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THE FAIR DEBT COLLECTION PRACTICES ACT AND CONVENIENCE FEES

Many creditors and loan or mortgage servicers provide the option to use certain payment methods, such as online or over-the-phone payments, to which they may apply convenience or service fees. Recently, class action plaintiffs have used state laws with a broader definition of "debt collector" than that in the Fair Debt Collection Practices Act to assert that these convenience fees violate the FDCPA's restrictions. This article will discuss a recent, significant Fourth Circuit Court of Appeals ruling regarding the Maryland Consumer Debt Collection Act that, in combination with other cases challenging the imposition of fees, should serve as a warning to creditors and mortgage servicers that impose convenience fees.

By Matthew C. Luzadder, Becca J. Wahlquist, and Nathan T. Jamieson *

Borrowers are frequently offered a number of different payment options for submitting payments, including ACH, mailed paper check, or in-person payments. Creditors and mortgage or other loan servicers may also accept debit cards, or third-party services can be used to facilitate payments via credit card. The servicer is generally responsible for the payment processing costs for such payment methods, unless the cost is paid by the borrower, and thus many servicers may charge borrowers a fee for opting to use these payment methods, rather than sending a check. This additional payment fee is commonly known as a convenience fee, but may also be called a service fee or platform fee.

Historically, because the Fair Debt Collection Practices Act ("FDCPA") applies only to debt collectors, its provisions do not apply to original creditors and would only apply to mortgage or loan servicers when a payment was in default. But state laws have carried FDCPA restrictions to a broader range of companies, as evidenced by a recent Fourth Circuit decision that involved allegations under Maryland's Maryland Consumer Debt Collection Act ("MCDCA") tied to $5 convenience fees that a mortgage servicer charged for online or phone payments. This issue of whether such fees could support MCDCA liability claims (and the FDCPA claims incorporated into the Maryland law) impacts not only mortgage servicers, but also most consumer lenders and companies servicing debt who offer various payment methods with convenience fees.

THE FOURTH CIRCUIT'S JANUARY 2022 *ALEXANDER* DECISION

In *Alexander v. Carrington Mortgage Services, LLC* ("*Alexander*"), Carrington Mortgage Services, LLC ("Carrington") charged borrowers a $5 convenience fee who opted to pay their monthly mortgage payments

* *MATTHEW C. LUZADDER and BECCA J. WAHLQUIST are partners and NATHAN T. JAMIESON is an associate at Kelley Drye & Warren LLP. Their e-mail addresses are mluzadder@kelleydrye.com, bwahlquist@kelleydrye.com, and njamieson@kelleydrye.com.*

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online or by phone rather than mailing a check to Carrington.[1] As the Fourth Circuit explained, the court below had erroneously granted Carrington's motion to dismiss, holding that Carrington was neither a "collector" under the MCDCA claim nor a "debt collector" under the FDCPA.[2] The district court had dismissed all the claims with prejudice after also finding that none of the mortgage documents expressly prohibited the fees and that plaintiffs had voluntarily chosen a payment method that included the $5 convenience fees.

On *de novo* review, the Fourth Circuit reversed in part, ruling that the plaintiffs' allegations that the convenience fee charged by Carrington violated the MCDCA survived Carrington's motion to dismiss. *Alexander* found that "it is plain that, by collecting borrowers' monthly mortgage payments, Carrington is collecting a debt" and that "Carrington counts as a 'collector' under the MCDCA."[3] *Alexander* further held that, while the FDCPA's definition of "debt collector" includes a requirement that the debt be in default, the MCDCA's definition has no similar limitation and the MCDCA did not incorporate the FDCPA's narrower definition of "debt collector."[4] But more problematic for cases outside of Maryland, the Fourth Circuit had "no trouble in concluding that convenience fees are an 'amount' under the FDCPA."[5] Significantly, the court also found that convenience fees not expressly provided for in the underlying mortgage agreement were not "permitted by law" simply because no law prohibited such fees, or because a consumer agreed to such fees in a later online clickwrap agreement.[6]

