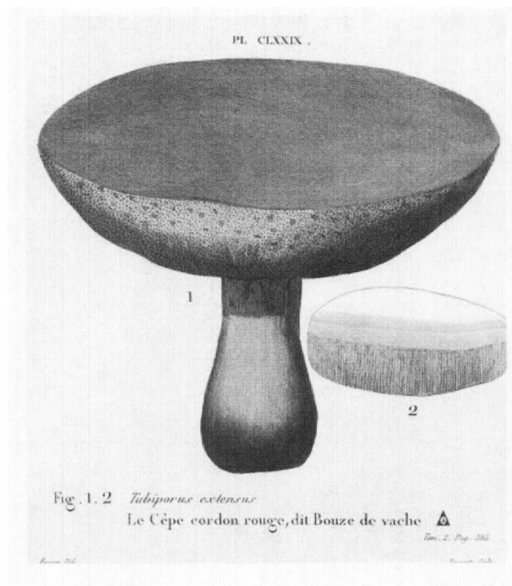
Consumer Law: Advances and Setbacks

In the opinion of the editors, the cases digested below "advance" or "set back" the consumer interest. These characterizations reflect opinions of the editors and do not in any way represent policies or positions adopted by ACCI or Advancing the Consumer Interest. Persons with differing viewpoints are encouraged to reply.

SETBACK: REGULATION OF CLAIMS ABOUT MUSHROOMS VIOLATES COMMERCIAL SPEECH RIGHTS

There is (believe it or not) a "Mushroom Promotion, Research, and Consumer Information Act" which mandates that fresh mushroom handlers pay assessments, which are used primarily to fund advertisements that promote mushroom sales. Believing that being compelled to pay for "generic" advertising sent a message contrary to one that conveyed the superiority of its own mushrooms, United Foods Corporation refused to pay the assessment claiming that it violated its First Amendment rights. United Foods first complained to the Secretary of Agriculture who brought suit to compel the assessments. After its administrative appeals were exhausted, United Foods pursued a review in the district court. The district court upheld the Act based, particularly on a case which determined that the First Amendment was not violated by an agricultural marketing order that required producers of California tree fruit to pay assessments for product advertising, a rule which was part of a larger scheme.



The Sixth Circuit reversed the district court. It held that the California case did not control because the mandated payments in the case of the Mushroom Act were not part of a comprehensive statutory agricultural marketing program. Justice Kennedy, speaking for the U.S. Supreme Court, agreed with the Sixth Circuit that the Act was unconstitutional, in his opinion in United States and Department of Agriculture v. United Foods, Inc., 121 S.Ct. 2334 (2001).

Considered either as noncommercial or commercial speech, Justice Kennedy wrote, the assessments could not be sustained. First Amendment values are at serious risk, he said, if the government can compel a citizen or group of citizens to subsidize speech on the side that it favors. Kennedy could find no principle to distinguish great debates about important causes from minor debates about whether a branded mushroom is better than just any mushroom. Thus, the Court stated,

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the Act was not merely an economic regulation but was required to pass First Amendment scrutiny.

Justice Breyer, joined by Justice Ginsburg and partly joined by Justice O'Connor, dissented. The Court, he wrote, "disregards controlling precedent, fails properly to analyze the strength of relevant regulatory and commercial speech interests, and introduces into First Amendment law an unreasoned legal principle that to the development of beneficial forms of economic regulation." In this case the Mushroom Act's goal was to maintain and expand uses for mushrooms. Overcoming "inaccurate consumer perceptions about a product" (such as the assumption that some brands or kinds were safer to eat than others) would bring valuable public benefits, and in the absence of the compelled payments there might be a "free rider" problem because some producers would "take a free ride on the expenditures of others."

The case has cast doubt on the ability of the Agriculture Department and other governmental entities to promote standards and grades through cooperative advertising programs. More fundamentally, it suggests that the line between mere economic regulation, that is generally upheld without severe scrutiny by the court, and commercial speech, to which the Court has been increasingly willing to afford significant First Amendment protection, has been more protectively redrawn. It should be noted, however, that the majority opinion suggested that it might have decided the case differently if there had been evidence that assessments were necessary to make voluntary advertisements "nonmisleading" for consumers.

