CONSUMER FINANCIAL SERVICES LAW REPORT

FOCUSING ON SIGNIFICANT CASELAW AND EMERGING TRENDS

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FAIR DEBT

CONSUMER AGREEMENTS CONTROL VALIDITY OF DEBT COLLECTION FEES

If debt collectors want to add a percentage-based fee to their collection costs, the fee likely will need to be expressly authorized in the consumer agreement between the debtor and the original creditor. That's the apparent result of an 11th U.S. Circuit Court of Appeals opinion, which held in a case of first impression that a debt collector — by collecting a third of the principal balance of a debtor's account as a collection fee — violated the Fair Debt Collection Practices Act because it collected an amount not expressly authorized by the agreement creating the debt or permitted by law. *(Bradley v. Franklin Collection Serv., Inc.* No. 13-12276, 2014 WL 23738 (11th Cir. 01/02/14).)

"This is not to say that [the plaintiff] and [the medical service provider] could not have formed an agreement allowing for the collection of the percentage-based fee," the court wrote in a *per curiam* decision. "It is the nature of the agreement between [them], not simply the amount of the fee that is important here."

The case actually involved two debtors who incurred medical debts — Melvin Bradley at North Alabama Urology PC and Kevin Calma at the University of Alabama at Birmingham Health System West. When Bradley and Calma failed to pay their debts, Urology and UAB West referred the accounts to Franklin Collection Service Inc. As part of the referral, Urology and UAB West added a charge for collection fees to the debtors' accounts, according to the contracts that Bradley and Calma each had signed.

Specifically, the agreement Calma signed with UAB West stated, in relevant part:

> I agree that if this account is not paid when due, and the hospital should retain an attorney or collection agency for collection, I agree to pay all costs of collection including reasonable interest, reasonable attorney's fees (even if suit is filed) and reasonable collection agency fees.

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on Bradley's claim under 15 U.S.C. § 1692f of the FDCPA. However, it affirmed the district court on all other issues raised in the appeal.

COLLECTION 'FEE' DOESN'T EQUATE TO 'COST OF COLLECTION'

The FDCPA at § 1692f(1) prohibits unfair or unconscionable means of collection, specifically "collection of any amount (including any interest, fee, charge, or expense incidental to the principal obligation) unless such amount is expressly authorized by the agreement creating the debt or permitted by law." Bradley argued that the collection fee he paid violates § 1692f because it was really liquidated damages rather than the actual cost of collection. The appellate panel agreed.

Noting that the 11th Circuit has not previously addressed this issue, the panel relied on the 8th Circuit's reasoning in *Kojetin v. CU Recovery, Inc.*, 212 F.3d 1318 (8th Cir. 2000). The *Kojetin* court held that the debt collector violated the FDCPA when it charged the debtor a collection fee based on a percentage of the principal balance of the debt due rather than the actual cost of collection.

"That is what happened here," the 11th Circuit panel wrote. "When Bradley signed Urology's patient registration form, he only agreed to pay 'all costs of collection.'" That is, the court explained, Bradley agreed to pay the actual costs of collection. His contract with Urology did not require him to pay Franklin's 33-and-1/3 percent fee that was assessed *before* Franklin attempted to collect the balance due, and therefore bore no correlation to the actual cost of Franklin's collection effort.

"Urology and Franklin cannot alter Bradley's obligations by the terms of their subsequent agreement," the 11th Circuit said. "Because there was no express agreement between Urology and Bradley allowing for collection of the 33-and-1/3 percent fee, that fee violates the FDCPA."

On the other hand, the appellate panel pointed out that, in the agreement that Calma signed with UAB West, he agreed to pay "reasonable collection agency fees." That did not preclude the collection of percentage-based fees — a conclusion underscored by the fact that Calma declined to argue on appeal that the agreement that he had with UAB West did not cover Franklin's percentage-based collection fee. "Courts examining other contractual language have also suggested that a percentage-based fee can be appropriate if the contracting parties agreed to it," the 11th Circuit panel further explained. The panel pointed to the 7th Circuit's decision in Seeger v. AFNI, Inc., 548 F.3d 1107, 1110, 1113 (7th Cir.2008), which suggested that the following contractual provision may allow the imposition of a percentage-based collection fee when a delinquent account was referred to a third-party collection agency:

> You agree to reimburse us the fees of any collection agency, which may be based on a percentage at a maximum of 33 percent of the debt, and all costs and expenses, including reasonable attorneys' fees, we incur in such collection efforts.

"But, Bradley's contract with Urology was not like Calma's contract with UAB West or the contracts from these other cases," the appellate panel said. "Under the contract at issue here, Bradley agreed to pay the actual costs of collection; he did not agree to pay a percentage above the amount of his outstanding debt that was unrelated to the actual costs to collect that debt."

