Overview

An agency has the affirmative responsibility to try to collect delinquent debts that are owed to the agency, or referred to the agency for collection. However, at some point in the collection process it may become evident that a debt is "uncollectible," and it may be appropriate to **terminate collection action, and/or write-off the debt.**

An agency fulfills its affirmative responsibility to try to collect delinquent debts by engaging in "active collection." "Active collection" means that the debt is being collected through the use of all appropriate debt collection remedies, including, but not limited to, demand letters, credit bureau reporting, offset, garnishment, foreclosure, litigation, and referral to the Department of the Treasury's (Treasury) Bureau of Fiscal Service (Fiscal Service) for collection (known as cross-servicing). See Chapter 6, Delinquent Debt Collection.

Termination of collection action occurs when "it appears [to an agency] that no person liable on the claim has the present or prospective ability to pay a significant amount of the claim or the cost of collecting the claim is likely to be more than the amount recovered." See 31 U.S.C. § 3711(a)(3). **Termination of collection action** is a decision to cease **active collection** action on a debt, in accordance with criteria set out in the Federal Claims Collection Standards, because such action is not economically worthwhile or is otherwise inappropriate. **Suspension of collection action** occurs when an agency decides to temporarily cease collection action.

Once an agency terminates collection action, it may pursue passive collection activities to try to collect the debt. "Passive collection" means that the debt is no longer being actively collected; that is, the debt remains secured by a judgment lien or other lien interest, has not been removed from the Treasury Offset Program (TOP) or is otherwise being collected by offset, and/or is scheduled for future sale.

Except for agencies with independent statutory authority to terminate collection activity on its own debts, Department of Justice

(DOJ) concurrence is required before an agency terminates or suspends **active collection** on a debt over $100,000 (principal only). DOJ has delegated to Fiscal Service the authority to approve termination of collection action on a debt with a principal amount of $500,000 or less when the debt is being serviced by Fiscal Service in its Cross-Servicing Program.

Write-off of a debt is an accounting action that results in reporting the debt/receivable as having no value on the agency's financial and management reports. The agency does not need DOJ approval to write-off a debt since the agency is only adjusting its accounting records. Generally, write-off is mandatory for debts delinquent more than two years, unless documented and justified to the Office of Management and Budget (OMB) in consultation with Treasury. However, in those cases where material collections can be documented to occur after two years, debt cannot be written off until the estimated collections become immaterial. See OMB Circular No. A-129, Section V.5.

Currently Not Collectible (CNC) and close-out are classifications for writing-off the debt that indicate whether or not the agency will continue debt collection actions after write-off. See OMB Circular No. A-129, Section V.5. At the time of write-off, an agency should classify the debt as CNC when it intends to continue cost effective debt collection action. An agency **closes out** a debt when it determines that further debt collection actions are prohibited (for example, a debtor is released from liability in bankruptcy) or the agency does not plan to take **any** future actions (either active or passive) to try to collect the debt.

When a debt is classified as closed-out, an agency must determine if the amount due on the debt should be reported to the Internal Revenue Service (IRS) as potential income to the debtor under Section 6050P of the Internal Revenue Code (26 U.S.C. § 6050P). An agency reports such debts to the IRS using IRS Form 1099-C.

The program decision to terminate collection action and the accounting decision to write-off a debt often coincide. For example, an agency that refers debts to Fiscal Service for cross-servicing normally should take concurrent actions to terminate collection action, write-off the debt and classify it as CNC when:

- the agency is notified by Fiscal Service that active collection action is no longer being taken through cross-servicing; and

- the debt will remain in TOP.

Similarly, an agency should terminate collection action, write-off the debt, and classify it as close-out when the debt is discharged in bankruptcy, and there are no other debtors from whom collection can be sought. **However, agencies should be aware that the determinations to terminate collection action and to write-off a debt are made for different reasons, and where appropriate and consistent with the agency's debt collection strategy for a particular class of debts, may be made at different times.**

The following charts provide some basic information concerning termination of collection action, write-off, and the classification of debts as CNC and close-out.