SETBACK: STATE TOBACCO REGULATIONS PREEMPTED

Responding to public concern about youth smoking, the Attorney General of Massachusetts promulgated comprehensive regulations governing the advertising and sale of cigarettes, smokeless tobacco, and cigars. A group of tobacco manufacturers asserted that the First Amendment and the Supremacy Clause of the Constitution

forbade the new regulations because they wrongly compelled speech and because they were pre-empted by the Federal Cigarette Labeling and Advertising Act (FCLAA), which had legislated mandatory health warnings for cigarette packaging and advertising, and pre-empted similar state regulations at the same time. The district court largely upheld the state's regulations. Among its rulings, the court held that restrictions on the location of advertising were not pre-empted by the FCLAA, and that neither the regulations prohibiting outdoor advertising within 1,000 feet of a school or playground nor the sales practices regulations restricting the location and distribution of tobacco products violated the First Amendment. The First Circuit affirmed the District Court's rulings that the cigarette advertising regulations were not pre-empted by the FCLAA and that the outdoor advertising regulations and the sales practices regulations did not violate the First Amendment under previously articulated standards (especially Central Hudson Gas v. Public Serv. Comm'n of N. Y., 447 U.S. 557), although it reversed the lower court's invalidation of new "point-of-sale" advertising regulations, concluding that the Attorney General was better suited than the courts to determine what restrictions were necessary.

The U.S. Supreme Court, however, reversed the First Circuit, in Lorillard Tobacco Co. v. Thomas F. Reilly, 121 S.Ct. 2404 (2001). Justice O'Connor, speaking for a unanimous Court (there were several concurrences and dissents in part) held that the language of the FCLAA pre-empts Massachusetts' regulations governing outdoor and point-of-sale cigarette advertising.

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The Court's analysis began with the statute's language and considered its legislative amendments, including a predecessor pre-emption provision and the legislative context in which the current language of preemption was adopted. The original provision simply prohibited any "statement relating to smoking and health ... in the advertising of any cigarettes the packages of which are labeled in conformity with the [Act's] provisions." Without question, the Court found, the current pre-emption provision's plain language was much broader. Rather than preventing only "statements," the amended provision reaches all "requirement[s] or prohibition[s] ... imposed under State law."

"Greater state tobacco regulation...faces statutory and constitutional obstacles."

Although the former statute reached only statements "in the advertising," the current provision governs "with respect to the advertising or promotion" of cigarettes. At the same time that Congress expanded the pre-emption provision of the law with respect to the States, it enacted another provision prohibiting cigarette advertising in electronic media altogether.

As a policy matter, the Court determined that Congress pre-empted state cigarette advertising regulations like the Attorney General's because they would upset federal legislative choices to require specific warnings and to impose the ban on cigarette advertising in electronic media in order to address concerns about smoking and health. The First Circuit had concentrated on whether the regulations were "with respect to" advertising and promotion, and concluded that they were regulations aimed at "youth" rather than cigarettes. The Supreme Court rejected that view. There is no question, it stated, that the regulations expressly targeted such advertising. Nor did the Court accept a distinction between regulation of advertising content and regulation of geographical location.

The Court decided that the state's ban on all smokeless tobacco products was unconstitutional. The Court used its four-part *Hudson* test for analyzing regulations of commercial speech asking (1) whether the expression is protected by the First Amendment, (2) whether the asserted governmental interest is substantial, (3) whether the regulation directly advances the governmental interest asserted, and (4) whether it is not more extensive than is necessary to serve that interest. Only the last two steps were placed at issue. The fourth step requires a "reasonable fit between the legislature's ends and the means chosen to accomplish those ends, a means narrowly tailored to achieve the desired objective." Under its analysis, the Court held that the outdoor advertising regulations prohibiting smokeless tobacco or cigar advertising within 1,000 feet of a school or playground violated the First Amendment. The "broad sweep" of the law indicated that the Attorney General did not "carefully calculate the costs and benefits associated with the burden on speech imposed." Regulations prohibiting indoor, point-of-sale advertising of smokeless tobacco and cigars lower than 5 feet from the floor of a retail establishment located within 1,000 feet of a school or playground also failed both the third and fourth steps of the Central Hudson analysis.

