# The Intersection of Bankruptcy and the FDCPA: the CFPB's Notice of Proposed Rulemaking

ABI Consumer Bankruptcy Committee Webinar

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***THIS IS NOT INTENDED TO PROVIDE LEGAL ADVICE***

# PRESENTERS

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NOTE: While the presenters are in leadership positions on the Consumer Bankruptcy Committee of the American Bankruptcy Institute, the views presented in this webinar do not – and are not intended to – represent the viewpoints of all members of the Consumer Bankruptcy Committee or the American Bankruptcy Institute as a whole.

# INTRODUCTION

- May 7, 2019 – Consumer Financial Protection Bureau issued its Notice of Proposed Rulemaking for debt collection.
- May 19, 2019 – Notice of Proposed Rulemaking published in the Federal Register.
- August 19, 2019 – Period for submission of public comments closes.
- Notice of Proposed Rulemaking precedes a final rule (Regulation F) implementing the Fair Debt Collection Practices Act.

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# INTRODUCTION

- FDCPA was enacted in 1977
  - Its intent and purpose was to address abusive debt collection practices and to ensure that debt collectors who did comply with the law would not be otherwise competitively disadvantaged.
- Forty-two years later, the FDCPA is showing its age.
- FDCPA has been left to the inconsistent interpretations of the courts, including with respect to bankruptcy issues.

# INTRODUCTION

- The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), created the CFPB.
- Dodd-Frank granted specific authority to the CFPB over certain enumerated consumer protection laws, including the FDCPA.
- The CFPB was tasked with writing rules of the road to provide creditors and consumers a clear understanding of what constitutes appropriate debt collection activity.
  - CFPB started the debt collection rulemaking process in 2013

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# INTRODUCTION

- **Communications by Email and/or Text**
  - Debt collectors will now be able to communicate with consumers by email and text, provided that the consumer is given the reasonable opportunity to opt-out.
  - No other social media channels will be available.
  - Debt collectors will need to have reasonable procedures in place to ensure that emails and texts are sent to the proper consumer and that the consumer was given proper notice that such a communication channel was used.

# INTRODUCTION

- **Limited Content Messages**
  - Debt collectors will now be allowed to leave a specific message for consumers, either by phone or text, in an effort to get a call back or response without running afoul of the FDCPA.
- **No More Than 7 Telephone Calls per Week per Account**
  - Furthermore, once a debt collector reaches a consumer, subsequent communication is limited to 1 call every 7 days. There are certain exceptions including if a consumer provides consent to be called or requests a call back from a debt collector.

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# INTRODUCTION

## Model Validation Notice

- The Bureau has proposed a standard model validation notice which provides clear cut disclosures a debt collector can use when initially communicating with a consumer.
- The proposed notice also provides consumers with an electronic means of disputing a debt. The Bureau is also considering the electronic delivery of these disclosures provided the debt collector and/or the original creditor has otherwise complied with E-Sign.

# INTRODUCTION

## Additional Prohibited Actions

- Debt collectors will not be permitted to sue or threaten suit on a debt if the debt collector knows or should know that the applicable statute of limitations has expired.
- Debt collectors cannot report collection items to consumer reporting agencies without first communicating with the consumer.
- Debts discharged in bankruptcy cannot be sold or otherwise transferred.

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# INTRODUCTION

- While the NPR touches on the bankruptcy discharge with respect to the transfer of debts, it contains no remedies to the confusion caused when a debt collector subject to the FDCPA is required to communicate with a consumer that has filed a bankruptcy case.
- With respect to the intersection of bankruptcy and the FDCPA, there are several issues on which guidance from the CFPB is essential.

