

PREJUDGMENT COLLECTION

A. EVALUATING THE CLAIM

1. Preliminary Steps

- a. [3:1] **Obtain facts from creditor:** As a first step toward effective claim evaluation, creditor's counsel must obtain all relevant information that the creditor possesses about the debt and the debtor.

- (1) [3:2] **Copies of relevant documents:** Counsel should request the creditor to provide complete legible copies of all relevant documents—e.g., purchase orders, sales agreements, promissory notes, guaranty agreements, leases, delivery receipts, invoices, statements, bills, ledger cards and/or computer printouts itemizing debits and credits, security agreements and evidence of perfection of the security interest (financing statements, certificates of ownership, etc.).

The creditor should also give counsel copies of any applications, financial statements and recent checks (or ABA numbers on such checks) that the debtor submitted to the creditor. These documents often include such useful information as the debtor's correct name, social security number, driver's license number, income and asset information, location of bank accounts, and spouse's/ domestic partner's name.

➡ [3:3] **PRACTICE POINTER:** It is crucial to review the original documents, or copies thereof, particularly where your client is not the original creditor; the client may not have the payment stream that preceded acquisition of the debtor's account and, therefore, the originating balance you are provided may be inaccurate or may contain added charges that are not recoverable (e.g., collection or attorney fees).

Ask the creditor to have available *original* executed documents such as promissory notes, and guaranty and security agreements. The originals may be required where your client is unable to lay an evidentiary foundation for copies for the documents to come within the business records exception to the hearsay rule (Ev.C. §1271).

It is also useful to obtain copies of the creditor's collection notes from telephone calls with

[3:4 — 3:6.2]

the debtor, which may reflect anything from verbal abuse to instructions not to contact the debtor. This information may be valuable in establishing a bona fide error defense to an alleged FDCPA violation.

(2) **Information re debtor**

- (a) [3:4] **Individual debtor:** To the extent possible, the creditor should also verify and furnish an individual debtor's current or last known address and place of employment; and advise counsel whether the debtor disputes the claim and what offsets or counterclaims the debtor might assert (if known). Credit bureau reports may reflect address history in case questions arise regarding the debtor's identity. The creditor should also provide all correspondence to and from the debtor (e.g., cease and desist letters, demand letters, disputes, etc.).
- (b) [3:5] **Business debtor:** If the debtor is a business, the creditor should provide any available Dun and Bradstreet Reports or other credit reports; or other available information regarding the business' assets, ownership, banking relationships and other creditors. A cancelled check from a prior debtor payment can be useful if a debt is disputed or when identifying an account upon which to execute. Also, determine whether the business has a website, which can provide information re the business' name and entity status.

b. **Determine type of claim**

- (1) [3:6] **Secured or unsecured:** The claim is secured if the debtor has given the creditor a security interest in its personal property or a deed of trust upon its real property interests as collateral. Counsel should verify that the security interest has been "perfected" under applicable law—e.g., by filing with the Secretary of State, recording with the county recorder, etc. If the lien has not been perfected, counsel should determine whether it can be perfected before suit is filed.
 - (a) [3:6.1] **Proceeding against debtor's security:** Again, this Practice Guide does not focus on the enforcement of real and personal property *security* interests. Briefly, however:
 - 1) [3:6.2] **Real property foreclosures:** Real property foreclosures are chiefly governed by the California Civil Code and Code of Civil Procedure (Civ.C. §2920 et seq.; CCP §725a et seq.). (See detailed discussion in Greenwald & Bank, *Cal. Prac. Guide: Real Property Transactions* (TRG), Ch. 6.)

- 2) [3:6.3] **Personal property foreclosures—“commercially reasonable” sale requirement:** Foreclosing and selling personal property collateral is governed primarily by Division 9 of the California Commercial Code (Comm'l C. §9101 et seq.). Among other things, a sale of the debtor's personal property security pursuant to Comm'l C. §9610(a) and (b) must be “*commercially reasonable*”—i.e., the foreclosure sale must be *adequately advertised* to ensure ample attendance by legitimate bidders, “so that the highest commercially reasonable price for the collateral [is] obtained.” [*Ford & Vlahos v. ITT Comm'l Finance Corp.* (1994) 8 C4th 1220, 1233, 36 CR2d 464, 472]

a) **Application**

- [3:6.4] A secured party's duty to advertise the sale of collateral is not met merely by placing legal notice in a newspaper. [*Ford & Vlahos v. ITT Comm'l Finance Corp.* (1994) 8 C4th 1220, 1233, 36 CR2d 464, 472]

