

## **HARASSMENT OF DEBTORS: WHEN TO SUE**

(presentation to Poverty Law Section of the State Bar of Texas on 2/1/08)

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### **A. Introduction**

In practicing consumer law over the past 28+ years, I have come to the conclusion that case selection is probably one of the most important features of any successful law practice. That conclusion also holds true for those who practice in legal services, as I once did in East Texas and Houston. As a legal services practitioner, you should want to utilize the limited resources available, your time, on those cases with the best chance of leading to a successful outcome. Here are a few general rules that I follow.

#### **1. Avoid trying to make new law.**

Don't forget that you practice in Texas. Given the current conservative climate prevalent in Texas courts, state and federal, I am very conservative professionally in my reading of the law.<sup>1</sup> I select cases largely on the basis of whether the law applicable to the facts of a particular case is accepted and not subject to challenge. I am not expecting any judges in this state to make any leaps and to extend the law to areas not previously recognized. To the extent the law grows to reflect changes in the current environment, I expect those changes to occur largely in other jurisdictions.

#### **2. Look for objective facts that support your claims.**

Reflecting my desire for the selection of successful cases, I prefer cases where the

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<sup>1</sup> Needless to say, my politics cannot be adjudged as conservative in any shape or form.

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factual positions of my clients are difficult to attack. In the context of fair debt collection, that means I prefer a case with a high level of objective proof. For example, I prefer tapes of telephone calls when abusive tactics are used; I prefer the testimony of third parties that are unrelated to the client in wrongful third-party cases; and I am always happy to work on a case based on a dunning letter. In all three cases, what actually happened is not seriously at issue. Similarly, I prefer cases where there is no obvious defense, like the bona fide error defense recognized by both the Fair Debt Collection Practices Act (FDCPA) and the Texas Debt Collection Act (TDCA). That means I prefer claims where it appears the conduct at issue seems to be widespread as reflected by complaints with the Better Business Bureau or the applicable Attorney General's office, because then the debt collector will have difficulty asserting that there are procedures in place which are reasonably adapted to prevent such conduct. See 15 U.S.C. § 1692k(c); Tex. Fin. Code § 392.401.

### **3. Think carefully about the court in which you appear.**

In evaluating the odds of a claim, one of my main inquiries relates to the court in which a suit is filed. Here in Houston, I often prefer to file new lawsuits under the FDCPA in federal court, because I actually think there is a better chance of getting a reasonable, open-minded judge. That rule of thumb, however, can be wrong (even in Houston). It depends on the judges in your jurisdiction and how well you can predict their behavior on the bench. In considering the merits of a counterclaim in a debt action filed in your local county court at law, you have to weigh the predilections of the sitting judge. If you have no prior experience, you need to ask around. In deciding where to file an affirmative

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FDCPA claim, you need to consider whether your chances are better in state court or federal court. To restate the obvious, the Rio Grande Valley is not the same as Amarillo or Houston.

Moreover, the availability of federal jurisdiction only exists when there is a federal claim. In short, you cannot file an unfair debt collection suit in federal court unless the FDCPA applies. Unlike the TDCA which covers all parties engaging in the collection of consumer debts, the FDCPA does not apply to original creditors seeking to collect their own debts unless they use a name other than their usual business name to collect. Nevertheless, the scope of the FDCPA is still broad enough to cover independent debt collection agencies, buyers of delinquent consumer accounts and law firms that regularly engage in the collection of consumer debt.

### **4. Recognize the statutory relief available in your case.**

In deciding what action to take, you need to recognize that the TDCA has a wider scope than the FDCPA but it prohibits less misconduct than the FDCPA. Similarly, while both statutes permit the recovery of actual damages, only the TDCA offers injunctive relief and only the FDCPA offers awards of statutory damages when there is no proof of actual damages.

### **5. Does the debt collector's behavior fail the smell test?**

Most importantly, you must consider whether the debt collector's conduct would appear to be deceptive or unfair to a typical juror. Run the facts by colleagues, friends and family to get some idea how others respond to the facts. The best cases are those

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in which persons of all stripes and backgrounds are offended by the conduct at issue.

