the Tenth Circuit, debts in no-asset Chapter 7 cases will even be discharged when not scheduled or noticed because 11 USC § 523(a)(3)(A) does not apply when there is no deadline to file a claim. *In re Parker*, 313 F.3d 1267, 1268–69 (10th Cir. 2002).

92. *Midland Funding*, 137 S.Ct. at 1414.

93. *Id.* at 1419.

94. *Santander*, 137 S.Ct. at 1725.

95. *Id.*; *Midland Funding*, 137 S.Ct. at 1421.