The 11th Circuit panel reversed the district court's decision granting summary judgment in favor of Franklin on Bradley's claim under § 1692f of the FDCPA. It also affirmed the district court's grant of summary judgment on the RICO claims, the remaining FDCPA claims, and state-law claims.

Aziz David Fawal, Katherine Taylor Powell, Butler Snow O'Mara Stevens & Cannada in Birmingham, Ala.; Darrell L. Cartwright of Birmingham; and Allan L. Armstrong, also of Birmingham, represented Bradley.

Rik S. Tozzi and Stephen J. Bumgarner of Burr & Forman in Birmingham, Ala., represented Franklin.

GUEST COMMENTARY

TAKING THE SIMPLE ROAD: HIGH COURT REJECTS 'CLAIM-BY-CLAIM' APPROACH

By Anthony Rollo, Michael Ferachi, and Kimberly Higginbotham

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the same group, writes for the blog, and is available at *khigginbotham@mcglinchey.com*.

"When judges must decide jurisdictional matters, simplicity is a virtue." The U.S. Supreme Court, in its unanimous decision last week in *Mississippi ex rel. Hood v. AU Optronics Corp.*, No. 12-1036 (U.S., 01/14/14), echoed its previous words in its landmark decision in *Standard Fire Ins. Co. v. Knowles*, 133 S. Ct. 1345 (2013). The similarities, however, end there.

Upon granting *certiorari*, the Court evaluated the 5th U.S. Circuit Court of Appeal's "claim-by-claim" approach for ascertaining the real party in interest in a state court attorney general lawsuit for purposes of determining whether the case is removable, pursuant to the provisions of the Class Action Fairness Act. The "claim-by-claim" approach supports removal, finding that attorney general class actions are really to recover damages for the individuals joined, who purportedly are the real parties in interest for the non-enforcement-related claims in the suits.

Despite its previous expansive interpretation of CAFA in the *Standard Fire* decision, the Court took a narrower approach in *Hood*. The Court used the restrictive language of CAFA's mass action provisions to reject the "claim-by-claim" approach and hold that, because the state of Mississippi through its attorney general was the only named plaintiff, the suit was not a CAFA mass action.

This article discusses the *Hood* decision, its contrasts with the *Standard Fire* decision, and the impact of the *Hood* decision on the future of class action litigation. *Parens patriae* suit removable as mass action or not?

Mississippi, through its attorney general, sued manufacturers and distributors of liquid-crystal display panels in state court, claiming that the manufacturers had engaged in a conspiracy to fix prices for LCD panels and that their conduct artificially inflated prices, harming the consumers who were forced to pay higher prices. The defendants removed the case from state to federal court, arguing that the case was removable under CAFA as either a class action or a mass action.

The district court ruled that the suit did not qualify as a class action, because it was "not brought pursuant to Federal Rule of Civil Procedure 23 or a 'similar State statute or rule of judicial procedure.'" The district court instead found that the suit met the requirements of a mass action, which is a "civil action ... in which monetary relief claims of 100 or more persons are proposed to be tried jointly on the ground that the plaintiffs' claims involve common questions of law or fact."

The district court, nevertheless, remanded the suit because it fell within CAFA's general public exception, whereby a suit is not a mass action if all of the claims in the action are asserted on behalf of the general public (and not on behalf of individual claimants or members of a purported class) pursuant to a State statute specifically authorizing such action. 28 U.S.C. § 1332(d)(11)(B)(ii)(III).

The 5th Circuit concurred with the district court's ruling that the suit was not a class action but rather was a mass action. The 5th Circuit, however, concluded that the suit did not fall under the general public exception, because individual Mississippi consumers were the real parties in interest to the State's restitution claim and all of the claims, thus, were not asserted on behalf of the general public.

On Feb. 19, 2013, Mississippi petitioned for *certiorari* to the Supreme Court to determine "[w]hether a state's *parens patriae* action is removable as a 'mass action' under the Class Action Fairness Act when the state is the sole plaintiff, the claims arise under state law, and the state attorney general possesses statutory and common-law authority to assert all claims in the complaint."

On Jan. 14, 2014, the Court unanimously struck down the "claim-by-claim" approach and held that "[b]ecause Mississippi is the only named plaintiff, this suit does not constitute a mass action under CAFA."

THE COURT'S REASONS WHY

The Court summarized its reasons for ruling as follows. CAFA's "100 or more persons" phrase in the mass action provisions did not encompass unnamed persons who were real parties in interest to claims brought by named plaintiffs.

"Congress chose not to use the phrase 'named or unnamed' in CAFA's mass action provision, a decision we understand to be intentional," the Court wrote. In deliberately excluding unnamed persons from the mass action definition, Congress clearly did not want the provision's numerosity requirement to be satisfied through counting unnamed individuals who possess an interest in the suit.

