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QUARTERLY CONSUMER CREDIT TRENDS

Recent trends in debt settlement and credit counseling

Consumer Financial Protection Bureau

This is part of a series of quarterly reports on consumer credit trends produced by the Consumer Financial Protection Bureau using a longitudinal, nationally representative sample of approximately five million de-identified credit records from one of the three nationwide consumer reporting agencies.*

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INTRODUCTION

At one time or another, many Americans struggle with or fall behind on their debts. In 2018, for example, roughly 28 percent of consumers with a credit file at a nationwide consumer reporting agency had a debt reported by a third-party debt collector, and nine percent had at least one 60-day delinquency on a credit card.[1] With the dramatic rise in unemployment due to the COVID-19 pandemic, consumers are facing unexpected economic pressures. Understanding trends in debt relief activity, especially during the Great Recession, can help deepen our understanding of how creditors, debt relief providers, and consumers may respond to this new crisis or future economic downturns. This work also helps inform market stakeholders' and policy makers' policies affecting debt relief options for consumers.

In this report we find that debt settlements increased sharply during the Great Recession and typically occurred faster relative to non-crisis times. Since 2016, as delinquencies on unsecured debt have risen and credit card access has tightened, debt settlement activity has risen as well, though there has not been a corresponding increase in reported credit counseling activities.

Creditors of unsecured debt, especially credit card debt, have several strategies to grant long-term concessions to consumers to make repayment more manageable and mitigate lender losses. These strategies are largely structured around account maintenance guidance issued by the Federal Financial Institutions Examination Council and financial regulatory agencies.[2] For instance, creditors can offer long-term hardship repayment programs for delinquent debts that have not yet been "charged-off," an accounting determination that classifies a debt as unlikely to be collected. These programs can involve the creditor closing the account and setting a repayment plan for the full account balance over a fixed term, often with concessions like waivers of certain fees and interest rate reductions. Within this structure, third-party credit counseling agencies can work with consumers to assess their hardship situation and enroll them in workout programs across multiple creditors through debt management plans (referred to as "credit counseling" in this report).

In contrast, a debt settlement is an agreement that the consumer will resolve the debt by paying less than the full balance owed and can occur before or after the creditor charges-off the debt.

[1] *See* Bureau of Consumer Financial Protection, *The Consumer Credit Card Market*, (Aug. 2019) at 138 and 41, *available at* https://www.consumerfinance.gov/data-research/research-reports/the-consumer-credit-market-2019/ (hereinafter The Consumer Credit Card Market (2019)).

[2] For example, national banks are subject to oversight by the Office of the Comptroller of the Currency. *See* Off. of the Comptroller of the Currency, *Comptroller's Handbook: Credit Card Lending, Version 1.2*, (Jan. 2017), *available at* https://www.occ.treas.gov/publications/publications-by-type/comptrollers-handbook/credit-card-lending/pub-ch-credit-card.pdf.

To align with financial regulatory guidelines, pre-charge-off settlements typically occur if the consumer can make a single lump-sum payment or pay the settlement within three months. Post-charge-off settlements can be structured over any length of time. As detailed in this report, most settlements occur after the lender classifies the account balance as charged-off. Additionally, most settlements reflect agreements directly between the consumer and the debt holder,[3] which can occur as a result of a consumer asking the holder for a settlement, the debt holder's proactive settlement offers, or sometimes as an agreement between the consumer and creditor as an alternative resolution to litigation proceedings.

Settlements may also occur via debt settlement companies (DSCs), which offer to manage the settlement process on the consumer's behalf for a fee. The Bureau's 2019 publication *The Consumer Credit Card Market* found that the relative volume of credit card balances settled through DSCs more than doubled between 2017 and 2018 while the reported share of settled outstanding debt remained steady.[4] Higher overall debt levels, increased market presence of DSC programs, and evolving creditor DSC policies likely drove this growth. At the Bureau's 2020 *Evolutions in Debt Relief Convening,* creditors, consumer advocates, and debt relief service providers discussed these trends and the imperative to develop new debt relief options that would improve transparency and better meet a variety of consumers' financial situations.[5]

