Representing the Pro Bono Client:

Consumer Law Basics 2014

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2

Taming the Collection Tempest: A Primer on Federal and State Restraints on Consumer Debt Collection

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BIOGRAPHY OF ROBERT W. MURPHY, ESQUIRE

Robert W. Murphy is in private practice in Fort Lauderdale, Florida, focusing on consumer class action litigation. He presently serves as an adjunct professor of law at the University of Florida College of Law in Gainesville Florida. He is a past chair of the Consumer Protection Law Committee of The Florida Bar and is a Board Member, Secretary and Florida State Chairperson for the National Association of Consumer Advocates. He has spoken at many seminars and conferences hosted by a variety of state and national organizations, including The Florida Bar, The Academy of Florida Trial Lawyers, the National Consumer Law Center, the National Association of Legal Aid and Public Defenders, and the United States Military Judge Advocate Corps as well as college and law schools. In October, 2007 and April, 2011, the Federal Trade Commission designated Mr. Murphy to be panel member for the Fair Debt Collection Practices Act Symposium in Washington, DC, which addressed the rising abuses in the consumer debt collection industry.

Mr. Murphy has been lead counsel in a wide variety of state-wide, regional and national consumer class actions throughout the United States . In 2003, Mr. Murphy obtained the first contested certified class under the Florida Retail Installment Sales Act as reported in *Brown v. SCI Funeral Services of Florida*, 212 F.R.D.602 (S.D. Fla. 2003), which was described in the South Florida Business Review as one of the most significant cases in South Florida in 2003. More recently, Mr. Murphy was lead counsel in a 2009 nationwide class action which provided over $50 million in relief to over 8,000 consumers whose vehicles had been wrongfully repossessed. To date, Attorney Murphy has obtained class benefits estimated to be in excess of $500 million with significant *cy pres* awards to consumer and legal aid organizations.

Mr. Murphy attended the U.S. Military Academy, and received his B.A. *cum laude* from Wake Forest University in 1984 and his J.D. from the University of Florida College of Law in 1987. He is admitted to practice in Florida and Georgia; the United States District Courts for the Middle District of Florida, Southern District of Florida, Northern District of Florida, Western District of Oklahoma, Northern District of Ohio, Middle District of Georgia, Northern District of Georgia; Western District of Michigan; Western District of Tennessee; United States Court of Appeals, Eleventh Circuit and has been admitted pro hac vice in numerous other state and federal courts.

A regular contributor to local and national news media on consumer law topics, Mr. Murphy most recently appeared on *ABC News Nightline* on January 19, 2007 on the topic of consumer debt collection. He has authored and contributed to many articles and papers on consumer litigation issues, including a recent treatise on debt collection.

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I. INTRODUCTION - OVERVIEW OF FAIR DEBT COLLECTION

A. Significance of Fair Debt Collection

Except for a small number of attorneys who do not have living, breathing persons as clients, a basic knowledge of applicable state and federal law concerning the collection of debts is essential to being a well-rounded legal practitioner. Such knowledge is especially important in providing legal services to persons of modest means, who are often victimized by unscrupulous businesses attempting to collect debt.

Since the 1970's, as a result of legislative initiatives on the state and federal level, the framework of the consumer protection statutes was developed to protect the public from unscrupulous business practices in connection with the purchase and financing of goods and services. The consumer law movement culminated with the enactment of the so-called Title 15, which included the Fair Debt Collection Practices Act of 1978, 15 U.S.C. §1692, *et sequi* ("FDCPA"), which promotes ethical business practices by debt collectors. The FDCPA establishes general standards of prohibited conduct, defines and restricts abusive collection acts, and provides specific rights for consumers.

The FDCPA constitutes the keystone in the system of laws governing fair debt collection. Since the enactment of the FDCPA, all but eight states have promulgated statutes dealing with abuses by debt collectors. *See, e.g.*, California Civ.Code §1788- 1788.32, known more commonly as the "Rosenthal Fair Debt Collection Practices Act ("Rosenthal Act"); Florida Statutes §559.55, *et sequi*, known more commonly as the "Florida Consumer Collection Practices Act, and George Code Annotated Section 7-3-1- *et sequi*," known more commonly as the "Industrial Loan Statute". In addition to specific statutes which address collection practices, special laws have been enacted at the state level to address specific collection issues, such as the collection of debts arising from repossessed automobiles and mortgage loans. *See, e.g.*, Florida Statutes §516.31(3).

With respect to the representation of members of the armed forces, the practitioner should recognize that unfair debt collection practices are experienced by service personnel at every rank. Indeed, a US senator with a stellar 800+ Fair Isaac Score may become the victim of identity theft and may find himself/herself being pursued by debt collectors. In a similar fashion, a person of lesser station may

become the focus of unrestrained collection activity to the extent that the service member is unable to perform his/her essential functions.

On the above point, under 15 U.S.C. §1692, setting forth the congressional findings of the FDCPA, Congress stated:

> "There is abundant evidence of the use of abusive, deceptive and unfair debt collection practices by many debt collectors. Abusive debt collection practices contribute to a number of personal bankruptcies, to marital instability, to loss of jobs, and to invasions of individual privacy."

The pervasiveness of unfair debt collection activities cannot be understated. As a result of the rise of information technology, debt collectors have become increasingly sophisticated and deceptive in their practices. As a sobering recent example of unfair collection practices, on September 27, 2005, Attorney Howard Katz, one of the state of Michigan's biggest debt collection lawyers, pled no contest to 136 counts of criminal contempt of court to avoid a potential jail sentence of 25 years. Apparently, Attorney Katz, in attempting to collect debts - including medical bills for Ford Hospital in Detroit - fabricated returns of service on hundreds of consumers, often with service information which were identical to other returns. In certain instances, Attorney Katz seized property and income tax returns of consumers before the consumers even knew that they were being sued.

B. Reasons for Including Consumer Collection Disputes in a Litigation Practice

Any lawyer who has litigated a consumer collection case on behalf of a client at one point or another questioned himself or herself as to why he or she would get involved in such a legal dispute. Most obvious is the glaring fact that a person who is being sued is usually in financial distress and of extremely limited financial means who can ill afford to pay an attorney. Moreover, the litigation itself tends to be a militant confrontation which challenges what appears to be, at least superficially, well-established business practices and procedures of the collection industry.