# BANKRUPTCY ISSUES

# BANKRUPTCY ISSUES – DEBT VALIDATION

- The FDCPA and proposed Regulation F requires debt collectors to send – either in their initial communication to the consumer or within five days of that initial communication – a written notice to the consumer containing, without limitation
  - the name and address of the debt collector;
  - the name and address of the consumer;
  - the account number (or a truncated version of that number);
  - the amount of the debt as of a designated itemization date;
  - an itemization of the debt including interest fees payments and credits since the itemization date;
  - the current amount of the debt; and
  - certain information about consumer protections, including requirements regarding the timing and manner of disputing the debt.

# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Conflicts with the Bankruptcy Claims Process*
  - The Bankruptcy Code and the Federal Rules of Bankruptcy Procedure set forth a process to determine the amount owed to a creditor as of the bankruptcy filing date.
  - Subject to limited exceptions, bankruptcy courts have the power to adjudicate disputes with respect to claims asserted in bankruptcy, providing debtors and creditors with a well-defined process for validating debts when a consumer has filed a bankruptcy case.

# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Conflicts with the Bankruptcy Claims Process*
  - Ninth Circuit Bankruptcy Appellate Panel observed that "the debt validation provisions required by FDCPA clearly conflict with the claims processing procedures contemplated by the Code and Rules" and noted that "the provisions of both statutes cannot compatibly operate."
  - The competing validation processes of the FDCPA and the Bankruptcy Code create unnecessary confusion for consumers, which defeats one of the underlying purposes of the FDCPA, which is "to assist consumers in making better-informed decisions about debts they owe or allegedly owe."

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# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Potential Stay/Discharge Violations*
  - Communications that may cause confusion as to whether the debtor is being pressured to make a payment can be considered a violation of the stay or discharge.
  - If a court finds that the communication could be construed as an attempt to pressure or coerce the debtor to make a payment, the court likely will find a violation.
  - This causes particular difficulty in the context of the debt validation notice requirement, as the debt collector must list the debt, including interest and fees.

# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Potential Stay/Discharge Violations*
  - The Third Circuit described the conflict between the FDCPA debt validation requirements and the Bankruptcy Code in its analysis of a consumer's FDCPA claims against a debt collector:
    - The Bankruptcy Code's automatic stay provision prevents collection steps after a bankruptcy case is filed.
    - A debt collector could not satisfy the FDCPA by including the notice of rights in a proof of claim, because "a communication in the form of a formal pleading" is not an "initial communication" under the FDCPA.
    - If a debt collector had to send the notice of rights to a debtor in a pending bankruptcy case to avoid an FDCPA claim, that communication could violate the automatic stay.
    - To omit the notice in order to avoid violating the stay could violate the FDCPA.

# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Financial Disclosures on the Debt Validation Notice*
  - Proposed Regulation F presents risk of consumer confusion with respect to the financial disclosures required, given the impact of bankruptcy on a creditor's debt.
  - Regulation F requires debt collectors to conform substantially to Model Form B-3.
    - In active bankruptcy cases, particularly cases pending under Chapter 13 of the Bankruptcy Code, the financial information set forth in Model Form B-3 may not accurately reflect the status of the debt in bankruptcy or may require additional disclosures or explanations.
    - Even then, the explanation may cause significant consumer confusion

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# BANKRUPTCY ISSUES – DEBT VALIDATION

- *Financial Disclosures on the Debt Validation Notice*
  - Long-term debts
    - Bifurcation of the creditor's claim into pre-bankruptcy and post-bankruptcy components in a maintenance and cure plan is inconsistent with Model Form B-3, which lacks the specificity necessary to avoid consumer confusion.
  - Cramdowns and Lien Strips
    - Cramdowns and lien strips typically are dependent on the consumer's successful completion of all payments required under the consumer's confirmed Chapter 13 plan.
    - If the bankruptcy case is dismissed, the proposed cramdown or lien strip is unwound, restoring the creditor's claim to its original contractual terms. Model Form B-3 does not address these nuances.