This *Quarterly Consumer Credit Trends* report analyzes data from the Bureau's Consumer Credit Panel (CCP) to provide insight into consumers' use of debt settlement and credit counseling debt management plans from 2007 through 2019.[6] This period includes debt relief activity observed both during the 2008 financial crisis and the succeeding period of credit loosening, a period which also includes amendments to the Telemarketing Sales Rule (TSR) in 2010 that address the telemarketing of debt relief services. The amendments to the TSR instituted various disclosure requirements and other consumer protections including the prohibition of upfront fees in the third-party debt settlement industry. Subsequently,

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[3] "Debt holders" include original creditors, who may hire third-party debt collectors, and debt buyers.

[4] Large credit issuers' policies toward DSCs vary and may include potential litigation, not negotiating with the DSCs, or treating settlements requested through DSCs the same as they would a consumer requesting a settlement directly or through a Power of Attorney. The Consumer Credit Card Market (2019) at 151 and 167.

[5] Potential developments include "tech-based" solutions for self-help, early hardship identification, and debt restructuring options, as well as expanding CCA programs to include more flexibility, longer repayment terms, and some principal forgiveness for certain hardship cases; *see* Consumer Financial Protection Bureau, *Evolutions in Debt Relief Convening*, March 10, 2020, https://www.consumerfinance.gov/about-us/events/archive-past-events/evolutions-in-consumer-debt-relief-event/ (hereinafter Evolutions in Debt Relief).

[6] The CCP is a 1-in-48 sample of de-identified credit records from one of the three nationwide consumer reporting agencies.

approximately 80 percent of DSCs exited the market,[7] though industry data suggest recent increases in the number of companies and enrollments.[8]

By exploring debt relief trends across time, this report provides insights into potential relationships between economic conditions, regulatory changes, creditor policies, and debt relief services, and, more generally, into the experiences of borrowers in financial distress. Specifically, this report shows the evolution of overall debt settlement use, including changes in the number of consumers using this option and in the amount of debt settled, and the time accounts spend between non-payment and charge-off before eventually reaching settlement.

This analysis focuses on the largest forms of unsecured debt other than student loans: credit cards, retail revolving and installment accounts, and personal revolving and installment accounts. The data represent nearly 34 million credit accounts that were settled through a creditor or had account payments managed by a CCA at some point between 2007 and 2019.[9] Of these accounts, 69.5 percent were credit cards, 26.6 percent were retail cards,[10] and 3.9 percent were personal revolving accounts or personal or retail installment loans. In all, these accounts represent more than 18 million consumers, or nearly one in thirteen consumers with a credit record at a nationwide consumer reporting agency between 2007 and 2019.

CHANGES IN DEBT SETTLEMENT AND CREDIT COUNSELING

The CCP data identify accounts where the creditor reports the account settled for less than the full balance and some accounts with payments managed by a CCA. The data do not indicate whether settlements occurred directly with the consumer or through a DSC. Conversely, the data show third party CCA activity, but not creditor workout plans made directly with the consumer. Relative to for-profit DSCs, most CCAs are non-profit, operate under different rules, and have different relationships with creditors. Nonetheless, comparing trends in overall debt

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[7] Regan, Greg. "Options for Consumers in Crisis: An Economic Analysis of The Debt Settlement Industry (Data as of December 31, 2012)" at 5, February 28, 2013 https://americanfaircreditcouncil.org/wp-content/uploads/Regan-Report-Options-for-Consumers-in-Crisis-as-of-Dec-121-1-1.pdf (hereinafter "Regan Report, 2012").

[8] Regan, Greg. "Options for Consumers in Crisis: An Economic Analysis of The Debt Settlement Industry" (Data as of March 31, 2017) at 7, February 5, 2018 https://americanfaircreditcouncil.org/wp-content/uploads/2018.02.05-AFCC-Report-Consumers-in-Crisis.pdf (hereinafter "Regan Report, 2018").

