

Chapter-9 Recovery Strategies

Certificate in Payment Cards and Collections

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Chapter - 9 Recovery Strategies

9.1 Recovery

According to Wall Street Words "Recovery" is

- Obtaining, getting back, or vindication of a right or property by judgment or decree; especially : the obtaining of damages
- An amount awarded by or collected as a result of a judgment or decree

9.1.1 Know the Collection Laws

- When the banks are looking to collect delinquent accounts, banks must comply with laws governing collection practices including the Federal Trade Commission Act and the Fair Debt Collection Practices Act. These laws make it illegal to use unfair or deceptive practices to collect a debt.
- Many states also have their own laws governing collections. Banks have to speak with their attorney to find out the local regulations they need to comply with.
- Failing to comply with collections laws puts banks and their business at risk. For example, a debtor can sue the bank for libel or harassment, and perhaps collect more than he or she owes the bank in the first place.

Banks are prohibited by law from doing any of the following:

- Pretending to be someone they are not. For example, banks cannot claim to be a law enforcement official or imply that they are an attorney. Nor can they use a fake identity on letterhead.
- Sending out collection notices that look like official court summonses or documents. Collection letters should look like regular business letters, but can state that they are for overdue accounts. They cannot give the appearance of being authorized, issued, or approved by a government agency or attorney-at-law.
- Knowingly collecting, attempting to collect, or asserting a right to any collection fee, attorney fee, court cost, or other expense unless such charges are justly due. Bank's contract or terms must state the penalties they will charge for late payment. If they don't, they cannot make claims to these fees.
- Threatening to turn an account over to a collection agency or take legal action unless the bank plans to carry through. If bank do not take this kind of action in the usual course of their business, they cannot use it as a threat.
- Making repeated phone calls, or calling too early or too late. Generally, calling after 8 a.m. and before 9 p.m. is fine. Otherwise, it may be considered harassment.

- Attempting to ruin a debtor's reputation by telling others that the customer owes bank the money. This includes sending collection notices on a postcard that anyone can read, or putting anything on the outside of the envelope suggesting it is a collection notice. Banks also cannot communicate or threaten to communicate the nature of a consumer claim to a debtor's employer before obtaining final judgment against the debtor.
- Furnishing information about a debtor without permission, except to individuals and groups with a specific interest, such as credit reporting agencies, banks, and other creditors. Banks also cannot disclose or threaten to disclose information concerning a debt known to be disputed by the debtor without disclosing that fact.
- Using intimidation to collect. Banks cannot threaten violence, use abusive language, or visit a debtor and refuse to leave.

9.2 Collection Recovery

The objective of Collection is to proactively manage, control and reduce Net Credit Loss (NCL) to the Institution

What is Recovery?

Delinquent accounts are first worked by Collectors. After charge off it's worked by Recovery team and during this stage the account is blocked or closed.

Efforts are made to recover any payment out of the total balance.

Why Recovery?

Once an account is written off, balance is removed from the books and considered as Loss. However, the Net Credit loss takes into account the amount recovered post account getting written off. This therefore offsets part of the overall loss to the Institution or in other words, Recovery helps reduce the net loss

Hence,

$$\text{Net Credit Loss} = (\text{Write off} - \text{Recovered Amount})$$

For example Carolina has been regularly defaulting on her credit card payments. Her current account is 180 days past due and the total outstanding at this point was \$ 1510.00. This was uncollectible and was subsequently written off.

If Recovery was successful in collecting \$ 500.00 of the written off amount \$ 1510.00, the Net credit loss is reduced to \$ 1010.00 from \$ 1510.00. Or otherwise NCL in this case is equal to Gross Credit losses (written off or GCL) minus Recovery.

Recovery helps

- Recover Charged off amounts
- Ensures Optimum Utilization of Collectors / Attorneys

- Reduce NCL
- Minimizes Collection Expense

9.2.1 Stages of Recovery

Delinquent accounts are first touched by the Collectors. This can be field collectors or tele-callers. After charge off, they are worked by Recovery.

