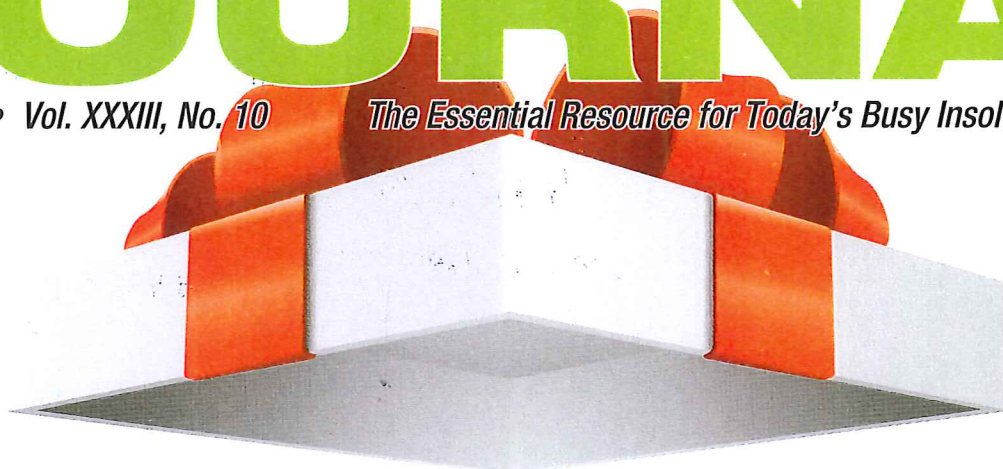


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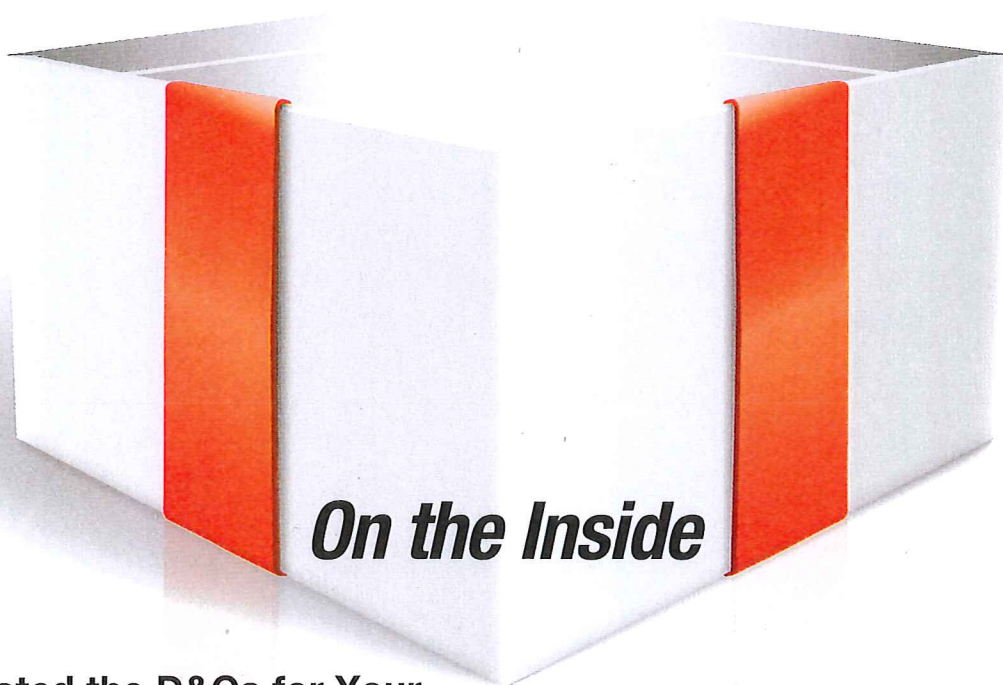
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The Essential Resource for Today's Busy Insolvency Professional



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Crawford Surprises: Stale Debt, FDCPA and Proofs of Claim

There is a question whether filing a proof of claim regarding a debt for which the statute of limitations has expired (referred to as “stale debt”) constitutes a violation of the Fair Debt Collection Practices Act (FDCPA).¹ The short answer is that despite the July 2014 holding from the Eleventh Circuit Court of Appeals in *Crawford v. LVNV Funding LLC*, the great weight of authority holds that it is not a violation of the FDCPA to file a proof of claim concerning otherwise-stale debt.

ties’ navigating disparate legal actions in various tribunals and independent-collection activities outside of bankruptcy.

