

U.S. Supreme Court Holds that Attorneys Engaged in Non-Judicial Foreclosures are not Subject to Full FDCPA

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On March 20, 2019, the U.S. Supreme Court issued its opinion in *Obduskey v. McCarthy & Holthus LLP*, holding that an attorney that engages in nothing more than non-judicial foreclosure is not a "debt collector" under the federal Fair Debt Collection Practices Act. The Court clarified that such attorneys would still be subject to 15 U.S.C. § 1692f(6), which prohibits certain unfair practices, including making false threats to repossess property.

The case began when Dennis Obduskey defaulted on his home mortgage loan. The holder of Obduskey's mortgage loan retained the law firm of McCarthy Holthus LLP to initiate a non-judicial foreclosure. The law firm sent Obduskey a letter notifying him of the foreclosure, stating the amount owed and the current creditor, and providing a mini-*Miranda* notice and a debt validation notice. The letter did not make any express demands for payment. Obduskey responded by disputing the debt. The law firm foreclosed without responding to Obduskey's dispute. Obduskey then sued the law firm, claiming that it violated the FDCPA by not handling his dispute properly.

The law firm moved to dismiss, arguing that it was not a "debt collector" under the FDCPA and, therefore, did not have to comply with the requirements in the FDCPA for responding to a debtor's dispute during the debt validation period. The trial court granted the law firm's motion, agreeing that it was not a "debt collector" for purposes of the FDCPA's debt validation notice and response requirements because it was only enforcing a security interest. Obduskey appealed, and the U.S. Court of Appeals for the Tenth Circuit affirmed. In doing so, the Tenth Circuit joined the Ninth Circuit in holding that the FDCPA does not apply to non-judicial foreclosures, but it split from the Fourth, Fifth, and Sixth Circuits, which have held that attorneys who foreclose mortgages non-judicially are debt collectors subject to the FDCPA. Obduskey petitioned for certiorari to the U.S. Supreme Court noting the circuit split, and the high court granted his petition in June of 2018 and heard oral argument in January of 2018.

The federal Circuits were split on the question of a specific but limited inclusion in the definition of "debt collector" in the FDCPA for persons engaged in a principal business of enforcing security interests. Specifically, under the FDCPA, those persons are considered "debt collectors" only for purposes of a single FDCPA limitation on conduct related to non-judicial enforcement of security interests (see 15 U.S.C.A. § 1692f(6)). The FDCPA

otherwise separately excludes from the definition of "debt collector" for purposes of the whole FDCPA a variety of entities, and those exclusions are far more commonly the subject of reported FDPCA cases. After the definition of "debt collector", there is no further mention in the FDPCA of persons whose sole perceived collection activity is the non-judicial enforcement of security interests, and there is relatively little reported case law on that inclusion.

During oral argument, the parties and the justices focused on several issues, including:

- the distinction, if any, between a repossession company that takes a vehicle in the dark of night without any communication with the debtor, and an attorney who communicates directly with a debtor in the context of foreclosing non-judicially;
- whether the "security interest enforcer" language in the FDCPA excludes a foreclosure attorney because the attorney is enforcing a security interest, or whether the language really only captures and brings within the definition of "debt collector," for purposes of one provision of the FDCPA, a subset of persons who enforce security interests against collateral but do not otherwise directly or indirectly engage with consumers; and
- federalism concerns, including the risk that holding that a foreclosure attorney is a "debt collector" could have the unintended consequence of the foreclosure attorney engaging in a practice required by state law but prohibited by the FDCPA.

The U.S. Solicitor General argued as *amicus curiae* in support of the law firm. A group of Democratic members of Congress, including Senator Elizabeth Warren, filed an *amicus* brief in support of Obduskey.

In its unanimous holding, the Court made clear that the FDCPA's exemption for security enforcers is limited to attorneys engaged in non-judicial foreclosure to the extent that the attorneys follow state-mandated procedure for non-judicial foreclosure. The Court left open the possibility that a foreclosure attorney that strays from state-required procedures could subject itself to more than just section 1692f(6) of the FDCPA, most significantly, the attorney could be subject to the highly technical debt validation procedures in section 1692g.

Further, the Court's holding probably does not give any regulatory relief to attorneys that attempt to collect deficiency balances. Generally, a foreclosure proceeding forecloses and extinguishes the creditor's lien. If the borrower still owes money after the foreclosure, that balance (the deficiency balance) is an unsecured, personal obligation of the consumer. As a result, a person attempting to collect a deficiency balance following a foreclosure is no longer simply enforcing a security interest, and is instead enforcing a personal, unsecured obligation of the consumer, not unlike a credit card or student loan debt. Because the Court's holding interprets an exemption from the FDCPA for a person engaged in a business "the principal purpose of which is the enforcement of security interests," the Court's holding likely will not extend to a foreclosure attorney who also attempts to collect an unsecured deficiency balance from the consumer.

Accordingly, if a foreclosure attorney's activities go beyond state-required procedures for effecting a non-judicial foreclosure (including, for example, pre- or post-foreclosure demands for payment), or if the foreclosure attorney attempts to collect a deficiency balance, the attorney may be subject to the full FDCPA notwithstanding the Supreme Court's holding.

Notwithstanding its relatively narrow scope, the case does bring some regulatory relief not only to vendors who foreclose non-judicially in the Fourth, Fifth, and Sixth Circuits (circuits that previously held that such attorneys were subject to the full FDCPA), but also to the creditors that retain those vendors. Specifically, the vendor oversight burden on creditors retaining attorneys to handle non-judicial foreclosures has eased some, as long as those attorneys' activities are limited to what state law requires to effect a non-judicial foreclosure, and do not include efforts to collect deficiency balances.

The Supreme Court has had a particularly active few years interpreting the FDCPA. In 2017, it decided cases concerning whether filing a proof of claim on a time-barred debt violates the statute, and whether the statute applies to creditors collecting debts that they own. The Court recently denied a petition for certiorari that asked it to address the scope of the dispute rights found among the debt validation provisions of the FDCPA.

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