Although the First Circuit decided that the restriction's burden on speech is very limited, the Supreme Court stated that there is no *de minimis* exception for a speech restriction that lacks sufficient tailoring or justification.

In reaching its decision, however, the Court did suggest that some additional regulations of tobacco might be upheld. Even assuming that tobacco sellers have a speech interest in displaying their products, the Court decided that regulations requiring retailers to place tobacco products behind counters and requiring customers to have contact with a salesperson before they are able to handle the products were held to withstand First Amendment scrutiny. The State demonstrated "a substantial interest in preventing access to tobacco products by minors and has adopted an appropriately narrow means of advancing that interest."

This case demonstrates that greater state tobacco regulation in furtherance of public health concerns will face statutory and constitutional obstacles. While the Court has not

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placed insurmountable constitutional barriers before the state legislatures, the problem of federal preemption remains daunting.

SPECIAL SECTION:

CONSUMER RIGHTS UNDER THE FAIR DEBT COLLECTION PRACTICES ACT

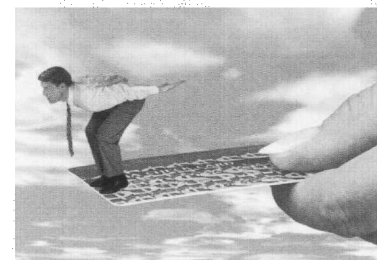
The Fair Debt Collection Practices Act is a federal statute which prohibits debt collectors from engaging in a variety of false, misleading, or deceptive practices. The FDCPA is an important consumer protection statute and will become an even more important subject of litigation in the future because of two recent phenomena. One reason is the impact of welfare reform legislation, which has increased the ranks of the "working poor," people who live paycheck to paycheck and frequently find themselves in debt. The second reason for the growing importance of the FDCPA is the recent enactment of a bankruptcy "reform" law, which significantly restricts the protection afforded to consumers under federal bankruptcy law. As a result, many consumers who previously would have been shielded from debt collection activities by the bankruptcy laws will no longer receive such protection. Courts consequently will be called on with increasing frequency to consider questions stemming from the FDCPA. This section considers a few of those questions, such as the relationship between the FDCPA and state laws, the appropriateness of garnishment procedures under the FDCPA, whether dishonored checks are debts within the FDCPA, and whether debts are designated "consumer" or "business" debts under the statute.

PARTIAL ADVANCE: FDCPA SECTIONS PROHIBITING FALSE OR MISLEADING REPRESENTATIONS IMPOSE STRICT LIABILITY

In January 1998, Andrew Kaplan received medical treatment at Columbia Aventura Hospital in Miami, Florida. At the time, Kaplan had insurance under a HMO health plan through Sunrise Healthcare. Under his policy, all treatments he received were covered by his insurance, and he was responsible only for the payment. Sunrise Healthcare had a billing arrangement with Columbia Aventura, and as a result of the treatments received by Kaplan, Sunrise owed the hospital $4,453.67. Kaplan met his deductible and co-payment obligation under his insurance policy. Nevertheless, on December 9, 1997, Kaplan received a letter from Columbia Aventura attempting to collect the $4,453.67 for medical services that should have been covered by Kaplan's HMO. Columbia Aventura sent the debt to Assetcare, a collection agency, which attempted to collect the alleged debt from Kaplan through a number of letters. Kaplan also received a letter from Equifax attempting to collect the same debt.

As a result of these collection activities, Kaplan filed suit, claiming that the actions of Assetcare and Equifax violated the Florida Insurance Code, which states that a provider of services, or representative of that provider, cannot collect or attempt to collect money from any HMO subscriber for services covered by the HMO. The alleged violation of the Florida Insurance Code was also the basis for Kaplan's claim under the FDCPA that the debt collector's actions were false. deceptive or misleading (i.e., because Kaplan never should have been billed for the healthcare services he received).

