CHAPTER 7: SPECIAL COLLECTIONS

7.1 INTRODUCTION

Although most borrowers fulfill their obligations, special collection efforts are sometimes required. This chapter describes the procedures for recovering unauthorized assistance; collecting debts owed the Agency due through administrative, salary and IRS offsets; and debt settlement.

It is the Agency's policy to collect unauthorized assistance, whether the assistance was received as a result of error or deception, unless any applicable Statute of Limitations has expired. Even if the error was made by Agency staff, the borrower is responsible for repaying the unauthorized amount. The Agency will provide assistance to help borrowers who received unauthorized assistance based on an error. Section 1 of this chapter provides instructions for identifying, investigating, and correcting instances of unauthorized assistance.

In the case of unauthorized assistance or any other debt owed the Agency, amounts owed to the Agency may be collected by offsetting payments due a borrower from Federal agencies including Internal Revenue Service (IRS) tax refunds and Federal employee salary and retirement payments. Section 2 of this chapter provides instructions for obtaining offsets of debt from these sources.

When all other collection attempts have failed, the Agency may elect to accept a portion of the remaining debt to settle and close the account. Debt settlement procedures are provided in Section 3.

SECTION 1: UNAUTHORIZED ASSISTANCE *[7 CFR 3550.164]*

7.2 OVERVIEW OF UNAUTHORIZED ASSISTANCE

The process used to collect unauthorized assistance differs depending upon the form of unauthorized assistance and whether it was received based on false information or an error.

Inaccurate information includes incorrect information inadvertently provided, used, or omitted without the intent to obtain benefits for which the borrower was not eligible. The error may be caused by the borrower, a third party, or the Agency; the source of the error is irrelevant. The Statute of Limitations for collecting unauthorized assistance as a result of inaccurate information is 6 years.

False information includes information that: (1) the borrower knew was incorrect or should have known was incorrect; and (2) was provided or omitted for the purpose of obtaining assistance for which the borrower was not eligible. If both false and inaccurate information was provided or omitted, the account is serviced as if the unauthorized assistance is solely the result of false information. A borrower is held accountable for false information provided by a third party if the borrower knew or should have known that the information provided was incorrect. The Statute of Limitations for collecting unauthorized assistance as a result of false information is 10 years.

A. Three Types of Unauthorized Assistance

1. Unauthorized Loan

Loans made to unqualified loan borrowers, written at the wrong interest rate, or made for an ineligible purpose are considered unauthorized assistance. Borrowers are not considered to have obtained unauthorized assistance if, due to inaccurate information, they obtained a loan despite inadequate payment ability, or received a program loan when private credit would have been available.

2. Unauthorized Subsidy

Subsidy received by a borrower for which they were not eligible. The Agency only seeks collection of the unauthorized assistance if the amount received is equal to or greater than $550, in which case the borrower must repay the full amount of unauthorized subsidy received.

Unauthorized assistance will not be pursued when an individual who is eligible for a same rates and terms assumption under HB-1-3550, Paragraph 13.14 B. has been occupying the security property, receiving subsidy based on their household income, and executes a same rates and terms assumption. As these cases are identified, the Unauthorized Assistance Unit will notify the individuals occupying the security property in writing that unauthorized assistance will be pursued unless an assumption agreement is signed within 90 days. A task will be sent to the Field Office informing them of the unauthorized assistance and a request to have the individuals execute a same rates and terms assumption. If the assumption is not executed within 90 days and the Field Office has not requested an extension to complete the processing of the assumption, collection of the unauthorized assistance will be pursued.

3. Unauthorized Grant

Grants made to unqualified borrowers, or for an ineligible purpose, are considered unauthorized assistance.

B. Consequences for borrowers

1. Assistance Based on False Information

Borrowers who obtained unauthorized assistance based on false information must pay off the loan and repay the subsidy within 30 days of the expiration of all appeal rights. A borrower who received a loan without being eligible, or the loan was approved for unauthorized purposes, must repay the outstanding loan balance.

A borrower who received unauthorized subsidy must repay the unauthorized amount in a lump sum. If the unauthorized subsidy is repaid within the required time frame, the loan may be continued. The borrower also may continue to receive payment subsidy for the authorized amount.

2. Assistance Based on Inaccurate Information

Borrowers who obtained unauthorized assistance based on inaccurate information also are required to correct the situation within 30 days of the expiration of all appeal rights. However, the Agency may permit the borrower to retain the loan, with some adjustments, and may assist borrowers who cannot repay delinquent amounts in a lump sum.

- **Loan to over-income borrowers**. If a Section 502 borrower's income was above the moderate-income level at loan approval or closing, the borrower must refinance with private credit, or the loan must be converted to a nonprogram loan. If a Section 504 borrower's income was above the very low-income level at loan approval or closing, the loan must be converted to a Section 502 loan.

- **Loan to ineligible borrowers.** If a borrower was not eligible for a loan, the Agency cannot continue the loan and must require that it be repaid within 30 days.