Bankruptcy’s proof-of-claim filing, documentation and objection procedures are governed by Fed. R. Bank. P. 3001-3008. From a conceptual perspective, unlike a collection lawsuit filed against a debtor, a proof of claim is filed against the debtor’s bankruptcy estate. Under the Bankruptcy Code, a “claim” is broader than a “debt” and is defined as the following:

FDCPA vs. Bankruptcy

The FDCPA typically governs non-court-supervised communications between an unrepresented debtor and a debt collector. The FDCPA applies only to debt collectors of consumer debt as statutorily defined therein,² and it protects consumers from unfair, abusive or deceptive practices of debt collectors.³ For example, the FDCPA precludes a debt collector from threatening to “take any action that cannot be legally taken or that is not intended to be taken.”⁴ Courts interpreting the FDCPA have prohibited a debt collector from threatening to file or filing a lawsuit on stale debts because it creates a false and misleading impression regarding the legal status of the debt.⁵

However, the FDCPA is not interpreted to expressly prohibit all collection activities concerning stale debt because the expiration of the statute of limitations does not normally extinguish the debt,⁶ and the creditor may still attempt non-lawsuit collections. In the event of a violation, the FDCPA provides a private cause of action and relief in the form of damages, which include actual and statutory damages and attorneys’ fees.⁷ Notably, the FDCPA does not apply to creditors collecting their own debts, nor to debt collectors collecting debts outside of the FDCPA’s definition.

In bankruptcy, all creditor collection activities must cease due to the automatic stay when a petition is filed.⁸ All creditors participate in a global proceeding, which includes a court-supervised claim submission and dispute process, as opposed to par-

(A) Right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or

(B) Right to an equitable remedy for breach of performance if such breach gives rise to a right of payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured or unsecured.⁹

A debt is restricted to “liability on a claim.”¹⁰ Therefore, claim and debt are two distinct concepts in bankruptcy. Pursuant to Fed. R. Civ. P. 8(c), the running of a statute of limitations is an affirmative defense against the enforcement of a debt (*i.e.*, liability on a claim), which is waived if not raised. Liability on the debt may not survive the expiration of the statute of limitations, but the claim itself (*e.g.*, the right to payment) is not extinguished when the statute of limitations expires. Because a creditor files a proof of *claim* — not a proof of *debt* — in order to share in the distribution from the bankruptcy estate, filing a claim on which the statute of limitations has expired is not an improper act under the Bankruptcy Code.

Extensive informational support is required as part of the filing of a proof of claim. Under no circumstance may a proof of claim, which is filed under penalty of perjury, be false or fraudulent. The remedy for presenting a fraudulent proof of claim includes subjecting the filer to criminal and civil penalties of up \$500,000, imprisonment for up to five years, or both.¹¹



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1 The Fair Debt Collection Practices Act is codified at 15 U.S.C. §§ 1692-1692p (2006).

2 15 U.S.C. § 1692.

3 15 U.S.C. § 1692f.

4 15 U.S.C. § 1692e(5).

5 15 U.S.C. § 1692e(2)(A).

6 *Delgado v. Capital Mgmt. Servs. LP*, No. 4:12-cv-4057-SLD-JAG, 2013 U.S. Dist. LEXIS 40796, at *10 (C.D. Ill. Mar. 22, 2013).

7 15 U.S.C. § 1692k.

8 11 U.S.C. § 362.

9 11 U.S.C. § 101(5).

10 11 U.S.C. § 101(12) (emphasis added).

11 See, e.g., Official Form 10. See also 18 U.S.C. §§ 152, 3571.

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Code to Code: Crawford Surprises: Stale Debt, FDCPA and Proofs of Claim

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Crawford: Background¹²

The debtor, Stanley Crawford, owed \$2,037.99 to a furniture company, which was charged off in 1999. In September 2001, the debt was acquired by LVNV Funding LLC. The last transaction on the account occurred on Oct. 26, 2001; the state law three-year statute of limitations applicable to the debt expired in October 2004.