[9] This analysis only includes settlements furnished by the creditor and not accounts furnished by a debt buyer. Debt buyer reporting practices varied over this period. For more information on debt buyer tradelines see CFPB. "Market Snapshot: Third-Party Debt Collections Tradeline Reporting." July 2019. https://www.consumerfinance.gov/data-research/research-reports/market-snapshot-third-party-debt-collections-tradeline-reporting/. Also, not all accounts managed by a CCA are necessarily reported as such by the furnisher, so the number of accounts is under-reported in these data. Analysis suggests relatively consistent furnishing practices by individual companies over this period.

[10] General purpose credit cards can be used for transactions at a variety of merchants, while retail (or private label) cards cannot be used as broadly (typically only at one merchant or a small group of merchants).

settlement and credit counseling through CCAs can provide a more complete picture of recent changes in the market for debt relief services.

Figure 1 shows that the number of settled accounts increased from 2007 to 2010 in response to the financial crisis and its immediate aftermath. From 2011 through 2015, debt settlement activity dropped dramatically as the economy expanded and the supply of potential settlement candidates decreased.[11] Accounts managed by financial credit counseling programs followed a similar trend during this post-recession period, except the decline began a year earlier in 2010. Given the relative lags in reporting for settlements versus credit counseling, we would anticipate seeing changes in credit counseling in the credit reporting data before changes in settlements, as seen here.[12] Both just before and after the 2010 TSR amendments went into effect, the overall trends for settlements and credit counseling activity largely moved together. While the drop in settlements during this period follows the TSR changes that took effect on September 27, 2010 (see the vertical line in figure 1),[13] there was also a drop in credit counseling, an industry which was not directly affected by these TSR changes. Moreover, these decreases also align with changes in related macroeconomic factors, such as the tightening of credit during the financial crisis and improvements in the overall economy after the crisis.

From 2016-2019, increased delinquencies and tightening credit access correspond to increases in settlements.[14] This increase in debt settlement appears to be a function of changing macroeconomic conditions, creditor account management strategies, and apparent increases in

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[11] *See* Bureau of Consumer Financial Protection, *The Consumer Credit Card Market*, (Dec. 2017) at 307, *available at* https://files.consumerfinance.gov/f/documents/cfpb_consumer-credit-card-market-report_2017.pdf (hereinafter The Consumer Credit Card Market (2017)).

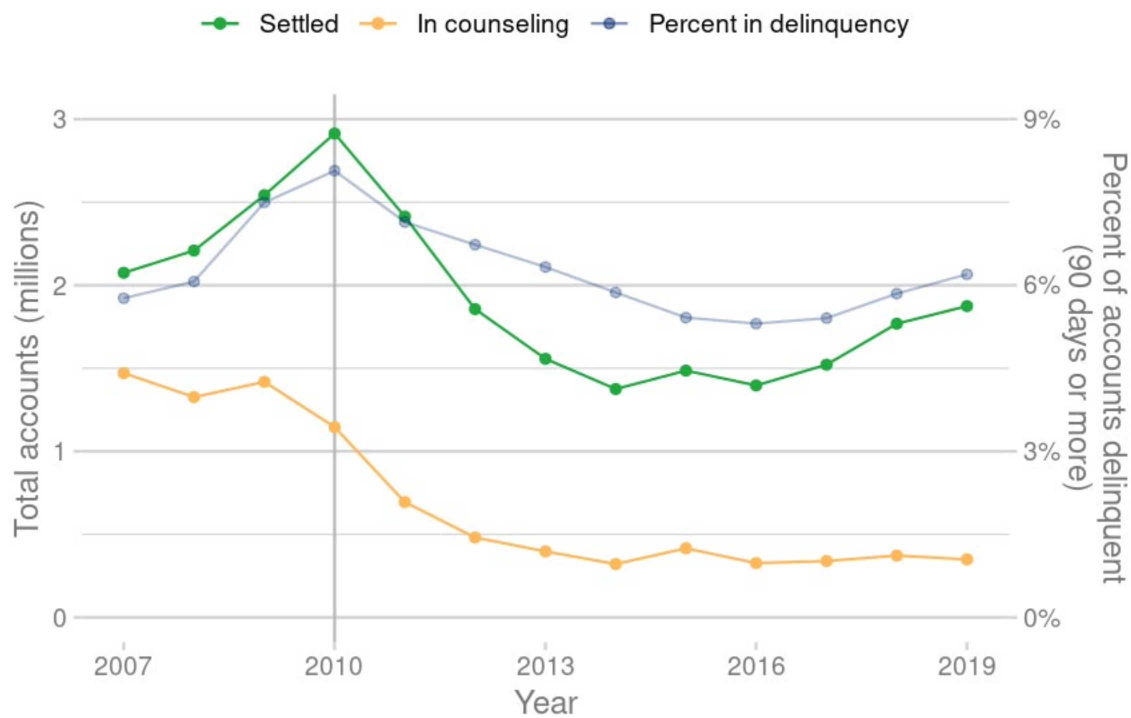
[12] Settled accounts are not reported as such until the conclusion of the debt settlement process while accounts managed via a CCA can be reported as settled as soon as the consumer enrolls. As a result, accounts that enter credit counseling are typically reported in the data months before accounts in debt settlement plans. Industry data indicate that the average successful settlement occurs 14 months after enrollment in a DSC program, with the first settlement occurring within four to five months; *see* Dobbie, Will. "Financial Outcomes for Debt Settlement." May 2, 2020. https://americanfaircreditcouncil.org/wp-content/uploads/Dobbie-Report-05022020-final.pdf (hereinafter "Financial Outcomes for Debt Settlement"). These patterns may differ for direct settlements between consumers and creditors.

