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ARTICLE: DEFENSE of Assigned Consumer Debts

**NAME:** By Clinton Rooney

**BIO:** Clinton Rooney
Attorney

Rooney & Lickel
1102 Cesar E. Chavez Parkway
San Diego, CA 92113
619.573.9547
rooneycdi@gmail.com

**LEXISNEXIS SUMMARY:**
... While original creditors file many collection suits, the easiest suits to defend, and thus the most fruitful to take on, are those filed by "debt buyers," who claim to be assignees of the original debts. ... At best, acceptance of an offer by use of the account should yield a verbal contract, with terms such as interest rate and fees unstated and thus determined by default under state law, which typically is far more consumer-friendly than the onerous terms in credit-card contracts. ... However, should a debt buyer be able to do so, we turn to affirmative defenses. ... For consumer-debt claims, certain states, including California, Delaware, and New Hampshire, have fairly progressive (i.e., short) statutes of limitations, barring suits after four years or less. ... Of course, the shorter the period in which the creditor or debt buyer may sue, the better for the consumer; thus your clients will be better off if tolling statutes do not apply. ... While many debt-collection suits are straightforward and clients have no defense, often the claim is time-barred or brought by a debt buyer who lacks standing or sufficient evidence to prove the claim.

**TEXT:**
[*542] Collection suits for consumer debts constitute a large portion of the civil calendar in most U.S. courts and, in view of current unemployment rates, are likely to continue to do so. In San Diego County, California, for example, the number of limited jurisdiction (under $ 25,000) collection cases more than doubled between 2005 and 2008, and as of the end of the 2008-2009 fiscal year, these cases are 75-80 percent of all civil filings other than restraining orders. n1 While a large and well-developed bar of collection firms files these cases, a relatively small bar of experienced counsel, many from the nonprofit sector, defends them. The need for an experienced defense bar for these often baseless, unenforceable, or inflated claims of debt is evident.

While original creditors file many collection suits, the easiest suits to defend, and thus the most fruitful to take on, are those filed by "debt buyers," who claim to be assignees of the original debts. I focus here on defenses against these debt-buyer suits, although many of the issues raised apply to collection suits by original creditors as well.

Because I practice in California and much debt defense is based on state law, some points I make may not apply in your state. However, most of the theories underlying collection suits and their defenses are based on common law and apply broadly.

I begin with the elements of collection causes of action and then with common affirmative defenses.

[*543] **Elements of Debt-Collection Causes of Action**

Most collection suits rely on either contract or common-counts theories or a hybrid of these in the form of an account stated; these theories are commonly used to assert liability for debts on credit-card accounts. n2 I discuss each theory after explaining standing, which is the common element to all three. Often challenging standing is the easiest way to dispose quickly of a meritless claim to an assigned debt.

Standing is the first element in any debt-buyer suit. Under basic common-law principles, a party must establish title to a debt in order to have standing to sue and prevail on that claim. n3 That a debt buyer must prove purchase of the debt in order to prevail on a claim may seem obvious, but the collection industry is typically so unaccustomed to having to prove its case, and so intent on spending nothing on litigation, that failure to produce sufficient evidence of ownership of the debt is common. For debts assigned more than once, debt buyers' problems are exacerbated, as they must prove a transaction to which they were not party and so must produce third-party witnesses.

Typically a debt buyer produces a one-paragraph document entitled something like "bill of sale," which occasionally refers to an earlier agreement. This bill of sale generally makes no mention of the alleged debtor or the account and instead refers to a separate section, exhibit, or attachment that is not supplied. At trial the bill of sale may be excluded as irrelevant on this basis alone since it has no tendency in reason to prove or disprove whether the original creditor sold or otherwise assigned the account. The debt buyer occasionally produces a single line of text and claims that it is the exhibit or attachment to which the bill of sale refers. The document is usually produced for purposes of litigation and is not a valid business record.

You can attack the bill of sale or similar document as irrelevant if, as is common, the document does not refer to the account or debtor alleged. If the debt buyer produces no other evidence of standing, you have likely already won your case.