On Feb. 2, 2008, Crawford filed for chapter 13. LVNV filed a proof of claim, even though the statute of limitations expired almost four years earlier. The chapter 13 trustee paid LVNV on its claim from wages committed by Crawford in his payment plan.

In May 2012, Crawford objected to LVNV's claim, asserting that the debt was unenforceable. He also filed an adversary proceeding against LVNV alleging that its filing of a proof of claim for a debt on which the statute of limitations had run violated the FDCPA.

Bankruptcy and District Court Opinions

The bankruptcy court dismissed Crawford's adversary proceeding, noting that the "filing of a claim in the bankruptcy court, even one barred by the statute of limitations, does not constitute a violation of the Fair Debt Collection Practices Act."¹³ On appeal to the district court, the debtor conceded that he could not win his appeal "without a change in the law."¹⁴ Indeed, the district court observed that the debtor was fighting an "uphill battle" and that the "elephantine body of persuasive authority" weighed against his position.¹⁵ The district court also remarked that, notably, the debtor had not alleged any conduct that amounted to an FDCPA violation; namely, he had never been threatened, tricked, lied to or deceived — in fact, no communication with the debtor whatsoever had occurred.¹⁶

The district court held that the filing of a proof of claim is not the equivalent of collecting a debt against a consumer debtor because it is simply "a request to participate in the distribution of the bankruptcy estate under court control."¹⁷ The district court further held that the FDCPA was never intended to preclude all efforts to collect debt — just those that were unfair, abusive or deceptive.¹⁸ The district court also noted a pragmatic distinction; namely, that the "structured environment of the bankruptcy court" protects even the least-sophisticated consumers from the abusive conduct of debt collectors and from the payment of invalid debt.¹⁹ For these reasons, the district court agreed with the bankruptcy court's hold-

ing that the filing a proof of claim on stale debt does not violate the FDCPA.²⁰ In May 2013, Crawford appealed the affirmance of the dismissal of his adversary proceeding to the Eleventh Circuit Court of Appeals.

At first blush, one might merely assume that the filing of a proof of claim on stale debt is impermissible.... However, Crawford suggests that chapter 13 trustees have a duty to root out and object to claims filed for out-of-statute debts.

Eleventh Circuit Opinion

Hon. Richard W. Goldberg of the U.S. Court of International Trade, sitting by designation, delivered the opinion and quickly noted in its very first paragraph that "a deluge has swept through the U.S. Bankruptcy Courts of late."²¹ This deluge consists of "consumer debt buyers — armed with hundreds of delinquent accounts purchased from creditors ... filing proofs of claim on debts deemed unenforceable under state statutes of limitations."²² Noting the "broad" language of the FDCPA, existing precedent and the record, the Eleventh Circuit reversed the bankruptcy and district courts and not only overturned the dismissal of Crawford's adversary proceeding, but also held that a debt collector's filing of a proof of claim on an out-of-statute debt violates the FDCPA.²³

The Eleventh Circuit noted that Congress passed the FDCPA in 1977 to protect consumers against the use of "abusive, deceptive, and unfair debt-collection practices by many debt collectors."²⁴ Congress surmised that the existing law was "inadequate" to protect consumers.²⁵ As a result of the FDCPA, consumers had a new private right of action rendering debt collectors liable for actual damages, statutory damages and reasonable attorneys' fees where a violation of the FDCPA was demonstrated.²⁶

According to the Eleventh Circuit, the filing of proofs of claim for stale debt in bankruptcy is facilitated by § 502 of the Bankruptcy Code and Fed. R. Bank. P. 3001(f) because a proof of claim is automatically allowed, and will be included in any distribution from the estate, unless an objection is filed.²⁷ The Eleventh Circuit accepted

12 Summary of background facts taken from *Crawford v. LVNV Funding LLC*, No. 13-12389, 2014 U.S. App. LEXIS 13221, at **2-3 (11th Cir. July 10, 2014). The other defendants in the adversary proceeding included the company that prepared and filed the proof of claim on LVNV's behalf and the company that acquired the debt at a later date from LVNV.