The court reasoned that the purpose of the FDCPA is to eliminate abusive debt collection practices and for any violation of the Act, a debt collector may be liable for actual damages sustained by the plaintiff, as well as statutory damages and attorney's fees. The determination of whether a debt collector's practices are false, deceptive or misleading is judged from the perspective of the "least sophisticated consumer." In order for a consumer to prevail under a FDCPA claim, the consumer must prove three things: 1) that they were the object of a collection activity arising from a consumer debt, 2) that the defendant is a debt collector within the meaning of the FDCPA, and 3) that the defendant engaged in acts in violation of the FDCPA. The defendants asserted that Kaplan's claim should be dismissed because



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he failed to allege any element of intent on the part of Assetcare and Equifax. The court held that no element of intent is necessary when dealing with a strict liability statute. In the sections of the FDCPA which formed the basis for Kaplan's suit, there is no mention of intent. As a result, knowledge or intent is not a factor in the liability determination.

The federal court refused to consider Kaplan's third claim, which involved interpretation of a Florida insurance statute. Because this was an issue never previously decided by Florida state courts, the federal court held that it should be determined by those courts.

SETBACK: CONSUMERS OF LONG DISTANCE CARRIER SERVICES ARE NOT "CONSUMERS" UNDER FDCPA.

Edward and Eileen Conboy used AT&T as their long distance carrier. During the time the Conboys used AT&T, the company had access to information contained in their billing statements, including their names, their unlisted phone number, their address, and details about their long distance calling patterns. The Conboys never authorized the release of their unlisted telephone number to any other company, and, in fact, paid a monthly charge for it to remain unlisted. At the same time, the Conboys' daughter-in-law, Maria Conboy, held a Mastercard issued by AT&T Universal Card Services ("UCS"), a subsidiary of AT&T. The Conboys had no connection with the credit card or debts owed by Maria. However, in May and June 1998, representatives of UCS called the Conboys at their home phone number between thirty and fifty times seeking information about their daughter-in-law, including her whereabouts. The calls were made repeatedly, and often at strange hours. The Conboys discovered that AT&T had disseminated the information to UCS when one UCS representative informed the Conboys that he knew their unlisted number and information about their long distance carrier.

The Conboys brought a class action suit in federal district court in New York, alleging that by revealing information contained in the long distance bill, AT&T violated the Federal Telecommunications Act, various provisions of New York state law, as well as the FDCPA, specifically provisions related to the use of false, deceptive or misleading representations. The Conboys alleged that AT&T mailed telephone bills to the Conboys for the purposes of gaining information to collect Maria's debt, and there was no language on the bill that indicated that the purpose was to collect a debt. The court in Conboy v. AT&T Corp. and AT&T Universal Card Services, 241 F.3d 242 (2d Cir. 2001), held that the Conboys were not considered consumers under the FDCPA and, therefore, the Act did not apply and the FDCPA claim was dismissed. Under the FDCPA, a consumer is any person obligated or allegedly obligated to pay a debt. Because the Conboys were in no way obligated to pay the debt of their daughter-in-law, they are not considered consumers of UCS. Even though the Conboys are consumers of the AT&T services, they are not considered to be consumers under the FDCPA. The Conboys argued that their civil complaint should be read more broadly to include other possible claims under the FDCPA that can be asserted by a person other than a customer. The court disagreed because the Conboys specifically asserted claims under the false, deceptive or misleading portions of the Act.

ADVANCE: GARNISHMENT OF BANK ACCOUNT WAS UNAUTHORIZED UNDER FDCPA

On April 29, 1997, Eric Picht deposited his paycheck in the personal checking account he shared with his wife, Shayleen. Between that date and May 7, 1997, the Pichts wrote four checks, totaling $50.25, from their account. However, the couple later learned that Picht's paycheck was dishonored, and as a result, Pichts' bank dishonored those four checks. The businesses receiving the checks sent them to a collection agency, which, in turn, engaged the law firm of Jon R. Hawks as counsel to pursue collection of the debt.

In January of 1998, Hawks served a summons and complaint on the Pichts regarding

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a collection action brought in Minnesota state court. The complaint claimed that the Pichts owed over $900, including $400 for the four dishonored checks. Prior to the entry of judgment in that suit, Hawks sent the Pichts a notice of intent to garnish. In July 1998, the Pichts filed suit in federal district court alleging violations of the FDCPA based. The Pichts claimed that the attorney's use of the garnishment procedure prior to entry of judgment violated Minnesota law on collection practices, and thus the FDCPA (the FDCPA prohibits the use of debt collection practices that violate state law).