If the debt was assigned more than once, the debt buyer is unlikely to produce a witness to the first step of the assignment. In this case the court may exclude, as hearsay and for lack of foundation, the bill of sale or other documents that the debt buyer offers as evidence of assignment. The debt buyer at times attempts to paper over this issue with an affidavit or declaration, often from another state. An affidavit that refers to an assignment but is not a foundation for a written agreement to sell the account (the bill of sale) may be excluded under the best-evidence or similar rule. n4

An affidavit that contains statements regarding a specific document may be subject to challenge as hearsay. Your state may allow exclusion on this basis if the affiant is not available for cross-examination at trial since admission of the affidavit would deprive your client of any meaningful opportunity to face accusers. n5 An affidavit or declaration may also be inadmissible as hearsay if it lacks certain required language, such as that it is sworn under penalty of perjury.

Standing, as a threshold issue, often determines the entire the case. While states have different mechanisms for disposing of baseless claims, in California the easiest approach is to raise the issue at the outset of trial, move to exclude as irrelevant or as hearsay any evidence of standing [*544] that the debt buyer offers, and then move for a nonsuit. At trial, many debt suits can be disposed of in this way in a matter of several minutes, saving your client the stress and risk of testimony.

A debt buyer who does prove standing must then prove the elements of at least one cause of action.

**Breach of Contract.** To prove breach of a written contract, the debt buyer must first prove that the contract exists. This is often where the claim fails since the debt buyer typically has only a form contract, which does not bear the consumer's signature or name. The consumer typically does not recall receiving a contract and likely did not receive one or received a contract different from the one on which the debt buyer relies.

Debt buyers often offer form contracts bearing the wrong year or the wrong creditor or offer two different contracts and claim that both are somehow the contract alleged. These can usually be disposed of at trial as hearsay, for lack of foundation, and as irrelevant.

To establish a contract's validity, the debt buyer must also prove that the consumer assented to the terms and received consideration. A common tactic of debt buyers is to introduce a signed application, which is usually merely an offer, and claim that the application establishes the consumer's assent to the terms of a nonexistent contract. Because courts are prone to accept this specious argument, at trial you must emphasize that the signed application is simply an offer, not a contract. The debt buyer must establish the contract itself in order to prevail on a claim of breach or, in the case of common-counts causes of action, to establish a right to charge interest or fees. The debt buyer may claim that *use* of the account constitutes acceptance of the offer. This is false, however, since the signed application typically contains no contract terms. At best, acceptance of an offer by use of the account should yield a verbal contract, with terms such as interest rate and fees unstated and thus determined by default under state law, which typically is far more consumer-friendly than the onerous terms in credit-card contracts.

Finally the debt buyer must prove that the consumer breached the contract by failing to repay the consideration received, and this the debt buyer is almost never able to do. When a consumer testifies at trial, the debt buyer may be able to extract an admission that the consumer received some consideration from the original creditor, but such an admission is insufficient to establish definite damages and does nothing to show that any consideration received was not repaid. The debt buyer, who lacks personal knowledge of the transaction, is forced to rely on the consumer's inexact recollection of events long past or on inadmissible hearsay from the original creditor.

Most debt buyers are unable to prove that a written contract exists or that the consumer assented to its terms or received unpaid consideration. Well-prepared defense counsel should prevail at trial under these circumstances.

**Open-Book Account.** Debt buyers' most common cause of action is the open-book account. Aside from account stated, which I discuss below, the elements of the other common-counts theories (e.g., goods, wares and merchandise, services rendered, or money lent) are nearly identical to the open-book-account cause of action, and so I do not take them up separately.

In California, under *Cowdery v. McChesney,* "[t]he only way an account can be proved ordinarily[] is by establishing by evidence the several items of the same ...." n6 Because the theory underlying common counts dates back at least to the late 1800s, this rule should be largely the same from state to state. The key to defending common counts, including an open-book account, is to force the debt buyer to prove the account's individual items.

[*545] The first step in forcing the debt buyer's hand is to request a complete list of the debits and credits, or charges and payments, composing the account alleged--known in California as a "bill of particulars." Not all states allow use of this mechanism, but all states should at least allow a list of the charges and payments on the account to be obtained through discovery. However you obtain it, the information you want is charges incurred and payments made.