- **Loan to other borrowers.** The loan can be continued on existing terms if the loan was approved for unauthorized purposes, or the borrower's income was incorrect, but the borrower still qualified as income-eligible.

- **Loan at wrong interest rate.** If the wrong interest rate was used on the promissory note, the account must be adjusted using the correct interest rate.

- **Subsidy.** If a borrower received unauthorized subsidy based on inaccurate information, the borrower must repay the unauthorized amount.

Loans Made at the Wrong Interest Rates

If a loan was made at the wrong interest rate, but the borrower was granted subsidy at the correct interest rate, the unauthorized assistance is zero for the period of the subsidy agreement. The promissory note must be corrected to reflect the appropriate interest rate.

3. Unauthorized Grants

Borrowers who received an unauthorized Section 504 grant should correct the situation within 30 days of the expiration of all appeal rights, regardless of whether it was received based on false or inaccurate information. The grant borrower must repay it in a lump sum or execute a promissory note agreeing to convert the grant to a Section 504 loan to be repaid over time, unless the borrower does not have repayment ability.

If a borrower is unable to repay the unauthorized grant in a lump sum, the Centralized Servicing Center (CSC) should evaluate the borrower's current financial situation. If the borrower has repayment ability and agrees to repay the unauthorized assistance, CSC must execute *Form RD 1940-16, Promissory Note*. If the borrower has repayment ability but refuses to repay, CSC should document the information and seek a judgment on the account.

Best Practice

If the grant was greater than $2,500, seek the best lien obtainable to secure repayment.

7.3 IDENTIFYING AND INVESTIGATING CASES

The Agency may identify instances of unauthorized assistance through file reviews conducted by the CSC, referrals made by a Field Office or private citizen, or audits conducted by the Office of the Inspector General (OIG) of the United States Department of Agriculture. Suspected cases of unauthorized assistance must be investigated to determine whether unauthorized assistance was actually received.

Suspension or Debarment

CSC Servicers should recommend suspension or debarment when false information has been provided by the applicant. The National Office will decide whether to accept or reject the recommendation. The ultimate decision is made by an Administrative Law Judge.

If the case does not involve false information, CSC must conduct the investigation and document all actions and findings. Any case of unauthorized assistance that may be the result of false information must be referred to OIG. OIG also becomes involved in cases discovered during OIG audits. Whenever OIG is involved, all CSC actions are deferred until the OIG investigation is completed, or OIG declines to handle the case and refers it to CSC. If OIG chooses to handle a case, no further CSC involvement is necessary, unless OIG requests assistance.

In the investigation of cases involving false information, OIG or CSC must determine whether the borrower was aware of or should have been aware of false information submitted by a third party. Borrowers will not be penalized for false information submitted by a third party if they were not aware of the submission. In such a case, the account is serviced as if the unauthorized assistance is the result of inaccurate information.

OIG requires reports on the results of the investigation into any audit cases, regardless of whether the case is handled by OIG or the Agency. Cases involving grants or pending liquidation are not closed until the account is paid in full, otherwise satisfied, or liquidation is completed.

7.4 NOTIFICATION AND APPEALS AND ADMINISTRATIVE COST

A. Notify Borrower

CSC must notify the borrower of the determination that unauthorized assistance has been received, specifying in detail the reasons the assistance was found to be unauthorized, and the amount to be repaid. The borrower has 30 days to consult with CSC or to dispute the claim.

B. Borrower Consultation

The borrower should contact CSC if he or she wishes to review the claim with the Agency. During the consultation, CSC should outline the reasons the assistance is believed to be unauthorized and document the borrower's responses. If the borrower requests additional time to assemble documentation, CSC may grant an extension that is long enough to gather such information. The number of days granted for the extension must be documented so that the notice of determination is not sent before the extension has elapsed.

C. Notice of Determination

At the end of the 30-day consultation period and after any extension period has elapsed, CSC should notify the borrower of the final amount of assistance determined to be unauthorized, where to send the payment, servicing actions to be taken by the Agency, and the borrower's appeal rights. Servicing actions to recover unauthorized assistance cannot proceed until the 30-day period allowed to request an appeal has elapsed and any appeal that is filed has been concluded.

D. Administrative Cost

Borrowers who are contractually obligated will be assessed a $300 administrative cost plus any additional third party costs if the borrower fails to repay unauthorized assistance or enter into an Agency approved repayment plan to repay the lump sum amount within 30 days after the borrower's appeal expiration date or final appeal determination date.

7.5 DETERMINING THE AMOUNT DUE

A. Determine Correct Interest Rate

If the loan was made at the wrong interest rate, CSC must determine the rate that should have been used at the time the loan was made.

- For borrowers who were income-eligible at loan approval and closing, CSC should use the Agency interest rate in effect at the time of loan approval or closing, whichever is lower.

- For borrowers who were not income-eligible for a Section 502 loan at loan approval or closing, CSC should use the nonprogram interest rate in effect at the time of loan approval. Appendix 6 contains a list of historical nonprogram interest rates.