Debt Collection Process Action

	Description	Authority	Timing	Comment
TERMINATION/ SUSPENSION OF COLLECTION ACTION	<u>Termination</u>: Agency stops all **active** debt collection action; may continue **passive** collection action. <u>Suspension:</u> Agency is likely to resume **active** collection action at a future time.	31 USC 3711(a)(3); 31 CFR Part 903	Not tied to write-off, but must occur before close-out.	Agency decision to terminate/suspend must comply with Federal Claims Collection Standards (31 CFR Part 903). DOJ concurrence required for debts over $100,000.

Accounting Action

	Description	Authority	Timing	Comment
WRITE-OFF	Agency reports debt as having no value on financial and management reports.	OMB Circular No. A-129	Usually no later than 2 years after debt delinquency; not tied to termination or suspension.	At time of write-off, agency must classify the debt as CNC or close-out.
CURRENTLY NOT COLLECTIBLE (CNC)	A classification after write-off when the agency has determined that debt collection efforts should continue.	OMB Circular No. A-129	Can only occur at the time the debt is written-off.	CNC classification does not affect agencies' statutory and regulatory responsibilities to pursue debt collection.
CLOSE-OUT	A classification after write-off when the agency has determined that no further active or passive debt collection action will be taken.	OMB Circular No. A-129	Must occur after write-off and termination of collection action; can occur after CNC classification, if debt was initially classified as CNC at time of write-off.	Agency will not take any collection action after closeout; if required by Internal Revenue Code and regulations, agency must report closed-out debt to IRS on Form 1099-C as potential income to the debtor.

Termination of Collection Action Criteria

An agency should terminate active collection when one or more of the following criteria apply:

1. **The agency is unable to collect any substantial amount through its own efforts or through the efforts of others.** The following items detail factors an agency should consider in determining the likelihood of recovering a substantial amount of a debt:

    - **the results of previous collection action taken by the agency**. A good indication that the debt is uncollectible is the return of a debt by a private collection agency or from Fiscal Service's Cross-Servicing Program without collection and with the recommendation for write-off, or the inability of DOJ to collect on a judgment.

- **the present and future financial condition of the debtor, taking such factors into account as assets and liabilities (as verified by a credit bureau report or a current financial statement), employment history and potential for future earnings, and inheritance prospects**. See Chapter 6, Delinquent Debt Collection, Installment Payments, page 6-20. In some circumstances, the debtor's future financial prospects may warrant suspension rather than termination of collection action. See page 7-10 of this Chapter.

- **the debtor's age and health, including disability status**. If the debtor is deceased, the agency should file a claim against the debtor's estate for liquidation of the debt at the time the estate is settled and all assets disposed.

- **the assets available for liquidation, including the possibility that assets were fraudulently transferred or concealed to avoid liquidation**. Agency personnel should consult with agency counsel regarding fraudulent transfers or concealments.

- **any state law restriction that applies, in the absence of Federal law, to collections taken within a state's borders**. Where a debtor is employed in a state that prohibits wage garnishment, an agency should consider the use of administrative wage garnishment under the Debt Collection Improvement Act of 1996 (DCIA), which authorizes wage garnishment notwithstanding state law. See Chapter 6, Delinquent Debt Collection.

2. **<u>The agency is unable to locate the debtor.</u>** The agency should attempt to locate the debtor using available sources

as described in Chapter 6, Delinquent Debt Collection, pages 6-71 through 6-73.

3. **Costs of collection are anticipated to exceed the amount recoverable.** An agency should not spend more to recover a debt than what is owed, unless a significant enforcement principle is at stake. For example, an agency should not spend $200 to collect a $100 debt. The agency's collection strategy should dictate what is reasonable in determining the costs and benefits of continuing enforced collection efforts. The items below contain factors the agency should consider when balancing the costs of collection against probable recoveries.