Typically debt buyers are unable to produce a list of the charges. If the debt buyer is unable to produce a list of the charges, then proceed with a motion to compel or a similar discovery motion; you should be able to exclude the introduction of any evidence of any portion of a debt that is not supported by a corresponding charge, resulting in a partial or complete defense to all common counts except an account stated. In other words, if a debt buyer can produce only $ 200 in listed charges, but claims a debt of $ 2,000, you should be able to exclude any testimony or other evidence at trial that the debt buyer might seek to introduce to prove a debt of more than $ 200.

**Account Stated.** The second most common cause of action pleaded and by far the most dangerous for consumers, an account stated is a new contract, formed by the acknowledgment of a debt and a promise to pay. Debt buyers try to use this theory as an end run around their inability to prove assignment and individual charges.

The elements of an account stated in writing are a preexisting debt, a closed account with the parties agreeing on the balance due, and a written agreement to pay. n7 Unlike the other common counts, an account stated is not an account

at all but a new contract, formed by a promise to pay, with consideration being the exchange of an old debt for a new promise to pay.

The debt buyer first argues that the consumer, by failing to dispute a claim of a debt, implicitly assented to the terms of an account stated. Absent assignment of a debt, this argument has some validity. If an original creditor sends a bill to a consumer who does nothing, viewing this inaction as an admission of the debt claimed, subject to defenses of inadvertence, mistake, surprise, or excusable neglect, is not unreasonable.

However, when a debt buyer unknown to the consumer sends a letter claiming to be owed a debt, common sense tells us that this is different. The consumer likely does not even recognize the name on the envelope, may throw it away, and probably lacks sufficient knowledge to admit or deny the debt buyer's claims, making assent impossible. However, I know of no California case law explicitly stating this rule, and thus we are left with the common-law defenses of mistake, inadvertence, excusable neglect, and surprise.

The debt buyer claims to be either party to or the assignee of an account stated in writing. The debt buyer's claim that the account stated was in writing is important because, like any written contract, the debt buyer must produce it. If the debt buyer cannot do so, then, just like any other contract, the account stated would be subject to the statute of limitations for verbal contracts.

Pinning the debt buyer down on the identity of this writing is vital and key to winning this cause of action. The debt buyer first claims that every account statement ever sent to the consumer is an account stated. This is nonsense. First, an account stated requires a final balance struck, which requires a closed account. n8 Second, an account stated is a contract, which means it must have a single date of execution.

[*546] The debt buyer will almost certainly not produce a single document but instead will obfuscate and identify a single document that the debt buyer claims is the written account stated only after the threat of discovery motions.

Next the parties to the account stated must be identified. If the debt buyer claims that the account stated was with the original creditor, the debt buyer still must prove standing, the first line of defense discussed above. However, a debt buyer who claims to be a party to the account stated will claim no need to prove standing.

Even a debt buyer who is a party to the account stated and thus has standing, however, still must prove that an underlying debt, owed to the debt buyer, exists and was assigned to the debt buyer--this cannot be accomplished simply by printing a letter and sending it to the consumer. n9 Even if your state does not have a case in point, you should be able to rely on common-law principles: with no debt owed *to the debt buyer,* there cannot be consideration to form a contract. Unless the debt buyer proves that a debt exists *to the debt buyer,* and not simply to the putative original creditor, the debt buyer cannot form a new contract, in the form of an account stated, without giving consideration in the form of release of a preexisting debt.

Next examine the document that the debt buyer sent to the consumer. If it is the initial written communication from the debt buyer and advises the consumer of the right to request verification of the debt, the document may not be used as an account stated. Such a letter is called a "1692g notice," in reference to one of the few areas in which federal law applies to consumer-debt defense. The Fair Debt Collection Practices Act specifically prohibits the use of these letters as an admission of liability by failure to dispute; using the letters as an admission of liability is precisely what debt buyers attempt to do. n10 Because 1692g notices may not be used as admissions of liability, they are irrelevant to proving an account stated.