- For borrowers who were not income-eligible for a Section 504 loan or grant, CSC should use the program or nonprogram interest rate that would have been applicable at the time the loan or grant was made.

Consequences if a loan account adjustment results in delinquency:

In the case of false information:
- Borrower must repay in a lump sum; or
- CSC accelerates loan.

In the case of inaccurate information:
- Borrower may repay in a lump sum; or
- Borrower may consent to reamortizing the account; or
- CSC accelerates loan.

B. Determine Correct Subsidy Amount

The amount of subsidy borrowers were eligible to receive will be calculated based on the amount they were eligible for at the time the unauthorized assistance began, even if their eligibility has changed over time.

C. Reverse and Reapply Procedures

For unauthorized assistance resulting from payment subsidy, a fee may be established in accordance with Paragraph 7.6 B.2. For all other types of unauthorized assistance, borrower accounts must be adjusted retroactively to establish the amount of unauthorized assistance. This adjustment or fee amount calculation involves determining the amount paid by the borrower since the unauthorized assistance began and applying that amount to the monthly installments that should have been charged, as illustrated in Exhibit 7-1. This may create an account delinquency in the amount of the unauthorized assistance that must be repaid.

Exhibit 7-1

Reverse and Reapply Procedures

Mr. Smith received a loan in January 1996. An incorrect interest rate was used to calculate Mr. Smith's monthly payment and the error was not identified until April 1996. Due to the error, Mr. Smith was making $400 payments but should have been making $450 payments. The following illustrates how his monthly payments were applied to his account at the incorrect rate and the application of payments at the correct rate after the account adjustments were made.

Month	Incorrect Rate	Correct Rate
January	400	450
February	400	450
March	400	450
April	400	250
TOTAL	1,600	1,600

Mr. Smith's account is now $200 past due.

7.6 SERVICING ACTIONS

A. Assistance to Borrowers

The Agency offers no assistance to loan borrowers who obtained unauthorized assistance based on false information. If the borrower is unable or unwilling to make the required payment within 30 days of the expiration of all appeal rights, the loan will be accelerated.

If a borrower obtained unauthorized assistance based on inaccurate information and is unable to repay the amount due in a lump sum, the Agency will assist the borrower by reamortizing the loan to include the delinquent amount. If the borrower fails to authorize reamortization within 30 days of the expiration of all appeal rights, the loan will be accelerated. Any lump sum payments received after the account is accelerated will be handled in accordance with Paragraph 6.5 B.5.

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Original mortgage interest rate must be restored when loan is accelerated for borrowers protected by the Act.

B. Processing Changes to the Account

1. Change in Interest Rate

Any time an interest rate must be changed, *Form RD 1940-16* must be amended and the borrower must initial the change. Based upon State law, and with the advice of the Office of General Counsel (OGC), the real estate mortgage or deed of trust may also need to be amended. If a borrower fails to execute *Form RD 1940-16* or other required documents within 30 days, CSC should obtain advice from OGC and accelerate the account.

2. Change in Subsidy

If the current subsidy agreement is incorrect, CSC must reverify the borrower's income, following the procedures discussed in Chapter 4, unless the required information has been gathered during the course of the unauthorized assistance investigation. CSC should send *Form RD 3550-21* to the borrower. If the borrower fails to provide the required information within 30 days, the installment at the promissory note interest rate will be due.

The amount of unauthorized assistance will be established as a fee on the account. The fee will be placed on the primary loan. The fee will be due and payable within 30 days. If a lump sum payment is made, it will be applied against the fee.

3. Reamortization

If a borrower received unauthorized assistance based on inaccurate information and is unable to repay the unauthorized amount within 30 days, the account can be reamortized to include the unauthorized amount using *Form RD 3550-18, if the borrower occupies the property*. If the borrower fails to sign Form *RD 3550-18* within 30 days, the account will be accelerated. Escrow will be required at the time of reamortization if the borrower is delinquent on real estate taxes and insurance or does not have insurance.

C. Reactivating Satisfied Accounts

If a former borrower with a satisfied account is found to have received unauthorized subsidy, the account must be reopened so that the necessary account adjustments can be made. CSC should attempt to contact the former borrower using the last known address and phone number to inform them of the unauthorized subsidy and to request repayment. If the borrower agrees to repay, he or she should execute *Form RD 1940-16*. The new *Form RD 1940-16* should be written at the interest rate that had been used for the initial loan. The term should be as short as feasible, given the former borrower's ability to pay, but generally not more than 5 years. If the real estate mortgage or deed of trust had not been released, OGC should be consulted about any changes in the documents necessary to secure repayment.

If the borrower fails to repay the unauthorized subsidy, CSC should attempt to obtain financial information about the borrower. If the borrower has assets, CSC should seek a judgment to secure repayment. If financial information is not available or the borrower cannot be located, CSC should debt settle the unauthorized subsidy as described in Section 3 of this chapter.

If the Real Estate mortgage or Deed of Trust has been released and the amount of unauthorized assistance is less than **$550**, the unauthorized assistance will not be pursued.