[13] These TSR changes were proposed in August 2009, and it is unclear what, if any, net effect they had on settlements for 2009–2010 as DSCs responded to the upcoming changes.

[14] Following improvements after the Great Recession, delinquency rates on credit cards began trending upward in 2016 and, around the same time, credit card access began tightening. For more on changes in delinquencies across products, see Federal Reserve Bank of New York, *Quarterly Report on Household Debt and Credit*, (February 2020), available at https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/HHDC_2019Q4.pdf. For more on changes in credit tightness, see Consumer Financial Protection Bureau, *Consumer Credit Trends*, available at https://www.consumerfinance.gov/data-research/consumer-credit-trends/.

for-profit DSC activity.[15] By comparison, there has been little change in credit counseling even as delinquencies and settlements have increased. This is consistent with reported market shifts such as DSCs gaining market presence and reductions in the availability of CCA programs.[16]

FIGURE 1: COUNTS OF ACCOUNTS SETTLED OR IN A CREDIT COUNSELING PROGRAM EACH YEAR



Consumers may have multiple accounts they are seeking to settle at any given time, but further analysis of the data indicates that these consumers generally settle one account at a time and ultimately settle an average of 1.6 accounts over a three-year period.[17] Conditional on settling

[15] The Consumer Credit Card Market (2019) at 151 and 167. Creditors also reported reductions in debt selling activities during this time period; see The Consumer Credit Card Market (2017) at 307.

[16] In 2016, a CCA trade organization reported an environment of shifting client volumes, shrinking funding, and emerging competition. The sector has continued to face these challenges, resulting in ongoing consolidation of agencies; *see* Keating, Susan. "State of the Credit Counseling and Financial Education Sector." NFCC Connect: 51st Annual Conference, Washington, D.C. September 26, 2016. However, CCA participants have recently reported efforts to develop new CCA debt management options and improve underlying technology are allowing the sector serve to more consumers with fewer resources; *see* Evolutions in Debt Relief Convening (Panel 4).

[17] Industry data show consumers who settle at least one account after entering a DSC program typically settle 3.37 accounts (half of their enrolled accounts) within three years, but the debt profile of a consumer working with a DSC

an account, consumers typically settled about 1.2 accounts per year, an average that was relatively constant over the full 13-year period. From 2007 to 2011, consumers with accounts reported to be in a credit counseling program had approximately 2.0–2.3 accounts enrolled in these programs.[18] In 2012, this began to decrease and stayed around 1.7–2.0 accounts per person through 2019. This decrease is somewhat smaller than the 20 percent drop in the average number of credit cards per consumer: in 2008 consumers had an average of five credit cards, but by 2018 they had four.[19]

CHANGES IN PRE-DEBT SETTLEMENT BALANCES

Furnishers do not typically report the final balance of the settled account or the amount the consumer pays the creditor (the "settlement amount"), but they do report the balance of the account in prior periods. As a result, the balance reported the quarter before settlement should generally provide a lower bound on the balance settled and a likely upper bound for the true settlement amount.[20] Figure 2 shows the total and average balance of all settled accounts for each year from 2007–2019. During the Great Recession, there was a steep increase in both the total debt settled and the average balance of accounts that settled.