Those attorneys who have litigated consumer collection cases have come to understand the benefits - to both the attorney and client - of the undertaking. For the client, the benefits are self-evident. While not an exhaustive list, the following benefits may be derived from the litigation of auto deficiency/repossession cases:

- *Source of Prospective Clients* - Often, the prospective consumer collection client has come to the attorney to seek legal advice concerning the defense of the collection lawsuit brought by the holder of the defaulted retail installment sale contract ("RISC") or a credit card debt. With respect to RISCs, based on published disclosures, the sub-prime auto finance industry is currently reporting a 25%-30% default rate. Accordingly, the number of prospective clients who need legal assistance is absolutely staggering.
- *"Skill Enhancement" Opportunity* - The litigation of consumer collection matters allows the consumer advocate to develop and sharpen his/her litigation skills, especially in trial practice.
- *Simplicity of Legal Area* - The litigation of consumer collection matters is not overly complex and can be mastered by the novice without much difficulty.
- *Fee Generating Potential* - As a salient example, during the past several years, one local San Francisco Bay area attorney Mark Chavez, Esquire, of Mill Valley has had outstanding success against the major auto finance companies with respect to their repossession practices. Mr. Chavez has obtained class awards of $58 million against Ford Motor Credit in Clark v. Ford Motor Credit, in the Superior Court, Alameda County, Case No. 6745257; $68 million against Nissan Motor Acceptance in Moultrie v. Nissan Motor Acceptance, in the Superior Court, San Francisco County, Case No. 302601. Most recently, Mr. Chavez certified a $125 million class against General Motors Acceptance Corporation. In the understated words of Mr. Chavez, "the ruling [in the GMAC case] is a wake up call for lenders who violate California law."

The author has more recently concluded major class actions against two California based finance companies that generated class relief of $6.6 and $11.7 million respectively.

C. Role of Consumer Advocacy Organizations

1. General

Since the enactment of Title 15, attorneys have worked together to advance the interest of consumer advocacy and the ethical pursuit of consumer client causes. In addition to assisting

attorneys in litigation issues, the advocacy organizations have provided guidelines with respect to the ethical representation of consumer clients.

2. National Association of Consumer Advocates

The National Association of Consumer Advocates ("NACA") is a nationwide association of more than 1,500 attorneys and consumer advocates who have a wide range of experience curbing the abuses of predatory business practices and the pursuit of justice for consumers. In addition to sponsoring continuing legal education conferences, NACA has published guidelines for litigating and settling consumer class actions. The speaker is a current member of the Board of NACA. For more information concerning NACA, contact:

National Association of Consumer Advocates, Inc.
730 Rhode Island N.W., Suite 805
Washington, D.C. 20036
Telephone: (202) 452-1989
Telefax: (202) 452-0099
Website info @ www.NACA.org

3. Trial Lawyers for Public Justice

Public Justice, formerly "Trial Lawyers for Public Justice" ("Public Justice") is a national public interest law firm dedicated to using trial lawyer's skills and resources to create a more just society. Public Justice litigates socially significant individual and class action issues and is designed to enhance and promote consumer victim's rights, environmental protection and safety, civil rights and civil liberties, workers rights, the American civil justice system, and the protection of the poor and powerless.

Public Justice may be contacted at:

National Headquarters
1717 Massachusetts Avenue, N.W., Ste. 800
Washington, D.C. 20036
Telephone: (202) 797-8600
Telefax: (202) 232-7203
Website information @ www.TLBJ.org

4. National Consumer Law Center

The National Consumer Law Center ("NCLC") is a non-profit corporation founded in 1969 which is dedicated to helping consumers, their advocates, and assisting public policy makers in enacting consumer laws on behalf of low income and elderly Americans seeking economic justice. The treatises of NCLC form the basis of any consumer law library.

The NCLC may be contacted at:

National Consumer Law Center
Washington Office
1629 K Street, N.W., Ste. 600
Washington, D.C. 200//06
Telephone: (202) 986-6060
Telefax: (202) 463-9462
Website information @ www.Consumerlaw.org

II. ROLE OF FAIR DEBT COLLECTION PRACTICES ACT

A. Role of Attorneys as "Debt Collectors"

An attorney who regularly collects consumer debts is subject to all of the restrictions and disclosure requirements of the FDCPA. Heintz v. Jenkins,115 S. Ct. 1489, 131 L.Ed. 2d 395 (1995)[the Act does apply to lawyers engaged in litigation …in ordinary English, a lawyer who regularly tries to obtain payment of consumer debts through a legal proceeding is a lawyer who regularly "attempts" to "collect" those consumer debts.]

In general terms, the FDCPA proscribes oppressive conduct, false and misleading statements, and unfair practices. As such, any activities by any attorney taken in the course of collecting a consumer debt are within the purview of the FDCPA.

B. Application to In-House Attorneys

The FDCPA may apply to in-house attorneys who fail to identify themselves as employees of a creditor. See, e.g., Dorsey v. Morgan, 760 F.Supp. 509 (D. Maryland 1991).

C. Issues Unique to Attorney Debt Collectors

1. Restraint on Communications

(a) Validation Rights Notice

(i) *General* - Pursuant to 15 U.S.C. §1692g, within five (5) days after the initial communication from the consumer in connection with the collection of any debt, a debt collector shall, unless the following information contained in the initial communication or the consumer has paid the debt, send the consumer written notice contained - (1) the amount of the debt; (2) the name of the creditor to whom the debt is owed; (3) a statement that unless the consumer, within thirty (30) days after receipt of the notice, disputes the validity of the debt or any portion thereof, the debt will be assumed to be valid by the debt collector; (4) a statement that if the consumer notifies the debt collector in writing within the thirty day period that the debt, or any portion thereof, is disputed, the debt collector will obtain verification of the debt or a copy of the judgment against the consumer and a copy of such verification or judgment will be mailed to the consumer by the debt collector; and (5) a statement that, upon the consumer's written request within a thirty day period, the debt collector will provide the consumer with the name and address of the original creditor, if different from the current creditor.