SECTION 2: OFFSETS *[7 CFR 3550.210]*

7.7 OVERVIEW OF OFFSETS

Any money that is or may become payable to an Agency borrower or debtor from the United States may be subject to offsets for the collection of a debt owed to the Agency. This section discusses three types of offsets.

Through an ***administrative offset,*** the Agency may collect money, such as retirement benefits or a Farm Service Agency contract payment, that is or may become payable to a borrower from a Federal agency. Administrative offsets must be conducted in accordance with the procedures in 7 CFR Part 3, Subpart B.

Applicability to Debtors

Offsets may be used to collect debts owed by present borrowers and former borrowers (debtors). For simplicity, the term "borrower" is used rather than stating borrower or debtor each time a reference is made.

Salary offsets must be conducted in accordance with 7 CFR Part 3, Subpart C. The Agency may use a salary offset to collect a debt owed from a borrower's pay if the borrower works for a Federal agency, the United States Postal Service, the Postal Rate Commission, or is a member of the United States Armed Forces or military reserve, or any other persons covered in 7 CFR Part 3, Subpart C.

The Agency may offset a borrower's Federal tax refunds to collect a debt owed. ***IRS offsets*** must be conducted in accordance with the provisions of 31 U.S.C. 3720A and 31 CFR 285.2.

Administrative and salary offset may be used simultaneously to cure a debt. Although the IRS offset is the tool most commonly used by the Agency, it can only be used if the debt cannot be obtained through administrative or salary offset and cannot be used in conjunction with the other two types of offset.

7.8 ANNUAL REVIEW OF DELINQUENT ACCOUNTS

At least once a year, delinquent accounts should be screened to identify borrowers eligible for offset. Offsets will not be considered unless the account is delinquent by more than 2 monthly payments and the delinquent amount is at least $25. Offsets are not permitted when any of the circumstances listed below exist.

- The account is accelerated and collection of the debt through offset would jeopardize foreclosure litigation or reinstate the borrower's account. CSC should consult with OGC for guidance on pending foreclosure cases;
- The account is under the jurisdiction of a bankruptcy account or has been discharged in bankruptcy;
- The borrower received the loan before entering full time active duty in the military service and is still on active duty;
- The account is current under an approved adjustment, moratorium, or delinquency workout agreement, or the account has a suspend code that indicates a problem with the account; or
- The statute of limitations has expired.

7.9 SALARY AND ADMINISTRATIVE OFFSETS

If a borrower has salary or other income that can be offset, CSC must determine whether the offset is appropriate and, if an administrative or salary offset will not be pursued, document the reasons. If CSC plans to collect a debt through an administrative or salary offset, the borrower must be notified within 15 days of the determination.

A. Amount of Offsets

Payments effected by administrative offset are collected in a lump sum. If the borrower has multiple Agency loans, any amounts collected are applied based on the advantage to the Agency.

For salary offsets, a borrower's disposable pay, after taxes, is offset 15 percent each pay period. Disposable pay includes basic, special, incentive, retired, retainer, or other authorized pay. The dollar amount offset from a borrower's pay may change if income increases or decreases. The borrower may volunteer to have a larger amount deducted by submitting to CSC *Handbook Letter 103(3550), Agreement to Increase Salary Offset*. If the borrower has multiple Agency loans, amounts collected are applied to the accounts based on the advantage to the Agency.

B. Notifying the Borrower

Handbook Letter 104(3550), Notification of Salary Offset should be used to notify the borrower of a salary offset, and *Handbook Letter 105(3550), Notification of Administrative Offset* should be used to notify the borrower of an administrative offset. The notification letter must be sent by both regular and certified mail with a return receipt requested. The letter should state the nature and amount of the debt, the intended date of collection, the facts giving rise to the determination, and an explanation of the borrower's rights.

Time Frames

An offset must not take effect until 30 days after the borrower receives notice of the Agency's intent to use offset. Time frames begin once the borrower signs for the certified mail. If the certified mail receipt is not signed, the time frame begins on the date of nondelivery for salary offset and 10 days after the regular mail was sent for administrative offset.

The Agency is not required to provide notification before effecting an administrative offset if providing the notice would substantially affect the Government's ability to collect the debt. However, if the borrower was not previously notified, the borrower should be notified as soon as possible using *Handbook Letter 105(3550)*.

C. Borrower Response and Appeals

Borrowers may avoid having their salaries or other payments offset by paying the delinquency within 30 days. If the account has been accelerated the full amount owed must be paid. If the account has not been accelerated, the borrower must make a payment sufficient to bring the account current.

Borrowers have the right to obtain copies of their records, provide evidence against the claim, have a consultation with CSC, and appeal the decision. Borrowers must make all requests in writing. CSC should send a letter to advise the borrower of the decision for all requests made, unless the borrower's request was for copies of documents only. If the borrower's request is denied, the letter should state the reasons for the denial and the borrower's appeal rights. All decisions should be documented in MortgageServ.