- **The amount of any fees associated with using a particular collection tool**. For most collection tools, such as Fiscal Service's Cross-Servicing Program, TOP, and private collection agencies, the agency will not pay a fee unless there are collections. In many cases, the agency may recover fees by adding these costs to the debt.

- **Agency expenses associated with the time and resources required to prepare and follow-up on a debt**. Costs may be minimal when most of the expenses are associated with operating an automated system for tracking account activity.

- **The agency's "success" rates for the available debt collection tools**. If a given tool has not been used successfully to collect a particular type of debt, then it may not be appropriate for the agency to require the use of that tool prior to termination, unless use of the tool is mandated by law.

- **The probability that the agency will be able to recover its collection costs.**

- **The need to pursue collection when a significant enforcement principle is at stake**.

4. **<u>The debt is legally without merit or enforcement of the debt is barred by applicable statute of limitations.</u>** A debt that is legally without merit is one that was never owed in the first place and should not have been classified as a debt. For example, a court determines that the agency's interpretation of a statute was incorrect and should not have resulted in a receivable to the agency. For purposes of receivables reporting on the Treasury Report on Receivables Due from the Public, the agency would "reclassify" the amount.

   An agency should not terminate debt collection activity based solely on the expiration of the statute of limitations for initiation of a lawsuit. An agency should consider the availability of other debt collection remedies that may not yet be time-barred, such as offset and administrative wage garnishment. For information on statute of limitations, see Chapter 6, Delinquent Debt Collection, page 6-61.

5. **<u>The debt cannot be substantiated.</u>** The agency does not or cannot produce the evidence, witnesses, or supporting documentation necessary to validate the debt and was not able to obtain a voluntary repayment of the debt. For example, the debtor signed a repayment agreement, but the agency cannot locate it in its files, has no record that the debtor ever agreed that the debt was owed, and the debtor refuses to repay or compromise the debt.

6. **<u>The debt against the debtor has been discharged in bankruptcy.</u>** The filing of a petition for bankruptcy is a clear sign that the debtor is either unable or unwilling to repay his/her debts; this by itself often justifies termination of collection action. All collection activity outside the bankruptcy process must cease upon the debtor's filing of a bankruptcy petition, except as allowed by law or by the bankruptcy court. The agency can, concurrently with terminating active collection, take action to protect its

interests by filing a proof of claim with the bankruptcy court. However, an agency may determine that monies to repay the debt are available through the bankruptcy process. An agency should consult with its agency counsel to determine this. See Chapter 6, Delinquent Debt Collection, page 6-57. For example, the agency may be able to pursue collection on payments provided under a bankruptcy reorganization plan, or may be able to obtain the court's permission to continue a foreclosure action.

In general, an agency shall terminate collection activity on a debt that has been discharged in bankruptcy, regardless of the amount, where there are no other debtors or guarantors from whom collection may be sought. However, if payments to the agency are provided for under a plan of reorganization, an agency may continue collection activity regarding those payments, subject to the provisions of the Bankruptcy Code. Offset and recoupment rights may survive discharge of the debtor in bankruptcy and under some circumstances, debts also may survive discharge. Agency personnel should seek legal advice from the agency's counsel to determine whether the agency's debts have survived a debtor's discharge.

Exception to Termination of Collection Activity. When a significant enforcement policy is involved, or recovery of a judgment is a prerequisite to the imposition of administrative sanctions, agencies may refer debts for further collection action, including litigation, even though termination of collection activity may otherwise be appropriate. Before terminating collection activity, the agency should have pursued all appropriate means of collection and determined, based upon the results of the collection activity, that the debt is uncollectible. Termination of collection activity ceases active collection of the debt. The termination of collection activity does not preclude the agency from retaining a record of the debt for purposes of:

- selling the debt, if, in consultation with or at the request of the agency, the Secretary of the Treasury determines that such a sale is in the best interest of the United States;

- pursuing collection at a subsequent date in the event there is a change in the debtor's status or a new collection tool becomes available;
- offsetting against future income or assets not available at the time of termination of collection activity; or
- screening future government loan applicants for prior indebtedness.

