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SEVENTH CIRCUIT FINDS SETTLEMENT OFFER ON TIME-BARRED DEBT VIOLATES FDCPA

The United States Court of Appeals for the Seventh Circuit recently held that a debt collector violates the federal Fair Debt Collection Practices Act if it uses language in a collection letter that would mislead an unsophisticated consumer into believing that the debt is legally enforceable, regardless of whether the letter actually threatens litigation. *McMahon v. LVNV Funding, LLC*, 2014 WL 929358 (7th Cir. March 11, 2014). Thus, the court upheld denial of the debt collector's motion to dismiss in one of the consolidated cases, and reversed the granting of the debt collector's motion to dismiss in the other case.

McMahon included two appeals — involving plaintiffs McMahon and Delgado — which were consolidated for purposes of the Court's opinion. The *McMahon* case stemmed from a 1997 utility company debt which, 14 years later, was sold to a debt buyer who then hired a collection agency to pursue the debt. The debt collector sent a letter that, among other things, offered to settle the debt for less than the amount owed. The letter gave no information as to when the debt had been incurred or that the applicable four-year statute of limitations under Illinois law had expired. In *Delgado*, the debt collector sent a letter attempting to collect an eight-year old debt that also, among other things, offered a settlement for less than the full amount owed. Again, the letter did not indicate when the debt had been incurred, nor that it was time-barred.

Each debtor sued alleging violations of the FDCPA. In *Delgado*, the district court was persuaded by the Federal Trade Commission's position that nondisclosure of the fact that a debt is time-barred might deceive a consumer. Thus, the court denied the collector's motion to dismiss. In *McMahon*, the court dismissed the plaintiff's class action allegations under the FDCPA, but denied the motion to dismiss his individual claims. After a series of procedural moves, the court eventually granted the collector's motion to dismiss for lack of jurisdiction. On appeal, the Seventh Circuit invited the FTC to file a brief as *amicus curiae* in *Delgado*, and the FTC, along with the Consumer Financial Protection Bureau, filed a joint brief with the court.

Adopting the "well-reasoned" positions of the FTC and CFPB, the Seventh Circuit applied an "unsophisticated consumer" standard in analyzing the collection letters received by the plaintiffs. The court noted that several sections of the FDCPA were relevant. Section 1692e prohibits "any false, deceptive, or misleading representation or means in connection with the collection of any debt," including (i) false representation of the character, amount, or legal status of any debt, (ii) threat to take any action that cannot legally be taken and (iii) use of any false representation or deceptive means to collect or attempt to collect any debt. Section 1692f prohibits debt collectors from using "unfair or unconscionable means to collect or attempt to collect any debt."

Whether the collection letters were confusing is a question of fact, with dismissal being appropriate only when "it is apparent from a reading of the letter that not even a significant fraction of the population would be misled by it," said the court. A letter may confuse even though it is not internally contradictory, and unsophisticated readers may require more explanation. Under the circumstances, the court found it plausible that an unsophisticated consumer could believe that a letter that offers to "settle" a debt implies that the debt is legally enforceable. As legal enforceability of the debt is central to the character and legal status of the debt, the Seventh Circuit affirmed the district court in the *Delgado* case and directed the district court in the *McMahon* case to reevaluate the class allegations.

The Seventh Circuit specifically noted that it was not holding that it is automatically improper to seek repayment of a time-barred debt. However, if a debt collector uses language that would mislead an unsophisticated consumer into believing that the debt is legally enforceable, regardless of whether the letter actually threatens litigation, the collector violates the FDCPA.

The Seventh Circuit recognized that its conclusion conflicts with that of the Third and Eighth Circuit Courts of Appeals, which focused on whether dunning letters actually threatened litigation. In the Seventh Circuit's view, a dunning letter seeking collection of a time-barred debt would violate the FDCPA if it stated that the collector could sue but promised not to do so.

The letters sent to Delgado and McMahon, the Seventh Circuit noted, gave no hint that the debts owed were vulnerable to a

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limitations defense. Unsophisticated consumers receiving such letters could be misled to believe that their debts were legally enforceable. As the letters could be read to misrepresent the legal status of the debt, they violate the FDCPA. Adding an offer to settle the debt could mislead a gullible consumer into making a partial payment that inadvertently resets the limitations period. The court deferred to the FTC's and CFPB's findings that most consumers do not understand their rights with respect to time-barred debts. A settlement offer on a time-barred debt, the court concluded, implies that the creditor could successfully sue on the debt.

Finally, the court observed that its decision will not require additional research on the part of collectors. If the collector does not know whether a debt it is seeking to collect is in fact time-barred, it can include general language about that possibility.

Collection of time-barred debts has received a lot of scrutiny over the past several years and likely will continue to do so. It is clear from the joint FTC-CFPB *amicus* brief that the agencies view the practice as problematic. Also, the CFPB's advanced notice of public rulemaking for possible debt collection regulations includes a section of questions regarding time-barred debts (*see our Alert* dated Nov. 13, 2013). Collectors should remain vigilant in their efforts to comply with applicable law when collecting on time-barred debts. □

✦ *Mike Tomkies and Margaret Stolar*

COURT EXAMINES PROOF NEEDED FOR DEBT BUYERS' ENFORCEMENT OF DEBTS

A New Jersey appellate court recently held in the context of a challenge to summary judgment in favor of debt buyers against consumer debtors in collection of assigned debt on a closed and charged-off credit card account that (i) lack of notice to the debtor of the sale of the debt does not affect the validity of the assignment, (ii) the assignment need not specifically reference the debtor's name or account number and instead may refer to an electronic data file containing that information, (iii) a plaintiff need not procure an affidavit from each transferor in its chain of assignments and may instead establish prima facie proof of ownership on the basis of business records documenting its ownership, and (iv) an electronic copy of the periodic billing statement for the last billing cycle is prima facie proof of the amount due on the account at charge off. *New Century Fin. Servs., Inc. v. Oughla*, 2014 WL 839180 (N.J. Super. A.D. March 5, 2014). The consolidated cases involved two debtors and the court ultimately upheld summary judgment against one debtor and reversed summary judgment against the other debtor. □

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