Requests for Records

Borrower requests for copies of their records should be met as quickly as possible to enable the borrower to review documents, provide evidence to CSC, or to file a petition. Copying costs may be charged to the borrower's account.

1. Consultation with CSC and NAD Appeals

A borrower who has any questions concerning the determination of the offset may consult with CSC. As a result of the consultation, the borrower may request that CSC review additional documentation to refute of the determination. Borrowers must state in the request the reasons for the review. If the borrower needs additional time to assemble documentation, an extension may be granted for the amount of time the Servicer believes will be needed to gather such information. All reviews are based on written evidence, unless otherwise agreed upon by the Agency and borrower. Payments are not offset until the borrower is sent a letter about the Agency's decision.

The borrower may appeal a CSC adverse decision to the National Appeals Division (NAD) following the procedures described in Paragraph 1.9. If a borrower appeals to NAD, action on the offset is suspended until NAD has made a determination.

2. Delinquency Workout Agreement

If a borrower requests a delinquency workout agreement, the offer should be accepted if the amount offered is not less than the Agency would obtain from an offset. Extreme hardship or unfairness to the borrower due to the offset may be a consideration in the decision. If a borrower is exempted from offset because of extreme hardship or unfairness, CSC and the borrower must agree on a delinquency workout agreement, and the debt must have adequate security. Any decision to reject an offer for payment in lieu of a salary offset must be based on an analysis of the borrower's financial situation.

3. Debt Settlement

A debt settlement offer in lieu of offset may be considered only if the account has already been accelerated or the delinquency is owed by a former borrower with an inactive account. If a borrower requests debt settlement, the borrower should be informed of the application procedures for debt settlement, but action on the offset should not be delayed. Debt settlement procedures are provided in Section 3 of this chapter.

4. Petitioning for a Salary Offset Hearing or Administrative Offset Appeal

Borrowers who wish to request a hearing or appeal conducted by an Administrative Law Judge or other official not under the control of the Secretary of Agriculture must submit a petition to CSC within 30 days of the notification of salary and administrative offset. The borrower must state in the petition the reasons supporting the request and sign it. Petitions filed late are only accepted if the delay was beyond the borrower's control.

CSC may choose to provide a borrower who has requested a salary offset hearing the opportunity for a review of file documents in lieu of a salary offset hearing, if the matter can be solved more efficiently in this manner. The borrower must be notified of the acceptance or non-acceptance of a petition and the time and place of the hearing, if applicable. Accepted petitions stay the collection of the debt.

Final decisions should outline the facts of the case and provide a repayment schedule, if applicable. Decisions are made within 60 days of the request for a salary offset hearing and 30 days of the hearing for administrative offset.

D. Processing Offsets

Paying agencies must be provided written certification that the debtor owes the Agency a debt. The certification outlines the basis for the offset, amount, due date, and a confirmation that the Agency abided by the regulations for offsets. If proper certification is not provided to the paying agency, the request will be returned to CSC. Once CSC receives notice from the paying agency that the offset has been effected, CSC should credit the borrower's account in MortgageServ for the amount offset.

1. Administrative Offset

To request an administrative offset, CSC should send *Handbook Letter 106(3550), Request for Administrative Offset* to the appropriate Federal agency. CSC must cancel administrative offset requests by written notification to the paying agency once the borrower's account is brought current or otherwise satisfied. An agency may decline an administrative offset request if the offset would substantially interfere with or defeat the purposes of a program.

Paying agencies should be notified as soon as practical of debtors eligible for administrative offset so that the paying agency can flag the debtor's account. Early identification can help alleviate problems with collecting the debt under the statute of limitations. If at least 1 year has elapsed since the original administrative offset was requested from the paying agency, the debtor may offer a repayment plan in lieu of the offset.

2. Salary Offset

To request a salary offset, CSC should submit *Handbook Letter 107(3550), Request for Salary Offset* to the paying agency and attach *Handbook Letter 103(3550)* if the borrower has agreed to an offset of more than 15 percent of the borrower's salary. CSC must notify the paying agency by letter of the cancellation once the borrower's account is brought current or otherwise satisfied.

Generally, the paying agency will contact CSC if an employee is resigning or retiring before the debt is complete. However, if CSC becomes aware of the resignation or retirement, they should contact the paying agency immediately to secure repayment of the debt. CSC should inform the paying agency of the remaining amount of debt owed by the borrower and request the borrower's final salary payment and lump-sum leave to liquidate the debt. If the delinquency will not be resolved, CSC should instruct the paying agency to put a hold on the borrower's retirement funds in order to offset the remaining debt and should submit a claim to the next paying agency. If the borrower changes employers and salary offset is still a viable option, CSC should submit a claim to the next paying agency. In this situation, the Agency is not required to provide the borrower with additional notification.

7.10 IRS OFFSET

Since most borrowers pay taxes to the IRS, offsetting tax refunds is an effective tool for collecting amounts owed from a large number of borrowers and is the type of offset used most frequently by the Agency. However, since taxes are refunded only once a year and borrowers must receive at least a 60-day notice before affecting an offset, the Agency must adhere strictly to IRS deadlines. Borrowers who are in debt both prior to and post acceleration may be offset.