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# BANKRUPTCY ISSUES – DEBT VALIDATION

- The bankruptcy process obviates the need for a separate debt validation notice under the FDCPA and Regulation F
  - Proof of claim process
  - Plan confirmation process in cases filed under Chapters 11, 12, and 13
  - Monitoring of the consumer's progress throughout the case by parties in interest,
- Arguably, the debt validation notice could create, rather than prevent, consumer confusion.

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# BANKRUPTCY ISSUES – MINI-MIRANDA

- FDCPA and proposed Regulation F require that in an initial communication with a consumer, a debt collector must inform the consumer that
  - the debt collector is attempting to collect a debt, and
  - any information obtained will be used for that purpose and
- In later communications, the debt collector must disclose that the communications are coming from a debt collector.
- The FDCPA and proposed Regulation F do not provide a bankruptcy-specific exemption from including this "Mini-Miranda" disclosure on communications to consumers that have filed a bankruptcy case.
- If a communication can be construed as an attempt to coerce payment, courts like will find a stay or discharge violation

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# BANKRUPTCY ISSUES – MINI-MIRANDA

- Courts have held that a debt collector's communication to a debtor falls under the FDCPA even if there is no explicit demand for payment if the general purpose is to collect.
- Debt collectors often find themselves at risk of noncompliance when the consumer has filed a bankruptcy case because "appellate and trial courts have reached varying and sometimes inconsistent conclusions about whether and when the Bankruptcy Code precludes FDCPA claims arising from communications to a debtor sent in the bankruptcy context
- While many courts have held that there is no broad categorical preclusion of the FDCPA by the Bankruptcy Code, there is no consensus as to whether the Mini-Miranda disclosure requirement in the FDCPA presents a direct conflict.

# BANKRUPTCY ISSUES – MINI-MIRANDA

- Court of Appeals for the Third Circuit held that the Mini-Miranda disclosure requirement directly conflicts with the Bankruptcy Code:
  - The Bankruptcy Code's automatic stay provision forbids "any act to collect, assess, or recover a claim against the debtor that arose before the commencement" of the bankruptcy proceeding.
  - Several courts have held that sending a § 1692e(11) notice violates the automatic stay.
  - If, as the [debtors] argue, a § 1692e(11) claim could arise from the fact that the . . . letters and subpoenas did not include the "mini-*Miranda* " notice, the firm would violate the automatic stay provision of the Bankruptcy Code by including the notice or violate the FDCPA by not including the notice.
  - This conflict precludes allowing a claim under § 1692e(11) for failing to include the "mini-*Miranda* " notice in the letters and Rule 2004 examination subpoenas sent to the Simons through their bankruptcy counsel. (citations omitted).

# BANKRUPTCY ISSUES – MINI-MIRANDA

- The Court of Appeals for the Second Circuit, however, indicated that no irreconcilable conflict existed between the Bankruptcy Code and the Mini-Miranda requirements, at least when a communication appears to have violated both the bankruptcy discharge injunction and the FDCPA:
  - In *Simon,* the Third Circuit held that the FDCPA could not require the creditor to include a mini-*Miranda* warning with its examination notice and subpoenas because a communication that included such a warning, sent prior to a discharge, would constitute a collection attempt forbidden by the automatic stay.
  - The Third Circuit ruled that subsection 1692e(11) conflicted with the Bankruptcy Code because including the warning would violate the Code and omitting it would violate the FDCPA.
  - This holding in *Simon,* however, whether or not we would agree with it, has no application to Garfield's subsection 1692e(11) claim. Ocwen's communication, even without a mini-*Miranda* warning, was an attempt to collect a discharged debt in violation of the Bankruptcy Code. The absence of a mini-*Miranda* warning also violated the FDCPA. There is no conflict.