(ii) *Request for Validation* - If a consumer notifies a debt collector in writing within the thirty day period described above, that the debt, or any portion thereof, is disputed or requests the original name and address of the original creditor, the debt collector shall cease collection of the debt, or any disputed portion thereof, until the debt collector obtains verification of the debt or a copy of the judgment, or the name and address of the original creditor, and a copy of such verification or judgment, and the name and address of the original creditor, is mailed to the consumer by the debt collector.

(b) Representation Concerning Amount of Debt - The requirements of 15 U.S.C. §1692g are such that an attorney violates the FDCPA by sending a dunning letter which does not

completely disclose the full amount of the debt. In one recent decision, the collection agency violated the FDCPA by disclosing that the principal indebtedness of the consumer loan as $478,844.65, but also providing that "this amount does not include accrued but unpaid interest, or unpaid late charges, escrow advances, or other charges for preservation and protection of lender's interest in the property." Miller v. McCaloa, Raymer, Padrick, Cobb, Nichols and Clark, LLC, 214 F.3d 872 (7th Cir. 2000); Person v. Stupar, 136 F.Supp. 2d 957 (E.D. Wis. 2001) [Plaintiff's complaint based on defendant's statement of the debt as "$987.71 plus attorneys fees," stated a claim for violation of 15 U.S.C. §§1692g(a)(1), e, and f(1)].

(c) False Threats of Lawsuits - The FDCPA contains a general proscription against the use of any false, deceptive or misleading representation or means in connection with the collection of any debt. 15 U.S.C. §1692e. The misrepresentation or exaggeration of the imminence of a suit on intent or authority to sue constitutes a violation of the FDCPA. Crossley v. Lieberman, 868 F.2d 566 (3rd Cir. 1989)[Demand letter referring to creditor as a plaintiff constituted a deceptive communication].

(d) Communication With Third Parties - Under 15 U.S.C. §1692c(b), except with limited exceptions or to effectuate post-judgment judicial remedy, a debt collector may not communicate in connection with the collection of any consumer debt, with any person other than the consumer, his attorney, a consumer reporting agency, a creditor, the attorney of the creditor, or the attorney of the debt collector.

2. Venue Restrictions

A debt collector can bring suit on a consumer debt only where the consumer resides or where the consumer signed the contractual obligation. 15 U.S.C. §1692i.

D. "Flat Rating" as Deceptive Practice

1. Description of Prohibited Practice

Pursuant to 15 U.S.C. §1692j, it is unlawful to design, compile, or furnish any form knowing that such form shall be used to create the false belief in a consumer that a person other than the creditor of such consumer is participating in the collection or any attempt to collect a debt such consumer allegedly owes such creditor when in fact such person is not so participating.

The aforementioned section was designed to address "flat rating," which is the practice of designing or selling to creditors form letters with the flat rater's name on the letterhead, thereby falsely suggesting the flat rater's active participation in the collection process.

2. "Meaningful Involvement" Requirement

In the context of law firms, an attorney must have a "meaningful involvement" in the collection of a debt in order to avoid potential liability under the FDCPA. See, Nielsen v. Dickerson, 307 F.3d 623 (7th Cir. 2000)[holding the FDCPA was violated when the attorney "knew nothing about the debtor and her potential liability beyond what (the client) had conveyed to him; and (the client) provided (the attorney) only their information that (he) required in order to complete the blanks in his form letter]; See, Clomon v. Jackson, 988 F.2d 1314, 7321 (2d Cir. 1993) ["the use of an attorney signature implies — at least without language to the contrary — that the attorney signing the letter formed an opinion about how to manage the case of the debtor to whom the letter was sent"]; See, also, Miller v. Wolpoff & Abramson, LLP, 2003 WL 462421 (2d Cir. 2003).

III. ROLE OF FAIR CREDIT REPORTING ACT

A. Review of Statutory Authority

The Fair Credit Reporting Act, 15 U.S.C. §1681, *et sequi* ("FCRA") regulates both the creation and use of "consumer reports." It defines a "consumer report"as :

> Any written, oral or other communication of any information by a consumer reporting agency, bearing on a consumer's creditworthiness, credit

> standing, credit capacity, or character, general reputation, personal characteristics, or mode of living which is used or except to use to collect in whole or in part for purposes of serving a factor and establishing the consumer's eligibility for — (A) a credit or insurance to be used primarily for personal, family, or household purposes; (B) employment purposes; or (C) any other purpose authorized under this §1681b of this Title. 15 U.S.C. §1681a(d).

As reflected above, the definition of "consumer report" encompasses much more than a credit report published by the three national credit reporting agencies, Equifax, Experian and Transunion ("CRAs"). If a report bears on one of the enumerated factors, it is a "consumer report" subject to the FCRA. Indeed, reports concerning check writing history [Estiverne v. Saks Fifth Avenue, 9 F.3d 1171 (5th Cir. 1993)], tenant background [Scott v. Real Estate Finance Group, 756 F.Supp. 5 (E.D.N.Y. 1997)], insurance underwriting experience, and the like are within the definition of "consumer report."

B. Use of Consumer Reports

1. General

The FCRA was enacted in part to protect confidential personal information accumulated by the CRAs. As a result, consumer reports can be acquired by a user for only defined purposes under the FCRA or with the express consent of the consumer.

2. Review of Permissible Purposes

As a general rule, a consumer report may be obtained under the following circumstances:

- in response to a court order or federal grand jury subpoena
- in response to the instructions of the consumer
- to the person which the CRA has reason to believe intends to use the information in connection with a credit transaction
- to a person which the CRA has reason to believe intends to use the information for employment purposes
- to a person which the CRA has reason to believe intends to use the information in connection with the underwriting of insurance involving the consumer
- to a person which the CRA has reason to believe intends to use the information in connection with the determination of the eligibility of the consumer for a license for other governmental benefit

- to a person the CRA has reason to believe intends to information to evaluate creditor risk associated with an existing credit obligation
- a person which the CRA has reason to believe has a "legitimate business need" for the information in connection with a business transaction involving the consumer
- in response to a request by a child support enforcement agency concerning a consumer

15 U.S.C. §1681b.

In obtaining a credit report, the CRA must receive certification from the user of the permissible purpose described above.