Agency procedures should require that terminating collection action of progressively higher dollar amounts be authorized by progressively higher-level agency officials. These procedures should also require that the signatures of all agency officials participating or concurring in each termination of collection action decision be obtained before the action is taken.

DOJ Concurrence for Terminating Collection Action

Each agency determines when it will terminate collection action on its debts in accordance with governmentwide policy, its own regulations, authorities, and debt collection strategy. Each agency is authorized to terminate active collection on debts with principal amounts of $100,000 or less. An agency may terminate active collection on debts with principal amounts in excess of $100,000 only with the concurrence of DOJ, unless the agency has its own statutory authority for terminating collection action. If the principal amount of the debt is $500,000 or less, and the debt has been serviced by Fiscal Service in its Cross-Servicing Program, Fiscal Service may approve the termination of collection action.

If DOJ concurrence is necessary, an agency should make every effort to request such concurrence at least one year before the expiration of the applicable statute of limitations for collection litigation. DOJ concurrence is requested by submitting a completed Claims Collection Litigation Report to the Department of Justice, Civil Division, Commercial Litigation Branch, 1100 L Street NW, Room 10057,

Washington, D.C., 20530. The Claims Collection Litigation Report instructions can be found at: *http://www.justice.gov/sites/default/files/jmd/pages/attachments/2014/12/12/cclr_instructions.pdf.*
and the form at: *http://www.justice.gov/sites/default/files/jmd/legacy/2014/05/26/cclr-form-fillable.pdf.*

As a practical matter, the agency does not need to request concurrence from DOJ for termination of collection action if:

- the agency referred the debt to DOJ for litigation and DOJ returned the debt to the agency;
- DOJ determined that litigation is not appropriate and returned the debt to the agency;
- the debt has been discharged or terminated in bankruptcy;
- the statute of limitations for initiating litigation has expired; or
- the agency determines that the debt is legally without merit or cannot be substantiated.

The agency should establish:

- a method to track and follow up on the debts referred to DOJ for its concurrence with termination of collection action; and
- procedures to ensure that proper action will be taken based on the agency’s decision to terminate collection, with DOJ concurrence. Such action may include passive collection, write-off, and/or cancellation of indebtedness.

Suspension of Collection Action

An agency may determine that certain circumstances warrant suspending, rather than terminating, collection action. When collection efforts are suspended, the agency, in effect, decides to defer its attempts to enforce collection, for a period of time specified in its regulations and/or collection strategy. During a period of suspension, passive collection action may continue when appropriate.

Collection action should be suspended only when the agency has reason to believe that the suspension will enhance the chances of recovery, or, at minimum, will not endanger the recovery of the debt. Such would be the case if the debtor agrees to repay the debt when the debtor's financial condition improves, as would occur if the debtor has been only temporarily laid-off from a permanent job.

The agency should suspend collection action when one or more of the following criteria apply:

1. **The agency cannot locate the debtor at the present time.** The agency should attempt to locate the debtor using available sources as described in Chapter 6, Delinquent Debt Collection, pages 6-71 through 6-73.

2. **The debtor's financial condition is expected to improve.** Suspension would be appropriate if the debtor owns no substantial equity in property and is unable to make payments, but: (a) the debtor's future financial prospects justify retaining the debt and the statute of limitations has not expired or has been tolled; or (b) future collections may be realized through administrative offset; or (c) the debtor has agreed to pay the interest accruing on the debt during the suspension. For example, suspension might be appropriate where the debtor has indicated that he/she is the recipient of a trust fund or inheritance and would be willing to pay interest until receipt of the trust fund or inheritance, at which time the debt would be repaid in full. Suspension may also be appropriate when the agency has evidence that

the collectibility of the debt will improve as the debtor's income potential improves over time (as has been the general case with education loans).