A. Amount of the Offset

Whenever possible, CSC should collect the amount equal to the debt. If this is not possible, CSC should collect the maximum amount of taxes and request an IRS offset again the following year. If an Agency borrower has multiple debts, the payment should be applied in the order the debts are accrued.

B. Processing

Each year, IRS provides CSC with a schedule for submitting preliminary and final lists of borrowers eligible for IRS offset. After MortgageServ screens borrower's accounts, CSC should submit to IRS a preliminary list of the borrowers eligible for offset.

Reporting Delinquencies to a Credit Bureau

It is especially important to report delinquencies to a credit bureau when requesting an IRS offset because the IRS will not offset a borrower's tax refund if the borrower has not been reported to a credit bureau.

Borrowers should be notified of the upcoming IRS offset using *Handbook Letter 108(3550), Notification of IRS Offset*. Borrowers have 60 days from the date of the letter to provide CSC with evidence against the determination in writing or to pay the delinquency. If the borrower provides documentation, CSC should determine whether offset will be exercised and send *Handbook Letter 109(3550), Confirmation of IRS Offset* advising the borrower of the decision.

If the documentation provided by the borrower demonstrates that the offset should not be used or should be for a lower amount, or if the borrower pays the amount owed, CSC should amend the list provided to IRS to reflect the changes. CSC must submit a final list of the borrowers eligible for offset to the IRS in accordance with the schedule provided by the IRS. Any revisions to the final list can only consist of removing borrowers from the list entirely or reducing the amount to be offset. Since an IRS offset cannot be canceled after the final request has been made, offset amounts that should not have been taken must be refunded to the borrower.

IRS notifies the borrower after his or her tax refunds have been offset. CSC will credit the borrower's account for the amount of the offset, less the IRS processing costs.

7.11 REFUNDS

Offsets received by the Agency in excess of the debt must be returned to the borrower. For administrative offsets only, the refund will include interest on the overpayment calculated at the 90-day treasury bill rate (Exhibit B of RD Instruction 440.1) within 45 days of determining that an overpayment was received.

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SECTION 3: DEBT SETTLEMENT

Debt settlement should be pursued when all other attempts to collect outstanding debt have failed. If the outstanding debt is secured, debt settlement cannot be pursued until the loan is accelerated or fully matured. If the outstanding debt is unsecured, debt settlement may be pursued at any time, whether or not it is due and payable. Settlement may be requested by the debtor or initiated by the Agency. Debt settlement, when complete, closes the debtor's account.

Debt settlement may take one of the following forms.

- **Compromise.** An agreement that permits the debtor to retain the security property and be released from further liability upon receipt of a specified lump sum that is less than the total amount due. In all instances a reasonable compromise offer is the most expedient and cost-effective method of settling the remaining balance on a debt.

- **Adjustment.** An agreement to release a debtor from liability, generally upon receipt of an initial lump sum and the promise of additional periodic payments over a period up to 5 years. The debtor is not permitted to retain the security property, except in cases of valueless liens.

- **Charge-off.** An action taken by the Agency when a compromise or adjustment cannot be negotiated, but the debtor is not to be released from liability.

- **Cancellation.** An action taken by the Agency to cease collection activities and release the debtor from personal liability for any remaining amounts owed.

Form RD 3550-20, Application for Settlement of Indebtedness, is used to process all four forms of debt settlement. However, CSC may enter into a verbal agreement for a compromise offer which will be documented on MortgageServ and confirmed by letter within 5 days to the borrower. The verbal agreement for the compromise should generally require payment within 30 days. Adjustment offers must always be documented on *Form RD 3550-20*. In addition, when the agency cancels debt without application, the basis for cancelling the debt will be documented on MortgageServ in lieu of a RD 3550-20.

7.12 COMPROMISE AND ADJUSTMENT OF DEBT [*7 CFR 3550.253]*

The Agency may agree to a compromise or adjustment for less than the debt owed and cancel the remaining debt. The debtor may request a compromise or adjustment by completing *Form RD 3550-20*. No payment should be accepted until an agreement has been approved; any payment submitted with *Form RD 3550-20* must be returned to the debtor.

Before accepting a compromise or adjustment offer, the Agency must establish that the offer represents the maximum amount the debtor is able to pay based on available financial information as described in Paragraph 7.15. The Agency will not agree to a compromise or an adjustment if there is doubt about a debtor's ability to pay that reduced amount.

A. Compromise

A compromise involves the acceptance of a lump-sum payment of less than the total amount owed and cancellation of the remaining debt. A debtor may retain the security property under a compromise offer if the compromise payment is at least equal to the net recovery value of the property and it is in the best interest of the Government.

