



NEGOTIATING SETTLEMENT OF A DEBT COLLECTION LAWSUIT

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NOTE: This instructional packet is not legal advice. You should not use this packet “as-is.” Instead, you should modify this packet after you carefully consider the facts of your case. If you need specific legal advice, you should consult an attorney.

BASICS OF SETTLEMENT

A settlement is an agreement to end a dispute. When a lawsuit is filed, a settlement is an alternative to going to trial, and can include the dismissal of the lawsuit. Most lawsuits settle before they get to trial.

Do I Have to Settle?

No. During the settlement process, it is up to both you and the person or company bringing the lawsuit to decide to offer, accept, or decline a settlement. You are not required to agree to anything during this process, and you can return to the court process at any time.

Statements made for settlement purposes and offers of settlement are both inadmissible to prove liability, which means they cannot be used against you (or the other side) at trial.¹

Terms of Settlement

If a settlement is reached, the defendant (the debtor) will typically agree to pay the plaintiff some monetary amount, and the plaintiff will agree not to ask for any more money.

The settlement agreement will lay out the details of the agreement. Settlement terms may also include:

- That the plaintiff will remove the debt from your credit report.
- When the payment must be received and when the plaintiff must dismiss the case.
- That there will be no additional legal action or demand for more money.

Timing of Settlement

You can try to negotiate a settlement at any point in the case - even before a lawsuit is filed. Once a lawsuit is filed, settlement can happen before the trial begins or during the trial itself. Settlement negotiations can happen in the courthouse, such as at a pre-trial hearing or other meeting scheduled by the judge, or outside the courthouse through phone, email, or in-person meetings.

Reasons to Settle

Even if you think you have a strong defense to the lawsuit, there are several reasons why it could be beneficial for you to settle the case. You might consider settlement if:

- If you believe you owe all of the debt, you might try to settle for less than the full amount owed. A debt collection lawsuit is about whether you owe the debt - not whether you are able to pay it back.
- You can afford to make payments.

¹ See Cal. Evid. Code § 1152(a).

In addition, settlement can:

- Save you time, since it usually will take less time to negotiate and write a settlement agreement than to go through a trial.
- Save you money, since you can save money on court costs and fees, and other expenses related to the case. You might avoid having to take time off from work, arranging transportation, etc. to go to court.
- Relieve any stress that you will have to endure by going to court.
- Give you more control over the case and the outcome. When settling, you can participate more actively in creating a favorable solution than if you go to court and leave the decision to a judge or a jury.

Reasons Not to Settle

On the other hand, there are several reasons why you may not want to settle the case. You should not consider settlement if:

- You cannot afford to make payments. Although you might not have to repay the full amount, you still have to pay *something* if you want to settle an account.
- The debt is not yours, you disagree with the amount of the debt, or you are a victim of identity theft. If these apply to you, you may have valid defenses to the lawsuit and might get the case dismissed without paying any money to the plaintiff.
- The statute of limitations has expired. A “statute of limitations” is the deadline that a creditor has to sue on a debt. In California, the statute of limitations for most debts is **four (4) years** from the “date of default” (usually 30 days after the date of your last payment). If a creditor sues you after the statute of limitations has expired, you should raise this affirmative defense in your response to a complaint. You should also let the creditor know this because it might choose to dismiss the case against you. If you have raised this issue and you still go to trial, be prepared to show the court proof that your last payment was more than four years and 30 days before the lawsuit was filed.

Other Considerations When Deciding Whether or Not to Settle

- Consider whether you are collections-proof. For example, if you do not own property and your only income is protected from collection by law, the plaintiff may not be able to collect any money from you, even if they get a judgment against you. If your income and assets are protected, you may decide to let the plaintiff get a judgment against you, rather than reaching a settlement and making a payment.