The total amount of debt settled more than doubled from 2007 to 2010, increasing from $5.4 billion to $11.4 billion; this was driven both by an increase in the number of accounts settled (see figure 1) and an increase in the average settled amount, as seen in the rise in average balances during this period (see figure 2).[21] By 2016, the total amount of debt settled dropped to $3.7 billion. This decrease was mostly driven by the large decrease in the number of accounts settled during this period, as seen in figure 1, as the supply of charged-off debts accumulated during the financial crisis resolved or became less likely to resolve over time. The average balance settled decreased from 2010 to 2014 and has remained relatively unchanged since.[22]

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may be different than the overall sample and these data likely also include accounts held by debt buyers; *see* Financial Outcomes for Debt Settlement.

[18] Actual number of accounts enrolled in credit counseling per consumer may be higher than observed in the CCP due to differences in creditors' furnishing practices for consumers enrolled in credit counseling programs.

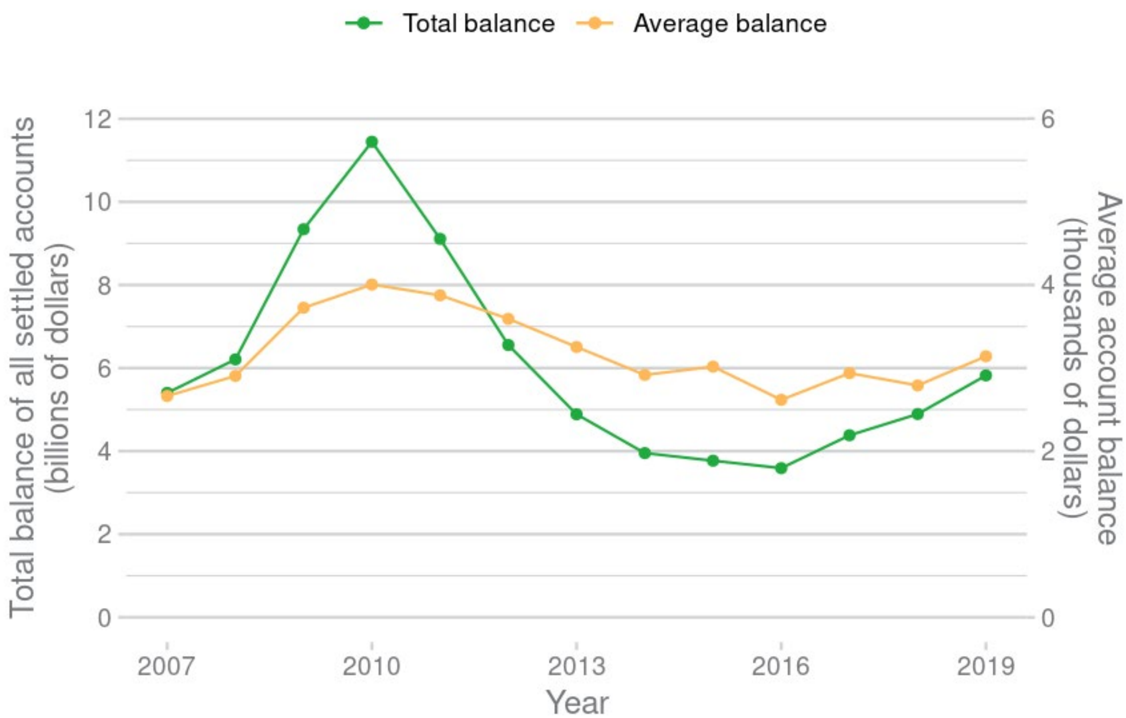
[19] The Consumer Credit Card Market at 35.

