Dealing with Debts in Collections

Part 1: The Facts

- Having a collection account on your credit report will have an extremely negative effect on your credit scores
- Paying off a collection account will temporarily hurt your credit score, as it is considered activity on a negative account.
- Having a collection with a $0 balance is better for your credit score than a collection account with a balance
- In the long run, paying off a collection account will be better for your scores
- Paying off a collection account will not remove it from your credit report, it will remain on your report with a $0 until the end of the 7 years from the date of collection
- Calling a collection agency or making a payment does not re-start the seven years that an account can be on your report

> According to the Fair Credit Reporting Act, negative entries can remain on your credit reports for 7 years, starting 6 months after the "Date of First Delinquency" (DOFD). The DOFD is the date a consumer first becomes late, never brings the account current, and then a charge off or collection ensues. Companies have 6 months to charge off or send to collections an account that is delinquent, which means a negative entry shouldn't remain on your credit reports for longer than 7 years and six months from the DOFD, or 7 years from the charge-off date. The confusion arises when consumers try to find their DOFD on their credit report and they get it confused with the Date of Last Activity (DOLA). The DOLA can be any transaction on an account, such as the most recent payment, the date the account was updated after a consumer dispute, or the date the account was sold to a collection agency or charged off.
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> To determine when an account will fall off your credit report, you need to identify either the DOFD (and add 7 ½ years) or the date submitted to collection by the original creditor (and add 7 years). You may be able to identify this on your credit report, or you may need to rely on your own records, as some collectors may report this information incorrectly, or not report it at all.

- When a collection account is no longer on your credit report, it does not mean you do not owe it. A collector can continue to try to collect until the debt is paid or negotiated.
- There are tax consequences to negotiating. Any debt or portion of a debt that is forgiven is considered taxable income in the eyes of the IRS. Creditors are required to report forgiven debts to the IRS if the amount forgiven is over $600. Debtors are required to report forgiven debts on their federal tax return (the debtor will receive a 1099-C). The Exceptions: Bankruptcy and part of Mortgage Forgiveness.
- If you have no way of paying or even negotiating your debt, and you want them to stop contacting you, you must write a letter to the debt collector telling them to do so. A phone call is not enough. The debt collector can contact you one more time to tell you they are going to stop contacting you or that they could or will take other action (such as a lawsuit).

Part 2: The Tips:
Dealing with collection accounts should only be done if cash flow is under control and all current obligations are being met. Follow the tips below to pay off as many collections as possible with the smallest amount of money out of your pocket and the most positive impact on your credit.

1. **Create a list of all collections including the following information:**
    - Original Creditor
    - Collection Agency
    - Amount Outstanding
    - Date the account was submitted to collections by the original creditor.

2. **Rank the collections in terms of urgency.** The order of priority will depend on the types of collection accounts you have. Some of the most effective ways to rank collection accounts are as follows:
    - **By the age of the accounts:** Lower priority should be given to collection accounts older than five years. They will be dropping off the credit report within two years regardless of payment status.
    - **By the amount owed:** With a set amount of money, you could pay down several small collection accounts or one large account. Having a smaller number of collection accounts with balances will result in a better credit score.
    - **By the types of accounts:**
        - High priority should be given to public records, such as tax liens, child support judgments and other judgments to avoid further legal issues.
        - High priority should be given to student loan collections to avoid wage and tax refund garnishment.
        - High priority should also be given to collection accounts that may prevent you from obtaining housing in the future, such as debts owed to apartment complexes, landlords or utility companies.
    - **By their collection status:** High priority should be given to accounts that are still with original creditor, but at risk of being sent to collections. Negotiating this before it is transferred to a collection agency would be beneficial in maintaining good credit.

3. **Try to avoid setting up a payment plan with a collection agency.**
A collection account is inherently negative. If you start to make ongoing payments, it may continue to get reported as recent activity on a negative account, prolonging the negative impact. ***The Exception: Student Loans.*** Many times a borrower's status can be returned to good standing by establishing a payment plan with the student loan collection agency and sticking to it.

4. **Collect a lump sum to offer as a settlement for each outstanding debt.**
If a collection debt balance is too large to pay off all at once consider the potential of:
    - Using an upcoming tax refund to settle the balance
    - Saving up for a few months and then offering a lump sum

5. **Contact the collection agency to negotiate a lump sum payment.**
Collection agencies will sometimes accept a reduced amount as payment in full. Making a first offer at about 33% of the actual outstanding debt can be a good place to start. (In the past, Foundation Communities clients have been able to settle for as little as 60% of the outstanding debt.)

- Never make or accept an offer that you cannot pay because you feel pressured to. You will only set yourself up for more problems by agreeing to pay an amount you can't really pay.
- Keep communications brief and to the point. Stay calm and professional.
- Keep record of all communications.
- ***Be sure they will accept that payment as "payment in full."***
- Things you should NOT do when negotiating with collection agencies
  - Do not let a collection agencies know how important or urgent it is to improve your credit.
  - Do not let Collection Agencies know if funds are available to pay the full amount.
  - Do not give them your bank information or pay by personal check. Mailing a money order or cashier's check is a good option.

6. Ask the Collection Agency to remove the account from your credit report.
The collection agency is *not* obligated to remove the account from the credit report until 7 years after the date of collection. Until then, this is another bargaining tool for them.

7. Before sending any payment, get the agreement in writing.
Ask the collection agency to send you written documentation, mailed, faxed, or e-mailed, of all actions and promises (i.e. accepting negotiated amount as payment in full, removing the account from the credit report) *before* sending a payment.

Part 3: Know your rights!
Research the Fair and Accurate Credit Transaction Act, the Fair Debt Collection Practices Act (www.ftc.gov) and the Texas Debt Collection Act (www.oag.state.tx.us)

Federal Laws – Collectors are prohibited from the following practices

- Debt collectors may contact other people in an effort to locate you (where you live, your telephone number, your employer). The debt collector may *not* disclose that you owe a debt nor may they contact the other person more than once unless they believe previously provided information was incorrect and that such person now has the correct information.
- Debt collectors cannot communicate by postcard or use an envelope or communication that indicates the communication is from a debt collector or related to the collection of a debt.
- If you inform a debt collector that the debt resulted from identity theft, the debt collector must inform the original creditor. At this point the creditor cannot sell the debt.
- Debt collectors can only call after 8 a.m. and before 9 p.m. (your time).
- Debt collectors cannot communicate with you at your place of employment if creditor knows that your employer prohibits such contact.
- Debt collectors cannot use threat of violence or other criminal means to harm your person, reputation or property
- Debt collectors cannot use obscene or profane language
- Debt collectors cannot cause the phone to ring or engage in telephone conversations repeatedly or continuously with intent to annoy, abuse or harass any person at the called number
- Debt collectors cannot give representation or implication that nonpayment of any debt will result in arrest or imprisonment or the seizure, garnishment, attachment, sale or property or wages unless lawful and the creditor intends to take such action.

Texas Law – In addition, collectors can not:

- In Texas, debt collectors can continue to charge interest on a collection account, up to the amount of interest that the original creditor was charging. However, many do not continue to charge interest.
- In Texas, a collection agency has a limited amount of time to sue you. A creditor (collection agency or not) can sue you for the amount you owe up to four years after the last payment was made.
- In Texas, the statute of limitations is four years. A creditor cannot sue you for the amount you owe more than four years after your most recent payment (different from the amount of time a collection account can be on your credit report).

If your rights are violated, file complaints with the Federal Trade Commission (www.ftc.gov) and the Attorney General's office (www.oag.state.tx.us).