If you are temporarily collections-proof because you are currently unemployed or temporarily disabled, you may not be collections-proof in the future if you start working again. If you are collections-proof *now*, you may want to use that as leverage in settlement negotiations. If you tell the plaintiff that your income is protected from collection, they may agree to a reasonable settlement, rather than risk getting a judgment they cannot collect.

For a list of income and assets that are currently protected from collection by law, visit: <https://selfhelp.courts.ca.gov/jcc-form/EJ-156>

- If you are planning to file for bankruptcy in the near future, you may not want to settle if the debt will be discharged (eliminated) in the bankruptcy proceeding.

For a list of bankruptcy resources, visit Public Counsel's Debtor Assistance Project: <https://publiccounsel.org/services/bankruptcy/>.

TIPS FOR NEGOTIATING A SETTLEMENT

It is important that you take the time to prepare yourself before you begin any settlement discussions. Preparation will give you more confidence going into the discussions and help you get a better result.

Determining Your Goals and Priorities

Before discussing settlement with the other side, you must know your goals and your priorities within those goals. Some issues may be more important to you than others, so make sure you understand your priorities before negotiating with the other side.

You should also consider whether money is the only goal, or whether you have any non-monetary goals. For example, you may want the debt removed from your credit report.

Developing a Negotiation Strategy

Here are suggestions that can help you achieve a better negotiated settlement.

- Determine if the statute of limitations has expired. Find out how old the debt is by checking your credit reports (www.annualcreditreport.com) to see the last time you made a payment on the debt. If the statute of limitations has expired, the creditor cannot sue you to collect. **Make sure that you do not accidentally restart the statute of limitations by making a partial payment on the debt (no matter how small).**
- If you have claims against the plaintiff, you could try to settle for a mutual release without paying any money to the plaintiff. In a mutual release agreement, both you and the plaintiff agree to give up any known and unknown claims you may have against each other that relate to the legal dispute.

- Before signing any type of mutual release agreement, make sure you know what your rights are and what you are agreeing to give up by signing.
- Before you make an offer to pay, consider your other financial obligations. Go over your income and expenses, figure out what you can afford to pay toward the debt, and only agree to pay a realistic amount.
 - Review your debt priorities. You should prioritize paying for necessities such as food and housing over paying credit card debt.
 - Allow some income left over to cover unexpected expenses and emergencies.
- If you decide to make an offer to pay, choose an offer that leaves you room to negotiate. You should expect your first offer to be rejected, so start your negotiations low. Decide how much you can afford to pay and then offer to settle for less money so that you have extra room to bargain.
 - For example, if you know you can only afford to pay 50% of your original debt, try offering around 10%.
 - **Never agree to pay more than you can afford.**
- If you can afford it, offer a lump sum. Creditors will often agree to accept a lot less than the full amount owed in exchange for a lump sum payment (if you pay all at once).
 - For example, if you owe \$500, you can suggest paying \$200 in one payment.
- If you cannot afford a lump sum payment, propose a payment plan. Offer to pay off the debt in monthly installments.
 - Make sure you understand the total amount you will pay.
- Negotiate how the creditor will report your debt to the credit reporting bureaus (Experian, Equifax, and Transunion). Ask the creditor to remove negative information from your credit report and ask them to report your account as “Paid in Full” once all payments have been made (instead of “Paid in Settlement”), even if you are paying less than the amount owed.
- Remain in control of the conversation and stand firm in what you are willing and able to pay. Do not let the plaintiff bully you into paying a very high amount and let your other financial obligations slide.
- Make sure you understand the potential tax consequences of any settlement, especially if you are settling for less than the full amount owed. If any debt is cancelled as part of a settlement, the cancelled debt may be considered income to you that can be taxed.

If you dispute the debt, you can ask to include in the settlement agreement a statement that the debt is disputed, which may mean that the canceled debt does not count as income.