3. **The debtor has requested a waiver or administrative review of the debt.** If the waiver review or administrative review is considered mandatory, and if suspension is mandated by law or regulation pending such review, then the agency must suspend collection action until the review is completed or the waiver granted. Otherwise, the agency may decide on a case-by-case basis whether to suspend collection action for the duration of the review. The agency should not suspend collection when an agency determines that the request for waiver or review is frivolous or was made primarily to delay collection.

4. **The debtor has filed a petition in bankruptcy.** When an agency learns that a bankruptcy petition has been filed with respect to the debtor, in most cases the collection activity on a debt must be suspended unless the agency can clearly establish that the automatic stay has been lifted or is no longer in effect. Agencies should seek legal advice immediately from their legal counsel and, if legally permitted, take the necessary legal steps to ensure that no funds or money are paid by the agency to the debtor until relief from the automatic stay is obtained. In such cases, the agency may then be able to offset such funds to collect on the debt. See also Chapter 6, Delinquent Debt Collection, page 6-57.

The agency's procedures for suspending collection action should:

- distinguish between the definition and treatment of suspended and terminated debts;
- describe the specific circumstances in which suspension is appropriate;
- provide for the review and monitoring of suspended debts on a regular basis;

- require that progressively higher-level agency officials authorize the suspension of progressively higher dollar amounts of debt, with the signature of each agency official participating or concurring in the decision included on the authorizing document;

- provide for obtaining the concurrence of DOJ with the suspension of any debts whose principal amounts exceed $100,000, or from Fiscal Service for debts in cross-servicing whose principal amounts are $500,000 or less; and

- provide for ending the suspension and for either: (1) reinstating active collection on the debt, or (2) terminating collection action on the debt, when circumstances warrant and after review of the specific details at the highest appropriate agency level.

Note that where a statute requires that the agency suspend collection action or when the debtor files for bankruptcy, as a practical matter, the agency does not need DOJ or Fiscal Service concurrence to suspend collection action. In these instances, the agency should seek the review of its agency counsel to assure that suspension of collection action is mandated by law.

Termination and Suspension of Collection Action and Compromise Regarding Fraud Claims

When an agency has a debt arising from fraud, false statements, or misrepresentations by a debtor, the agency must ask DOJ for authority to terminate or suspend collection action, or compromise the debt**, regardless of the amount**. An agency should consult with agency counsel to determine whether action under Title 31, Chapter 38, “Administrative Remedies for False Claims and Statements” (31 U.S.C. §3801 - 3812) is appropriate.

Regarding write-off and reporting discharges of indebtedness to IRS, the same rules apply to fraud debts as apply to generally all other types of debts. DOJ approval is not needed by the agency to write-off the debt as currently not collectible. Similarly, no further DOJ approval is needed to close-out the debt or report the debt to IRS as potential income to the debtor once the agency is given the authority to terminate collection action on the debt by DOJ.

Write-off

Write-off of a debt should occur when the agency determines that the debt has no value for accounting purposes. As previously indicated in the overview of this chapter, write-off may occur *before, concurrently with* or *after* the agency determines that collection action should be terminated. Generally, write-off is mandatory for debts delinquent more than two years, unless documented and justified to OMB in consultation with Treasury. However, in those cases where material collections can be documented to occur after two years, debt cannot be written off until the estimated collections become immaterial. See OMB Circular No. A-129, Section V.5.

All debt must be reserved for in the allowance account, and all write-offs must be made through the allowance account. Under no circumstances are debts to be written off directly to expense. See OMB Circular No. A-129, Section V.5

Once the agency determines that a debt has no value for accounting purposes, it must determine whether or not collection action on the debt should continue. Specifically, at the time the debt is written-off, the agency must determine whether the debt should be further classified as one of the following:

- **Currently Not Collectible (CNC)**: If the agency determines that cost effective collection efforts should continue after write-off, then the debt will be classified as CNC. Debt collection activities, such as referral to Fiscal Service for collection action for cross-servicing or TOP, should continue.