3. Review of Impermissible Purposes

(a) Use in Civil or Criminal Litigation - An attorney using a consumer report in litigation that does not concern the collection of a pre-existing debt does not have a permissible purpose in obtaining the consumer report. Mallory v. City of Chicago, 678 F.Supp. 703 (N.D. Ill. 1987). In short, an attorney does not have the right to obtain a consumer report solely to satisfy the attorney or client's desire to know whether litigation is worth pursuing against a tortfeasor.

(b) Location of a Witness - It is a violation of the FCRA to use a consumer report to locate a witness. Mullen v. Al Castrucci Ford, Inc., 537 N.E. 2d 1307 (Conn. 1986).

(c) Use in Divorce Proceeding - An attorney cannot obtain a consumer report to verify credit card use by a spouse in a divorce action. Yobay v. City of Alexandria Employee Credit Union, Inc., 827 F.2d 967 (4th Cir. 1987).

IV. ROLE OF CREDIT REPAIR ORGANIZATION ACTS

A. General Overview

In response to a growing problem with credit repair agencies ("CROs") committing fraud on both consumers and the CRAs, Congress enacted the Credit Repair Organizations Act, 15 U.S.C. §1679, *et sequi* ("CROA"). Florida, like most states, has enacted a similar statute. Fla. Stat.§817.7001, *et sequi*. The federal and state CROA applies to the conduct of any business — including attorneys — who offer credit repair services to consumers.

B. Broad Definition of "Credit Repair Organization"

Under 15 U.S.C. §1679a(3), the term "credit repair organization" — (A) means any person who uses any instrumentality of interstate commerce or the mail to sell, provide, or perform (or represent that such person can or will sell, provide or perform) any service, in return for the payment of money or other valuable consideration, for the express or implied purpose of — (i) improving any consumer's credit record, credit history, or credit rating; or (ii) providing advice or assistance to any consumer with regard to any activity or service described in clause (i); and (B) does not include — (a) any non-profit organization which is exempt from taxation under §501(c)(3) of Title 26; (i) any creditor to the extent the creditor is assisting the consumer to restructure any debt owed by the consumer to the creditor; or (iii) any federal depository institution or federal or state credit union, or any affiliate or subsidiary of such a depository or credit union.

Without question, the definition of a CRO includes attorneys. See, Gill v. Federal Trade Commission, 265 F.3d 944 (9th Cir. 2000) [Court affirming equitable relief in favor of the FTC in the amount of $1,335,912.14 against a law firm, including without limitation consumer remedies, restitution, and disgorgement].

C. Disclosure Requirements

1. Contract Disclosures

Pursuant to 15 U.S.C. §1679c, a CRO shall provide a consumer with written statements concerning the rights of the consumer under state and federal law separate from any written contract or other agreement between the CRO and the consumer.

2. Right of Recission

Pursuant to 15 U.S.C. §1679e, a consumer may cancel any contract with the CRO without penalty or obligation by providing the CRO with the consumer's intention to do so at any time before midnight of the third business day after the date on which the contract or agreement between the consumer and the CRO is executed. Additionally, the CRO is required to provide a specific form of notice of cancellation separate from contract of the consumer.

D. Time of Payment

Pursuant to 15 U.S.C. §1679b(b), a CRO may not charge or receive any money or other valuable consideration for the performance of any service which the CRO has agreed to perform for any consumer before such service is fully performed. In other words, a CRO — including an attorney — cannot obtain payment before the work is completed.

E. Prohibited Practices

Pursuant to 15 U.S.C. §1679b contains general provisions with respect to the proscription of fraudulent conduct concerning the performance of any services by a CRO. Accordingly, a CRO is prohibited from making, directly or indirectly, any statements that are untrue or misleading to a consumer's creditworthiness, credit standing or credit capacity to either a CRA or a prospective creditor.

F. Effect of Non-Compliance

1. Void Contract

If a CRO fails to provide the required disclosures under the CRA, the contract is void and may not be enforced by any federal or state court pursuant to 15 U.S.C. §1679f(c).

2. Civil Liability

A CRO that fails to comply with the requirements of the CRA, may be liable for actual and punitive damages pursuant to 15 U.S.C. §1679g. Actual damages is the greater of the amount of any actual damage sustained by the consumer or any amount paid by the consumer to the CRO. Furthermore, the CROA authorizes class actions with an unlimited ceiling unlike other consumer protection statutes such as the FDCPA and the Truth in Lending Act. Under the state and federal statutes, attorney's fees are authorized to the prevailing consumer.

3. Federal Trade Commission Enforcement

Over the last several years, the FTC has been extremely active in pursuing law firms that perform "credit repair services" for consumers in purported compliance with the FCRA. In FTC v.

Jack Schrold, a Fort Lauderdale practitioner was fined $11,000 by the FTC for failing to provide with the CROA. Even more sobering, in FTC v. Keith H. Gill, a California law firm was fined $1.3 million dollars and was subjected to unlimited disgorgement.

V. ADDRESSING UNSECURED DEBT CLAIMS

A. Synopsis of Overview of Debt Collection Industry

Until recently, unsecured debts – namely credit cards and signature loans – were collected by the initial credit grantor. However, with the rise of information technology , the majority of charged-off consumer debts are sold in the secondary market to debt buyers. This development has also been fostered by the concern of retailers and lenders of involvement in collection litigation which exposes the initial credit provider to potential consumer ill-will and counterclaims by the consumer, including class actions.

In 2008, over 123 billion dollars in charged-off debts were sold to third party purchasers. According to many consumer advocates, the trend has created a veritable industry of "zombie debt collectors" or "debt scavengers." The business plan of disposing of uncollectible consumer accounts is known more commonly in the media as "debt scavenging," "zombie debt collection," or "junk debt collection." See, generally, *"Zombie Debt: The Bills That Won't Die,"* ABC Nightly News, February 28, 2008; *"Zombie Debt Comes Back to Haunt Consumers,"* Sun-Sentinel, June 25, 2006. In the typical business model employed by businesses such as "zombie collectors" the debt collection agency will buy charged-off accounts from original lenders for pennies on the dollar. Businesses adopting the aforementioned business model will attempt to collect the principal indebtedness of the charged-off debt together with accrued interest from the consumer obligor using tactics which implicitly or even expressly state to the least sophisticated consumer that the stale, time-barred debt is an obligation which is enforceable through judicial means and is reportable to the credit reporting agencies despite such debts being "obsolete" and not reportable under the Fair Credit Reporting Act.

