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ELEVENTH CIRCUIT SAYS COLLECTION ACTION ON TIME-BARRED DEBT TREATED NO DIFFERENTLY IN BANKRUPTCY

The United States Court of Appeals for the Eleventh Circuit recently has held that a debt buyer violated the federal Fair Debt Collection Practices Act when it filed a proof of claim in a Chapter 13 bankruptcy on debts deemed unenforceable under state statutes of limitations. *Crawford v. LVNV Funding, LLC*, 2014 WL 3361226 (11th Cir. July 10, 2014). Thus, the court reversed the dismissal of the debtor's challenge to the proof of claim in the bankruptcy court, which had been upheld by the district court.

Crawford involved a debt that had been charged off by the original creditor in 1999 and then sold to a debt buyer in 2001. The last transaction on the account was made on October 26, 2001. The debt was governed by Alabama law, which made the debt unenforceable after three years (*i.e.*, October 26, 2004). In February 2008, the debtor filed for Chapter 13 bankruptcy and the debt buyer filed a proof of claim to collect its debt, despite the running of the limitations period in 2004. The debtor objected, arguing that the debt buyer violated the federal FDCPA in attempting to make a claim on the time-barred debt. The bankruptcy judge dismissed the debtor's objection and the district court affirmed.

On appeal, the court framed the issue as whether a proof of claim to collect a stale debt in Chapter 13 bankruptcy violates the federal FDCPA. In examining the FDCPA, the court concluded that it needed to determine whether the debt buyer's conduct in filing and attempting to enforce a claim it knew to be time-barred would be unfair, unconscionable, deceptive or misleading (in violation of Sections 1692e and 1692f of the FDCPA) to the "least-sophisticated consumer."

The debt buyer acknowledged that its actions likely would result in FDCPA liability had it filed a lawsuit to collect the debtor's time-barred debt in state court. As the court noted, federal circuit and district courts uniformly have held that a debt collector's threats to sue on a time-barred debt and/or filing a suit to recover that debt violates Sections 1692e and 1692f of the FDCPA. Citing *Phillips v. Asset Acceptance, LLC*, 736 F.3d 1076 (7th Cir. 2013), the court noted the reasons the FDCPA outlaws stale suits as unfair to include (i) unwitting acquiescence to lawsuits by unsophisticated consumers

who would be unaware that the statute of limitations could be used as a defense against such suits, (ii) the dulling of memories regarding the debt after the passage of time and (iii) the increase in the chance that the debtor no longer will have personal records regarding the debt.

The limitations period, the court concluded, shows a "pervasive legislative judgment that it is unjust to fail to put the adversary on notice to defend within a specified period of time" and the need to "protect defendants and the courts from having to deal with cases in which the search for truth may be seriously impaired by the loss of evidence." The same is true in the bankruptcy context, the court concluded. Just like the filing of a stale lawsuit, a debt collector's filing of a time-barred proof of claim, the court said, creates the misleading impression to the debtor that the debt collector can legally enforce the debt. The unsophisticated consumer may not know that a claim is time-barred and thus fail to object to the claim. Since the Bankruptcy Code automatically allows the claim in the absence of an objection, an otherwise unenforceable debt will be paid as part of a Chapter 13 repayment plan. Thus, the court found, filing a time-barred proof of claim in bankruptcy is "unfair," "unconscionable," "deceptive," and "misleading" within the broad scope of Section 1692e and 1692f. Just as the debt buyer would have violated the FDCPA by filing a lawsuit on stale claims in state court, the court said, the debt buyer violated the FDCPA by filing a stale claim in bankruptcy court.

In reaching its conclusion, the court rejected the debt buyer's arguments that (i) the proof of claim was not a "collection activity" regulated by the FDCPA and (ii) to consider the filing of a proof of claim as a "means" used "in connection with the collection of a debt" under the FDCPA would be at odds with the Bankruptcy Code's automatic stay provision. The court also declined to determine whether the Bankruptcy Code preempts the FDCPA.

Time-barred debts have garnered increased attention in the last decade. Numerous courts have found debt collectors liable under the FDCPA and state law if they file suit or threaten legal action to collect time-barred debts. However, courts generally have not found debt collectors liable for merely attempting to collect time-barred debts. If the underlying debt has not been extinguished, it may be permissible to collect the debt as long as any communications with the debtor could not be interpreted by a "least sophisticated

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consumer” to include explicit or implicit threats of future legal action that may not be taken (although a court recently found liability for misleading an unsophisticated consumer into believing that a debt is legally enforceable in the absence of threatened litigation, see our Alert, “Seventh Circuit Finds Settlement Offer on Time-Barred Debt Violates FDCPA,” dated March 18, 2014). In a few states the running of the statute of limitations clearly extinguishes the underlying debt in addition to barring judicial remedies.

Collectors must exercise caution when seeking to collect time-barred debts and should review their procedures for settlement and bankruptcy, in addition to general disclosures regarding time-barred debt, in light of recent cases and consent orders. We can assist in such reviews. □

✧ *Mike Tomkies, Margaret Stolar and Chuck Gall*

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