B. Adjustment

An adjustment provides for payment of an initial lump sum representing the maximum amount the debtor can afford to pay and a new schedule of regular payments over the shortest period the debtor can afford, but no longer than 5 years. If the adjustment offer is for less than the full outstanding debt, any remaining balance is canceled once all payments under the adjustment agreement have been made. The debtor is not permitted to retain the security property, except in the case of a valueless lien.

When an adjustment offer is approved, CSC must establish an adjustment account, send regular billing statements, and archive any account balance in excess of the adjustment offer. In the event of a default on the agreement, the entire debt should be reinstated. The archived account balances should not be written off and reported to the IRS until the adjustment offer has been fulfilled or the entire remaining debt is canceled because the debtor has defaulted on the adjustment agreement.

A debtor whose adjustment account becomes past due should be contacted as soon as a payment is missed to determine their circumstances and to aggressively seek collection. Any account under an adjustment agreement that becomes past due should immediately be referred for offset, as described in Section 2 of this chapter.

Based on an analysis of the debtor's present circumstances, CSC may decide to modify the adjustment agreement. The Servicer may approve only one amendment to an adjustment agreement. Any further amendments must receive prior authorization from the next-level supervisor. If the adjustment agreement is modified, it must be documented on *Form RD 3550-20*, or in MortgageServ by CSC and confirmed by letter to the borrower.

If the debtor is unable or unwilling to repay the debt, CSC must notify the debtor, in writing, that the adjustment agreement is canceled and inform the debtor of all available appeal rights. If an adjustment agreement is canceled, payments made by the debtor prior to the cancellation are retained by the Agency.

7.13 CHARGE-OFF OF DEBT

A debt is charged off when a compromise or adjustment cannot be negotiated with a debtor, but available information indicates that the debtor is able to repay some part of the debt now or in the future. The Servicer should use *Form RD 3550-20* to charge off a debt.

A charge-off does not release the debtor from liability. Debtors whose debts have been charged off will be referred to Treasury for collection. If the Department of Treasury determines the debt is uncollectible and returns to the account to the Agency, the Agency will cancel the debt under paragraph 7.14. An account that has been charged off can be settled through a compromise, adjustment, or cancellation at any time. The debtor is not permitted to retain the security property, except in the case of a valueless lien or when the total debt against the secured property is $2,500 or less.

7.14 CANCELLATION OF DEBT

Debt will be canceled only if other means of debt settlement cannot be used and there is no security remaining and the available information indicates that the debtor is unable to repay any part of the debt and has no prospects of doing so in the future or if the security is remaining, the total debt against the secured property is $2,500 or less and the account has been accelerated. *Form RD 3550-20* is used to cancel a debt. If a cancellation is approved based on a review of the borrowers account without the submission of Form RD 3550-20, the decision will be documented in MortgageServ without use of the RD Form.

A. Application from Debtor

Upon application by the debtor, the debt may be canceled when there is no deficiency judgment or the debtor is unable to pay any part of the debt and has no reasonable prospects of doing so in the future.

B. No Application from Debtor

Without an application from the debtor, the debt may be canceled in any of the circumstances listed below.

- OGC has provided a written opinion indicating that the claim is not legally enforceable.
- The debt has been serviced by the Department of Treasury and returned to the Agency as uncollectible unless it can be documented that further monies can be collected (for example, if a debtor is due to receive an inheritance at a specific point in time). .

- The debtor is deceased, and there are no other known assets from which collection could be made if: (1) a final settlement has been made and confirmed by the probate court, and the Agency has received all the funds to which it is entitled; or (2) a final settlement has not been made and confirmed by the probate court, but there are no assets from which there is reasonable prospect of recovery.

- The debtor has been discharged from the debt through bankruptcy. Such debtors are not personally liable for the debt, and no attempt should be made to collect. However, if debts were discharged, but the debtor executed a new promise to pay prior to the discharge that was properly affirmed by the court, the debtor is liable for the debt and cancellation would not be appropriate.

- A judgment has been obtained, the Department of Justice (DOJ) file is closed, and:

  ◊ The debtor has no known assets or future debt-paying ability, has disappeared and cannot be found without undue expense, and there is no existing security for the debt; or

  ◊ Three years have elapsed since any collections were made on the judgment and the debtor has no equity in the subject property.

- A property sold at a foreclosure sale does not generate sufficient proceeds to satisfy the outstanding debt, deficiency judgment was obtained, and OGC has advised that no further collection efforts may be pursued.

- Based on a review of the debtor's case file and other available information, the debtor is unable to pay any part of the debt and has no reasonable prospects of doing so in the future. The decision will be thoroughly documented in the MortgageServ system.

7.15 NEGOTIATING A SETTLEMENT

Settlements must be negotiated consistently to avoid disparate treatment. If a living debtor is unable to act, an offer of debt settlement may be made by a party having legal authority to act for the debtor.

A. Assessing the Debtor's Financial Condition

CSC must assess the financial condition of the debtor before negotiating a settlement. Only the financial situation of signatories to the note and any cosigners should be considered, except in common property States. The Servicer should consider the following factors in evaluating offers:

- Prior liens against the security;
- Value of the existing security, as determined by a current appraisal;
- Debtor's equity in assets not pledged as security for the Agency debt;
- Debtor's total present income and probable income over the next 5 years, including any possible inheritances; and
- Amount of other debt.