- **<u>Close-out</u>**: If the agency determines that collection action is legally barred or it is no longer cost effective to pursue collection, the debt should be classified as close-out. In most cases, the closed-out debt must be reported to IRS as potential income to the debtor.

Cost effective collection efforts should continue if an agency determines that continued collection efforts after mandatory write-off have some potential to result in collections. This is especially true if the debt has not yet been referred to Fiscal Service for collection action, as required by the DCIA. See Chapter 6, Delinquent Debt Collection.

In summary, *within two years of the date of delinquency*, the agency should be able to evaluate the likelihood that it will collect on a delinquent debt and either:

- write-off and classify the debt as CNC, which will allow for further collection action;

- write-off and classify the debt as close-out, which means that the agency will cease all debt collection activities on the debt; or

- document and justify why the debt is not being written-off.

If the debt is written-off and classified as CNC, the debt may be reclassified as close-out in the future, when all collection activities pertaining to the debt cease.

The agency does not need DOJ approval to write-off a debt since the agency is only adjusting its accounting records. Except for agencies having independent statutory authority, DOJ concurrence or Fiscal Service concurrence as applicable, is required, however, when an agency suspends or terminates debt collection action on debts over $100,000. See page 7-9 of this Chapter.

Pursuit of Collection After Write-off/CNC

When pursuing collection of a debt after write-off and classification as CNC, an agency should:

- if material to its financial statements, disclose its actions regarding the pursuit of collection on its written-off debts in a note to its financial statements (i.e., the agency should specifically state the amount of written-off debts under collection and whenever possible based upon historical experience, the amount it expects to collect); and
- establish accounting procedures to account for collections on written-off debts (e.g., if the agency receives a one-time payment on a written-off debt, it may restore the amount collected as a receivable at the time of collection or credit the amount to a recovery account; and/or if the payment on a written-off debt is recurring and/or regular, the agency should restore the total amount of the debt as a receivable in both its General and Subsidiary Ledgers and record each collection as if the debt had never been written-off).

Write-Down

Rather than writing-off the entire amount of a collateralized debt, an agency may *write-down* the debt to the collateral's net realizable value. The agency may not write-down non-collateralized debts. The agency must appraise the value of the collateral in relation to the amount of the debt. If the value of the collateral has declined to the point where its liquidation would not satisfy the debt in full and there is no other source for the collection of the debt, then the agency should reduce the amount of the debt to the new appraised value of the collateral. The written down amount should be recognized as a loss. For information on real estate appraisals, see Chapter 3, Credit Extension, page 3-13.

As is true for write-off, the agency does not need DOJ concurrence to write-down a debt since the agency is simply adjusting its records to more accurately reflect the amount it expects to collect through the liquidation of the collateral.

Close-out Classification and Discharge of Indebtedness/Issuance of Form 1099-C

Close-out Classification. As previously stated, the classification of a debt as close-out occurs when an agency, after determining that additional future collection efforts on a debt are prohibited or would be futile, determines to cease all collection activities on the debt. This action may occur concurrently with the initial write-off of a debt, or at a later date, depending upon the agency's own collection strategy and its determination that no further collection activity is warranted. The determination that a debt should be classified as close-out is different than the determination that collection action should be terminated or suspended. When collection action for a debt is terminated or suspended, there is a determination to cease active collection action on the debt. The agency may still pursue debt collection activities at its discretion, for example, maintaining the debt in TOP. The determination that the debt should be classified as **close-out occurs only after the agency has determined to cease all collection activity on the debt.**

The decision to classify a debt as close-out triggers the need to determine if the debt must be reported to the IRS as potential income to the debtor on Form 1099-C, "Cancellation of Debt." Close-out and Form 1099-C reporting are linked because both actions occur as a result of the agency's decision to cease all collection activity. **Additionally, the two actions are linked because further collection action on the debt is generally prohibited once the agency reports the uncollected amount to the IRS on Form 1099-C as potential income to the debtor**.