The mass action provision's "100 or more persons" are not unspecified individuals who have no actual participation in the suit. Instead, these are the "plaintiffs" who are proposing to join their claims in a single trial. Congress made this understanding evident first in using the words *persons* and *plaintiffs* the same way they are used in Federal Rule of Civil Procedure 20, which refers to "persons" as individuals who are proposing to join as "plaintiffs" in a single action.

Second, when attempting to meet CAFA's requirement that the claims of the 100 or more persons be proposed for joint trial on the ground of common

questions of law or fact, the Court found that it would be "difficult to imagine how the claims of one set of unnamed individuals could be proposed for joint trial on the ground that the claims of some completely different group of named plaintiffs share common questions. The better understanding is that Congress meant for the '100 or more persons' and the proposed 'plaintiffs' to be one and the same." *Id.*, at *6.

The Court outlined that, using *plaintiffs* in reference to unnamed parties would have to be applied consistently in CAFA's mass action provisions, which are limited to those plaintiffs whose claims in a mass action satisfy the jurisdictional amount requirement of $75,000. The Court explained that stretching the term *plaintiffs* to include all unnamed individuals with an interest in the suit would create an "administrative nightmare that Congress could not possibly have intended," in which district courts would have to engage in "unwieldy inquiries" to identify hundreds (or in this case, hundreds of thousands) of unnamed parties whose claims are less than $75,000 and then to decide how to dispose of their claims.

The Court went on to note that statutory context further reinforces its reading of CAFA's mass action provision. First, the provision of CAFA governing transfer motions confirms that the term *plaintiffs* refers to actual named parties as opposed to unnamed real parties in interest. CAFA provides that once removal occurs, a case shall not be transferred to another court "unless a majority of the plaintiffs in the action request transfer." 28 U.S.C. § 1332(d)(11)(C)(i). The Court found that including unnamed parties in the definition of *plaintiffs* would make it "surpassingly difficult for a court to decide in a case like this one whether an action may be transferred."

Moreover, the Court referenced the mass action provision as a "backstop to ensure that CAFA's relaxed jurisdictional rules for class actions cannot be evaded by a suit that names a host of plaintiffs rather than using the class device." The Court found that "if Congress had wanted representative actions brought by States as sole plaintiffs to be removable under CAFA on the theory that they are in substance no different from class actions, it would have done so through the class action provision, not the one governing mass actions."

CONSIDERING THE 'CLAIM-BY-CLAIM' APPROACH

In addressing the propriety of the "claim-by-claim" approach, the Court acknowledged that it has interpreted the diversity jurisdiction statute to require courts in certain contexts to look behind the pleadings to ensure that parties are not improperly creating or destroying diversity jurisdiction. However, Congress did not intend this background inquiry to apply to the mass action provision.

First, the Court said, a background inquiry has never been applied in a similar manner to "count up additional unnamed parties in order to satisfy the mass action provision's numerosity requirement." Second, Congress repeatedly used the word *plaintiffs* to describe the 100 or more persons whose claims must be proposed for a joint trial.

"That word refers to actual, named parties — a concept inherently at odds with the background inquiry into unnamed real parties in interest, who by definition are never plaintiffs," the Court emphasized. "Congress, thus, clearly displaced a background real-party-in-interest inquiry."

Therefore, utilizing a narrow interpretation of CAFA to strike down the "claim-by-claim" approach as contrasted with expansive interpretation of CAFA employed in *Knowles*, the Supreme Court reversed the judgment of the Firth Circuit and remanded the case for further proceedings.

HOOD EXALTS FORM OVER SUBSTANCE

In rendering its decision, the Court referenced its earlier unanimous opinion in *Standard Fire* and noted that "[w]hen judges must decide jurisdictional matters, simplicity is a virtue." *Hood*'s narrow, simplistic interpretation was necessitated by the strict language of CAFA's mass action provision.

The unambiguous language did not provide for an opportunity to look into the substance of CAFA's legislative history where an amendment was proposed "clarifying that State attorneys general should be exempt from S. 5 [the proposed bill to amend procedures that apply to consideration of interstate class actions to assure fairer outcomes for class members and defendants, and for other purposes] and be allowed to pursue their individual State's interests as determined by themselves and not by the Federal Government." (151 Cong. Rec. S1157-02 (daily ed. Feb. 9, 2005).) Although Congress rejected the proposed amendment, legislative history could not be considered in rendering the *Hood* decision. (151 Cong. Rec. S1163-64 (daily ed. Feb. 9, 2005).)