If the debt buyer produces a document that instead identifies the original creditor, aside from the assignment or standing defense, analyze this document to see if it reflects a closed or open account. Only a closed account can be an account stated, and so if the document reflects credit still available, or similar indicia of an open account, object to this document as irrelevant at trial and move to strike this cause of action. Also, if at trial the debt buyer attempts to introduce verbal testimony of a written account stated, object under your state's best-evidence or similar rule.

Account stated is a flexible and dangerous theory, and therefore forcing the debt buyer to specify which document is the account stated is vital. Once you do force the debt buyer to so specify, you will likely be able to exploit a weakness in

the document chosen by the debt buyer, whether that weakness be lack of standing (if the document names the original creditor), lack of consideration (if the document names the debt buyer), failure to state a final balance (if the document shows indicia of available credit or states a balance other than the balance alleged in the complaint), or relevance (if the document is a dunning letter covered by *15 U.S.C. § 1692g).*

Debt buyers are usually unable to prove standing and beyond that are likely not able to prove the other elements of their claims. However, should a debt buyer be able to do so, we turn to affirmative defenses.

**Affirmative Defenses**

A variety of affirmative defenses may apply to assigned consumer debt. I discuss four: statute of limitations, the language used to negotiate for credit, Fair Credit Billing Act disputes, and identity theft.

**Statute of Limitations.** For consumer-debt claims, certain states, including [*547] California, Delaware, and New Hampshire, have fairly progressive (i.e., short) statutes of limitations, barring suits after four years or less. Others, such as Missouri, allow debt buyers to sue more than a decade after the last transaction on the account. Thus the utility of a statute-of-limitations defense varies with your state's statutes. With that caveat, if you are dealing with an older, "stale" claim of a debt, which is not uncommon with an assigned debt, the statute-of-limitations defense is usually the only useful affirmative defense at your disposal.

*Domestic Statute of Limitations.* Written contracts may be subject to different statutes of limitations, depending on whether the document itself is simply a contract or is a negotiable instrument such as a promissory note.

*Foreign Statutes of Limitations.* If the contract at issue contains a choice-of-law clause specifying a foreign jurisdiction's law, such as Delaware (Chase Bank), Arizona (Bank of America), or South Dakota (Citibank), you may have a statute-of-limitations defense that is not available under your state's law. If your state does not honor these clauses, the analysis stops there. If your state does honor these clauses, the next question is whether your state will apply the foreign state's statute of limitations. Most states decide which portion of foreign laws to apply by distinguishing substantive law from procedural law. If your state considers foreign statutes of limitations procedural and so does not enforce them, your state's own statute of course applies.

California applies the "governing interest" test: due to a public policy against prosecuting stale claims, California enforces foreign statutes of limitations shorter than its own, but not longer. If this is the case in your state, contracts that contain choice-of-law clauses specifying states with short statutes of limitations, such as Delaware and New Hampshire, are a boon to your client. If, however, your state enforces foreign statutes of limitations of any length, your client faces a two-edged sword. Be sure to analyze the situation before bringing it up with the court or with opposing counsel.

*Domestic Tolling Statutes.* Several state statutes toll the statute of limitations while a party is not "present" in the state. Of course, the shorter the period in which the creditor or debt buyer may sue, the better for the consumer; thus your clients will be better off if tolling statutes do not apply. In *Bendix Autolite v. Midwesco Enterprises* the U.S. Supreme Court found an Ohio tolling statute to be unconstitutional as an undue burden on interstate commerce. n11

The Ninth Circuit first upheld California's tolling statute in 1990 in *Abramson v Brownstein;* the court found that the state's interest outweighed any burden on interstate commerce. n12 In 2001 the Ninth circuit again considered the issue in *Argonaut v. Halvanon.* After the district court applied the *Abramson* holding and refused to toll the statute, in 2001 the first appellate court to review this finding distinguished *Argonaut* from *Abramson* and found that the defendant was not subject to the personal jurisdiction of the courts during the period in question. n13 In 2002 a second appeals court overturned this ruling; the court held that California's long-arm statute did establish jurisdiction over the defendant, that under *Abramson* California's tolling statute was unconstitutional, and that the statute of limitations was not tolled. n14 The U.S. Supreme Court denied certiorari. The *Abramson* rule seems to be that California's tolling statute is unconstitutional providing that long-arm jurisdiction could have been established over the defendant during the statute of limitations, and this includes periods not just in other states but also abroad.

