

# When Does Communication Turn Into Collection?

How well do innovative loss mitigation techniques and campaigns jibe with long-standing debt-collection rules?

by Carolyn A. Taylor

*Editor's note: This article is the third in a multi-part series addressing the Fair Debt Collection Practices Act and potential compliance hazards that warrant attention.*

Loss mitigation is the mantra of the mortgage industry. With no foreseeable end to the mortgage crisis, the environment has shifted from a paradigm where foreclosure made business sense in many cases to one in which loan resolution is necessary, suggested and often required to avoid negative consequences affecting our country's troubled economy. A successful loss mitigation solution is a win-win situation for all involved: The economically depressed customer remains in his home, the lender converts a nonperforming loan into a performing loan and the collateralized real estate does not become part of the exponentially increasing population of real estate owned properties on the market, thereby helping to preserve property values and the integrity of local neighborhoods.

Loss mitigation covers a broad range of options, including non-curing repayment plans, reinstatement agreements, loan modifications, deeds-in-lieu of foreclosure, short sales and consent judgments. However, loss mitigation works only in those situations where the borrower and the lender effectively communicate with each other and reach a mutually beneficial solution. The process presupposes a verbal or written dialogue

between the borrower and the lender or servicer, and thus, falls squarely within the types of activities covered under the Fair Debt Collection Practices Act (FDCPA) and comparable state statutes.

The FDCPA applies only to third-party debt collectors of consumer debts. The FDCPA definition of "debt collector" does not include an assignee of



a debt that was not in default at the time it was obtained. By contrast, many state statutes are broader in scope and cover the activities of creditors collecting their own debts. The line between loan workout communications and debt

collection is often a gray area. The determination that a loan resolution is not economically feasible often precipitates allegations of deceptive, misleading, confusing, coercive and/or unfair practices. Further, alleged violations are analyzed from the viewpoint of the "least sophisticated consumer."

The federal and state debt collection practices statutes provide fertile ground for litigation. In March of this year, 960 cases were filed in U.S. district courts alleging violations of the FDCPA and the Telephone Communications Privacy Act (TCPA) - a record number of cases filed in a single month. Year-to-date, 2,542 such lawsuits have been filed. If this trend continues, the number of lawsuits this year will likely exceed the 10,000 cases filed last year. Interestingly, 15% of the cases were filed in districts in which the plaintiff did not reside. The most common violations alleged were collector harassment, the content of collection letters, overshadowing (i.e., conveying conflicting messages) and voice-mail messages - one or more of which may occur during the loss mitigation process.

Despite the record number of debt-collection lawsuits, only seven circuit appellate courts and the Federal Trade Commission (FTC) have rendered opinions that involve the FDCPA and a loan modification, a loan workout and/or a related communication. If a court finds that the creditor is a "debt collector" for the purposes of the FDCPA and/or the applicable state statute, the court must then determine whether the communication in question was "in connection with collection of any debt" and, if so, whether the creditor's actions and/or omissions constitute illegal debt-collection practices.

The FTC advisory opinion dated March 19, 2008, provides some instruction on these issues. That opinion states that a debt collector does not violate the FDCPA by discussing foreclosure loss mitigation options in the initial or subsequent communication with the borrower. However, the opinion adds the caveat that this does not preclude a fact-based finding that a specific communi-

would bear this expense), that the lender requested that Titanium contact the borrower "because of certain payment arrearages" on the loan," and/or that "We must collect information from you to analyze your current financial situation"; enclosed a "financial information form" for the borrower to sign and return; and requested copies of pay stubs and federal income tax returns.

solve your delinquency," requested a return call and closed with the statement, "We look forward to working with you, and while no guarantee can be made, we believe it would be beneficial for all parties to attempt to work out a resolution." The second letter was identical to the first but also included the California Rosenthal FDCPA notice and the FDCPA Mini-Miranda warning.

The court ruled that the letters were in the "nature of providing information" rather than "in connection with the collection of any debt," even though the ultimate goal was to ensure payment. Further, inclusion of the statutory mandated disclosures did not alter the nature of the communication. Similarly, in *Santoro v. CTC Foreclosure Service Corp.*, the Ninth Circuit Court held that a letter suggesting loan workout options sent by the mortgage servicer directly to borrowers was not "in connection with the collection of any debt," notwithstanding knowledge that the borrowers were represented by counsel.

While few appellate courts have weighed in specifically on whether loan modification agreements violate the FDCPA, several courts have found other "settlement" type offers not to be per se violations. The leading opinions on the issue are the Sixth Circuit's *Lewis v. ACB Business Services Inc.* (and its offspring, *Gillespie v. Chase Home Finance LLC*, which applied the same concept to a mortgage servicer) and the Seventh Circuit's *Bailey v. Security National Servicing Corp.*

In the *Lewis* case, the debtor sent a "cease communication" letter in accordance with Section (§) 1692c of the FDCPA. Thereafter, the collection agency sent to the borrower a letter that contained the statutory debt disclosure language and outlined several plans to settle the delinquent credit card debt. In response, the borrower filed suit alleging several FDCPA violations, including the cease-communication provision of §1692c(c). The court found that the debt collector's letter notifying the debtor of various payment plans was a permissible communication, stating, "We believe that Lewis' interpretation of §1692c(c)(2), which would prohibit collectors from sending non-coercive settlement offers as a remedy, is plainly at variance with the policy of the legislation as a whole."