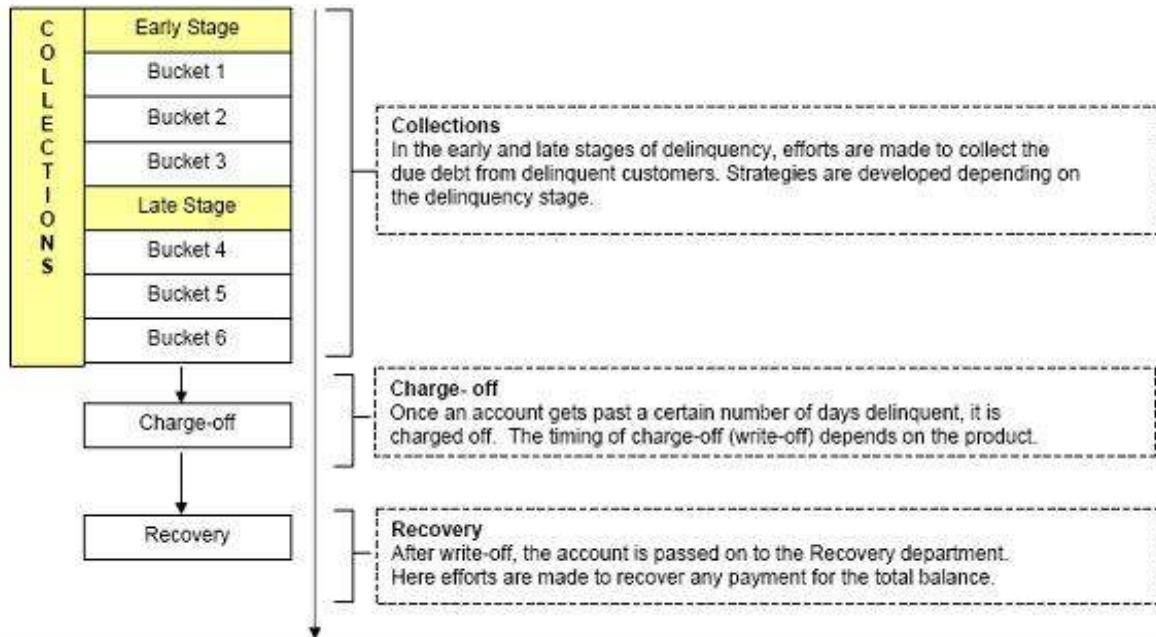


Figure 1 Stages of Recovery

Every institution will have their own ways of formulating the charge off balances based on certain criteria which is normally - "Days Past Due" or otherwise Days of outstanding or delinquency.

9.2.2 Collection Loss Recognition & Recovery

- If collections have been unsuccessful in obtaining debt, the recovery process is initiated. The recovery process varies depending on the product.
- Enclosed are the examples of action provided against different products in order to reduce NCL

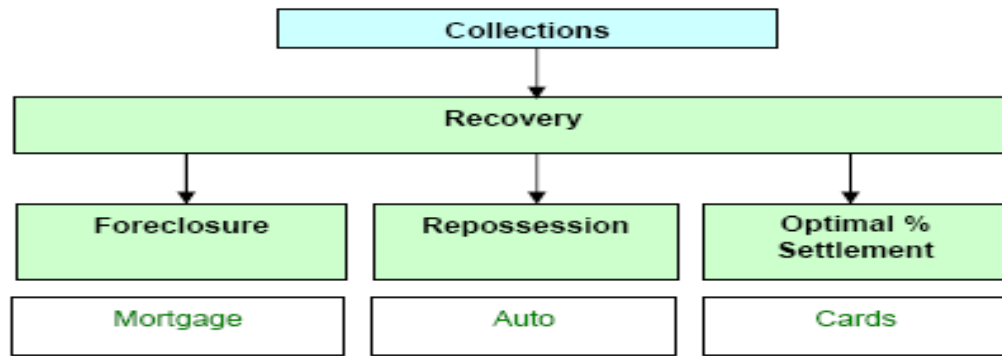


Figure 2 Recovery Action for Products

9.2.3 Recovery of Cards

- In unsecured portfolio, two main strategies are adopted throughout the delinquency period. In recovery stage, these strategies involve following types of tactics :
- Accounts are grouped according to similar characteristics :

Classification	Litigation : Segment of accounts with strong characteristics of successfully being litigated is sent to Litigation
	Recoveries : When there is a possibility of payments coming in from the customer with a recent history of payments, its kept inhouse for recovery collections.
	External Agency : These set of accounts have strong characteristics of paying an outside agency.

Figure 3 Classification of Accounts

- Depending on the type of delinquency of the class, a treatment follows to recover as much of the due amount.

Treatment	Program or Payment alternatives : An arrangement whereby the customer agrees to pay the balance over a certain period of time
	Settlement program : Program where the Bank writes off a partial amount and offers a payment program for rest of the amount, mutually agreed upon for certain period of time.