[20] The full debt owed at the time of settlement may be higher, though the consumer is still likely to settle for less than the full balance owed in the quarter before settlement. Most lenders will cut off credit access on accounts far enough into delinquency for settlement to occur, so actual balances owed may be higher to the extent fees and interest accumulate and are unlikely to be lower as consumers are typically making no payments just prior to settlement.

[21] Since this report excludes accounts purchased by debt buyers, the actual total amount of unsecured debt settled through both creditors and debt buyers is likely higher than the $11.4 billion reported by creditors in 2010. In more recent years, creditors were more likely to hold these delinquent debts through settlement and not sell them to third party debt buyers.

[22] Regan Report, 2018 at 10.

FIGURE 2: TOTAL AND AVERAGE BALANCES OF SETTLED ACCOUNTS BY YEAR



WHEN DOES SETTLEMENT OCCUR IN DELINQUENCY?

The period between initial delinquency and settlement often reflects a period of financial distress for consumers and uncertainty for creditors. Creditors generally seek to work out a resolution before charging off the debt and may offer various workout plans and eventually settlements to certain consumers as the delinquency becomes more severe. Throughout the delinquency, the consumer is subject to creditor or third-party debt collection efforts and eventually may be subject to litigation.[23] Settlement timing largely depends on creditors' policies and consumers' ability to get the money to fund settlements. While analysis of these data cannot disentangle these two drivers, these data can provide insight into how these forces have changed over time on net. Specifically, these data show how the length of time between the last successful payment on an account and when it settles has changed over time.

[23] For additional information on consumers' experiences with debt collection, see Consumer Financial Protection Bureau, "Consumer Experiences with Debt Collection: Findings from the CFPB's Survey of Consumer Views on Debt" (January 2017) *available at* https://files.consumerfinance.gov/f/documents/201701_cfpb_Debt-Collection-Survey-Report.pdf.

Most accounts are charged-off by the debt holder prior to settlement. Specifically, more than 70 percent of accounts settled since 2013 were first charged-off.[24] Accounts that are not reported as charged-off prior to settlement are typically in collections or another severe delinquency status such as 150 days or more past due.

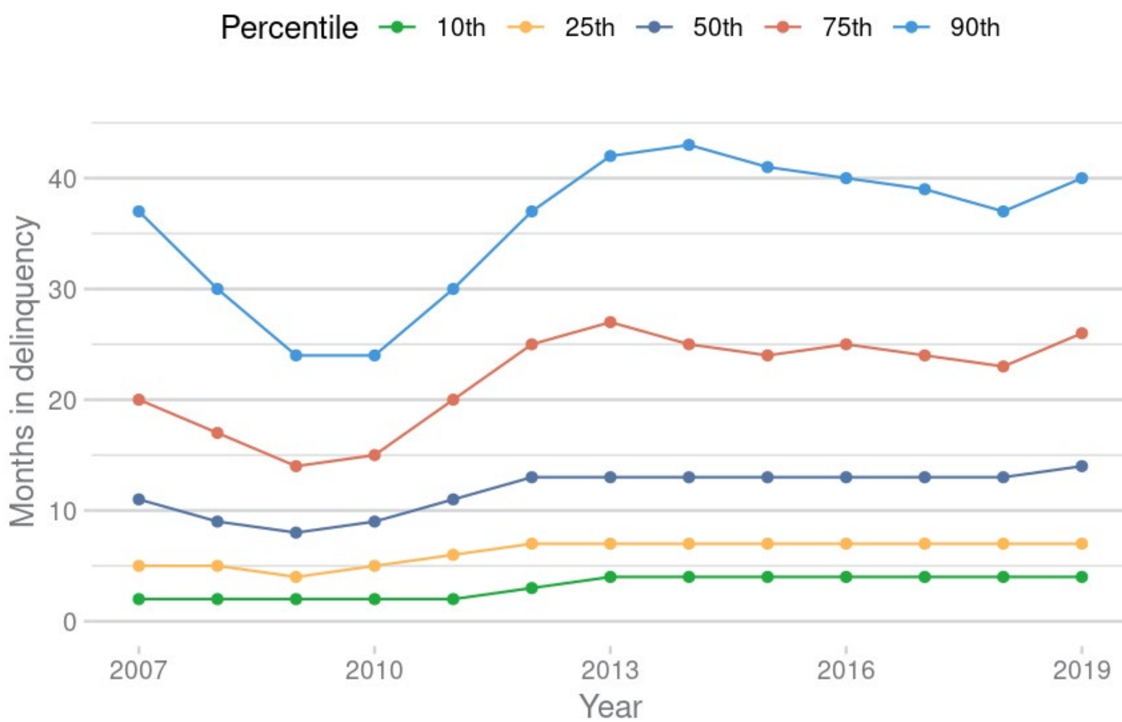
Accounts can remain in a charge-off status for many months before settlement and did so for an average of 12 months in this sample. Figure 3 shows percentiles of the number of months between when an account was last current and when it settled (including time in charge-off). From 2007 to 2019 the 25th percentile remained relatively stable at around four to seven months, meaning that about one-quarter of all accounts that settled over the last 13 years were past due for seven months or less before settling. In contrast, the median account spent 27 percent less time (three fewer months) in delinquency before settling in 2009 than in 2007. Decreases were even larger for accounts at the 90th percentile, which dropped from 37 months to 24 months (or 35 percent). That is, during the Great Recession many distressed accounts settled faster relative to after the crisis, possibly driven by lenders' greater willingness to settle. Specifically, to the extent there was increased competition for the collection of consumers' limited funds and some motivation for lenders to reduce the impact of the crisis on their loan loss reserves, debt holders may have accelerated their efforts to reduce expected losses during the Great Recession.[25]