### **B. Common unfair debt collection claims**

In my practice, I see a number of common FDCPA and TDCA claims that are easy to prove factually and involve the application of well-accepted law. What follows is a non-exclusive list of such claims.

#### **1. Threats of arrest and prosecution related to payday loan debt**

Like many of your clients, many of mine are sometimes so desperate for cash that they will seek out payday loans, a form of lending with 500+% interest rates which is also associated with quite aggressive debt collection practices. The high rates of interest in these loans do reflect objectively the high risk of potential default, given the absence of any serious underwriting of these loans and the obvious financial desperation of those willing to seek these loans. Nevertheless, payday loan companies are generally quite profitable. How can that be explained? My explanation, based on years of anecdotal experience (and admittedly no empirical study), is that payday loan borrowers make payments on these loans repeatedly (on average, 8-10 times according to a number of studies), because they fear arrest and prosecution if they fail to make the payments.

Payday loan borrowers fear arrest and prosecution, because payday lenders and their third-party debt collectors implicitly or explicitly indicate that the bouncing of a debit or check given as security for the loan constitutes a hot check misdemeanor or a theft by check felony. NOT TRUE. Giving a bad check as compensation during a sale or loan transaction is only a criminal offense if the party accepting the check (here the payday

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lender) had reason to believe that the check was actually good on the day it was given. In the typical payday loan transaction, the consumer gives a check to the lender on the day she signs the note and receives the proceeds of the loan, but the lender agrees not to deposit that check or debit the account until the due date of the loan, typically 2 weeks later, and then only if the consumer fails to pay off the loan or to renew it by paying the amount of interest earned over the short term of the loan. In effect, the check given by payday borrowers is like a post-dated check, because the payday lenders agree not to cash the check or debit the underlying account until 2 weeks in the future. As a result, payday lenders know that the check is not any good on the day it is given, as no one in their right mind would seek one of these high-interest loans if she had the money she needed in her own bank account. Under these circumstances, the subsequent bouncing of the check is not a crime in the eyes of most prosecutors, because there is no presumption of criminal intent. *Jones v. Kunin*, 2000 U.S. Dist. LEXIS 6380, \*3-4 (S.D. Ill. 2000); *Turner v. E-Z Check Cashing*, 35 F.Supp.2d 1042, 1051-1052 (M.D. Tenn. 1999); *Hartke v. Ill. Payday Loans, Inc.*, 1999 U.S. Dist. LEXIS 14937, \*9 (C.D. Ill. 1999).

Let me add that, in my experience, payday lenders have not commonly sought to prosecute borrowers who default and whose checks or debits then bounce. There may be exceptions to this general rule, as I recall last year hearing from a payday loan borrower in a town south of Dallas who was prosecuted in J.P. court for this purported criminal conduct.

If a third-party debt collector makes a threat of criminal arrest or prosecution arising

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from failure to pay a payday loan, you probably have an FDCPA claim under 15 U.S.C. § 1692e(4), (5) and (7). See *Nance v. Ulferts*, 282 F.Supp.2d 912 (N.D. Ind. 2003). It likewise constitutes a TDCA claim under Tex. Fin. Code § 392.301(a)(2). See *Brown v. Oak Lawn Bank*, 718 S.W.2d 678, 680 (Tex. 1986), The claim arises for two reasons: (1) the accusation that the borrower committed a crime is false, and (2) the threat of actual prosecution is probably false as well. Given that both statutes are violated, you could seek actual damages under both, statutory damages under the FDCPA and injunctive relief under the TDCA.

The best of these claims include evidence of taped telephone calls or written communications in which the debt collector made the wrongful threat. In one of my pending cases, *Joebert Silva v. Capital Collections LLC* (Civil Action No. A 07 CA 283 LY; In the United States District Court for the Western District of Texas, Austin Division), the debt collector not only made two written threats of criminal prosecution, it also threatened to file these charges in a court that does not even exist, the Magistrates Court of Williamson County, Texas.