[3:6.5-6.9] *Reserved.*

- b) [3:6.10] **Effect of noncomplying sale:** Nonetheless, a secured party's failure to conduct a sale of the collateral in a commercially reasonable manner does not require reversal of a deficiency judgment. The debtor remains liable for any deficiency, but “only if the balance of the indebtedness immediately before the disposition exceeds the amount which the secured party establishes would have been realized had the disposition been conducted” in a commercially reasonable manner. In other words, liability is limited to the excess. [*Clark v. EZN, Inc.* (1997) 57 CA4th 852, 858, 67 CR2d 403, 406 (internal citation omitted)]

- (2) [3:7] **Consumer or commercial:** Commercial claims arise out of debts incurred in the course of business operations. Consumer claims are based on debts incurred by an individual for personal, family or household purposes. Consumer claims are generally more difficult to collect than commercial claims, partly because consumer debt collection practices are extensively regulated by state and federal law; *see Ch. 2 for detailed discussion.*

[3:7.1 — 3:8.1]

- (a) [3:7.1] **Statute of frauds limitation on enforcement of certain commercial loan commitments:** A contract to make a *commercial* loan or extension of credit (not primarily for personal, family, or household purposes) exceeding \$100,000, made by a person in the lending business, is enforceable only if evidenced by a writing. [See Civ.C. §1624(a)(7)]

However, if the loan is to be secured solely by residential property consisting of one to four dwelling units, it is considered a *consumer* loan and thus exempt from the statutory writing requirement. [Civ.C. §1624(a)(7)]

[3:7.2-7.4] *Reserved.*

- c. [3:7.5] **Ascertain whether claim prohibited by law or against public policy:** Creditor’s counsel also must determine whether suit on the particular type of claim is prohibited by law or against public policy. For example, California has a strong public policy against the judicial resolution of civil claims arising from *gambling* contracts or transactions. [See *Tak Chun Gaming Promotion Co. Ltd. v. Long* (2023) 96 CA5th 1027, 1033-1040, 314 CR3d 890, 895-901 (extensive discussion supporting common law rule barring litigation of gambling debts); *Kelly v. First Astri Corp.* (1999) 72 CA4th 462, 476-489, 84 CR2d 810, 818-827 (action to recover gambling losses for alleged cheating by casino managers barred)]

Likewise, for out-of-state clients, determine whether the claim is prohibited by California public policy.

- d. [3:8] **Ascertain statute of limitations:** The next step is to determine the applicable statute of limitations governing suit on the claim . . . and particularly whether the claim might already be “stale” under the applicable limitations period.

- [3:8.1] For example, the limitations period for money had and received (i.e., no written agreement) is *two years* (CCP §339); and *four years* for an action on a written sales agreement or note or for breach of written warranty (CCP §337(a); see *Piedmont Capital Mgmt., L.L.C. v. McElfish* (2023) 94 CA5th 961, 964-965, 970-972, 312 CR3d 664, 667, 672-675—lawsuit filed to collect amounts due under HELOC agreement was timely under CCP §337 as to all monthly payments missed within 4 years before its filing as well as all future payments, where agreement had fixed maturity date and lender exercised discretion to accelerate balance due within 4-year “look back” period; *White v. Moriarty* (1993) 15 CA4th 1290, 1299, 19 CR2d 200, 205—4-year statute of limitations begins running against each note installment as it becomes due; see also Comm’l C. §2725). [*Cavalry SPV I, LLC v. Watkins* (2019) 36 CA5th 1070, 1081, 249 CR3d 334,

[3:8.2 — 3:8.6a]

343—“the statute of limitations is four years for a breach of contract claim based on a written contract, but only two years for a breach of contract claim based on an oral agreement”; for further discussion in connection with common counts, see ¶3:406 ff.]