Figure 4 Treatment depending on the type of delinquency

9.2.4 Recovery- Outsourcing Collection

- Agency Supported activity for a specific period
- Runs based on Fee based or % age based agreement

Other activities carried out by them are:

- General Correspondence
- Dispute support and resolution

- Credit Bureau Disputes (CBU)
- Deceased Correspondence
- Exception mail



Figure 5 Recovery Strategies

9.2.5 Recovery- Asset Sale

An Asset sale is a recovery strategy used to minimize losses of *charged off products*. It involves the sale of *non-performing or under-performing assets* to an external agency when the Net present Value is higher than the anticipated future *cash flows*.

In these transactions the buyer can collect or further liquidate the pool of acquired accounts or loans. While seller might receive higher cash flow from the sale, he would have to forego all future cash flow value of the accounts.

Asset sales can be looked at to liquidate many assets that are in pre-charge off stage i.e. while in bucket 3/4/5/6.

The goals of Asset sale option for the Institution /bank is to:

- Minimize risk of uncertain future collections & maximize realization
- Avoid potential litigation
- Pre-empt & avoid Future negative publicity

When should companies resort to Asset Sales?

- Asset sales to be considered as a component and not a replacement for an overall recovery strategy

- Where there is a need for inventory management by optimizing Net liquidation of assets i.e. when there is an expected increase of expense in recovering assets over the long run. Constant re-evaluation of all charged off assets should be undertaken to incorporate changes in expenses, market pricing, & technology.
- Sale of under-performing assets should be attempted when the market offers a premium for the assets.

9.2.5.1 Inventory Management Strategies

Two common inventory management strategies under Asset Sales are:

1. One time Sales: To sell the debts that is greater than a period of time, say, 18-24 months. Reason being, selling older assets result in immediate financial benefit, and collection resources to be reallocated to more productive activities.
2. Recurring Sales: Resorted to when the volumes are sufficient. Proceeding collection practices are stable & price offered is greater than the discounted cash flow, a sample accounts are retained to benchmark agency performance, probably, a strategy adopted to get premium price from other agencies.

9.2.6 Recovery Strategies- Probate

What is Probate?

The review or testing of a will before a court of law to ensure that the will is authentic is termed as probate. It is the process by which an executor (if there is a will) or a court-appointed administrator (if there is not a will) manages and distributes a decedent's property.

9.3 In-house Recovery, Deceased and Legal Group

- Liaison between agency management, callbacks, and presidential unit and outside collection agencies to increase dollars collected
- Handle written and verbal inquiries from cardholder in a timely and accurate manner
- Handle incoming calls that have charged off
- Set up payment arrangements and/or offer settlements with cardholder or Authorized Third Parties to liquidate the account balance in the shortest amount of time
- Skip Trace - Help track the customer if whereabouts unknown
- Litigation Management support
 - Validate "To be Litigated Cases"
 - Disaster Check
 - Debtor admits full debt

- Ignores repeated follow ups by collector
 - Part admission
 - Contests full debt
 - Disputing debt as fraud / unknown
 - Delays or avoids legal procedures or debt payment
- Attorney Management & Support
 - Attorney Management Specialists
 - Attorney Financial Assistance
 - Attorney Media support
 - Legal Assistant

9.3.1 Deceased

Deceased is someone who is no longer alive. In property law, the alternate term decedent is generally used.

The deceased department works on such accounts; once it's determined that the customer is deceased. They might require little paperwork to carry out this process and may also pursue collections depending on the situation

It is important to know the laws and rights for the relatives of deceased. The joint account or add-on holder is legally responsible to settle the outstanding dues.

In case of death of a customer, the recovery strategies are applied

- Verify date of death with responsible parties
- Determine if there is an estate or asset equivalent
- If an estate, file proof of claim to Probate Court and follow up accordingly
- If no estate
 - Determine if payment will be in soon
 - If not enquire local tax reporting requirements

9.3.2 Legal Group

Activities carried out by legal group

- Collating data & carry out ground work to carry out Litigation
- Cases where Bankruptcy is filed, Legal helps collect maximum outstanding
- Liaison with Credit Counseling Group (CCG) or Debt Management Group
- Liaise with customer's Insurer
- Attorney checks and support to file a case

- Re-writing of case in case not favorable to the institution
- Dealing with the collection agencies
- Preparing of training modules and assistance to collectors in cases of difficulties / legal issue
- Legal support for Deceased in case of Probate

9.3.3 Recovery Strategies adopted by Legal

Legal Recovery

- In case account is identified for litigation the recovery strategies include
 - Pre Legal Phase (Prepare account for suit)
 - Pre Service Phase (attempt debt resolution)
 - Post Service Phase (attempt Debt resolution prior to obtaining judgment)
 - Post judgment Phase (Proceed with garnishment if permitted by local law-a court order permits an employer to deduct a portion of customer's salary & send it to lender as part of customer's payment)
 - Active Dormant Judgments

For unsecured products like cards, recovery involves continuing to work with customers on repayment options or pursuing legal remedies when the customer does not pay.