- Avoid including a confidentiality provision in the settlement agreement, unless the plaintiff or their attorney insists on including one. At the very least, you can use this as leverage in your negotiations to get the plaintiff to agree to something that you want. For example, if the

plaintiff agrees to remove negative information from your credit report, you will agree to include the confidentiality provision.

- Before making any payment, make sure you get the terms of the settlement agreement in writing and review them carefully. Also make sure you have a copy of the agreement signed by you AND the other side. Then, after your debt is paid off, request a written confirmation that you have fully settled your debt.

Contents of the Settlement Agreement

If you reach a settlement, the written agreement should include the following terms:

- The agreement should detail the settlement amount, whether it is being paid in a lump sum or over time, and the payment due dates.
 - The creditor should reduce the overall amount of the debt.
- If you agree to a payment plan, a statement of the payment due dates, how and when interest will accrue, and the address where you should send the payments.
- If you agree to a payment plan, make sure that it provides for late payments, either by giving you a “grace period” automatically, or by requiring the plaintiff to provide you with a written notice of late payment and an opportunity to cure (extra time to make the payment).
 - Try to get at least 10 days to make the late payment.
- A statement that the creditor agreed to accept the amount as payment in full for the debt and that the creditor will not demand more money in the future.
- A statement that the creditor will waive any interest, fees, and court costs.
- A statement that the plaintiff will not sell, assign, give, or otherwise transfer the debt.
- A statement that the debt is disputed.
- A statement that the creditor will remove the debt from your credit report, or at the very least, report your account to the credit bureaus as “Paid in Full” instead of “Settled” or “Paid in Settlement.”
- If the debt is disputed, a statement similar to the following “This Agreement is a result of a “contested liability” that was disputed in good faith, and does not constitute a discharge or cancellation of any debt for the purposes of 26 U.S.C. § 61(a)(11). Plaintiff therefore agrees that it will not issue an IRS 1099-C notice. Defendant, however, is advised to obtain independent tax advice concerning the tax consequences of this Agreement. This Section represents an agreement among the Parties that no Party will contend that anything in this Agreement constitutes a discharge of indebtedness, but does not constitute legal or tax advice regarding the consequences of this Agreement.”

- A statement that no judgment will be entered against you.
- A statement that the case will be dismissed with prejudice, and when it will be dismissed. This means they will not be able to file the case again.

BEST PRACTICES WHEN NEGOTIATING A SETTLEMENT

- Always get everything in writing, read everything carefully, and ask questions if there is something you do not understand.
- You do not have to provide proof about your income, assets, or bank accounts, if you do not want to. If you decide to provide that information, you can redact or block out account numbers and the names of your employer and your bank.
- Try to stay calm, no matter what the plaintiff or their attorney says. If you are worried the process is getting out of control, take a break or ask to continue the discussion another day.
- Never provide your bank account information to the other side or agree to automatic withdrawals from your account(s).
- Be careful not to sign any deal that is not in your best interests. Before you sign, ask yourself questions like:
 - Does this agreement protect the interests that are most important to me?
 - Does this agreement contain all of the things I believe we agreed to when we negotiated?
 - Do I believe settling this dispute is my only choice? Am I feeling pressured to settle?
 - What are the chances I could get a better outcome at trial?
- Settlement negotiations do not automatically stop the lawsuit. If a lawsuit was filed and you do not respond in time, the plaintiff can still get a default judgment against you.²

If you attempt negotiations *before* filing a response to a lawsuit, you should ask the plaintiff for additional time to respond to the lawsuit, in case your negotiations fall through. The plaintiff can agree to give you 15 additional days to file a response to the lawsuit.

- Be sure any agreement you reach for an extension of your deadline is in writing (for example, email).

² If you have been personally served with the lawsuit (the court documents were given directly to you), you have 30 days from the date you were served to respond. If you were served by substitute service (the court documents were left with an adult at your residence and mailed to you), you have 40 days from the date of the mailing to respond. If you do not respond in time, the plaintiff can ask the court to enter a default judgment against you.