- [3:8.2] An *action for a deficiency judgment* following foreclosure of a trust deed must be commenced within *three months* after the foreclosure sale. This applies both to *nonjudicial* sales under private power of sale (see CCP §580a) and *judicial* sales following a judgment of foreclosure (see CCP §726(b)—separate action required to determine amount of deficiency). [*Citrus State Bank v. McKendrick* (1989) 215 CA3d 941, 945, 263 CR 781, 783; *Life Sav. Bank v. Wilhelm* (2000) 84 CA4th 174, 177, 100 CR2d 657, 660]
 - [3:8.3] The three-month statute of limitations on actions for deficiency judgments applies where a *junior lienholder* is the purchaser at foreclosure sale. [*Citrus State Bank v. McKendrick* (1989) 215 CA3d 941, 948, 263 CR 781, 786]
 - [3:8.4] But a junior lienholder who is “sold out” by foreclosure of a senior lien is *not* bound by the three-month statute of limitations and may sue within the four-year period provided by CCP §337. [*Roseleaf Corp. v. Chierighino* (1963) 59 C2d 35, 41, 27 CR 873, 876]
- [3:8.5] An action on the liability of a *deceased debtor* that survives the decedent’s death generally must be commenced, at the very latest, no later than *one year after the date of decedent’s death*. [CCP §366.2; see ¶3:289.10]
- [3:8.6] An action based upon a *spouse’s/domestic partner’s liability for a deceased spouse’s/domestic partner’s “necessaries of life”* (Fam.C. §914(a), ¶3:21) ordinarily must be commenced, at the latest, within *one year of the death* pursuant to CCP §366.2 (¶3:8.5). However, if the surviving spouse/domestic partner had actual knowledge of the debt before expiration of the one-year limitations period and the personal representative of the decedent’s estate fails to provide the creditor asserting the claim with timely written notice of the probate administration (pursuant to Prob.C. §9050), a statute of limitations of *two years* (CCP §339) or *four years* (CCP §337) applies. [Fam.C. §914(c); see also Fam.C. §297.5 (¶3:18.1)]
- [3:8.6a] A bank’s cause of action for *unjust enrichment* based on its mistaken request for recordation of reconveyance of an unpaid trust deed on a borrower’s home was

[3:8.6b — 3:9.1]

subject to a *three-year* statute of limitations for an “action for relief on the ground of fraud or mistake” (CCP §338(d)) where the bank’s mistaken request resulted in loss of its security interest in the borrower’s property and its ability to foreclose on the trust deed upon default. [*FDIC v. Dintino* (2008) 167 CA4th 333, 346-348, 84 CR3d 38, 49-50]

- [3:8.6b] An action to enforce liability under the *Private Student Loan Collections Reform Act* (Civ.C. §1788.200 et seq.) must be brought within one year from the date of discovery by the plaintiff of the last violation, or, in the event of a default judgment against the debtor, one year from the date the borrower first received a writ, notice or order, whichever is later. [Civ.C. §1788.208(e); see *discussion at ¶12:343.10d*]

⇒ [3:8.7] **CAVEAT—Contracts shortening limitations period:** If you’re suing for a breach of contract or the liability otherwise arises out of a contractual relationship, carefully review the underlying contract to determine whether it provides for a *shortened statute of limitations*. [See *Soltani v. Western & Southern Life Ins. Co.* (9th Cir. 2001) 258 F3d 1038, 1042-1045—contract shortening statute of limitations for wrongful termination or unfair business practices actions to 6 months enforceable]

⇒ [3:8.8] **CAVEAT—Actions accrued and lapsed in other states:** A cause of action that arose in another state (or foreign country) and that is time-barred under the laws of that jurisdiction may *not* be maintained in California “*except* in favor of one who has been a citizen of this State, and who has held the cause of action from the time it accrued.” [CCP §361 (emphasis added); see *Cossmann v. DaimlerChrysler Corp.* (2003) 108 CA4th 370, 376-378, 133 CR2d 376, 380-382]

⇒ [3:9] **PRACTICE POINTER:** Many creditor claims will settle short of a lawsuit. But if the limitations period is about to run, suit should *always* be filed regardless of the status of debtor-creditor negotiations (thereby avoiding a potential malpractice claim for failure to file before the statute of limitations has lapsed). Creditors have *no* negotiating power in regard to “stale” claims (other than to report the claim as delinquent to credit bureaus). Once filed, there is still time to determine if an extrajudicial resolution is possible.

- (1) [3:9.1] **Written waiver of statute of limitations:** Debtors may agree in writing to *waive* the statute of limitations applicable to a claim against them (e.g., as part of a

guaranty agreement). Waivers signed *before* expiration of the limitations period may extend the time for filing suit for up to four years from the date of expiration of the limitations period. Waivers executed *after* the limitations period has run may extend the filing period for up to four years from the date the waiver was signed. (But waivers may be successively renewed for further four-year periods.) [See CCP §360.5; *California First Bank v. Braden* (1989) 216 CA3d 672, 676, 264 CR 820, 822]

(a) [3:9.2] **Effect on junior lienholders:** Waivers signed *before* expiration of the limitations period are binding on junior lienholders. [See *Kaichen's Metal Mart, Inc. v. Ferro Cast Co.* (1995) 33 CA4th 8, 15-16, 39 CR2d 233, 237—statute of limitations defense not available to junior lienholder after debtor timely forfeits same (junior lienholder stands in debtor's "shoes")]

➡ [3:9.3] **PRACTICE POINTER:** Review all pertinent documents (e.g., promissory notes, guaranties, leases, etc.) to see whether the debtor has agreed to extend the time for filing suit and, if so, for how long (up to four years, per CCP §360.5, subject to additional "renewed" four-year waivers).

