

Arm Your Shop Against FCRA Violation Claims

The FDCPA and the FCRA have conflicting provisions that often place collectors in a precarious position.

by Carolyn A. Taylor

Editor's note: This article is the second in a multi-part series that addresses FDCPA minefields that creditors might potentially cross during the collections process.

The first article in this series provided a historical overview of the Fair Debt Collection Practices Act (FDCPA) and the "Hobson's Choice" faced by third-party debt collectors who choose to use voice-mail messages as part of their collection efforts.

This article will analyze the interplay between the FDCPA and the Fair Credit Reporting Act (FCRA) that regulates the collection, dissemination and use of consumer credit information. The analysis will focus on dispute resolution, consumer mortgage loan credit reporting issues that have been addressed by the Circuit Courts of Appeal, and credit reporting vis-à-vis the bankruptcy automatic stays and the discharge injunction.

The FCRA is designed to protect the integrity and accuracy of consumer credit information provided to consumer credit-reporting agencies. The statute vests certain federal agencies, including the Federal Trade Commission (FTC), with the oversight and enforcement of statutory compliance by credit-reporting agencies, as well as by furnishers and users of consumer credit information. The FCRA imposes civil liability for willful or negligent violations by a credit-reporting agency. Congress specifically precluded a private cause of action for a consumer

against a furnisher of inaccurate or incomplete credit reporting in an attempt to avoid subjecting data furnishers to lawsuits by each consumer dissatisfied with the credit information furnished. Enforcement of "accurate" reporting by data furnishers is delegated to federal agencies.

Dispute-resolution procedures are embodied in both the FCRA and the FDCPA. While third-party debt collectors must comply with all applicable FDCPA requirements, only those who also furnish information to credit-reporting agencies must additionally comply with the FCRA provisions. A debt collector's dispute-resolution obligations depend on the form of the dispute notice (whether it is verbal or written) and on who receives the notice (the debt collector who furnishes the credit information or the credit-reporting agency).

Under both statutes, a debt is disputed if the consumer believes it is disputed. Consumers are not required to articulate the reason for the dispute; the simple statement "I dispute this debt" will trigger the duty to report the debt as disputed. A debt collector has no authority to determine whether the dispute is valid and must follow the FDCPA dispute-resolution procedures, even if the collector believes the dispute is frivolous. The debt continues to be disputed until the consumer states it is no longer disputed or the debt collector has fully complied with the statutory dispute-resolution procedures. By contrast, a data furnisher has no duty to investigate a complaint re-

ceived directly from the consumer that is "frivolous" or "irrelevant," either because insufficient information was provided or because the dispute is substantially similar to one previously submitted.

When a consumer verbally disputes the debt, the debt collector must mark the account as "disputed." If the debt collector has reported the account to a credit-reporting agency, the collector must notify the reporting agency that the debt is "disputed." Note that a verbal notice does not trigger the FDCPA debt-validation provisions.

If a consumer disputes a debt in writing within the 30-day FDCPA debt-validation period, the debt collector must mark the account as "disputed" and cease collection activity until verification of the debt is mailed to the consumer. If the debt collector is also the data furnisher, its duties to investigate and respond to the dispute depend on whether the dispute was lodged with the data furnisher or the credit-reporting agency.

A data furnisher that receives a written dispute directly from the consumer must conduct a "reasonable investigation," review all information provided by the consumer, complete the investigation and respond to the consumer within 30 days of receipt of the dispute and correct any inaccurate information with the credit-reporting agency. By contrast, if the consumer sends the dispute to the credit-reporting agency, the agency is responsible for notifying the data furnisher of the dispute and reporting the results of the data furnisher's investigation to the consumer.

Not surprisingly, these well-intended statutes have conflicting provisions that often place a debt collector in a precarious situation. One such problematic scenario arises when the consumer disputes

the debt and demands that the debt collector cease further communications pursuant to the FDCPA, yet also submits an FCRA dispute to a credit-reporting agency.

Faced with a no-win situation, the debt collector must either honor the cease-and-desist demand to comply with the FDCPA or respond to the consumer's FCRA dispute and violate the FDCPA. The only authority that has addressed this reoccurring issue is the FTC advisory opinion dated June 23, 2009, stating that a debt collector's communication solely to inform the consumer of the results of the dispute investigation or that the dispute is frivolous or irrelevant does not violate the FDCPA. Because the wheels of legislature and the judiciary move slowly, advisory opinions from regulatory agencies may be the only safety net available to debt collectors and mortgage servicers in the foreseeable future.

With the unprecedented number of foreclosures and borrower bankruptcy filings to stop those foreclosures continuing with no end in sight, one would expect that the number of lawsuits alleging willful or negligent FCRA violations would increase commensurately. This is simply not so. Only four of the 12 circuit courts of appeal have rendered opinions that involve some aspect of mortgage servicing. Two of those decisions - *Huick v. Aurora Loan Services* and *Ocwen Loan Servicing, and Bridge v. Ocwen et al*, both rendered in 2009 - provide some refuge for servicers and debt collectors battling the seemingly endless barrage of legal firestorms.