The case was eventually appealed to the United States Court of Appeals for the Eighth Circuit. In Picht v. Jon R. Hawks, Ltd., 236 F.3d 446 (8th Cir. 2001), the appeals court held that the decision on whether a creditor may commence a garnishment action prior to a judgment against the debtor in a lawsuit depends on whether the creditor would be entitled to receive a default judgment. Under Minnesota law, a default judgment is only allowed when the creditor's claim against the debtor is "upon a contract for the payment of money only." Thus, a creditor may only use garnishment proceedings when the creditor's claim is only for the payment of a *specified* amount of money. The court held that a default judgment could not be entered in this case. While checks certainly create contractual obligations, the court interpreted the meaning of "contracts for the payment of money" to mean contracts where a definite contractual sum is involved, and where there is no discretion on the part of the court as to the total amount the debtor would owe. Under Minnesota's bad check law, the court has discretion over how much of a penalty to award against the debtor (i.e., "up to" $100 per bad check). Moreover, because the amount at issue in Hawks' lawsuit against the Pichts included a request for costs and attorney's fees associated with the dishonored checks, the amount was not definite. Therefore, Hawks' attempt to use the garnishment procedure before the entry of judgment in his case against the Pichts violated Minnesota's bad check law because a default judgment could not be obtained under that law. Hawk's actions in violation of Minnesota law violated the FDCPA's prohibition against threatening "to take any action that cannot legally be taken." Thus, in this case the court applied the FDCPA to a debt that involved the tender of personal checks, something about which the courts are not in agreement, as the next excerpt reveals.

SETBACK: CHECKS ARE NOT DEBTS UNDER THE FDCPA

Sanford Krevsky purchased consumer goods with a check. His bank dishonored the check and the store turned the check over to Equifax Check Services for collection. Equifax sent Krevsky several letters demanding payment, as well as a $20.00 dishonored check fee. Krevsky filed suit in Pennsylvania, alleging that the letters sent from Equifax violated the FDCPA.

The United States District Court for the Middle District of Pennsylvania held in Krevsky v. Equifax Check Services Inc., 85 F.Supp.2d 479 (M.D. PA. 2000), that a check is not considered a debt under the FDCPA. According to the court, the FDCPA covers consumer debts involving the extension of credit to the consumer. Because payment by check is equivalent to payment in cash, no extension of credit is required and thus the FDCPA does not apply to a debt collector's attempts to collect a dishonored check. The court then dismissed the complaint based on the fact that Krevsky no longer had a claim under the FDCPA.

Courts from other jurisdictions have ruled otherwise. The Seventh Circuit Court of Appeals held in Bass v. Stolper, Koritizinsky, Brewster & Neider, 111 F.3d 1322 (7th Cir. 1997), that there is no requirement of "extension of credit" in the FDCPA's definition of a debt. The Seventh Circuit reasoned that a debt arises when a consumer creates an obligation to pay, regardless of the nature of the underlying transaction. A check, like a credit card, creates an obligation to pay. Since the courts are divided on this important issue, it is likely that the United States Supreme Court will resolve the dispute at some point in the future.

When is a payment by check an "extension of credit?"

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ADVANCE: PURCHASE OF BACKHOE FOR PERSONAL USE WAS CONSUMER DEBT

The FDCPA applies only to those debts that are considered "consumer" in nature. Thus, debts that are incurred as a result of a business transaction are not within the purview of the Act. In the case of Slenk v. Transworld Systems, Inc., 236 F.3d 1072 (9thCir. 2001), Robert Slenk defaulted on a loan to finance a backhoe that he purchased for personal use. Slenk claimed that the backhoe was a "consumer debt" because it was for personal use. He purchased the backhoe in 1993 to assist in the construction of his house and driveway. While Slenk owns and operates his own carpentry business, Slenk Builders, he claims the backhoe was never used for any job in connection with his business. Evidence at the trial court indicated that Slenk held a contractors license only for carpentry, and his business was not licensed to use a backhoe. In addition, Slenk sold the backhoe immediately after completing his home. On the other hand, there was evidence that Slenk purchased the backhoe for business purposes: the invoice for the sale lists "Slenk Builders" as the purchaser and indicates a reduced tax rate given for business purchases. Further, Slenk listed the backhoe as the property of Slenk Builders on his tax returns, thereby authorizing a deduction on his personal income tax.