As a result, consumer advocates must become skilled in addressing the collection efforts of such debt collectors.

B. Challenging the Legal Claims of Debt Buyers

1. Overview

In a typical debt purchase, the creditor will sell only "information" – e.g., the name and address of the debtor, the account number and the account balance. Until recently, the information was sold with the debt package in electronic form such as a C.D. or magnetic tape. In the last five years, however, the information is typically downloaded by DSL directly into the computer system of the debt buyer. In most instances, the debt buyer does not acquire any back-up documentation, including account agreements, account statements and the like.

2. Adequacy of Documentation

During the representation of a consumer in a collection action brought by a debt buyer, the advocate must scrutinize the pleadings of the debt buyer to determine if all required records are attached. In many instances, the debt buyer will attach internally generated documents to support its claim. Certain creditors will refer to the "proof" as a "statement of account," "officer's certificate" or "verification of debt." In any event, the document is typically manufactured solely for the purpose of litigation and has no evidentiary value.

Under most rules of pleading practice, all documents upon which any action may be brought or a defense made must be incorporated in or attached to the pleading, If a pleader fails to attach a required document or incorporate it in its pleading, the proper objection is a motion to dismiss the pleading seeking affirmative relief for failure to state a cause of action or a motion to strike a defense as an insufficient legal defense. See, Sachse v. Tampa Music Company, Inc, 262 So.2d 17 (Fla.2nd DCA 1972); Safeco Insurance Company of America v. Ware, 401 So.2d 1129 (Fla.4th DCA 1981); Samuels v. King Motor Company of Ft. Lauderdale, 782 So.2d 489 (Fla. 4th DCA 2000)[where complaint is based on a written instrument, complaint does not state a cause of action until instrument is attached to the complaint]; Hughes v. Home Savings of America, 675 So.2d 649 (Fla2nd DCA 1996) In light of the foregoing, in the absence of an application signed by

the consumer – the debt collector has failed to state a cause of action for which relief may be granted.

3. Inappropriateness of "Open Account" or "Account Stated" Claims

In order to "simplify" the collection process, debt buyers will attempt to create expedited claims for an "open account", "account stated" or nebulous "*quantum meruit*." With respect to the claim for "open account", debt buyers cannot typically bring such a claim in light of the existence of a credit card agreement between the consumer and the original credit grantor.

In H & H Design Builders v. Travelers Indemnity Company, 639 So.2d 697 (Fla. 5th DCA 1994), the Florida 5th District Court of Appeal addressed the distinction between claims based on written contracts and actions on "account":

> "An obligation does not become an 'open account' simply because the amount due under a contract requires calculation. An obligee under a contract cannot avoid the requirement of pleading and proving a cause of action based on a contract, by placing its demand on a "statement of account" and mailing it to the obligor. We conclude, therefore, that H & H was correct in asserting the affirmative defense that the Travelers complaint failed to state a cause of action because the "statement" relied upon does not meet the requirements of an "open account".

Id. at 700.

Most state rules of pleading require that "a copy of the account showing items, time of accrual for each, and amount of each must be attached." Typically, the debt buyer will attach exhibits which it contends constitutes an "account." A cursory review of the exhibits typically demonstrate that the "account stated" does not reflect the item, time of accrual of each, and the amount of each, as required under most state rules concerning pleadings. See, e.g., Note to Form 1.932, Forms for Use With the Florida Rules of Civil Procedure.

4. Inappropriateness of Equitable Claims

Debt buyers — especially those who purchase accounts from other debt buyers — often have very little documentation to support the claim. Accordingly, a debt buyer will attempt to bring a lawsuit based on equitable concepts of "unjust enrichment" or "*quantum meruit."* However, under most state law, equitable

claims for unjust enrichment and *quantum meruit* are not available where an express agreement exists as the rights and obligations of the parties are governed by an agreement. See, e.g., Snyderburn v. Moxley, 652 So.2d 945 (Fla. 5th DCA 1995); Honn v. Pate Construction Company, Inc., 607 So.3d 423 (Fla. 4th DCA 1992); Quayide Associates, Ltd. v. Triefler, 506 So.2d 6 (Fla. 3rd DCA 1987).

The inappropriateness of equitable claims to collect on unsecured debts is even more compelling as much of the debt consists of contractually generated items such as late fees, over the limit fees and default interest rates. Very few debt buyers are able to discern the actual principal indebtedness owed by a consumer.

VI. ADDRESSING AUTO REPOSSESSION DEFICIENCY CLAIMS

A. Overview of Auto Deficiency/Repossession Parties

1. The Client

As in most every consumer litigation matter, the types of clients which have auto deficiency/repossession disputes run the entire economic and social spectrum. However, clients can be divided into essentially two groups: sub-prime consumers and prime consumers. The sub-prime consumers tend to be persons of lesser sophistication, economic means and experience. Somewhat counter-intuitively, sub-prime consumers are more risk tolerant of consumer litigation as their credit scores, salaries and attachable property are more limited.

2. Description of Typical Defendants

a. "Small Players"

Typically, "small players" are the "buy-here pay-here" dealerships and captive finance companies (i.e., common ownership between dealership and finance company). Generally speaking, small player compliance with most state and federal consumer protection laws is abysmal. Such businesses tend to gravitate towards the use of general practitioners and collection lawyers to litigate contested auto deficiency/repossession matters.

As with "big players", the smaller industry participants are also disinclined to resolve an auto deficiency/repossession claim in favor of a consumer. Psychologically, the secured party is unable to accept the notion that their conduct may result in a monetary award to the consumer. The problem is even more acute when the claim of the consumer is derivative in nature and focuses on the actions of the dealership as opposed to the finance company.

b. "Big Players"

The large finance companies - Ford Motor Credit, General Motors Acceptance Corporation and the like - are characterized by established practices and procedures which have been reviewed for compliance by corporate lawyers. In most instances, the large lenders employ national law firms to defend lawsuits, even small claims proceedings.