# BANKRUPTCY ISSUES – ATTORNEY COMMUNICATIONS

- The FDCPA and proposed Regulation F provide that – without the prior consent of the consumer given directly to the debt collector or the express permission of a court of competent jurisdiction – a debt collector may not communicate with a consumer in connection with the collection of any debt if:
  - the debt collector knows the consumer is represented by an attorney with respect to such debt; and
  - has knowledge of, or can readily ascertain, such attorney's name and address, unless the attorney fails to respond within a reasonable period of time to a communication from the debt collector or unless the attorney consents to direct communication with the consumer

# BANKRUPTCY ISSUES – ATTORNEY COMMUNICATIONS

- In many bankruptcy cases, the consumer's contact with his or her bankruptcy attorney decreases drastically once the bankruptcy case is filed.
- The bankruptcy attorney, while closely involved in the preparation of the initial bankruptcy filing and in obtaining confirmation of the consumer's bankruptcy plan, is unlikely to regularly communicate with the consumer regarding ongoing monthly payments to creditors and the specific status of particular loans or accounts.
- This lack of communication leads to tension among the FDCPA, the Bankruptcy Code and certain CFPB communication requirements set forth in Regulation Z.

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# BANKRUPTCY ISSUES – ATTORNEY COMMUNICATIONS

- Example – Regulation Z
  - Subject to limited exceptions, Regulation Z requires creditors to provide periodic statements to consumers that are in an active bankruptcy case or that have received a discharge in bankruptcy.
  - Regulation Z does not directly address the fact that consumers may be represented by counsel.
  - The CFPB's March 20, 2018 answers to frequently asked questions recognize the conflict with the FDCPA, but do not directly address the difficulties associated with delivering these statements monthly to the attorney instead of the consumer:
    - If a borrower in bankruptcy is represented by counsel, to whom should the periodic statement be sent? *In general, the periodic statement should be sent to the borrower. However, if bankruptcy law or other law prevents the servicer from communicating directly with the borrower, the periodic statement may be sent to borrower's counsel.*

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# BANKRUPTCY ISSUES – ATTORNEY COMMUNICATIONS

- United States Bankruptcy Court for the Northern District of New York
  - Debtor's attorney noted that the mailing of the periodic statements to him instead of the consumer placed his firm "in the position of being the post office for monthly mortgage statements," which increased both the "clerical time spent on the re-mailing function" as well as liability to his firm in ensuring that the statements are re-mailed. The parties entered into an agreement that statements would be mailed directly to the consumer going forward.
  - Notably, the court's confirmation order in the case appeared to direct the creditor to send such statements directly to the consumer, which would constitute "express permission of a court of competent jurisdiction" under proposed Regulation F.
  - However, bankruptcy courts are not uniform with respect to plans and confirmation orders, and a one-off approach to the issue is not practical.
  - The information in the periodic statements is intended to provide the consumer with monthly updates regarding the status of the loan.
  - The expense and delay associated with sending these statements to the consumer's bankruptcy attorney defeats the purpose of the regulation.

# CONCLUSION

- Members of the ABI's Consumer Bankruptcy Committee are submitting a public comment to the Notice of Proposed Rulemaking, requesting that:
  - Regulation F contain an exemption from the debt validation notice requirements for debts included in an active bankruptcy case and debts for which the consumer has received a bankruptcy discharge **or** permit bankruptcy-specific modifications to any required debt validation notices.
  - Regulation F contain an exemption from the Mini-Miranda disclosure requirements for debts included in an active bankruptcy case and debts for which the consumer has received a bankruptcy discharge **or** permit bankruptcy-specific modifications to any required Mini-Miranda notices.
  - Regulation F contain an exemption from the requirement that a debt collector communicate with the consumer through the consumer's attorney with respect to the modified bankruptcy periodic statements required by Regulation Z.
- **The Consumer Bankruptcy Committee represents a diverse group of practitioners, ranging from debtor's attorneys and consumer advocates to creditor's attorneys and in-house counsel at financial institutions. The public comment, while seeking CFPB guidance on a limited number of bankruptcy-specific issues, is not intended to represent the viewpoints of all Consumer Bankruptcy Committee members or the American Bankruptcy Institute as a whole.**

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# QUESTIONS?