Following 2009, this trend reversed: through 2013 time in delinquency increased by 63 percent and 75 percent for the 50th and 90th percentiles, respectively. The median number of months accounts spent in delinquency stayed at 13 months through 2018 and rose to 14 months in 2019. The 75th and 90th percentiles show similar trends: both remained relatively stable through 2018 before increasing in 2019. In recent years, settlements consistently occur after consumers spent more time in delinquency than during the Great Recession.

[24] We cannot cleanly identify the account status just prior to charge-off prior to 2013 due to changes in reporting codes and because the CCP data are quarterly during this period. To the extent debt holders charged off accounts fewer than three months before settlement, the share of settled accounts first charged-off may be higher than reported here.

[25] For an overview of loan loss reserve guidelines, see "Allowance for Loan and Lease Losses (ALLL)," Federal Reserve Board. https://www.federalreserve.gov/supervisionreg/topics/alll.htm.

FIGURE 3: TIME IN DELINQUENCY (INCLUDING CHARGE-OFF) BEFORE DEBT SETTLEMENT (BY PERCENTILE OF MONTHS IN DELINQUENCY)



CONCLUSION

The CCP data reveal substantial changes in debt settlement activities over the last 13 years. During the Great Recession, the volume of debt settlements rose dramatically. Between 2007 and 2009, most settlements occurred within a year of the start of delinquency, perhaps as creditors sought to ensure recovery of some funds during the recession. However, as the economy rebounded and the supply of charged-off debts from the financial crisis decreased, settlements dropped, and the time before a delinquent account settled grew. Since 2017, there has been an uptick in reported settlement activity and balances settled alongside an increase in delinquency, but no corresponding increase in credit counseling. These changes may reflect evolving creditor account management, CCA and DSC policies, as well as apparent increases in DSCs' market presence. While recessions differ in their underlying causes and in their effects on different types of households, to the extent the effects are similar, we may see patterns like those from the Great Recession repeat themselves in future downturns as consumers and lenders face increased pressures: increases in debt settlements and less time in severe delinquency or charge-off before settlement occurs. CCA activities may not see corresponding increases if current trends hold and the menu of debt relief options for consumers does not change. Further monitoring of debt relief trends will help deepen our understanding of how creditors and consumers manage their debts portfolios in response to this crisis.