

Zombie debt collectors dig up your old mistakes

There's a hot new growth industry: companies that buy bad debts for pennies and squeeze you to pay in flagrant violation of federal law. Here's how to get them off your back.

By [Liz Pulliam Weston](#)

Debbie made a mistake when she was in college.

As a student in Fort Worth, Texas, she maxed out a Citibank credit card with a \$300 limit and never paid the bill. Debbie said Citibank charged off the debt sometime between 1987 and 1989, and the liability has long since disappeared from her credit report.

Besides that, the statute of limitations -- the amount of time a creditor can sue over an old debt -- expired in the early 1990s. Both her old home state of Texas and her current state of California generally prohibit creditors from suing once a debt is more than four years old.

That's why she was stunned when a collection agency called her last summer, demanding she pay the 17-year-old bill. The calls have continued off and on since then, along with monthly bills listing varying amounts that the collection agency wants her to pay.

"The last time [they called], I told them the statute of limitations had run out on the debt and to stop harassing me," Debbie said. "They said it hadn't. I finally had to hang up on the man."

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There's money in old debt

A decade ago, most people who reneged on debts could rest easy after several years passed, since few creditors tried to collect on old bills, particularly for small amounts.

Today, however, collecting on old debts is a rapidly expanding industry. Aggressive companies can buy charged-off credit card accounts from the original lenders for pennies on the dollar. Then, they use credit scoring and other new technologies to identify which debtors are most likely to pay. The players in this "junk debt" market range from fly-by-night outfits to well-established companies funded by Wall Street investors.

It's a business that barely existed 10 years ago. In the last three years, it's been growing at a 30% annual rate, according to credit industry analyst Sean McVity of Keefe, Bruyette & Woods. Among the signs of the

industry's maturity:

- Four debt-buying companies have gone public in recent years, including Asset Acceptance of Warren, Mich., which had its \$150 million IPO in February.
- Some buyers have attracted major funding from investment banks such as Bear Stearns and Goldman Sachs.
- Last year, more than \$75 billion in old debts were sold.

The biggest debt buyers			
Debt buyer	Headquarters	2002 revenue	Debt purchased*
Sherman Financial Group	New York	\$325 million	\$7 billion
Risk Management Alternatives	Duluth, Ga.	\$295 million	Not available
Arrow Financial Services	Niles, Ill.	\$156 million	\$2.9 billion
Asset Acceptance	Warren, Mich.	\$101 million	\$5.2 billion
OSI Portfolio Services	Duluth, Ga.	\$100 million	\$3 billion

Figures are self-reported for 2002.

*"Debt purchased" is the face value of the accounts bought in 2002. Source: Credit & Collections World.

The amount that companies pay for bad debt depends on the type of account and its age. In general, McVity said:

- Debts that have recently been charged off: 6 to 7 cents on the dollar.
- Accounts that are slightly older and on which a collection agency or two has already taken a whack: 1.5 cents to 2 cents on the dollar.
- Years-old, out-of-statute debts: A penny or less.

A growing number of companies are discovering that these very old accounts, once thought to be uncollectible, are just the opposite. Squeezing even a small payment from these debtors can make collection activities worthwhile.

"The economics are pretty simple. For \$100 of (old debt), you pay 25 basis points -- a shiny quarter," said McVity, whose investment banking firm tracks debt-buying trends. "If you get (the debtor) to pay you \$1, you got your money and covered your costs."

Opportunity frequently turns into abuse

Where some are finding profits, though, others are spotting abuses. Consumer attorneys say the explosive growth of this industry has led to widespread violations of the federal Fair Credit Reporting Act and the

Fair Debt Collection Practices Act.

"I don't advocate people not paying their bills," said Shreveport, La., lawyer David Szwak, who specializes in consumer law. "But there's an element of the debt collections field that is rabid." Some collectors, he said, "will go to any lengths to harass people and defraud them."

Among the worst practices attorneys have seen:

- Suing or threatening to sue over debts even though the statute of limitations has long expired.
- Illegally "re-aging" debts on credit reports. The collectors tell credit bureaus that an old debt is, in fact, a new one. The goal: To extend the seven-year limit on reporting negative items and put more pressure on the consumer.
- Promising to delete a negative mark from the consumer's credit report in exchange for a token payment. Not only does the collector fail to follow through, but the payment can revive the statute of limitations and lead to a lawsuit. Even if the collector does back off, the unpaid debt could be sold to another company that might renew collection activity.
- Bait-and-switch credit cards. Some credit card companies have offered borrowers low-rate credit cards and then tacked old, charged-off debts -- often purchased from other lenders -- onto the balance. The card issuers typically insist they disclosed that the old debts would come with the cards, Szwak said, but the borrowers say no such disclosure was made.
- Verbally abusing and harassing consumers. My readers have reported being cursed, berated and called repeatedly despite requests to stop -- all violations of federal laws.