13 *Crawford v. LVNV Funding LLC*, NO. 2:12-CV-701-WKW [WO], 2013 U.S. Dist. LEXIS 66169, at *4 (M.D. Ala. May 9, 2013) (quoting from the bankruptcy court's earlier decisions in "No. 2:12-CV-701-WKW, Doc. #2-7, at 1; No. 2:12-CV-729-WKW, Doc. #2-17, at 1").

14 *Id.* at *4 (M.D. Ala. May 9, 2013).

15 *Id.*

16 *Id.* at *5.

17 *Id.* (quoting from *In re McMillen*, 440 B.R. 907, 912 (Bankr. N.D. Ga. 2010)).

18 *Id.* at *6.

19 *Id.* at **7-8.

20 *Id.* at *9.

21 *Crawford v. LVNV Funding LLC*, NO. 2:12-CV-701-WKW [WO], 2013 U.S. Dist. LEXIS 66169, at *1 (11th Cir. Ala. July 10, 2014).

22 *Id.*

23 *Id.* at *2.

24 *Id.* at *6 (quoting 15 U.S.C. § 1692a, *et. seq.*).

25 *Id.* at *4 (citing to *Jeter v. Credit Bureau Inc.*, 760 F.2d 1168, 1173 (11th Cir. 1985)).

26 *Id.* at *5.

27 *Id.* at **8-9.

Crawford's argument that a proof of claim filed by a creditor was analogous to the filing of a lawsuit by a debt collector.²⁸ The court noted that had Crawford not filed for bankruptcy protection and that had LVNV filed a state court lawsuit on the debt instead, the act of filing the lawsuit would have clearly violated the FDCPA (a point that LVNV conceded). The court further observed that the "distribution of funds to debt collectors with time-barred claims then necessarily reduces the payments to other legitimate creditors with enforceable claims."²⁹

The court rejected LVNV's argument that the filing of a proof of claim was not "a collection activity" aimed at Crawford.³⁰ The court opined that the filing of a proof of claim is "the first step in collecting a debt in bankruptcy and is, at the very least, an indirect means of collecting a debt."³¹ It also noted that stale debt creates problems of proof and misleads the debtor that the debt can be legally enforced.³²

The court remarked that the U.S. Supreme Court also considered the definition of "to collect a debt" and turned to the dictionary's definition: "To collect a debt or claim is to obtain payment or liquidation of it, either by personal solicitation or legal proceedings."³³ The court ultimately held that LVNV's filing of a proof of claim on stale debt violated the FDCPA because it sought payment of a debt through a legal proceed-

ing.³⁴ Consequently, the Eleventh Circuit reversed the bankruptcy and district courts.³⁵

Conclusion

At first blush, one might merely assume that the filing of a proof of claim on stale debt is impermissible. It *seems* like something that the courts would be inclined to police. However, *Crawford* suggests that chapter 13 trustees have a duty to root out and object to claims filed for out-of-statute debts.³⁶

From a conceptual standpoint, however, a distinction lies in the fact that the expiration of the statute of limitations only renders a creditor unable to resort to the courts to determine and enforce the debtor's liability on the claim. While a creditor violates the FDCPA if it knowingly files a collection lawsuit on a stale debt, the fact remains that the expiration of the statute of limitations does not extinguish the underlying right to payment.

Consequently, a debtor's bankruptcy filing may have the unintended effect of breathing new life into claims that would be considered stale due to the expiration of the statutes of limitations. While the Eleventh Circuit's opinion in *Crawford* seems to snuff out the viability of stale claims when they are filed in the bankruptcy context for "debt collectors," it is unknown whether other courts will follow suit.³⁷ **abi**

28 *Id.* at **14-17.

29 *Id.* at **14-15.

30 *Id.* at *15.

31 *Id.* at *17.

32 *Id.* at *14.

33 *Id.* at *16 (quoting from *Heintz v. Jenkins*, 514 U.S. 291, 294 (1995)).

34 *Id.* at **17-18.