- (2) [3:9.4] **Compare—tolling of statute:** The statute of limitations may be tolled where:
- Debtor is absent from the state. [See CCP §351; see ¶6:517 ff.]
 - Debtor in the military. [50 USC §3936; see ¶3:106.18]
 - Injunction or statutory prohibition applies. [CCP §356]
 - Debtor has filed for bankruptcy. Where the debtor files bankruptcy, the statute may be tolled by 11 USC §108(c), which extends the statutory deadlines for commencing or continuing civil actions against the debtor (or a Chapter 12 or 13 codebtor) until 30 days after notice of termination or expiration of the automatic stay (or codebtor stay) unless the time would expire later. [11 USC §108(c); *Kertesz v. Ostrovsky* (2004) 115 CA4th 369, 377-378, 8 CR3d 907, 914—creditors' commencement of new action on unpaid judgment was tolled by debtor's bankruptcy proceedings and resulting automatic stay; *Schumacher v. Worcester* (1997) 55 CA4th 376, 379-380, 64 CR2d 1, 3-4—automatic stay imposed upon landowner's bankruptcy filing extended limitations period for bondholder's foreclosure action by length of time stay in effect; but see *In re Gilman* (9th Cir. BAP 2019) 603 BR

[3:9.5 — 3:9.10]

437, 445—§108(c) did not extend state law deadline for creditors to request attorney fees incurred postpetition; *see further discussion at ¶6:530*

In addition, the bankruptcy discharge injunction (11 USC §524(a)(2)) has been found to trigger the CCP §356 limitations period suspension under CCP §356. [*In re Brown* (9th Cir. BAP 2019) 606 BR 40, 50]

(3) [3:9.5] **Expiration of CCP §337 limitations period bars future legal proceedings:** Where the limitations period has run under CCP §337 (*see ¶3:8.1, 3:406*), a person may not bring suit or initiate an arbitration or other legal proceeding to collect a debt. [CCP §337(d)]

(a) [3:9.6] **Exception—promise in writing by party to be charged:** The period in which an action may be commenced under CCP §337(a)-(c) can only be extended under state law pursuant to CCP §360. The period may be extended where a new acknowledgment or promise, in writing, is signed by the party to be charged. Payment made on a promissory note by the party to be charged, where the statute has not run, is a sufficient acknowledgment or promise of a continuing contract to stop, from time to time as payment is made, the running of time in which an action may be commenced. In the absence of such an agreement, no payment shall revive the cause of action once the limitations period has run. [CCP §§337(d), 360]

Cross-refer: For a comprehensive treatment of statutes of limitations, see Banke & Segal, *Cal. Prac. Guide: Civ. Pro. Before Trial—Statutes of Limitations* (TRG).

[3:9.7-9.9] *Reserved.*

e. [3:9.10] **Determine whether claim must be submitted to ADR prior to filing:** Creditor's counsel should review all applicable agreements and laws to determine whether some form of alternate dispute resolution (ADR) is required prior to filing suit. [See, e.g., Bus. & Prof.C. §6200 et seq. (mandatory prelawsuit arbitration of attorney-client fees/costs disputes if requested by client); CCP §1280 et seq. (contractual arbitration generally)] Most creditors will instruct counsel to sue on a claim subject to mandatory ADR so the case will either proceed by default or to force the debtor to petition the court to compel ADR; the debtor's failure to so move may constitute a waiver of the right to ADR.

Cross-refer: For a review of important statutes requiring some form of prelawsuit ADR, see Knight, Chernick, Quinn & Gupta, *Cal. Prac. Guide: Alternative Dispute Resolution* (TRG), Appendix A. See also Ch. 5 of that Practice Guide for a comprehensive discussion of contractual arbitration.

f. [3:10] **Determine whether claim should be assigned for collection:** Creditor's counsel should also determine whether the claim should be assigned for collection.