### **2. Filing suit in the wrong venue**

Under 15 U.S.C. § 1692i, a suit to collect a consumer debt in any venue other than the jurisdiction in which the consumer debtor resides at the time suit is filed or the jurisdiction in which the underlying contract was signed by the consumer debtor violates the FDCPA. *Addison v. Braud*, 105 F.3d 223 (5<sup>th</sup> Cir. 1997); *Fox v. Citicorp Credit Services, Inc.*, 15 F.3d 1507 (9<sup>th</sup> Cir. 1994); *McKnight v. Benitez*, 176 F.Supp.2d 1301

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(M.D. Fla. 2001). The Texas Deceptive Trade Practices Act also prohibits this distant forum abuse but only a county level. See Tex. Bus. & Com. Code § 17.46(b)(23). Here, the law is not only clear, but the facts are usually indisputable.

This type of collection abuse happens all of the time in Texas. A debt buyer may sue a consumer in the wrong county or even the wrong J.P. court precinct and thereby violate section 1692i. When it happens in these cases, I sometimes move to transfer venue to the correct venue and then claim the attorney fee paid to transfer venue as a form of actual damages, together with statutory damages of \$1,000, as an FDCPA counterclaim. Many times this leads the law firms to offer a mutual dismissal, a great outcome for our clients. In other cases, I have encountered law firms that have intentionally filed suit in the wrong venue with the intent of likely obtaining a default judgment — what I call a “default trap.” In some of those cases, I have actually sued the law firm for filing suit in the distant forum. See *Hester v. Graham, Bright & Smith*, 2004 U.S. Dist. LEXIS 28923 (E.D. Tex. 2004). Similarly, in an investigation I handled when I was serving as an assistant attorney general in the Texas Attorney General’s office, we received complaints that an appliance store chain was suing defaulted debtors exclusively in Jefferson County, even though they resided and signed the contracts in San Antonio, Austin and Houston. Since this violated the DTPA, the AG was authorized to seek an injunction under Tex. Bus. & Com. Code § 17.47 but ultimately accepted an assurance of voluntary compliance under Tex. Bus. & Com. Code § 17.61.

### **3. Threat of wage garnishment or seizure of homestead**

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Another common form of unfair debt collection claim involves threats of wage garnishment or seizure of homestead made either in a written dunning letter or over the telephone (and preferably taped). As you know, Texas law permits wage garnishment only for the collection of child support and alimony, while federal law tends to limit its use of this collection tool to student loan and income tax debts. Likewise, only purchase money, home equity, home improvement and property tax loans are allowed to impose liens on homesteads in Texas, and judgment liens arising from abstracts of judgment based on other debts, such as credit card debt, do not even impose a lien on a homestead. A threat of suit coupled with a threat of wage garnishment or seizure of one's home is not uncommonly used by debt collectors and debt buyers seeking to collect credit card and other debts, even though this tool is unavailable. As a result, the use of these wage garnishment and home seizure threats during an effort at collecting a consumer debt in Texas violates 15 U.S.C. § 1692e(4) and (5) and Tex. Fin. Code §§ 392.301(a)(8) and 392.304(a)(19).

I recently asserted a wage garnishment claim in a class action against Drive Financial, an original creditor that used a name other than Drive in a dunning letter to Texas consumers that also falsely threatened to seek garnishment of wages, and this claim settled on excellent terms for the class ---- the payment of \$250,000 in statutory damages to a little less than 1200 consumers. In an individual case, this type of claim can be used to seek the maximum statutory damages award of \$1,000 under 15 U.S.C. § 1692k(a)(2)(A).

### **4. Threats and filing of suit on time-barred debt**

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Under Texas law, most debts, including credit card and automotive deficiency debt, have 4-year statutes of limitation. Threatening to file suit on a credit card debt when the statute of limitations has run is a violation of 15 U.S.C. § 1692e(5), while actually filing suit on such a stale claim violates both §§ 1692e(5) and 1692f. The ultimate source for this proposition of law is *Kimber v. Federal Financial Corporation*, 668 F.Supp. 1480 (M.D. Ala. 1987). For more recent examples of this theory, see *Harvey v. Great Seneca Financial Corporation*, 453 F.3d 324, 332 (6<sup>th</sup> Cir. 2006); *Freyermuth v. Credit Bureau Services, Inc.*, 248 F.3d 767,771 (8<sup>th</sup> Cir. 2001); *Goins v. JBC & Associates*, 352 F.Supp.2d 262 (D. Conn. 2005). Most recently, I have raised this theory in response to petitions to confirm arbitration awards sought by MBNA on credit card debt, because the debt buyer or the law firm failed to file the confirmation petition within the 1-year period permitted by the Federal Arbitration Act that traditionally applies to credit card debt claims.