35 *Id.* at *2.

36 *Id.* at **9-10, n.5 (suggesting that the trustee can and should object to improper or stale claims: "Here, however, it appears the trustee failed to fulfill its statutory duty to object to improper claims, specifically LVNV's stale claim.")

37 As of the publication of this article, a petition for rehearing or rehearing *en banc* has been filed but not yet decided.

Last in Line: Limits on Foreign Goods Sellers' § 503(b)(9) Priority Rights

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of "receipt" as used in the UCC, and that the terms should be interpreted identically.¹⁰ The court ruled that "received" means "having taken into physical possession" the goods and should be applied as a "federal definition" for purposes of interpreting § 503(b)(9).¹¹

Applying this definition of "received," the *Circuit City* court ruled that for purposes of determining when goods sold to the debtor on consignment are "received" under § 503(b)(9), the operative date is when the debtor physically received possession of the goods, not the subsequent date when the debtor sells the consigned goods to a customer and the title passes to the debtor and the debtor's customer pursuant to the terms of the consignment agreement.¹² In other words, the date when title and risk of loss passes to the buyer is irrelevant as to when goods are received for purposes of § 503(b)(9).

In *In re Momenta Inc.*, the U.S. Bankruptcy Court for the District of New Hampshire, agreeing with the *Circuit City* court's analysis, similarly applied the UCC's definition of

"receipt" to the term "received" contained in § 503(b)(9).¹³ The *Momenta* court then considered whether "received" could encompass a situation whereby goods were drop-shipped to the debtor's customer. The court explained that under the UCC, a seller may stop delivery of goods in transit until the buyer receives the goods.¹⁴ The UCC lists four events that terminate a seller's right to stop the delivery of goods;¹⁵ however, only one of these events requires the buyer to take physical possession of the goods.¹⁶ Accordingly, the court found that under the UCC — and by extension, § 503(b)(9) — a seller can stop delivery until the buyer receives the goods either by having physical or constructive possession (such as when the buyer's agent or a carrier acknowledges that it is holding the goods for the buyer).¹⁷ However, the court held that the seller was unable to prove that the debtor had even constructive possession of the goods, and therefore denied the creditor's motion for allowance of its § 503(b)(9) priority claim.¹⁸

10 *Id.* at 229.

11 *Id.* at 230. Utilizing similar arguments, the *Circuit City* court had previously ruled that the UCC's definition of "goods" should be applied in determining whether a creditor has a valid priority claim under § 503(b)(9). See *In re Circuit City Stores Inc.*, 416 B.R. 531, 537 (Bankr. E.D. Va. 2009). Other courts have similarly applied the UCC's definition of "goods" when adjudicating § 503(b)(9) claims. See *In re Plastech Engineered Prods. Inc.*, 397 B.R. 828, 836 (Bankr. E.D. Mich. 2008); *In re Pilgrim's Pride Corp.*, 421 B.R. 231, 237 (Bankr. N.D. Tex. 2009); *In re SemCrude LLP*, 416 B.R. 399, 405 (Bankr. D. Del. 2009).

12 See *Circuit City*, 432 B.R. at 230.

13 See *In re Momenta Inc.*, 455 B.R. 353, 358-59 (Bankr. D.N.H. 2011), *aff'd*, *Ningbo Chenglu Paper Prods. Manf. Co. Ltd. v. Momenta Inc.*, 2012 WL 3765171 (D.N.H. Aug. 29, 2012).

14 See *Momenta*, 455 B.R. at 359; see also U.C.C. § 2-705.

15 See *Momenta*, 455 B.R. at 359; see also U.C.C. § 2-702(2).

16 See *Momenta*, 455 B.R. at 360; see also U.C.C. § 2-705(2)(a).

17 See *Momenta*, 455 B.R. at 360; see also *In re Trico Steel Co. LLC*, 282 B.R. 318, 324 (Bankr. D. Del. 2002) (stating that "'delivery' of the goods, where risk of loss and transfer of title pass to the buyer, does not necessarily constitute 'receipt' of goods, which requires transfer of actual physical possession"), *aff'd*, 302 B.R. 489 (D. Del. 2003).

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