In 1994, Slenk obtained a loan from a credit union to finance the payment of the backhoe. The loan was issued to Slenk, rather than his company. Slenk defaulted on the loan and it was turned over to Transworld Systems, a collection agency. Transworld attempted to collect the debt through both written and oral communication with Slenk and his wife. Slenk filed suit in federal district court, alleging assorted violations of the FDCPA. Transworld asserted that the debt was not a "consumer" debt and, therefore, the FDCPA did not apply to its collection efforts. The district court ruled in Transworld's favor, dismissing the case. It decided that Slenk's loan was for business, not consumer, purposes.

Slenk appealed the decision to the Ninth Circuit Court of Appeals. The appeals court held that there was an undecided issue of fact as to whether the backhoe was purchased for personal or business use. Under the FDCPA, a consumer debt relates to a transaction involving a debt for personal or household purposes. In determining whether a loan is for personal or business use, the court noted that it must view the transaction as a whole and elevate substance over form: "neither the lender's motives nor the fashion in which the loan is memorialized are dispositive of this inquiry." In order to decide what type of debt Slenk incurred in this case, the trial court should have examined the substance of the transaction, as well as Slenk's purpose in borrowing the money. The appeals court decided that is was not absolutely clear that the loan was for a business purpose, so the case should not have been dismissed. As a result, the decision of the lower court was reversed and the case sent back for trial on the issue of whether the debt could be classified as "consumer" or "business" for the purposes of the FDCPA. However, the court noted that a debt does not becomes a consumer debt merely because a debt collector contacts a consumer at home with respect to the debt. On the contrary, it is the initial transaction that will determine the nature of the debt for purposes of the FDCPA.

SETBACK: HOMEOWNERS ASSOCIATION IS NOT A DEBT COLLECTOR UNDER THE FDCPA

William and Audrey Feldmann are homeowners in a planned development community maintained by the Davis Lake Community Association. Under a number of restrictive covenants that govern the community, the Community Association has the authority to collect assessments and other maintenance charges from those living in the development. The assessments are collected on a quarterly basis. The Feldmanns failed to pay the assessments for four consecutive quarters in 1996 and 1997. The past due assessments totaled $200.95. The Community Association sent the Feldmanns several letters demanding payment, eventually retained counsel, and

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filed a collection lawsuit against the Feldmanns. In response to the letters and the lawsuit, the Feldmanns tendered a check for the outstanding balance, which the Community Association returned to them because it did not include payment for attorney's fees. Counsel for the Community Association filed an affidavit claiming attorney fee's in the amount of $2378.90, ten times the amount of the outstanding balance.

The Feldmanns filed a counterclaim, alleging violations of the FDCPA. The trial court dismissed their counterclaim and ordered them to pay the outstanding balance, in addition to the attorney's fees. In Davis Lake Community Association v. Feldmann, 138 N.C.App. 292 (N.C.App. 2000), the Court of Appeals for North Carolina held that the trial court properly dismissed the Feldmann's case because a homeowner's association is not considered a debt collector under the FDCPA. According to the FDCPA, 15 U.S.C. § 1692(a) (1998), a debt collector is any person who regularly collects on behalf of others. The FDCPA does not apply to creditors trying to collect their own debts, and because the Community Association was collecting a debt owed to itself, the FDCPA does not apply to their collection practices. Thus, while a homeowner is considered a "consumer" for the purposes of the FDCPA, a homeowner's association is not considered a "debt collector."

Compiled by Stephen Meili & Marcy Philips
Center for Public Representation

Melanie Ryan
University of Wisconsin Law School

ACCI

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For additional information contact:
Carrie Paden, Executive Director, ACCI,
240 Stanley Hall, University of Missouri,
Columbia, MO 65211
http://acci.ps.missouri.edu

• Website

consumerinterests.org

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