Despite promoting the virtues of simplicity, the *Hood* decision is in sharp contrast to *Standard Fire* where the Court took an expansive view of CAFA that looked at substance over form to find jurisdiction. In particular, the Supreme Court in *Standard Fire* stated that treating a nonbinding stipulation as a binding stipulation would "exalt form over substance, and run directly counter to CAFA's primary objective: ensuring federal court consideration of interstate cases of national importance."

The "claim-by-claim" approach sought substance over form by making an assessment of what was really being sought and who the real party in interest was and appeared consistent with the *Standard Fire* warning against exalting form over substance. However, in striking down the "claim-by-claim" approach, *Hood* prohibited a background inquiry for purposes of assessing removal jurisdiction and, ultimately, appears to have been decided on form over substance.

EXPECTATIONS FOR CLASS-ACTION LITIGATION

In the wake of the *Hood* decision, fewer hurdles will exist for bringing a *parens patriae* action and avoiding removal.

Therefore, an increase in partnered *parens patriae* actions where states are represented by both state attorneys general and plaintiffs' attorneys may be expected.

Considering the sharp contrast between its interpretations of CAFA in *Standard Fire* and *Hood*, it is less predictable where the Court will go from here.

CAFA CLASSROOM

KEEPING AN EYE ON CLASS ACTION FAIRNESS ACT DEVELOPMENTS

Local-controversy exception. *Walters v. Flag Credit Union, et al.*, No. 4:13cv241, 2014 WL 129055 (N.D. Fla. 01/13/14). The U.S. District Court, Northern District of Florida has decided to retain jurisdiction in an auto-loan insurance case, concluding that the case should not be remanded to state court, based on the Class Action Fairness Act's local-controversy exception. A consumer arranged a loan with Flag Credit Union to purchase a vehicle and also bought "guaranteed asset protection" from CUMIS Insurance Society Inc. — a product that purportedly would pay off the loan if the vehicle was damaged or destroyed and other insurance was insufficient to cover the unpaid balance. The borrower sued Flag and CUMIS in Florida state court for various injuries, seeking to represent three classes, all comprised of similarly situated Florida consumers. CUMIS removed the case to federal court and the borrower challenged, based on CAFA's local-controversy exception codified at 28 U.S.C. § 1332(d)(4).

Here, the court found that the borrower easily met four of the requirements for exception — Flag is a citizen of Florida; the borrower seeks significant relief from Flag on behalf of the class; principal injuries resulting from the alleged conduct of both Flag and CUMIS occurred in Florida; and during the three years before he filed his first class-action allegations in this case, no other class action involving these facts had been filed against Flag or CUMIS. However, the borrower/plaintiff fell short on the other two requirements. First of all, although the borrower said that he could amend his complaint to become compliant with the local-controversy exception provision at § 1332(d)(4)(A)(i)(I) that "greater than two-thirds of the members of all proposed plaintiff classes in the aggregate are citizens of" Florida, the court concluded that the exception still would not apply. That's because he did not meet another CAFA requirement at § 1332(d)(4)(A)(i)(II)(aa) to qualify for the exception — *i.e.*, that class members seek "significant relief" from Flag.

"Here the class members seek to recover all the fees paid for guaranteed asset protection contracts obtained from Flag or CUMIS," wrote Judge Robert L. Hinkle. "The best information in the record is that CUMIS issued 128,012 GAP contracts in Florida and that Flag sold 852 of them. The fees on CUMIS' contracts totaled $10,329,819. The fees on the contracts placed by Flag totaled $144,503. In absolute terms, $144,503 may be significant, but that amount is not significant in relative terms, when compared to $10.3 million. The class members also assert a claim for trebling, but they do so against both Flag and CUMIS. Trebling would not affect the relative significance of the claims. So the relief sought from Flag is not "significant" within the meaning of § 1332(d)(4)(A)(i)(II)(aa). The plaintiffs are not entitled to remand based on § 1332(d)(4)(A)."

The district court added that "the result is the same under § 1332(d)(4)(B). Under that section's plain language, the section applies only if two conditions are met. First, 'two-thirds or more of the members of all proposed plaintiff classes in the aggregate' must be citizens of the forum state," a condition that the plaintiff did not meet. "Second and more importantly," said Judge Hinkle, "the 'primary defendants' must be citizens of the forum state. This means *all* the primary defendants. CUMIS is plainly a primary defendant. And CUMIS is not a citizen of Florida."

Local-controversy exception. *Quicken Loans Inc. v. Alig, et al.*, Nos. 12-342, 13-1073, 13-1077, 2013 WL 6671618 (4th Cir. 12/19/14). The 4th U.S. Circuit Court of Appeals, in yet another local-controversy exception case, has vacated a district court's decision remanding the case to state court. The appellate court instead has remanded the case to the district court to determine whether the lender