### **5. Failing to validate a debt before collecting**

Most debt collectors send dunning letters with a particular notice required by 15 U.S.C. § 1692g that informs the recipients that the debt will be verified if all or part of the debt is disputed. When these letters are sent, you may want to advise your clients to dispute the debt in writing (by fax or certified mail to prove receipt), particularly when you think the letter is addressed to the wrong person, the debt has been paid off or the limitations period has run. Under this same section, the debt collector is required to refrain from all collection efforts until such time as written verification is provided. While not much is required in terms of verification, many debt collectors violate the FDCPA by continuing

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to collect after receiving notice of a dispute. 15 U.S.C. § 1692g(b). This allows you to raise a claim for \$1,000 in statutory damages.

### **6. Contacting consumer after being told not to call at work**

Section 1692c(a)(1) and (3) also prohibits calling a consumer at work if the debt collector has been told that it is not convenient to make calls at the workplace or that the employer prohibits such calls. While these claims are not always subject to being taped, testimony from a non-plaintiff employer or supervisor is hard to attack. Again, this permits you to seek \$1,000 in statutory damages.

### **7. Contacting a consumer directly when known to be represented by counsel**

Section 1692c(a)(2) prohibits debt collectors from contacting a consumer debtor directly when the debt collector is aware the debtor is represented by counsel unless the attorney for the debtor fails to respond within a reasonable time to a communication from a debt collector. I find that many debt collectors violate this provision, permitting a claim for \$1,000 in statutory damages.

### **8. Inappropriately contacting a third party**

Debt collectors are allowed to contact third parties to obtain location information, but they cannot disclose that debt is involved or even the name of their employer unless asked. 15 U.S.C. § 1692b(1) and (2). Calling friends and family of a debtor and discussing without solicitation the debt at issue is a clear violation of this provision.

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### **9. Leaving message for debtor without disclosing that the call is from a debt collector**

Section 1692e(11) requires debt collectors to identify themselves as debt collectors whenever they call a debtor. If they leave a message on the debtor's telephone without this disclosure, this provision is violated. *Foti v. NCO Financial Systems, Inc.*, 424 F.Supp.2d 643 (S.D.N.Y. 2006). The problem for debt collectors is that if they call a home where family members other than the debtor's spouse or children live, leaving this message could violate the law against third party contact. Despite the heavy risk, debt collectors continue to leave these messages.

### **10. Collecting debts against the wrong person**

Given the prevalence of identity theft and a number of prevalent last names, debt collectors often pursue the wrong parties. If your client receives a letter with a Section 1692g notice and she has no idea what this letter is about, you should urge your client to dispute the debt and to state specifically that it is not her debt. If your client knows the claim arises out of identity theft, that should be stated in the dispute letter as well. If the debt collector continues to pursue an individual after being informed that it is dunning the wrong person, you can allege that the debt collector has violated 15 U.S.C. § 1692e(2)(A), because it has misrepresented the character and legal status of the debt. By sending a dispute letter and awaiting further collection effort before raising the claim, you also avoid much of the risk of a successful bona fide error defense.

## **C. Conclusion**

My first six years of practice (1979-1985) was spent working in two legal services

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programs in Beaumont, Jasper, Nacogdoches, Tyler and Houston. I remember practicing in small towns across East Texas and discovering consumer law to be my professional passion. During those early years of my career, I benefitted from the opportunity of frequent trial experience as well as mentoring by more experienced counsel, such as Brenda Willett. I know that I would have liked more contact with private attorneys in the field that I was adopting as my specialty, so that I could have learned even more about the in's and out's of consumer law. Given that understanding, I am happy to respond to inquiries about consumer law matters, including fair debt collection issues. Feel free to call or e-mail me if I could help.