(1) [3:10.1] **Legal assignment defined; should be in writing:** “[An] assignment, to be effectual, must be a manifestation to another person by the owner of the right indicating his intention to transfer . . . the right to such other person, or to a third person.” [*Dameron Hosp. Ass'n v. AAA Northern Calif., Nev. & Utah Ins. Exchange* (2022) 77 CA5th 971, 989-990, 293 CR3d 129, 143 (internal quotes omitted)] (However, an equitable assignment is implied from the parties' conduct; *Dameron Hosp. Ass'n v. AAA No. Calif., Nev. & Utah Ins. Exchange*, supra, 77 CA5th at 990, 293 CR3d at 144.)

Although not required by statute, an assignment for collection should also be in writing.

- **FORM:** Creditor's Assignment of Claim, see *Form 3:A*.

(2) [3:11] **Effect:** Persons assigned claims for collection purposes are considered real parties in interest and may sue on the assigned claims notwithstanding their assignors' retained interest. [*National Reserve Co. of America v. Metropolitan Trust Co. of Calif.* (1941) 17 C2d 827, 831, 112 P2d 598, 601; *Fink v. Shemtov* (2012) 210 CA4th 599, 610, 148 CR3d 570, 578; see *Sprint Communications Co., L.P. v. APCC Services, Inc.* (2008) 554 US 269, 271, 128 S.Ct. 2531, 2533—assignee of legal claim for money has standing in federal court even where assignee promised to remit litigation proceeds to assignor]

Absent contrary intent, an assignment normally transfers to the assignee all related tort actions and includes, by operation of law, any guarantees on the debt. [See Civ.C. §1084; *National Reserve Co. of America v. Metropolitan Trust Co. of Calif.*, supra, 17 C2d at 832-833, 112 P2d at 601-602; *Champion Home Builders Co. v. Sipes* (1990) 219 CA3d 1415, 1423-1424, 269 CR 75, 79]

By the same token, an assignee generally acquires no greater rights than its assignor (*but see* ¶3:15.1 *ff.* re holders in due course). Thus, the assignment ordinarily is taken subject to any defenses the obligor had against the assignor prior to notice of the assignment. [*Great Western Bank v. Kong* (2001) 90 CA4th 28, 32, 108 CR2d 266, 268; *Royal Bank Export Finance Co., Ltd. v. Bestways Distributing Co.* (1991) 229 CA3d 764, 767-768, 280 CR 355, 357; and see Civ.C. §§1804.2, 2983.5 (retail installment and automobile sales contracts)]

⇒ [3:11.1] **PRACTICE POINTER:** Most collection agencies prefer to take accounts by assignment and sue in the agency's name. Carefully review the agreement between the creditor and the collection agency to ascertain if and when the account can be "recalled" by the creditor should the agency fail to collect the debt within an agreed time period.

- (a) [3:12] **Caution—assignment to co-obligor:** Where co-obligors share *primary* liability on a joint and several debt, assignment of the debt to one of them *extinguishes* the debt. [*Great Western Bank v. Kong* (2001) 90 CA4th 28, 32, 108 CR2d 266, 269—"the assignment amounts to payment"]

If the assigned debt has been reduced to judgment, the assignee/co-obligor may not sue the other obligors on the judgment. However, other remedies may be pursued—e.g., equitable contribution under Civ.C. §1432. [*Great Western Bank v. Kong*, *supra*, 90 CA4th at 33, 108 CR2d at 269; *see also* ¶12:765 *ff.*]

- (b) [3:13] **Caution—no assignment of claim resulting from identity theft:** The Fair Credit Reporting Act prohibits a creditor from selling, transferring for consideration or placing for collection a debt where a consumer reporting agency has notified the creditor that the debt has resulted from identity theft. [See 15 USC §1681m(f); *and* ¶2:342 *ff.*] Consequently, the agreement between creditor and counsel should set forth any representations the creditor made to counsel re notice of identity theft claims. The account should be properly flagged to avoid any subsequent sale or assignment.

(3) **Advantages of assignments**

- (a) [3:14] **Creditor anonymity:** An assignment for collection permits a collection suit to be brought in the name of someone other than the creditor-assignor. Attorneys, doctors and other professionals frequently assign claims for fees for this reason. Even so, while the name of the plaintiff will not reveal the creditor-assignor's identity, it should be set forth in the body of the complaint to establish standing for the plaintiff to bring the action. In any event, the identity of the original creditor cannot be concealed entirely and the creditor's testimony may be required at trial for foundational purposes.