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cation overshadows or is inconsistent with disclosure of the right to dispute or validate debt or that a specific communication is false, deceptive or misleading upon consideration of all facts. Significantly, the opinion does not address the issue of whether a communication informing a consumer of workout options may be characterized as either a demand for payment or a communication "in connection with the collection of" a consumer debt.

Innovative loss mitigation techniques have not gone unchallenged. Use of third-party "door knockers" to initiate a loss mitigation dialogue with the borrower have been the subject of several federal class-action lawsuits filed in the Midwest alleging false and misleading representations, unfair and unconscionable debt-collection practices and failure to give the Mini-Miranda warning.

In the cases of *Lappin v. Titanium Solutions Inc.*, *Lige v. Titanium Solutions Inc.* and *Gburek v. Litton Loan Servicing*, the lenders retained Titanium Solutions to contact the borrower and elicit financial information to analyze loan workout options.

In each case, a letter, signed by Titanium as an "independent agent for (your lender)," was sent to a borrower on Titanium letterhead. Each letter disclaimed Titanium's status as a debt collector; contained a reference subject line that included the lender's name, loan number and the property address; stated that Titanium is not a debt collector, that Titanium's services were at no cost to the borrower (implying the lender

Despite its disclaimer of debt-collector status, it is significant that Titanium's website boasted "communications to over 50,000 homeowners annually relative to mortgage debt collection." Remarkably, all three cases settled early in the litigation process for damages of \$25,000 or less, before class certification and before the lenders joined as defendants in the suits.

Some courts distinguish between loss mitigation letters that demand payment and those that are informational only. These cases emphasize that the purpose of the FDCPA is to prohibit abusive collection practices, not to inhibit peaceful resolution of debts. ("...To hold that a debt collector cannot offer payment options as part of an effort to resolve an outstanding debt, possibly without litigation, would force honest debt collectors seeking a peaceful resolution of the debt to file suit...something that is clearly at odds with the language and purpose of the FDCPA," found one 1998 court ruling.) Factors considered by these courts include whether the letter demands payment or advises of the current status of the debt; contains the terms of payment and deadlines; implies that an amount is past due; references prospective, rather than prior, dates; and/or threatens collection action.

In *Gillespie v. Chase Home Finance LLC*, the borrower challenged two letters sent by the servicer's homeowner assistance department informing him of options to avoid foreclosure. The first letter advised that there were a "variety of workout options which might help re-

The court went on to harmonize the practice of sending settlement letters with the FDCPA prohibitions against abusive debt-collection practices: "Allowing debt collectors to send such a letter is not only consistent with the act, but also may result in resolution of the debt without resorting to litigation, saving all parties involved the needless cost and delay of litigation as is exemplified by this very case...it is certainly within the purpose of the act to allow a debt collector to make a truthful statement that various payment plans are available."

In *Bailey v. Security National Servicing Corp.*, the Seventh Circuit held that the mortgage servicer was not a debt collector under the FDCPA, even though the underlying debt was in default because the loan was under a forbearance agreement that was current when the mortgage servicer acquired the loan.

The court noted in dicta that the borrower's claim would have failed on the secondary reason that the letters were not communications "in connection with the collection of any debt." The letter did not demand payment, but merely listed future payments due, the current status of the debtor's account and a warning of the consequences of default - communications that, in the Seventh Circuit's view, were not subject to the FDCPA.

While the judiciary tends to favor loan workouts, any settlement overture that is misleading, false or deceptive from the viewpoint of the "least sophisticated consumer" will be deemed an FDCPA violation. The Third Circuit, in a case of first impression, considered

whether a settlement letter was deceptive when it was signed by a member of the creditor corporation's executive management. The court held that the least-sophisticated debtor, after reading the letters in their entirety, would understand the letters came from the creditor corporation, not the officers individually. The court seemed to assume that the creditor's letters were "in connection with the collection of [a] debt" and defended the use of settlement notices generally, saying, "There is nothing improper about making a settlement offer....Nevertheless, in keeping with the statutory requirements, collection agencies may not be deceitful in the presentation of the settlement offer."

In *Dutton v. Wolpoff and Abramson*, a law firm's letter offering to release a judgment in return for a settlement payment was found to be in violation of §1692e(11) of the FDCPA because it did not contain the Mini-Miranda warning disclosing that the purpose was debt collection and any information obtained would be used for that purpose. This court was particularly emphatic that the literal language of the statute required that these disclosures must be made in all communications to collect a debt.

Likewise, the Fifth Circuit found a debt collector's letter offering to settle the debt at a 30% discount if paid in 30 days to be misleading where the debt collector was permitted to offer a 50% discount without a time limit.

"While we agree that it is important to permit collection agencies to offer settlement... [a] collection agency may... not be deceitful in the presentation of

that settlement offer," the court stated.

In *Evory v. RJM Acquisitions Funding LLC*, Seventh Circuit Judge Richard Posner drafted language that he believed offered a safe harbor for debt collectors wishing to make settlement offers. The language is intended to protect against the least-sophisticated consumer perceiving the offer as a one-time offer, when in reality, the debtor collector has authority to renew the offer if the consumer fails to accept it initially. Posner suggested that a settlement offer include the following language: "We are not obligated to renew this offer." In Posner's view, the word "obligated" is strong, and even the unsophisticated consumer will realize that there is a renewal possibility but that it is not assured."

In today's environment, creditors engaging in loss mitigation may be braving untested waters. Until loss mitigation is afforded a safe harbor, the tension between prohibited third-party disclosure and adequately informing the consumer that the communication is from a debt collector, among other issues, will continue to present significant challenges for the consumer mortgage industry. **SM**



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