Therefore, before making the decision to cease all collection activity and to classify the debt as close-out, an agency must take all appropriate steps to collect the debt, including, as applicable: (1) TOP, (2) non-centralized administrative offset, (3) referral to Fiscal Service, Treasury-designated debt collection centers or private collection contractors, (4) credit bureau reporting, (5) administrative wage garnishment, (6) litigation, and (7) foreclosure. Typically, once a debt has been through Fiscal Service's cross-servicing process (as described in Chapter 6, Delinquent Debt Collection) and returned to the agency, any remaining balance due will be classified as close-out.

Discharge of Indebtedness. After it is determined that the debt will be classified as close-out, the amount of indebtedness is reported to the IRS as potential income to the debtor via Form 1099-C, "Cancellation of Debt." Under the Internal Revenue Code (26 U.S.C. § 61(a)(12)), income from discharge of indebtedness is defined as "gross income." Section 6050P of the Internal Revenue Code, as amended by the DCIA, requires all Federal agencies and private financial institutions to report certain discharged debts to the IRS. The reporting requirement covers debts owed by individuals, sole proprietorships, partnerships, and corporations. Types of debts include those arising from loan programs, as well as administrative actions such as the assessment of fines, fees, and penalties.

The discussion that follows concerning reporting discharges of indebtedness to IRS contains some of the general rules. For more detailed information, agencies should refer to IRS regulations 26 CFR 1.6050P-l and any other applicable IRS publications and guidance.

Section 6050P(a) of the Internal Revenue Code requires the filing of Form 1099-C for discharges of indebtedness of $600 or more. IRS regulations list eight identifiable events that trigger the reporting requirement. Note that these identifiable events, listed below, generally dovetail with the reasons an agency would cease all collection activity on a debt and classify the debt as close-out.

The following are identifiable events that trigger reporting discharge of indebtedness to IRS on Form 1099-C:

- a discharge of indebtedness under Title 11 of the United States Code (bankruptcy). Note that reporting is required only if the agency knows from information included in its books and records pertaining to the debt that the debt was incurred for business or investment purposes;

- a cancellation or extinguishment of an indebtedness that makes a debt unenforceable in a receivership, foreclosure, or similar Federal or state court proceeding;

- a cancellation or extinguishment of an indebtedness where a debtor's affirmative statute of limitations defense is upheld and can no longer be challenged by appeal, or a cancellation or extinguishment upon expiration of a statutory period for filing a claim or commencing a deficiency judgment proceeding. Note that Federal agencies may still have the ability to collect by offset after the statute of limitations for enforcing a claim in court has expired; no Form 1099-C should be filed if collecting by offset;

- a cancellation or extinguishment of an indebtedness that occurs when the creditor elects foreclosure remedies that by law extinguish or bar the creditor's right to collect the debt;

- a cancellation or extinguishment of an indebtedness that renders a debt unenforceable pursuant to a probate or similar proceeding;

- a discharge of indebtedness pursuant to an agreement between the creditor and the debtor to discharge indebtedness at less than full consideration (a “compromise,” see page 7-21 of this Chapter);

- a discharge of indebtedness pursuant to a decision by the creditor, or the application of a defined policy of the creditor to discontinue collection activity and discharge the debt; and

- the expiration of the non-payment testing period (generally a rebuttable presumption of this identifiable event occurs when the creditor agency does not receive any payment on a debt for a 36 month lookback period as of December 31).

See 26 CFR § 1.6050P-1(b)(2) for more information on identifiable events.