The Fourth Circuit held that the complained-of convenience fee was statutorily prohibited in Maryland on this basis, and that the MCDCA allegations should not have been dismissed by the lower court. The Fourth Circuit then remanded the case, and three months later (on April 25, 2022), the parties filed notice in the district court that the plaintiffs and the mortgage servicer will be agreeing to a class-wide settlement of the claims filed in the Fourth Circuit, as well as settlement of similar class actions pending in the Ninth Circuit and Eleventh Circuit.[7] The Fourth Circuit's reasoning thus will not be further tested (and no decision will now issue in the related Ninth Circuit appeal that had been brought), but the court's reasoning gives a glimpse in what may be an evolving issue and one that the Consumer Financial Protection Bureau ("CFPB") is tracking.

This also gives a view on state regulators' focus on the issue of convenience fees. On May 12, 2022, the Maryland Office of the Commissioner of Financial Regulation published Industry Advisory Regulatory Guidance summarizing the Fourth Circuit's ruling and urged lenders and servicers to review their records and reimburse improper fees to affected borrowers. The guidance also cautioned lenders and servicers from attempting to circumvent the MCDCA by directing consumers to a payment platform associated with the lender or servicer, or requiring consumers to amend their loan documents to permit convenience fees.[8]

BACKGROUND OF 15 U.S.C. § 1692F

The FDCPA regulates the practices of debt collectors, requiring that debt collectors refrain from any "unfair or unconscionable means to collect or attempt to collect any debt."[9] Among other prohibitions, the FDCPA prevents a debt collector from collecting "any amount (including interest, fee, charge, or expense incidental to the principal obligation) unless such amount is expressly

[1] *Alexander*, 23 F.4th 370 (4th Cir. 2022).

[2] *Id.* at 374.

[3] *Id.* at 375.

[4] *Id.* at 375-76.

[5] *Id.* at 377.

[6] *Id.* at 379.

[7] Joint Notice of Settlement and Motion to Stay, *Alexander v. Carrington Mortg. Servs.*, LLC, No. 1-20-cv-02369-RDB, (D. Md. filed on Apr. 25, 2022), ECF. No. 45 (announcing that settlement is imminent, but not disclosing terms of class settlement).

[8] *Notice to Lenders and Servicers: Court Decision on So-Called "Convenience Fees" (Fees For Loan Payments Might Not Be Collectable)*, May 12, 2022, Maryland Commissioner of Financial Regulation, Industry Advisory Regulatory Guidance. *Available at*: https://www.dllr.state.md.us/finance/advisories/advisory-conveniencefees.pdf.

[9] 15 U.S.C. § 1692f ("Section 1692f").

authorized by the agreement creating the debt or permitted by law."[10] Some borrowers have filed lawsuits, including the *Alexander* case, claiming that this prohibition (which the MCDCA incorporates) applies to convenience fees because they are an additional "amount" that was not "expressly authorized by the agreement creating debt or permitted by law."[11]

Courts have not uniformly accepted this argument that the Fourth Circuit adopted in *Alexander*. Some courts have ruled that an agreement to pay a convenience fee amounts to a separate contract unrelated, and thus not "incidental," to the contract creating the debt obligation.[12] Through this reasoning, these courts have found that a convenience fee simply does not implicate the FDCPA.