[*548] California state courts have been more reticent in overturning the state's tolling statute. n15 Nonetheless, the *Bendix* holding and logic are clear, and the Ninth Circuit has been willing to apply the ruling to strike down California's

state tolling statute. There is little reason to believe that the outcome would be significantly different in other circuits. Federal case law may be more favorable to consumers in using the commerce clause to reject state tolling statutes since this is an area where federal interest in facilitating interstate commerce conflicts with states' interest in prosecuting valid claims.

*Foreign Tolling Statutes.* Despite the *Bendix* and *Abramson* holdings, the application of foreign tolling statutes was a gray area in California until recently. While there was a clear line of cases making clear that California would enforce choice-of-law clauses, including foreign statutes of limitations longer than its own, no case held explicitly that California would not enforce foreign tolling statutes in this situation. n16

Whether California would enforce foreign tolling statutes comes into play regularly in cases involving credit-card debt. In Delaware, for example, the statute of limitations for breach of written contracts is three years. However, Delaware law also tolls that statute during absence from the state. Thus, if the debtor never lived in Delaware, the statute theoretically runs forever. This issue has now been resolved; a California court of appeal recently rejected enforcement of Delaware's tolling statute on the grounds that it rendered the statute of limitations illusory. n17

This logic should apply to any foreign tolling statute, but even if it does not, there is no reason to think that a foreign tolling statute is enforceable when a domestic tolling statute violates the commerce clause under *Bendix*--if a domestic statute is unconstitutional, so is a foreign statute. n18

*Cellphone Contracts.* Cellphone carriers are subject to the two-year federal statute of limitations contained in the Federal Communications Act. n19 This federal law preempts longer state statutes of limitations on this issue, one of the rare instances in which federal preemption actually favors the consumer instead of the creditor. n20 The debt buyer may attempt to argue state preemption, but I know of no case law that would support that position.

**Language Issues.** If your client speaks little English and did not negotiate for credit in English, you have a good argument that the client could not give meaningful consent to the contract's financial terms underlying the debt buyer's claim for interest and fees. And, if you can eliminate the right to collect exorbitant interest and fees under the form contracts commonly used for credit cards, you can likely eliminate most or all of the outstanding debt. The argument that consumers cannot consent to contractual terms that they cannot understand because they do not speak English is compelling, especially if the creditor knew the consumer did not speak English. In effect, the creditor had unclean hands. Your state may also require that if consumer-credit transactions are negotiated in a language other than English, the creditor must give a copy of the contract in that language; if so, the client may have a defense or a right to rescind the contract. n21

[*549] **Fair Credit Billing Act.** Under the federal Fair Credit Billing Act, part of the Truth in Lending Act, if a consumer disputes in writing an incorrect or unauthorized charge on an account statement, the creditor must investigate the dispute within sixty days and may not collect this portion of the debt pending the investigation. n22 A creditor who ignores the dispute effectively waives the right to collect the disputed portion of the debt (and any resulting interest). If you have the good fortune to have a client with this problem, you have at least a partial defense.

**Identity Theft.** If the underlying debt is partially or entirely the result of identity theft, your client has a defense to the portion of the charges that were unauthorized and to any resulting interest or fees. You may also have state-law remedies available. California, for example, allows individuals to sue affirmatively and seek injunctive relief in the form of a finding that the individual does not owe a debt--a useful tool to clear your client's credit report of false claims of a debt. n23

. . .

While many debt-collection suits are straightforward and clients have no defense, often the claim is time-barred or brought by a debt buyer who lacks standing or sufficient evidence to prove the claim. Given the overwhelming number of collection suits being filed, legal aid advocates must offer clients a competent defense to these often meritless suits.