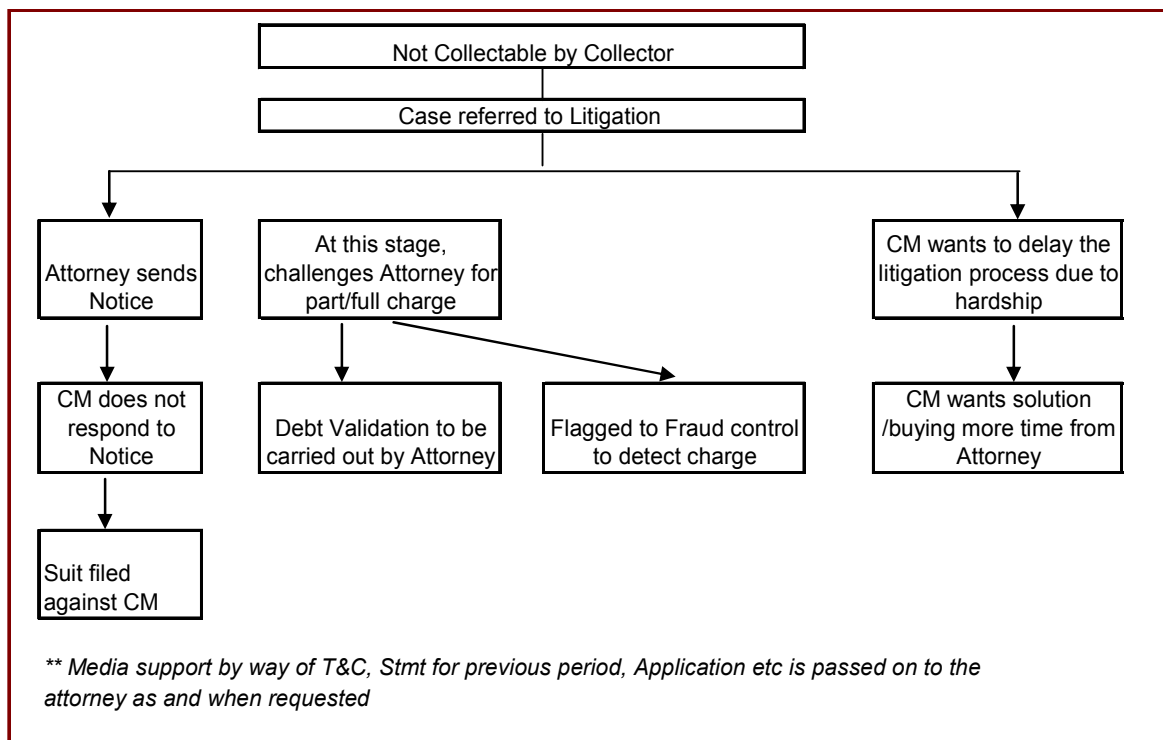


Figure 6 Litigation Process

9.4 Bankruptcy

What is Bankruptcy?

Bankruptcy is a legal declaration of inability to pay off debts over a reasonable period of time.

When bankruptcy is filed, the *debtor's* personal obligation to repay the *loan is discharged*.

If collateral is attached to the loan, the debt is not completely discharged and relevant action is taken to secure the collateral.

While bankruptcy cases are filed in United States Bankruptcy Court (units of the United States District Courts), and federal law governs procedure in bankruptcy cases, state laws are often applied when determining property rights.

For example, law governing the validity of liens or rules protecting certain property from creditors (known as exemptions), derive from state law. Because state law plays a major role in many bankruptcy cases, it is often unwise to generalize some bankruptcy issues across state lines.

Chapter 11 allows you to remain in possession of your assets, but a repayment schedule must be negotiated with creditors.