In other decisions, however, courts have focused on either the statute's expansive rationale or expansive language in holding that the FDCPA encompasses allegations concerning convenience fees. Some courts held that convenience fees were impermissible under the FDCPA because they were incidental to the underlying debt obligation, interpreting "incidental" broadly given that a court "must construe the FDCPA liberally in favor of the consumer."[13] As one court noted, "the majority of courts have found that 'convenience fees' derived from debt-payment methods are incidental to the debt being paid," and thus a viable basis for a FDCPA violation.[14] Still, other courts relied on the expansive statutory language to conclude that Section 1692f(1) does not limit its prohibition to only those fees that are "incidental" to the underlying debt obligation, but rather prohibited the charging of any amount even if not incidental to the underlying debt obligation.[15] They held that Section 1692f(1) prohibits the collection of any amount not authorized expressly in the agreement created by debt or permitted by law, and then elaborates that such an amount could "include[e] any interest, fee, charge, or expense incidental to the principal obligation."[16]

Indeed, this statutory text recently examined by the Fourth Circuit has served as the basis for a number of court rulings on this issue. For example, the U.S. District Court for the Eastern District of California held that "[w]hether a fee is 'incidental to the principal obligation' is not dispositive."[17] To the contrary, "[t]he only inquiry under [Section] 1692f is whether the amount collected was expressly authorized by the agreement creating the debt or permitted by law."[18] A court in U.S. District Court for Central District of California reached the same conclusion, ruling that "it is unnecessary to determine whether the alleged $4.00 convenience fee is incidental to the underlying debt, because the alleged fee is necessarily an 'amount,'" and Section 1692f(1) prohibits the charging of "'[a]ny amount.'"[19] Thus, there is a conflict in the rulings of federal courts nationwide.[20]

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[10] 15 U.S.C. § 1692f(1).

[11] *Id.*

[12] *Flores v. Collection Consultants of California*, No. SACV-140771-DOCNBX, 2015 WL 4254032, at *10 (C.D. Cal. Mar. 20, 2015) (dismissing the case because "the [convenience] charge was not 'incidental' to the principal obligation," given that it "would be imposed only if the debtor elected to pay via credit card"); *Lish v. Amerihome Mortg. Co., LLC*, No. 220CV07147JFWJPRX, 2020 WL 6688597, at *3 (C.D. Cal. Nov. 10, 2020) (holding that a convenience fee was not incidental to the underlying debt obligation because "Plaintiff voluntarily chose to make a payment by telephone rather than by other, cost-free methods, [and thus] she entered into a separate agreement with Defendant," unrelated to the underlying debt obligation).

[13] *See, e.g., Wittman v. CB1, Inc.*, No. CV 15-105-BLG-BMM, 2016 WL 3093427, at *2 (D. Mont. June 1, 2016); *McFadden v. Nationstar Mortg. LLC*, No. 20-CV-166-EGS-ZMF, 2021 WL 3284794, at *3 (D.D.C. July 30, 2021); *McWhorter v. Ocwen Loan Servicing, LLC*, No. 2:15-CV-01831-MHH, 2017 WL 3315375, at *7 (N.D. Ala. Aug. 3, 2017); *Lembeck v. Arvest Cent. Mortg. Co.*, 498 F. Supp. 3d 1134, 1136 (N.D. Cal. 2020).

[14] *McFadden*, 2021 WL 3284794, at *3 (internal quotations omitted).

[15] *See, e.g., Simmet v. Collection Consultants of California*, No. CV1602273BROPLAX, 2016 WL 11002359, at *6 (C.D. Cal. July 7, 2016) (quoting 15 U.S.C. § 1692f(1) (quoting 15 U.S.C. § 1692f(1)); *Lindblom v. Santander Consumer USA, Inc.*, No. 1:15-CV-990-LJO-BAM, 2016 WL 2841495, at *6 (E.D. Cal. May 9, 2016).

[16] 15 U.S.C. § 1692f(1).

[17] *Lindblom*, 2016 WL 2841495, at *6 (quoting 15 U.S.C. § 1692f(1)).

[18] *Id.*

[19] *Simmet*, 2016 WL 11002359, at *6 (quoting 15 U.S.C. § 1692f(1)).

[20] *McFadden*, 2021 WL 3284794, at *3; *Simmet*, 2016 WL 11002359, at *5 ("While the Ninth Circuit has yet to determine whether an optional convenience fee is permissible under the FDCPA, the majority of district courts in the Ninth Circuit have held that similar fees violate the FDCPA.").