A challenge to the forms used by an industry giant is usually (but certainly not always) an exercise in futility. The primary focus of litigation of an auto deficiency/repossession matter against large institutions should be on the underlying transaction (i.e., what did the dealership do to rip off the consumer?), the repossession itself (i.e., what did the repossession agent do to violate the law?) and whether the disposition of the vehicle occurred in the manner which the finance company said it did (i.e., was the vehicle sold under the terms and conditions as represented?).

B. Overview of "Consumer Weapons"

1. Uniform Commercial Code

The starting and ending point of any competent representation is Article IX, Part VI of the Uniform Commercial Code ("UCC") and in California, California Code, Sections 2981-2984.6, the "Rees-Levering Act."

Specifically, with respect to the UCC, the following sections are critical and should be committed to memory:

Section 9 - 613: Disposition of Collateral - General

Section 9 - 614: Disposition of Collateral - Consumer

Section 9 - 623: Right to Redeem

Section 9 - 625: Remedies

2. "Anti-Holder" Statutes

i. FTC Holder Rule

(1) Overview of Rule

Under 16 C.F.R. 433, any person in the ordinary course of business who lends purchase money or finances the sale of goods or services to consumers on a deferred payment basis must include the following language:

NOTICE

ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.

Most vehicle sales involving an assignment of the RISC to a third party finance company are within the ambit of the FTC Holder Rule. Accordingly, the "sins of the dealership" will be visited upon the lender.

ii. Limitations

(1) Damages capped at amount paid

The FTC Holder Rule limits the consumer's recovery against the lender for dealer related claims to the "amounts paid by the debtor hereunder." Schauer v. GMAC, 819 So.2d 809 (Fla. 4th DCA 2002).

(2) Application to Truth in Lending Claims

Most courts have held that the Truth in Lending Act, 15 U.S.C. §1601, *et sequi* ("TILA") trumps the FTC Holder Rule in cases where the plaintiff alleges fraud based on the financing contract. See, e.g., Eromon v. Grant Auto Sales, Inc., 2004 WL 1794916 (N.D. Ill., Aug. 14, 2004); Keller v. Quality Hyundai, Inc., 150 F. 3d 689 (7th Cir. 1998).

b. State Holder Rule

Many states have state "holder rules" which mirror the FTC Holder Rule. See, e.g., N.J. Statute §17:62C-38.2; Florida Statute §516.31(2) ["a holder or assignee of any negotiable instrument or installment contract, other than a currently dated check, which originated from purchase of certain consumer goods or services is subject to all claims and defense of the consumer debtor against the seller of those goods and services"].

c. Uniform Commercial Code Holder Rule

Under Section 9-404(d), in a consumer transaction, if the finance agreement lacks the disclosure notice required under the FTC Holder Rule, the consumer account debtor has the same right to obtain the recovery from the assignee as the consumer would have had against the assignee had the agreement contained no required notice.

3. State Consumer Protection Acts

a. Retail Installment Sales Finance Act

b. Unfair and Deceptive Trade Practices Act

c. State Consumer Finance Acts

- especially anti-deficiency statutes. See, e.g., Florida Statute §516.31(3) [when the unpaid balance of a loan subject to the Consumer Finance Act of $2,000.00 or more, the creditor shall be entitled to recover from the consumer a deficiency, if any, resulting from deducting the fair market value of the collateral from the unpaid

balance due. If the unpaid balance at the time of default was $2,000.00 or less, the creditor is not entitled to a deficiency. Periodically published trade estimates of retail value presumed to be fair market value].

d. Attorney Fee Shifting Statutes

Many states have statutes which provide that if a contract contains a provision allowing attorney's fees to a party when he or she is required to take any action to enforce the contract, the court may also allow reasonable attorney's fees to the other party when that party prevails in any action, whether it is plaintiff or defendant, with respect to the contract. See, e.g., Florida Statute §57.105(7); Washington Code annotated, Chapter 4.84.330; Connecticut Statutes Annotated §42-150BB; Montana Code Annotated 28-3-704; Oregon Revised Statutes Annotated, §20.096; California Civil Code, §1717. Such reciprocal attorney's fees statutes are invaluable to the consumer practitioner in the absence of another statutory fee entitlement.

4. Federal Consumer Protection Acts

a. Truth in Lending Act ("TILA")

Caveat - TILA only applies if the violation is apparent on the face of the RISC.

b. Fair Credit Reporting Act ("FCRA")

- especially useful if the consumer obtained a high interest rate loan based on his/her consumer report. The failure to get the "best rate" may be an "adverse action" for which the statutory notice is required under the pre-revision FCRA.

c. Motor Vehicle Information and Cost Savings Act ("Odometer Act")

- the Odometer Act may be useful when there is:
  - Concealment of vehicle history by dealership - See, Owens v. Samkle Automotive, Inc., 425 F.3d 1318 (11th Cir.2005); see also, Hobbs v. BH Cars, Inc., 2004 WL 1242838 (S.D. Fla. 2004); *contra*, Bodine v. Graco, 533 F. 3rd 1145 (9th Cir. 2008).
  - Forgery of title documents

d. Magnuson-Moss Warranty Act

- the Magnuson-Moss Act is especially useful when the used vehicle was purchased from a "small player" dealership which provides a written warranty or service contract on a vehicle. As many practitioners have seen, a hapless consumer purchasing a used vehicle at high interest rates can rarely afford to pay the installments if he/she is required to repair the vehicle shortly after purchase. Indeed, a majority of repossessions are caused by the consumers inability to pay both the RISC and repairs.

e. Equal Credit Opportunity Act

- limited use when the financing is completed as the consumer has "accepted" an offer. However, with a "yoyo" sale, the consumer can bring a claim under the ECOA for the failure of the dealership/finance company to provide the required "adverse action" notice. See, Cannon v. Metroford, 242 F. Supp. 2d 1322 (S.D. Fla. 1002); Treadway v. Gateway Chevrolet/Oldsmobile, 362 F.3rd 971 (7th Cir. 2004).