✓ **Bankruptcy in the United States**

- The following are the steps followed for Bankruptcy declaration process
 - The customer's attorney files bankruptcy & notifies the creditors
 - The creditors verify the filing information, account status and the collateral
 - The bank decides to protect the collateral & the loan is written off after 180 days past due
 - The bank places the account in the active bankruptcy status and all collection procedures are stopped
 - Court orders the bank to stop all collection activities regarding this customer
 - The bank meets the customer in the court of law

✓ **Bankruptcy & its Impact on Collections**

Collection works on obtaining the debt due from delinquent customers. When notification is received that a customer has filed bankruptcy, the collection process is affected in the following manner

- The court orders the bank to stop collection activities
- The account is kept in bankruptcy status
- System automatically stops all the invoices/ Statements
- All contacts with the customer will be stopped

- All unsecured loans, credit and charge cards must be written off in the month following the bankruptcy petition filed
- For loans with collateral, the write off timings vary
- These actions have direct impact on the bank by affecting the Net Credit Loss.
- When the customer files for bankruptcy protection any kind of account is no longer considered as receivable, this will form part of the total credit loss incurred by the bank.

Bankruptcy cases are typically referred to by the chapter under which the petition is filed.

These chapters are described below.

Chapter 7	Liquidation
Chapter 9	Reorganization for municipalities
Chapter 11, 12, 13	Reorganization
Chapter 15	Cross-border insolvency

Chapter 7: Liquidation

- Liquidation under a Chapter 7 filing is the most common form of bankruptcy.
- Liquidation involves the appointment of a trustee who collects the non-exempt property of the debtor, sells it and distributes the proceeds to the creditors. Because each state allows for debtors to keep essential property, most Chapter 7 cases are "no asset" cases, meaning the debtors keep all their property.

Chapter 9: Reorganization for municipalities

- Main article: Chapter 9, Title 11, United States Code
- A Chapter 9 bankruptcy is available only to municipalities. Chapter 9 is a form of reorganization, not liquidation. A famous example of a municipal bankruptcy was in Orange County, California.

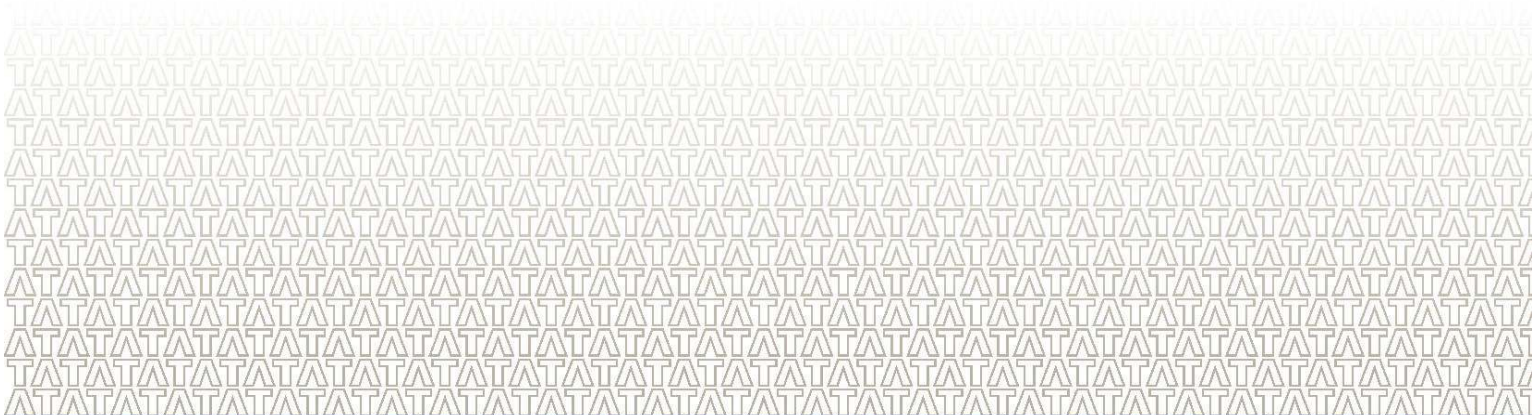
Chapters 11, 12, and 13: Reorganization

- Bankruptcy under Chapter 11, Chapter 12, or Chapter 13 is more complex reorganization and involves allowing the debtor to keep some or all of his or her property and to use future earnings to pay off creditors.
- Consumers usually file chapter 7 or chapter 13. Chapter 11 filings by individuals are allowed, but are rare.
- Chapter 12 is similar to Chapter 13 but is available only to "family farmers" and "family fisherman" in certain situations. Chapter 12 generally has more generous terms for debtors than a comparable

- Chapter 13 case would have been available. As recently as mid-2004 Chapter 12 was scheduled to expire, but in late 2004 it was renewed and made permanent.

Chapter 15: Cross-border insolvency

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 added Chapter 15 (as a replacement for section 304) and deals with cross-border insolvency: foreign companies with U.S. debts



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