**Legal Topics:**

For related research and practice materials, see the following legal topics:

Contracts LawDebtor & Creditor RelationsContracts LawDefensesStatutes of LimitationsGovernmentsLegislationStatutes of LimitationsTime Limitations

**FOOTNOTES:**

n1 Robert C. Longstreth (Superior Court Judge) & Cindy D. Davis (Commissioner), Superior Court of California, San Diego County, Presentation on Civil Collections: Mandatory Settlement Conference Program (Nov. 5, 2009). Superior court figures for limited jurisdiction collection cases filed in San Diego County were 14,886 in the 2005-2006 fiscal year, 18,530 in the 2006-2007 fiscal year, 26,037 in the 2007-2008 fiscal year, and 31,226 in the 2008-2009 fiscal year (*id.*).

n2 "Common counts" refers to a set of theories of liability for debts based on the keeping of book accounts or ledgers.

n3 In California see *Cockerell v. Title Insurance and Trust Company, 267 P.2d 16, 21 (Cal. 1954)* ("[t]he burden of proving an assignment falls upon the party asserting rights thereunder"); see also *Mission Valley East Incorporated v. County of Kern, 174 Cal. Rptr. 300, 305 (1981)* ("the assignment must describe the subject matter with sufficient particularity to identify the rights assigned"), and *Cobb v. San Francisco Residential Rent Stabilization and Arbitration Board, 119 Cal. Rptr. 2d 741, 745 (2002).*

n4 See, e.g., CAL. EVID. CODE § 1423 (West 2010).

n5 See, e.g., *CAL. CIV. PROC. CODE § 96* (West 2010).

n6 *Cowdery v. McChesney, 57 P. 221, 222 (Cal. 1899).*

n7 In California, under *Mercantile Trust Company v. Doe, 146 P. 692, 695 (Cal. 1914),* "to turn an account into an account stated, it must have been rendered with a view of ascertaining the balance and making a final adjudication of the matter involved in the account ...." Under *Mike Nelson Company v. Weston Hathaway, 2005 U.S. Dist. LEXIS 27377, at 8,* a claim of account stated has three elements: an underlying debt from one party to another, a balance struck, and a promise to pay.

n8 *Mercantile Trust, 146 P. 692.*

n9 In 1968 the California Supreme Court stated that "the rendering of an account, although not objected to, cannot create a liability where no liability existed before" (*Trafton v. Youngblood, 442 P.2d 648, 654 (Cal. 1968)).*

n10 Fair Debt Collection Practices Act, *15 U.S.C. § 1692g.*

n11 *Bendix Autolite v. Midwesco Enterprises, 486 U.S. 888 (1988).*

n12 *Abramson v. Brownstein, 897 F.2d 389 (9th Cir. 1990).*

n13 *Argonaut Insurance Company v. Halvanon Insurance Company, 24 F. App'x 756 (9th Cir. 2001).*

n14 *Argonaut Insurance Company v. Halvanon Insurance Company, 35 F. App'x 598 (9th Cir. 2002).*

n15 See *Filet Menu v. Cheng, 84 Cal. Rptr. 2d 384 (1999)* (attempted to limit exceptions to tolling statute to out-of-state business travel), and *Heritage Marketing v. Chrustawka, 73 Cal. Rptr. 3d 176 (2008)* (California's tolling statute violated the right to interstate travel).

n16 See *Nedlloyd Lines B.V. v. Superior Court, 834 P. 2d 1148 (Cal. 1992).*

n17 *Resurgence Financial v. Chambers, 92 Cal. Rptr. 3d 844 (Cal. Ct. App. 2009).*

n18 For a contrary result, however, see *Avery v. First Resolution Management Corporation, 2007 WL 1560653 (D. Or. 2007).*

n19 *42 U.S.C. § 415*(a).

n20 See *Castro v. Collecto Incorporated, 2009 WL 650856 (W.D. Tex. 2009).*

n21 See, e.g., *CAL. CIV. CODE § 1632*.

n22 *15 U.S.C. § 1666.*

n23 See *CAL. CIV. CODE § 1798.92*-.97 (West 2010).