While the Fourth Circuit in *Alexander* adopted the latter position, holding that the FDCPA prohibits convenience fees regardless of whether they are incidental, we will not see whether the Ninth Circuit would have agreed with the *Alexander* decision. The class-wide settlement recently announced by Carrington (which will end actions pending in Maryland, California, and Florida) will halt the determination of the Ninth Circuit on the question already addressed by the Fourth Circuit in regard to fees charged by a mortgage servicer and Section 1692f(1). In the California-based *Thomas-Lawson* case against Carrington, as in *Alexander*, the plaintiffs alleged that the convenience fees charged by Carrington violate the FDCPA. One issue in the appeal was whether Section 1692f(1) narrowly prohibits a debt collector from collecting only those amounts "*incidental* to the principal obligation," or broadly prohibits collecting "*any* amount" that is not "expressly authorized by the agreement creating the debt or permitted by law."[21] The CFPB elected to weigh in on the dispute before the Ninth Circuit, and adopted the latter position in an amicus brief filed in the *Thomas-Lawson* appeal.

The CFPB, the agency tasked with enforcement of the FDCPA, argued that Section 1692f(1) prohibits the charging of any additional fee — whether incidental or not — unless the fee is expressly permitted either by the debt agreement or by law. According to the CFBP, "[t]he district court [in *Thomas-Lawson*] correctly held that whether the pay-to-pay fees are 'incidental to the principal obligation' is irrelevant in determining whether such fees are covered by Section 1692f(1)."[22] To support its argument, the CFPB pointed to the FDCPA's syntax and the prohibition on "[t]he 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."[23]

The CFPB argued that the term "including" and its location within a parenthetical clause underscores that the phrase following that term — "any interest, fee, charge, or expense *incidental* to the principal obligation" — is not a limitation or "all-embracing definition," but rather a merely parenthetical illustration of items that could potentially be considered "any amount."[24] Given the deference courts often give government bureaus and agencies with regard to their interpretation of the laws and regulations they enforce, courts facing such arguments from the CFPB are likely to give them significant weight.[25]

FDCPA'S DEFINITION OF 'DEBT COLLECTOR'

The soon-to-be-settled *Alexander* and *Thomas-Lawson* cases brought other issues to the surface. The FDCPA defines debt collectors as "any person who regularly collects, attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another."[26] FDCPA applies to those collecting, or attempting to collect, a debt owed or due to *another*, but a mortgage servicer that is owed or due the debt *directly* would thus fall outside of the FDCPA. "The legislative history of section 1692a(6) indicates conclusively that a debt collector does not include the consumer's creditors, a mortgage servicing company, or an assignee of a debt, as long as the debt was not in default at the time it was assigned."[27] But in the two class actions against Carrington, that mortgage servicer found itself facing allegations of FDCPA violations via state debt laws for providing optional payment services with fees collected by Carrington.

The FDCPA excludes from the definition of debt collector "any person collecting or attempting to collect any debt . . . to the extent such activity . . . concerns a debt which was not in default at the time it was obtained by such person."[28] Mortgage servicers primarily collect mortgage payments on loans that are ***not*** in default and are, therefore, excluded from the definition of debt

[21] 15 U.S.C. § 1692f (emphasis added).

[22] Brief for the Consumer Financial Protection Bureau ("CFPB") as Amicus Curiae Supporting Appellants at 24, *Thomas Lawson v. Carrington Mortg. Servs., LLC*, No. 21-55459 (9th Cir. filed on Oct. 21, 2021), ECF No. 22.

[23] 15 U.S.C. § 1692f(1) (emphasis added).

[24] Brief for the CFPB as Amicus Curiae Supporting Appellants at 11, *Thomas Lawson v. Carrington Mortg. Servs., LLC*, No. 21-55459 (9th Cir. filed on Oct. 21, 2021).