5. Common Law Claims

a. Fraud.

b. Negligent Misrepresentation

c. Breach of Contract

d. Civil Conspiracy

C. Litigation Against Auto Dealerships and Small Finance Companies

1. Systematic Noncompliance

a. Synopsis of Business Practices

For the most part, the "buy-here pay-here" dealerships and small regional finance companies have little or no compliance with the state and federal consumer protection laws. Thus, litigation against such parties provides an excellent opportunity to hone skills and to "experiment" with new ideas.

b. "Churning" or "Revolving Repossessions" as a Business Model

The systematic noncompliance by automobile dealerships and small finance companies - especially in high interest rate loans - is a direct result of the business model employed by such enterprises. In many instances, it is apparent to even the most casual observer that such actors are engaged in deceptive practices.See, Repossession and Foreclosure, National Consumer Law Center, 5th Edition, Section 10.9.4; see, e.g., Chisholm v. Transouth Finance Corp, 95 F.3d 331 (4th Cir. 1996), *appeal after remand*, 164 F.3d 623 (4th Cir. 1988), *class certified*, 184 F.R.D. 556 (E.D. Va. 1999); Miles v. N.J. Motors, 32 Oh.App.2d 530, 291 N.E. 2d 758 (1972).

2. ***Article 9 Issues***

a. Failure to Provide Revised Article IX Information

i. General

By 2001, most states had adopted the revised Article 9. The most significant changes to revised Article 9 as it pertains to consumer transactions concern the specific information provided to the consumer in the notice of sale under Sections 9-613 and 9-614. Not surprisingly, most auto dealerships and small finance companies have failed to update their notice of sale forms to address the revisions.

Under comments to Section 9-614, the UCC drafters stated:

> "A notification that lacks any of the information set forth in paragraph (1) is insufficient as a matter of law."

Thus, the omission of even a telephone number or redemption information is fatal to the notice. Moreover, after it has been established that the information is omitted, the trial court can decide the Article 9 violation on summary judgment.

ii. Failure to Designate Private or Public Sale

Currently, the single most common defect in the repossession notice of sales is the failure of the secured party to designate a private or public sale. The former version of Article IX did not explicitly require that the creditor describe the method by which it intended to dispose of the collateral. However, a number of courts found describing the specific methods of disposition to be an implicit requirement, and held that the notice must state whether the sale be public or private. *See*, e.g., Union Safe Deposit Bank v. Floyd, 76 Cal.App. 4th 25 (1999) [California U.C.C. requires strict compliance and "does not permit the creditor to leave the debtor guessing regarding the type of sale contemplated"]; Landmark First National Bank v. Gepetto's Tale of the Whale, Inc., 498 So.2d 920 (Fla.1986). Revised Article 9 makes the requirement explicit; the creditor must state the method of disposition — whether public or private — in order to comply with the Uniform Commercial Code. See, Section 9-613 and 679.614, Uniform Commercial Code.

iii. Termination of Redemption Rights

Many auto dealers/small finance companies will terminate the right of redemption prior to the sale of the repossessed vehicle to a third party. The rationale for this blatant violation of the Uniform Commercial Code is that the vehicle typically is brought back to the same dealership lot from where it was initially sold. In short, the dealership does not want a dispossessed consumer to reclaim the vehicle once it has been placed back on the lot as it interferes with another sale.

3. "Reverse Engineering" of Consumer Claims

a. Truth in Lending Claims

i. Improper Disclosures

The Truth in Lending Act requires that the annual percentage rate and finance charge be "more

conspicuously" disclosed. As many dealerships and small finance companies draft and publish their own forms to save money, the potential for noncompliance is significant.

ii. Hidden Finance Charges

iii. Odometer Claims

In every repossession matter, a consumer attorney should order the title history for the repossessed vehicle. It is recommended that the title history be ordered at a point in time when the vehicle would have been re-titled to a subsequent consumer. The reason for ordering the title history is simple: the dealership/finance company would never anticipate that a consumer would be interested in the title history of a ***repossessed vehicle***.

The title history will reveal such things as whether the vehicle had a branded title, had been previously used in a rental fleet and the like, all of which must be disclosed under most state laws. The failure to make the disclosures may lead to claims for violation of the Federal Odometer Act, Unfair and Deceptive Trade Practices, for fraud and misrepresentation. See, Yazzi, *supra*.

More sobering, is the fact that many dealerships/ finance companies are often brazen enough to forge the name of the consumer to the title of the vehicle both at the time of sale **and after its repossession**. Most state Department of Motor Vehicles will charge a dealership/ finance company a fee of approximately $25.00 to $45.00 to process a repossession certificate. To avoid paying the administrative fee, the secured party will simply record a transfer from the dispossessed consumer to either the dealership or to a third party purchaser.

iv. Retail Installment Sales Finance Act Claims

It is imperative that the practitioner review in detail the RISC for a repossessed vehicle. In many instances, the RISC is at variance with the state Retail Installment

Sales Finance Act requirements. For example, many state statutes have restrictions with respect to the ability of a secured party to recover attorney's fees in an auto deficiency matter. As the finance companies are interested in recovering for its legal fees in the event of a repossession, the finance companies often vary from the requirements of the act.

D. Litigation Against Major Finance Companies

1. General Overview - "Thinking Outside the Box"

As stated earlier, litigation of a contested auto deficiency/ repossession case against a major auto finance company is quite different from matters involving automobile dealerships and regional lenders. In most instances, it will be difficult, if not impossible, to challenge the lender with respect to the forms used. This position is especially compelling in the aftermath of the California litigation; simply put, most every major lender has obtained state law compliance assurance from local counsel. Accordingly, it is necessary for the consumer advocate to engage in fact finding to uncover defenses and claims in order to successfully litigate against a major lender.

2. Synopsis of Repossession Fact Finding

a. Informal Presuit Discovery

b. "Reverse Engineering"

Most repossession/deficiency disputes will require a modest amount of "reverse engineering" - going back to the underlying purchase and finance transaction to uncover the fraud and non-compliance of the dealership and/or lender. The practice of "reverse engineering" will necessarily involve the review of the paperwork related to the transaction. Most of the discovery is germane to any auto fraud case.