In *Huick*, the U.S. Court of Appeals for the Seventh Circuit held that the two servicers did not violate the FCRA when they reported delinquencies to a credit-reporting agency about a borrower who failed to comply with his contractual obligations to pay property taxes directly to the taxing authorities and buy his own insurance and forward proof to the lender, to pay monthly escrow payments for taxes and insurance after a contractually authorized escrow account was created and to remit a payment shortfall that resulted from a bank error in incorrectly processing the amount of a money-order payment.

The Seventh Circuit also dismissed the borrower's breach of contract and

tortious interference economic advantage (credit expectancy) claims based upon its findings that there was no inaccurate credit reporting, no false reporting of default and no evidence that either servicer knew or had "reasonable cause to know the information was inaccurate." The fact that the loan was a six-figure mortgage, the borrower's cavalier attitude and the repeated requests of both servicers for contractual compliance clearly influenced the court's decision.

The *Bridge* case also involved a six-figure mortgage loan and a personal check that was dishonored due to a bank processing error. The borrowers replaced the dishonored check twice, but neither of the two loan servicers would acknowledge receipt of the double payment, despite being supplied with proof of payment. Instead, a late fee was assessed against the dishonored mortgage payment, and thereafter, payments were applied first to accrued late charges, and then to ongoing mortgage payments, rendering the loan in a constant state of default.

After collection activity commenced, the borrowers filed suit against the servicers, alleging, among other claims, that the failure to properly credit payments and subsequent collection attempts constituted false representations about the legal status of the debt, threats to take illegal action, and annoyance and harassment in violation of the FDCPA and the FCRA. The court dismissed all claims as a matter of law on procedural grounds, noting to the servicers that the FCRA does not provide a private cause of action against data furnishers.

The *Huick* and *Bridge* decisions provide a glimmer of hope for servicers and debt collectors. Only time will tell whether a borrower's bad actions and/or procedural impediments will continue to influence judicial decision-makers.

Bankruptcy discharge injunction

Whether credit reporting while a borrower is in bankruptcy and/or after the discharge constitutes an act to collect a debt in violation of the automatic stays or the discharge injunction is an ongoing debate. In the typical scenario, the debt is collected and charged off pre-petition, the creditor reports the debt as a "charge off" to the credit-reporting agencies, the debtor receives a bank-

ruptcy discharge, and the creditor does not update the credit reporting during the bankruptcy or after the discharge. In most instances, the creditor does otherwise attempt to collect the debt post-petition. In those situations, the debtor frequently contends that the creditor's failure to "correct" or remove the negative reporting impedes his "fresh start" and/or violates the discharge injunction.

This discussion began with *In re Sommersdorf*, a 1991 decision of an Ohio bankruptcy court. In that case, the creditor reported a charge-off of a pre-petition debt for both the debtor and a non-debtor co-obligor to the credit-reporting agencies, notwithstanding a confirmed Chapter 13 plan that provided for a 100% payout. The non-debtor co-maker claimed that the negative credit reporting prevented him from getting a loan. The debtor requested deletion of the charge-off notation, but the creditor refused. The *Sommersdorf* court concluded that the adverse credit reporting was a "flagrant" violation of the automatic stay and "just the type of creditor shenanigans intended to be prohibited by the automatic stay."

The post-*Sommersdorf* court decisions are far from consistent, and many are fact-specific: "It is largely a matter of the court knowing when it smells it," one decision states. Further, many of the opinions relate to motions to dismiss for failure to state a claim for relief or for summary judgment and do not reach the merits of the case. The courts that have considered the merits of such claims tend to focus on whether the pre-petition credit information was accurate; whether the creditor has a duty to update credit information while the bankruptcy is pending and/or after the discharge; whether the act of furnishing credit information alone constitutes an illegal attempt to collect a debt; and/or the creditor's intent in reporting the delinquent obligation, such as coercing a debtor to pay a discharged debt.

Debtors who challenge the accuracy of credit information furnished pre-petition argue that no credit information should be provided or that the debt should be shown as "discharge in bankruptcy with a zero balance" in accordance with accepted industry practice as endorsed by the FTC. However, these arguments are

fatally flawed, because they overlook a fundamental principle of bankruptcy law: A bankruptcy discharge does not eliminate the debt; it merely extinguishes the debtor's personal liability to pay the debt. Stated differently, the bankruptcy discharge converts a recourse obligation into a nonrecourse obligation. As the Irby court commented, if "...[a]ll that is being reported is the truth," the sole act of reporting a debt that continues to exist cannot violate the discharge injunction.

A more in-depth analysis of the post-Sommersdorf cases confirms that irrespective of the theory advanced by the debtor, creditor liability is found only where the

creditor has engaged in affirmative post-discharge credit reporting and/or collection activity. Some courts impose an even higher standard and require evidence that the creditor persisted in post-discharge collection reporting in knowing violation of the discharge injunction and/or with the intent to increase the likelihood that an inexperienced, unsophisticated and/or ill-advised debtor would voluntarily repay a discharged debt to clean up his credit report.

Although the waters remain muddied and the hidden minefields continue to pervade the servicing landscape, servicers that provide accurate pre-petition

credit reporting and that do not engage in additional collection activity or credit reporting during the bankruptcy case and/or after the discharge will be best positioned to defend against violations claims. **SM**



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