When reporting a debt to the IRS, the agency is responsible for all of the actions detailed below:

- the agency should capture and provide to the IRS all information required by the statute and IRS regulations, including taxpayer/debtor taxpayer identification number, date of the final debt disposition/discharge, and amount of the debt. To obtain a taxpayer identification number, the agency should request that the debtor complete and return a Form W-9, "Request for Taxpayer Identification Number and Certification" available through the Internal Revenue Service website at *www.irs.gov/formspubs* or other applicable form, to the extent authorized by law. The debtor is obligated to provide this information under the Internal Revenue Code;

- the agency must report the debt after all collection efforts have been exhausted. The agency is not obligated to wait to report a debt until the statute of limitations (SOL) has expired, even though the expiration of the SOL constitutes a reason for the debt to be considered discharged;

- the agency must report amounts of $600 or more, but has the option of reporting amounts less than $600;

- the agency must report the outstanding principal, administrative costs (but not contingency fees), and penalties for non-lending transactions. In the case of lending transactions, only the principal must be reported. In both lending and non-lending transactions, reporting interest is at the discretion of the creditor;

- the agency must report any deficiency judgment once the agency has stopped its attempts to collect on the judgment (note that once the agency determines to file a Form 1099-

C, the agency must officially release any judgment relevant to the debt);

- the agency should not report a debt if it has a lien against the debtor's property, unless it decides to release that lien. The agency must notify and obtain the concurrence of DOJ prior to closing-out a debt with an outstanding lien if the principal amount of the debt is $100,000 or more;

- the agency must provide the debtor with a copy of the Form 1099-C to be filed or a written statement of the impending Form 1099-C report by January 31 of the year following the agency's decision to stop all collection on the debt; and the agency must send the Form 1099-C to the IRS by February 28 of the year following the calendar year in which the identifiable event occurs (March 31 if filed electronically).

Note that IRS regulations provide that reporting is not required for the release of one debtor if the remaining debtors are liable for the full unpaid amount of the debt.

For debts referred to Fiscal Service's Cross-Servicing Program, an agency may request Fiscal Service to report the debt to the IRS on the agency's behalf.

Once a debt is reported to the IRS, the agency can take no further collection action. It may, however, accept voluntary repayments of the debt at any time, without any obligation to notify IRS of a change in the debt. For example, voluntary payments may occur where a delinquent debtor seeks to satisfy the debt and remove the statutory bar from receiving Federal loans or loan guarantees. See Chapter 6, Delinquent Debt Collection, page 6-65. The agency does, however, have an obligation to notify IRS of debts that were reported in error. The agency would handle voluntary payments as it would payments received before classification of the debt as close-out.

Compromise of Debts

When an agency accepts less than full payment—or in other words "compromises" the debt—it may have to follow the requirements for termination, write-off, and close-out for the portion of the debt released/discharged. When compromising, the agency must determine whether the proposed compromise meets appropriate standards. See Chapter 6, Delinquent Debt Collection, page 6-23.

In compromising a debt, the agency must: (a) get approval from DOJ to compromise the debt when the principal balance of the debt before compromise exceeds $100,000, or, if the debt is $500,000 or less and the debt is in Fiscal Service's Cross-Servicing Program, get approval from Fiscal Service unless the agency has independent statutory authority to compromise the debt; (b) write-off as closeout the amount of the debt forgiven by compromise; and (c) report the discharged amount to the IRS on Form 1099-C, assuming the requirements of IRS regulations are otherwise met. For example, if an agency agrees to accept anything less than the full amount owed for a $300,000 debt because the debtor claims an inability to pay, the agency must seek DOJ approval for such compromise. If DOJ decides not to seek enforcement and approves the compromise, then the amount discharged should be written-off as close-out and reported to the IRS on Form 1099-C.

If, however, an agency determines that part of the debt is not owed, then the agency does not need to seek DOJ approval to terminate collection or compromise such amounts, and the filing of a Form 1099-C is not required. For example, if a debtor argues that the amount of the debt should be $150,000, instead of $300,000, based on the debtor's records, and the agency accepts the debtor's analysis, then the amount may be adjusted without seeking DOJ approval or filing a Form 1099-C. In addition, the agency should make an adjustment to the total receivables on the "Treasury Report on Receivables Due From the Public" to account for the lesser amount owed, rather than report the amount of the reduction as a write-off.