Mickey, a Virginia resident, said he was the target of "colorful words" when he told a collection agency to cease bothering him about an old debt. Mickey stopped paying on his \$4,000 Discover card balance in 1994; the account no longer appears on his credit report and the statute of limitations ended years ago.

"They would usually start out with a normal tone. . . . It went downhill fast," Mickey said. "They were calling a couple of times a day for awhile."

Sometimes, it's smarter just to hang up

Consumer advocates say this is exactly the kind of behavior Congress and state lawmakers were trying to prevent when they put curbs on collection behaviors such as statutes of limitations, the seven-year credit reporting limit and prohibitions against abusive collection practices.

"We don't have debtors' prisons," Szwak said. "We have laws to protect people from being harassed by debt collectors for the rest of their lives."

In fact, paying these old debts -- or even talking to the collection agency about them -- can make a bad situation worse.

As mentioned above, the smallest payment can revive the statute of limitations in some states, leading to more aggressive collections and lawsuits. Even acknowledging that the debt is yours can restart the clock in some jurisdictions.

That's why Robin Leonard, author of the "[Money Troubles: Legal Strategies to Cope with Your Debts](#)," advises consumers simply to put the phone down and walk away if collectors call about an out-of-statute debt. (This [chart at Bankrate.com](#) summarizes state statutes of limitations, but details can vary by state.)

Paying off can hurt your credit score

What's more, paying an old debt potentially can wreak havoc on a consumer's credit score. Such a payment can update a delinquency so that it looks more recent and takes a heavier toll on a credit score.

Paying the debt is also no guarantee that the nightmare will stop. The collector may decide that if you're willing to pay at all, you could be made to pay more. Settling a debt for a smaller amount than the collectors says you owe could result in another agency trying to collect the unpaid portion. Or the collector might inform the Internal Revenue Service (IRS) that you've received "income" in the form of forgiven debt. (Yes, there are tax consequences to forgiven debt. See my colleague Jeff Schnepfer's article "[5 truly nasty tax surprises](#).")

Even if you manage to wrangle written promises from the collector that none of the above will happen, you would have to be willing to go to court if the agency reneged -- and possibly face an unsympathetic judge or one who doesn't know much about collections law.

If you're being contacted about an old debt, here's what consumer attorneys advise:

Know the statute of limitations. If you racked up a debt in another state, you might want to check the statute of limitations there as well. But generally, it's the statute of your current state that applies. If the statute has expired, the collection agencies' legal remedies are limited.

Know your rights. Credit and debt collections can be an extremely complicated area of the law. Consider arming yourself with a book such as Leonard's "Money Troubles" and -- if the amounts at stake are considerable or the level of harassment unbearable -- consider contacting an attorney. The [National](#)

[Association of Consumer Advocates](#) can provide referrals.

Consider ignoring the call. If the statute of limitations has expired, Szwak said, put the phone down and walk away. There's little to gain and a lot to lose if you keep talking. You could inadvertently extend the statute of limitations or find yourself roped into a repayment agreement that might not be in your best interest. "The debt collector is a lot smarter than (consumers) are, a lot more savvy," he said. "They don't have any obligation to tell you your rights."

Write them. If ignoring them isn't working, consider writing a letter demanding the agency stop contacting you. Send it certified mail, return receipt requested. Federal law requires them to comply with your request. Make sure in the letter you specifically say that you aren't acknowledging you owe the debt.

Negotiate carefully. If the statute of limitations hasn't expired, you may want to negotiate a settlement rather than risk a lawsuit. (Again, a lawyer's advice could come in handy here.) Read "[12 tips for negotiating with debt collectors](#)."

Keep an eye on your credit report. If a collection agency tries to repost an old debt or lie about the date it went delinquent, you'll need to fight back vigorously. Dispute the entry with the credit bureaus and with the collection agency.

If the collector persists in its deception, you can demand that the collector produce a copy of the documentation that created the debt, such as the credit card agreement you originally signed, along with an account history, said consumer attorney Daniel Edelman of Chicago. Chances are the collector won't have this documentation, and continuing to report the account without providing proof that you owe the money is a violation of the [Fair Debt Collection Practices Act](#), Edelman said.

Again, an attorney experienced in debt collection law might prove helpful in particularly difficult cases.

Liz Pulliam Weston's column appears every Monday and Thursday, exclusively on MSN Money. She also answers reader questions in the [Your Money message board](#).

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