[25] On June 29, 2022, the CFPB issued an advisory opinion amplifying its position that debt collectors are prohibited by the FDCPA from charging extra fees for making a payment online or by phone, when those fees are not expressly authorized by the original agreement creating the debt or expressly permitted by law. *Advisory Opinion, Debt Collection Practices (Regulation F); Pay-to-Pay Fees*, June 29, 2022. *Available at*: https://www.consumerfinance.gov/rules-policy/final-rules/advisory-opinion-on-debt-collectors-collection-of-pay-to-pay-fees/ (last visited, July 4, 2022).

[26] 15 U.S.C. § 1692a(6).

[27] *Perry v. Stewart Title Co.*, 756 F.2d 1197, 1208 (5th Cir. 1985) (internal citations omitted).

[28] 15 U.S.C. § 1692a(6)(F).

collector under the FDCPA.[29] And whether a mortgage is in default, as opposed to merely past due, is determined by the specific contractual language.[30] But the *Alexander* Court had no problem finding that, at least under Maryland's counterpart to the FDCPA, a servicer need not be dealing with a defaulted mortgage loan to be deemed a "collector."

POTENTIAL IMPLICATIONS OF THE *ALEXANDER* DECISION

The Fourth Circuit's acceptance of the plaintiff's state-law based arguments in *Alexander* illustrated how claims regarding convenience fees can reach outside of FDCPA's limited definition of debt collector and yet apply FDCPA's restrictions. The arguments combine a state statute's broad definition of debt collector with a finding that the FDCPA broadly prohibits convenience fees not (1) provided for by the underlying mortgage agreement or (2) specifically allowed by law. In summary, application of a broadly written state statute, such as the MCDCA in Alexander, mortgage servicers and others may be encompassed in a state law's definition of "debt collector" and subject to liability under state consumer protection statutes, including liability for imposing a convenience fee.

Carrington argued that it could not have violated the MCDCA based on any purported violation of the FDCPA because it — by definition — could not have violated the FDCPA, given that the FDCPA does not apply to mortgage servicers like Carrington. The Fourth Circuit, however, largely ignored this logic. Instead, the Fourth Circuit held that the MCDCA incorporated only the "substantive provisions" of the FDCPA, and not its definitions. The fact that the FDCPA does not apply to Carrington as a mortgage servicer did not prevent the Fourth Circuit from partly reversing the district court's dismissal of the action after finding Carrington was subject to the MCDCA.

Although the Fourth Circuit remains the first federal court of appeals to address the question of whether the FDCPA prohibits certain kinds of convenience fees, the California state Court of Appeal reached a similar conclusion under California's debt collection statute, the Rosenthal Fair Debt Collection Practices Act ("Rosenthal Act"). The Court of Appeal reversed a trial court's demurrer to hold instead that a mortgage servicer can be a "debt collector" under the Rosenthal Act.[31] In that case, the plaintiff alleged he had been hassled and harassed into incurring $5 transaction fees to use an electronic payment method for his monthly payments, even though he was current on his mortgage payments.[32] The Court of Appeal noted that (as in the MCDCA), the Rosenthal Act's definition of debt collector is broader than that of the FDCPA, and that the Rosenthal Act also prohibits any conduct that also violates the FDCPA.[33]

In another case involving California's debt laws, and with facts paralleling those in *Alexander*, the plaintiff in *Torliatt v. Ocwen Loan Servicing, LLC* argued that the $7.50 convenience fee imposed by his mortgage servicer every time he paid his mortgage online violated the Rosenthal Act because it violated the FDCPA, even though Ocwen Loan Servicing, LLC — the plaintiff's mortgage servicer — would not meet the definition of debt collector under the FDCPA. The *Torliatt* court, however, concluded that this deficiency would not sink the lawsuit and refused to dismiss the claims. The court ruled that, "[w]hile conduct that violates the FDCPA also violates the Rosenthal Act, . . . that does not mean that a plaintiff must also satisfy the stricter requirements of the FDCPA with respect to the definition of 'debt collector' in order to state a Rosenthal Act claim."[34] Recently, the *Torliatt* court granted a motion to certify a nationwide class of persons who mortgaged property located in California, finding that one common question was whether the collection of convenience fees "violates

[29] *See, e.g., Ayres v. Ocwen Loan Servicing, LLC*, 129 F. Supp. 3d 249, 277 (D. Md. 2015).