3. "Rescuing the Co-Signer"

i. Synopsis of Problem

Often times, the consumer client who is seeking assistance with respect to the deficiency is a co-signer for a third party. This situation is especially common with parents, grandparents and other family members who agree to assist younger or credit impaired relatives. Such persons often have very good credit as well as assets. Most often, co-signers are the primary target for major lenders after repossession. Indeed, as a result of the underwriting practices of such lenders, the extension of credit was typically predicated on the consumer report of the co-signer. In comparison, many self-financing dealers/small lenders do not engage in risk based lending; thus co-signers are not as common.

ii. Application of the FTC Co-Signer Rule

The Federal Trade Commission Credit Practice Rule, 16 CFR §444, known more commonly as the "FTC Co-Signer Rule", requires all "co-signers" in a consumer credit transaction to be given notice prior to adding their signature to any debt. Under the FTC Co-Signer Rule, the co-signer must be given a separate document ("FTC Co-Signer Notice") containing only the following language:

> **Notice to Co-Signer.**
>
> You are being asked to guarantee this debt. Think carefully before you do it. If the buyer doesn't pay the debt, you will have to. Be sure you can afford to pay if you have to, and that you want to accept this responsibility.
>
> You may have to pay up to the full amount of the debt if the borrower does not pay. You may also have to pay late fees or collection costs, which increases the amount.
>
> The creditor can collect this debt from you without first trying to collect from the borrower. The creditor can use the same collection methods against you that can be used against the borrower, such as suing you, garnishing wages, etcetera. If the debt is ever in default, that fact may become *your* credit record.
>
> This notice is not the contract that makes you liable for the debt.

(emphasis added by Federal Trade Commission).

Pursuant to the Federal Trade Commission Credit Practice Rule, it is a deceptive act or practice to misrepresent the nature or extent of a co-signer liability or to obligate the co-signer before informing him or her of the nature of the liability as a co-signer. Although there is no private cause of action under the Federal Trade Commission Credit Practice Rule, a violation of the rule is typically a *per se* violation of the state UDTPA. As most state UDTPA statutes allow for equitable relief, the consumer can at times avoid liability for a deficiency if the FTC rule has been violated.

iii. Failure to Provide Notice of Sale to Co-Signer

Under Section 9-611, Uniform Commercial Code, the secured party is required to provide notice of sale not only to the debtor but to any secondary obligor, including a co-signer. In many instances, a lender will send the required notice only to the primary obligor.

4. Securitization Challenges

a. Dimension of Problem

Lenders such as Ford Motor Credit and General Motors Acceptance Corporation are extremely sophisticated organizations that participate in the capital investment markets. In many instances, the lender named on the RISC will immediately transfer its ownership in the consumer paper to a third party trust which subsequently sells its interest in the investment on Wall Street. The securitization of consumer paper presents ripe opportunities to defeat deficiency claims against consumers. It is basic tenet of the law of most states that only the "holder" of a debt may seek to enforce the debt in court. As the "nominal lender" has effectively transferred its interest in the RISC, it should have no claim to bring against a consumer.

b. Discovery Issues

Most major lenders are extremely sensitive concerning inquiries into how assets are held. Accordingly, discovery directed towards the securitization of the finance agreement in dispute will often dissuade the lender from pursuing a deficiency.

5. Misconduct of Repossession Agent

a. Strict Liability of Lender

Under the UCC, the secured party is liable for any acts and omissions of its repossession agent. See, Clark v. Associates Commercial Corp., 870 F. Supp. 1011 (D. Kansas 1997)[non-delegable duty of creditor not to breach the peace]; Mbank El Paso, N.A. v. Sanchez, 836 S.W. 2d 151 (Texas 1992). Thus, if the repossession agent commits a breach of the peace, the lender is exposed to actual and statutory damages under Article IX.

b. Role of Deception

Many repossession agents employ some form of deception with respect to carrying out the act of repossession. For example, the repossession agent may pretend that he or she is a police officer with a badge. Unfortunately, the majority of states hold that such misconduct is not adequate to create liability against the lender. See, e.g., Ford Motor Credit v. Cole, 503 SW 2d 853 (Texas C.A. 1973).

c. Breach of Peace

If the repossession agent breaches the peace, the secured party is liable for Article 9 damages.

6. "Creative Resistance Breaks Creditor Persistence"

The ability for the consumer advocate to "think out of the box" will enhance the lawyer's ability to prevail in auto repossession disputes. For example, prior to the 2002 revisions to the Fair Credit Reporting Act, some lawyers had success in arguing the failure of the creditor to provide an "adverse action notice" when

offering less than favorable interest rates for a consumer constituted a violation of the Act.

After the repossession of a vehicle, the consumer advocate can enhance the position of the client by sending out or causing to be sent out (i.e., ghost-write for client if allowed under state ethics rules):

- Estoppel Demands to Lenders - Under most state retail installment sales acts and Uniform Commercial Code, the consumer is entitled to obtain information concerning the amount owed under the RISC, together with the dates and amounts of payments made to the lender. The failure to respond to an estoppel demand is typically a violation of the state Retail Installment Sales Act.
- Consumer Request for Re-investigation to the Credit Reporting Agencies - If the consumer disputes the accuracy or incompleteness of any information which has been furnished to a consumer reporting agency, the information furnisher may not in the future report information unless it notes that a dispute has been made by the consumer. 15 U.S.C. §1681s - 2(a)(3).

VII. CONCLUSION

Representing a consumer in a collection defense matter is not glamorous and usually does not bring the admiration of the bar or the judiciary. Advancement of the consumer's position in the face of unrepentant opponents is daunting and time consuming. However, the service provided to the consumer is often immeasurable. The elimination of a consumer claim against a struggling family can make a difference between a lifetime of debt and the accumulation of real wealth in the form of a home and savings. Similarly, the extraction of a senior citizen from the debt he/she co-signed on behalf of a child or grandchild may prevent the senior from depleting limited resources to satisfy a high interest loan.

The greatest satisfaction in litigating consumer collection cases is obtained when the industry wrongdoers are punished through a monetary award of statutory damages. As a salient example, as reflected above, most of the statutory damage formulas in repossession cases are based on the "finance charge". For a sub-prime loan - when the interest rates climb upwards of 18% - the wrongdoer truly experiences old fashioned biblical justice. Indeed, in the rare occasions where a jury is empaneled, the

attorneys for the finance company are troubled to learn that the jury instructions typically do not address damages as the lawyers were hoping to appeal to the jury against a "windfall for a deadbeat for a 'technical violation' of the law". (actual quote). Instead, the trial court usually determines damages subsequent to finding by the jury of liability. In cases where multiple claims are asserted, the recovery can be staggering.

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