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3rd Circ. FDCPA Opinion A Rude Awakening For Debt Buyers

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Purchasers of delinquent debt who slept more soundly after the U.S. Supreme Court's decision in Henson v. Santander Consumer USA Inc. had a rude awakening in February, when the U.S. Court of Appeals for the Third Circuit held that debt buyers may nonetheless be subject to the Fair Debt Collection Practices Act. In Barbato v. Greystone Alliance LLC, the Third Circuit sidestepped the Supreme Court's 2017 holding in Henson and found that a purchaser of defaulted debt qualified as a debt collector subject to the act.

The defendant in Barbato, Crown Asset Management, purchased defaulted debt and outsourced the collection function to a third party.[1] Crown was sued for allegedly violating the FDCPA, and the U.S. District Court for the Middle District of Pennsylvania denied Crown's motion for summary judgment.[2] In doing so, the district court concluded that Crown was "acting as [a] debt collector" because it acquired the plaintiff's debt while it was in default, and because the summary judgment record supported that Crown's "principal purpose" was debt collection.[3]

On interlocutory appeal, the Third Circuit considered whether Crown, as an entity that purchased charged-off receivables and outsourced the actual collection activity, was subject to the FDCPA. In analyzing the issue, the court explained that the FDCPA's definition of the term "debt collector" has two prongs, and if an entity satisfies either of them, it is covered by the act.[4] Under the "principal purpose" prong, a debt collector includes any person who "uses any instrumentality of interstate commerce or the mails in any business the principal purpose of is the collection of any debts."[5] Under the "regularly collects" prong, a debt collector includes any person who "regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another."[6]

Crown argued (among other things) that under the Supreme Court's decision in Henson, the act did not apply to it because Crown owned the debts and thus did not regularly seek to collect debts owed to another.[7] In response to this argument, the Third Circuit explained that while Henson clarified the scope of the "regularly collects" prong of the definition and found that it did not cover purchasers of debt, the Supreme Court "went out of its way in Henson to say that it was not opining on whether debt buyers could also qualify as debt collectors under [the principal purpose prong]."[8] The Third Circuit

stated that Henson held that debt buyers were not "debt collectors" for purposes of the "regularly collects" prong of the definition, but they could nevertheless qualify under the "principal purpose" prong.

Applying the principal purpose prong to Crown, the Third Circuit found that the company fit squarely within the statutory definition because "Crown's only business is the purchasing of debts for the purpose of collecting on those debts [ ]."[9] The court went on to reject Crown's argument that Congress did not intend the FDCPA to apply to a passive debt owner that outsources the actual collection. The court reasoned that unlike a traditional creditor that is incentivized to "cultivate good will among its customers and for which debt collection is one of perhaps many parts of its business," Crown's only need for consumers is to make them pay their debts.[10]

According to the court, this makes Crown more like the "repo man" the FDCPA was intended to cover than a first-party creditor. It also gives Crown a good reason to outsource the collection function to repo man-like service providers.[11] And because the text of the principal purpose definition refers to "any business the principal purpose of which is the collection of any debts," regardless of whether it delegates the collection function, the Third Circuit held that Crown acted as a "debt collector" even though it contracted out collection activities to third-party collection agencies and attorneys.[12]

Although several federal appellate courts have cited to Henson in the nearly two years since it was decided, the Third Circuit's decision provides the most in-depth analysis of whether Henson completely excludes debt buyers from coverage under the FDCPA. The Fifth, Sixth, Seventh and D.C. Circuits have also cited to Henson, but they have not provided detailed discussions about the reach of the decision.

For instance, the Fifth Circuit has couched Henson as only applying to the "regularly collects" definition, in a manner similar to the Third Circuit, leaving open the possibility that debt buyers may be subject to the FDCPA under the "principal purpose" alternative.[13] The Sixth Circuit, citing to Henson, found that a bank that purchased a mortgage loan from the originating lender was not a debt collector, regardless of whether the loan was in default at the time of purchase, because the bank was "attempting to collect its own debt."[14] However, the court did not discuss the "principal purpose" prong in the context of the bank, so it is not clear whether its decision would have differed if it were considering an institution that focused on debt collection.

In Schlaf v. Safeguard Property LLC, the U.S. Court of Appeals for the Seventh Circuit stated that "[t]he Supreme Court has clarified recently that even parties who 'regularly purchase debts originated by someone else and then seek to collect those debts for their own account' are not debt collectors under the FDCPA because they are not collecting debts owed another."[15]

However, the court in Schlaf also referenced the "principal purpose" prong of the debt collector definition, raising the question of whether it views Henson as excluding all debt purchasers, or only those being considered under the "regularly collects" prong. [16] Finally, the U.S. Court of Appeals for the D.C. Circuit in Bank of New York Mellon Trust Co. N.A. v. Henderson cited to Henson in support of the view that "an entity collecting a debt for its own account is not a debt collector under the FDCPA," but it also noted that there was "no evidence to indicate that the Bank's 'principal' business is debt collection."[17]

Perhaps because the Third Circuit was ruling on a certified question of whether Henson precluded debt buyers from being subject to the FDCPA, Barbato contains a much more detailed examination of the text of the FDCPA and Henson than other federal appellate decisions applying Henson. Because of this, other

federal courts may look to Barbato as the leading analysis of whether debt purchasers are subject to the FDCPA, and follow the Third Circuit's lead in sidestepping Henson.

In light of the Barbato decision, debt purchasers may need to wait until the Supreme Court weighs in again to finally settle whether they are subject to the FDCPA. Until then, purchasers of debt in the Third Circuit whose principal purpose is debt collection might want to consider reviewing their practices to determine whether they are in compliance with the FDCPA.

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[1] Barbato v. Greystone Alliance, LLC, 2019 WL 847920, at *1 (3d Cir. Feb. 22, 2019).

[2] Id. at *2.

[3] Id.

[4] Id. at *4.

[5] 15 U.S.C. § 1692a(6).

[6] Id.

[7] Barbato, 2019 WL 847920 at *5.

[8] Id.

[9] Id. at *7.

[10] Id.

[11] Id.

[12] Id. at *6.

[13] Infante v. Law Office of Joseph Onwuteaka, P.C., 735 Fed. Appx. 839 (5th Cir. 2018).

[14] Garner v. Select Portfolio Servicing, Inc., 2017 WL 8294293, at *3 (6th Cir. Oct. 27, 2017).

[15] Schlaf v. Safeguard Property, LLC, 899 F.3d 459, 466 (7th Cir. 2018).

[16] Id. ("Creditors are therefore not subject to the FDCPA as long as they are collecting their own debt in their own name *and their 'principal purpose' as an entity is not debt collection."* (emphasis added)).

[17] Bank of New York Mellon Trust Co. N.A. v. Henderson, 862 F.3d 29, 34 (D.C. Cir. 2017).