[30] *See, e.g., Torliatt v. Ocwen Loan Servicing, LLC*, No. 19-CV-04303-WHO, 2020 WL 1904596, at *4 (N.D. Cal. Apr. 17, 2020) ("Because the FDCPA does not define 'default,' district courts employ the definition set forth in the parties' contract, at least where the contractual definition is unambiguous, determine whether the debt at issue was in default when assigned." (internal quotation omitted)).

[31] *Davidson v. Seterus*, 21 Cal. App. 5th 283, 304 (Cal. Ct. App. 2018) (affirming that a mortgage service who engages in debt collection practices in attempting to obtain repayment of mortgage debt is a "debt collector" subject to the Rosenthal Act).

[32] *Id.* at 291.

[33] *Id.* at 303 ("In contrast to the FDCPA, the Rosenthal Act does not so limit the definition of 'debt collector.' Rather, the Rosenthal Act considers *anyone who regularly engages in the act or practice of collecting money, property or their equivalent* that is due or owing by a natural person as a result of a transaction between that person and another person in which the natural person acquired property, services, or money on credit, primarily for personal, family, or household purposes to be a 'debt collector.'"). CAL. CIV. CODE § 1788.17 ("[E]very debt collector . . . shall comply with the provisions of Sections 1692b to 1692j [of the FDCPA].").

[34] *Torliatt*, No. 19-CV-04303-WHO, 2020 WL 4495480, at *2 (N.D. Cal. June 22, 2020).

15 U.S.C. § 1692f(1) and, therefore, the Rosenthal Act?"[35]

In summary, a state debt-collection statute that prohibits conduct violating the FDCPA may apply to entities, including mortgage servicers and other entities that process payments for debt obligations, that would otherwise fall outside the scope of the FDCPA's restrictions. Accordingly, depending on a particular state statute's definition of "debt collector," a mortgage servicer may be exposed to potential liability for charging borrowers a convenience fee for faster, more convenient methods of payment.

KEY TAKEAWAYS

A debt servicer hoping to offer a convenient method of payment subject to an additional fee should consider the litigation around convenience fees, which has resulted in several recent decisions that are placing enormous statutory damages at issue on a class-wide basis under state debt collection laws with a broader definition of "collector" than the FDCPA. It is imperative for mortgage service providers and other companies likely to be targeted by similar litigation to be aware of these developments and to speak with their counsel about assessing convenience or other fees.

Going forward, one option that may be available to some lenders is to include a provision in the debt instrument explicitly reserving the lenders' or any subsequent debt servicers' right to impose a convenience fee. (Notably, this may be a challenge for mortgage lenders that use Fannie Mae/Freddie Mac Uniform Instruments. In addition, an amendment or addendum to existing debt instruments would likely not be effective and run afoul of FDCPA and other federal and state consumer lending regulations.) Moreover, in order to offer customers "instant" or "same-day" payment options, lenders may consider presenting third-party services to customers so that convenience fee transactions are governed by agreements that are between only the borrower and the third-party payment processor or money transmitter, and do not involve the lender or loan/mortgage servicer.

Careful consideration is necessary to determine how third-party payment options are presented to a borrower, as class action litigation focused on FDCPA allegations tied to convenience or service fees is all but certain to continue in light of the Fourth Circuit's ruling in *Alexander*. ■

[35] Order Denying Daubert Motion and Granting Motion for Class Certification, *Torliatt*, Case No. 19-CV-04303 (N.D. Cal. Nov. 8, 2021), ECF No. 152.