SCOTUS Update: Recent Bankruptcy Rulings
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Two recent decisions from the Supreme Court of the United States have narrowed the protections available to consumers through the Fair Debt Collection Practices Act (FDCPA).\(^1\) In *Midland Funding, LLC. v. Johnson*, 137 S.Ct. 1407 (2017), the Court held 5-3\(^2\) that the filing in a bankruptcy court of an obviously time-barred proof of claim was not a violation of the FDCPA. In *Henson v. Santander Consumer USA Inc.*, 137 S.Ct. 1718 (2017), the Court held unanimously that a party who owns the debt it is attempting to collect is not a “debt collector” for purposes of the FDCPA. However, unanswered questions in *Henson* and calls for legislation in both decisions leave regulators and the industry with some uncertainty.

In *Midland*, the Court determined whether the filing in bankruptcy court of a proof of claim that is time-barred on its face is false, misleading, deceptive, unfair, or unconscionable so as to be a violation of the FDCPA. The Court held it was neither.

Whether a time-barred filing is false, misleading, or deceptive may depend on relevant state law, which the Court noted will determine whether a person has “a right to payment,” otherwise known as a claim.\(^3\) Essentially, the Court explained that if one has a claim, it cannot be false, misleading, or deceptive to assert a proof of claim, so long as the relevant state law provides that the right survives even after any relevant limitations period has passed. Because the law has “long treated unenforceability of a claim (due to the expiration of the limitations period) as an affirmative defense,” the Court held that the claim exists and is enforceable until the assertion and success of such defense, meaning the filing of a proof of claim is neither misleading nor deceptive.\(^4\)

The *Midland* Court stated that whether such a filing is unfair or unconscionable requires considering several circumstances that distinguish the bankruptcy setting from that of an ordinary civil suit.\(^5\) The Court asserted consumers likely will not unwittingly pay a time-barred debt during a bankruptcy because consumers initiating Chapter 13 bankruptcy are of greater sophistication than the average, because a knowledgeable trustee is available, because procedural rules in bankruptcy more directly guide the evaluation of claims, and because the claims resolution process is “generally a more streamlined and less unnerving prospect for a debtor than facing a collection

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2 Arguments were held before Justice Gorsuch had assumed the bench.
3 *Midland*, 137 S.Ct. at 1411-12.
4 *Id.* at 1412.
5 *Id.* at 1413.
lawsuit.” The Court finally pointed to the “delicate balance” that exists between a debtor’s protections and obligations in bankruptcy, asserting that it would upset this balance to require a civil court to determine which affirmative defenses could render the assertion of a proof of claim a violation of the FDCPA.

Justice Sotomayor wrote on behalf of the dissent, disagreeing strongly with the majority’s position that the filing of an obviously time-barred claim is not “unfair” or “unconscionable.” The dissent pointed out that “every court to have considered the question has held that a debt collector that knowingly files suit in court to collect a time-barred debt violates the FDCPA” and opined that “[d]ebt collectors do not file these claims in good faith.” Finally, the dissent characterized the majority opinion as a “trap for the unwary,” and calls for Congress to clarify that the filing of such a claim violates the FDCPA.

Nuances of state law may affect the impact of *Midland*.* Midland* itself dealt with a claim under Alabama state law, under which a person has a right to payment of even a time-barred debt until any relevant defenses are asserted and prevail. Like Alabama, Texas’ statute of limitations does not affect the substantive rights of a party or prevent it from filing a lawsuit; rather, they operate to bar the enforcement of a right, and only when the proper affirmative defense is raised. However, other states may treat their statutes of limitations differently, possibly even barring the filing of a claim after the expiration of the limitations period. In any event, as the dissent said, outside of the bankruptcy context, a debt collector’s filing of an obviously time-barred claim is a violation of the FDCPA. However, the Supreme Court later in the session addressed the question of who faces the possibility of private lawsuits and government enforcement under the FDCPA.

In *Henson*, the “nub,” as Justice Gorsuch put it in his first opinion authored as a Supreme Court Justice, is who exactly is a debt collector for purposes of the FDCPA. The statute defines “debt collector[s]” to include anyone who “regularly collects or attempts to collect...debts owed or due...another.” Petitioners and respondents agreed that a third party acting on behalf of the debt owner is certainly a debt collector; they likewise agreed that the loan originator seeking to collect payment on the debt it owns is also not a debt collector under the FDCPA. However, the question before the Court was whether a party who did not originate the loan but who attempts to collect a purchased debt, is a “debt collector” under the FDCPA.

It is important to note that the Court delayed two related questions for later days. First, the Court declined to consider petitioners’ arguments that because Santander regularly engaged in the collection of debts that it does not own, it should be treated as a debt collector in all its collection practices, noting that petitioners did not raise the theory in their petition for certiorari. Second,

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6 *Id.* at 1413-14.
7 *Id.* at 1415.
8 *Id.* at 1417 and 1419.
9 *Id.* at 1421.
10 See *City of Dallas v. Etheridge*, 152 Tex. 9, 14 (1952).
12 *Henson*, 137 S.Ct. at 1721.
13 *Id.*
both parties raised arguments about another statutory definition of “debt collector,” which includes those engaged in “any business the principal purpose of which is the collection of any debts,” but the Court did not agree to address it in granting certiorari. The answer to either of these questions could drastically dampen the effect of Henson on the industry.

The Court readily dismissed petitioners’ grammatical argument differentiating a debt “owed” versus a debt “owing,” stating that a clear reading of the FDCPA forces one to conclude that “owed” means a debt currently due at the time of collection, and cannot be used to distinguish one who subsequently acquires a debt originated by another. The Court was likewise unreceptive to petitioners’ alternative argument that everyone who attempts to collect a debt is either a “debt collector” or a “creditor,” but not both. Petitioners argued that the definition of “creditor” excludes those who seek to collect a debt obtained in default, and because respondents did so, they cannot be a “creditor” and must be a “debt collector.” However, the Court stated that this “creditor” definition exclusion only applies “when the debt is assigned or transferred “solely for the purpose of facilitating collection of such debt for another.” The Court posited that, even if petitioners are correct and one must be either a “debt collector” or a “creditor,” until a party attempts to collect on debts owed another, the exclusion does not apply.

The Court dismissed petitioner’s policy argument that Congress was not aware of the looming debt purchasing industry that flourished in the time since Congress considered the FDCPA, characterizing it as too speculative, noting that the Court is limited to “apply[ing], not amend[ing], the work of the People’s representatives.”

Some state debt collection practices acts may include a broader definition of “debt collector,” such that some claims under those laws will not be affected by Henson. For example, The Texas Debt Collection Act (“TDCA”) definition of “debt collector” as a person who directly or indirectly engages in “debt collection,” which is defined as “an action, conduct, or practice in collecting, or in soliciting for collection, consumer debts that are due or alleged to be due a creditor.” Note that unlike the FDCPA, the TDCA does not require the debt be owed to another, which underlies the “nub” in Henson. Likewise, the California Fair Debt Collection Practices Act defines “debt collector” as anyone who “in the ordinary course of business, regularly, on behalf of himself or herself or others, engages in debt collection,” defined as “any act or practice in connection with the collection of consumer debts.”

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15 Henson, 137 S.Ct. at 1721.
16 Id. at 1722-23.
17 Id. at 1724 (quoting U.S.C. § 1692a(4)).
18 Id. at 1724.
19 Id. at 1726.
20 TEX. FIN. CODE ANN. § 392.001(5)-(6) (West 2017) (emphasis added).
21 CAL. CIV. CODE § 1788.2(b)-(c) (West 2017).
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