This information can be obtained from *Form RD 3550-20* which includes a section on household expenses and provides a formula by which the amount of income available for debt payments can be established. *Form RD 3550-20* may be completed either by the debtor, by CSC (in the absence of the debtor), or as a joint effort between CSC and the debtor.

Once *Form RD 3550-20* has been completed, CSC should send a letter requesting that the debtor submit additional information within 30 days, so that their financial situation can be verified. CSC should review the following information as part of the financial assessment:

- Verification of income such as paystubs or copies of Social Security checks;

* Debtors' expense verifications such as medical expenses;

* Tax returns and bank statements;

* County records, such as personal property tax rolls, to determine what other assets the debtor has or may have recently disposed of; and

* Department of Labor wage information, where available.

Some of this information may already be available if there has been a recent subsidy renewal. If additional verifications are needed, they should be conducted in accordance with the policies described in Chapter 4. Any costs involved in obtaining the needed financial information are charged to the debtor's account. Credit reports will only be obtained if there is reason to believe the debtor has not provided complete and accurate financial information.

* If a compromise, adjustment, or cancellation agreement is to be reached with one of several joint debtors because the other parties will not or cannot join the application, the Servicer must document the reasons the other parties are not included on *Form RD 3550-20* in order to justify settlement with those joint debtors. Joint debtors can not be included on the application if they are deceased, discharged in bankruptcy, or have disappeared.

B. Special Case Debtors

1. Deceased Debtors

An offer to settle the debt of a deceased debtor may be made by a duly-appointed executor or administrator. Claims against estates are to be settled based on the value of the security property and the expected value of the estate after paying expenses that have priority over Agency claims, such as the cost of administration, allowances of minor children and/or surviving spouse, allowable funeral expenses, and dower or curtsey rights.

2. Debtors Who Have Disappeared

Before charging off or cancelling the debt of a debtor who has disappeared, reasonable efforts must be made to locate the debtor. Such efforts generally include contact with Post Offices, motor vehicle licensing authorities, telephone or city directories, utility companies, local, State, and other Federal Government agencies (such as Health and Human Services and the Department of Labor), known relatives and friends, former neighbors and employers, the children's schools, skip-tracing agencies, and the Social Security Administration. Efforts to locate the debtor must be thoroughly documented.

3. Settlement Where Debtor Owes More Than One Type of Agency Loan [7 CFR 3550.252(c)]

A loan on a property should not be settled while other USDA Agency (such as FSA) loans on the same security property remain active, unless settlement is in the best interest of the Government.

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7.16 PROCESSING DEBT SETTLEMENTS

A. Escrow and Unapplied Funds *[7 CFR 3550.252(h)]*

Escrow disbursements continue until debt settlement is complete or the Agency no longer has a security interest in the property. All remaining funds held in escrow or unapplied when the debt is settled will be applied against the debt.

B. Approved Settlements

Once a settlement has been approved, CSC must take the following actions.

* Execute *Form RD 3550-20.*

* Notify the debtor, in writing, that a settlement offer has been approved. The notification should outline the specific terms and conditions of the settlement and *Form RD 3550-20* should be attached.

* In the case of a cancellation that has not been requested by the debtor, notify the debtor that the debt has been canceled.

* In the case of a compromise, adjustment, or cancellation, cancel the offset by notifying the paying agencies that have been contacted for offset.

C. Rejected Settlements

When a settlement offer is rejected, CSC must document the reasons for rejection on *Form RD 3550-20* and execute the form. The debtor must be notified, in writing, of the reasons that his or her settlement offer has been rejected and must be informed of their appeal rights. The original form should be sent to the Field Office for filing in the debtor's case file and a copy should be attached to the debtor's settlement rejection letter.

D. Notify the IRS and Credit Agencies *[7 CFR 3550.252(e)]*

In accordance with the requirements of the IRS, CSC must report to the IRS debts that have been settled. *IRS Form 1099-C, Cancellation of Debt* is used to report any debt (principal balance and any administrative costs) settled through cancellation, compromise, or adjustment. After reporting the debt to the IRS, no further efforts to collect the debt should be made. Credit reporting agencies also must be notified of debt settlement actions.

7.17 DISPOSITION OF PROMISSORY NOTES AND RELEASE OF SECURITY INSTRUMENTS

When the debt is satisfied through any of the debt settlement mechanisms, CSC must generate the appropriate satisfaction and/or release letter and send the original hard copy to the Field Office.

If the debtor requested the settlement, the Field Office should indicate on the note the method by which it was satisfied and return it to the debtor, along with the satisfaction and/or release letter and the mortgage.

If the debtor did not request settlement and the Agency chooses to cancel the debt, the satisfaction letter should be sent to the Field Office and retained in the debtor's case file. In cases of cancellation or chargeoff, the note will not be returned to the debtor.