Consumer Concerns for Older Americans

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Credit Card Debt and Credit Counseling

An increasing number of older Americans are now "aging into debt." Seniors generally get into debt to pay for groceries, prescription drugs, major home repairs, loans to children or grandchildren, and other necessities. Seniors are experiencing problems not only with mortgage and other types of secured debt, but with credit card debt as well. The average credit card debt of Americans over 65 increased by 89 percent between 1992 and 2001, to a self-reported household average of $4,041.[1] Seniors are also filing for bankruptcy in record numbers.

Seniors with unmanageable credit card debt have a number of options. Many turn to credit counselors for help. When done well, credit counseling can be very helpful for consumers in financial distress. However, if a senior falls prey to an unscrupulous agency, she is likely to end up even deeper in debt.

The ABCs of Credit Counseling

Brief History

The credit counseling industry developed in the mid-1960's through the efforts of credit card companies that saw a creative opportunity to recover overdue debts. Creditors created the industry and provided the bulk of the funding needed to keep the agencies in business.[2] At first, most of the agencies were non-profit and called

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[1] Tamara Draut and Heather C. McGhee, Demos, "Retiring in the Red", (February 2004). This report is available on the Demos web site, http://www.demos-usa.org. See also Jennifer Bayot, "Tear Up the Mortgage? Not Yet: Elderly Face Rising Debt Load", New York Times, July 4, 2004.

[2] For a summary of the credit counseling industry and current problems with the industry, see National Consumer Law Center and Consumer Federation of America, "Credit Counseling in Crisis", (April 2003). Available on-line at: http://www.nclc.org/initiatives/credit_counseling/content/creditcounselingreport.pdf. See also U.S. Senate Permanent Subcommittee on Investigations, "Profiteering in a Non-Profit Industry: Abusive Practices in Credit Counseling", (March 2004). Available on-line at: http://govt-aff.senate.gov/_files/032404psistaffreport_creditcounsel.pdf.

themselves the Consumer Credit Counseling Service (CCCS) of the regions they served. The CCCS agencies were affiliated with the National Foundation for Consumer Credit (NFCC), now called the National Foundation for Credit Counseling. Presently, there are many other types of credit counseling agencies and other trade associations such as the Association of Independent Consumer Credit Counseling Agencies (AICCCA).

The vast majority of credit counseling agencies have been granted tax-exempt status by the Internal Revenue Service (I.R.S.).[3] Yet not all agencies behave like true non-profits. The I.R.S. is currently taking a closer look at this issue and investigating agencies that have non-profit status, but in reality operate like for-profit businesses.

Credit Counseling Agency Services

Debt Management Plans

Through debt management plans (DMPs), a consumer sends the credit counseling agency a lump sum, which the agency then distributes to the consumer's creditors. In return, the consumer is supposed to get a break usually in the form of creditor agreements to waive fees and to lower interest rates. Consumers also gain the convenience of making only one payment to the agency rather than having to deal with multiple creditors on their own.

In the past, agencies charged little or no fees to consumers enrolling in debt management plans. This was mainly because of a creditor policy known as Fair Share through which creditors voluntarily returned to the agency a set percentage of the funds that were disbursed to them. As creditors have cut back on Fair Share payments, most agencies have been charging consumers higher fees. Some agencies charge as much as a full month's consolidated payment simply to establish an account.

Counseling, Education and Other Services

Because DMPs are the primary, or even sole, source of revenue for most agencies, there is a built-in bias toward enrolling consumers in these plans. However, particularly early on in the development of the industry, most agencies offered services other than

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[3] Non-profit status is technically a state law concept, making an organization eligible for certain benefits, such as state sales, property, and income tax exemptions. Although most federal tax-exempt organizations are non-profit, organizing as a non-profit at the state level does not automatically grant the organization exemption from federal income tax. The terms "tax-exempt" and "non-profit" organizations or corporations are used interchangeably even though there are some differences between them. For more information, see Internal Revenue Service, "Charities and Non-Profits", and I.R.S. Publication 557, *Tax-Exempt Status for Your Organization*, available at www.irs.ustreas.gov.

DMPs as well. Agencies often used excess revenues from DMPs to fund these other services, including counseling for consumers who were not enrolled in DMPs and consumer education seminars and courses. Despite growing financial problems, many agencies still offer a wide range of services. In fact, agencies should only be granted non-profit status if they provide meaningful educational services and meet other I.R.S. requirements.

Industry Abuses

The newer credit counseling agencies have pioneered more business-like methods of making debt management plans convenient for consumers, including flexible hours, phone and Internet counseling, and electronic payments. These improvements, in turn, have forced the "old guard" to be more responsive to their clients. Some of these newer agencies are responsible, effective and sensitive to their client's needs. However, as the newer agencies have gained market share, a number of serious problems have surfaced as well.

Common problems associated with many agencies include:

- **Lack of face-to-face or individualized contact with consumers.**
- **Nothing but DMPs.** The trend is away from providing a range of services such as consumer education and counseling for non-DMP clients and towards offering DMP-related services only.
- **Aggressive and sometimes deceptive marketing tactics.**
- **Higher costs for services.**
- **Close connections to for-profit businesses.**

WARNING SIGNS: SEVEN REASONS TO REJECT A CREDIT COUNSELING AGENCY (TIPS FOR CONSUMERS)

1. **High Fees.** Beware high fees! If the agency is vague or reluctant to talk about specific fees, go elsewhere.

2. **"Voluntary" Fees that Aren't So Voluntary.** Some agencies publicly claim that their fees are voluntary, but don't pass this information on to consumers. Others will tell you that their fees are voluntary, but will put a lot of pressure on you to pay the full fee, even if you can't afford it. When you ask about what the agency charges, be sure and ask if they consider any fees to be voluntary.

3. **The Hard Sell.** If the person at the other end of the line is reading from a script and aggressively pushing debt "savings" or the possibility of a future "consolidation" loan, hang up.

4. **Employees Paid by Commission.** Most credit counseling agencies are non-profit organizations that are supposed to consider your best interests when offering you counseling options. Employees that receive commissions for placing consumers in debt management plans are more likely to be focusing on their own wallets than yours.

5. **They Flunk the "Twenty to Thirty Minute" Test.** Any agency that offers you a debt management plan in less than twenty to thirty minutes hasn't spent enough time looking at your finances.

6. **One Size Fits All.** The agency should talk to you about whether a debt management plan is appropriate for you rather than assume that it is. If the agency doesn't offer any educational options, such as classes or budget counseling, consider one that does.

7. **Aggressive Ads.** Many agencies that advertise treat consumers fairly. However, some are being investigated or sued for deceptive practices. Many others charge unreasonable fees or offer no real counseling. Avoid choosing an agency based on advertising alone. Get referrals from friends or family, find out which agencies have been subject to complaints and talk to a number of agencies before making a decision.

Possible Legal Claims

There are a number of possible remedies available to challenge problems with credit counseling. The closest statutory scheme at the federal level is the Credit Repair Organizations Act (CROA). [4] The CROA applies only to agencies that offer credit repair services. The definition is broad, encompassing any person who performs or offer to perform any service, for a fee or other valuable consideration, for the express or implied purpose of i) improving any consumer's credit record, credit history, or credit rating; or ii) providing advice and assistance to any consumer with regard to any activity or service described above.[5] Many credit counseling agencies should fit this definition. However, a critical problem with the CROA and its state analogues[6] is that it does not apply to non-profit organizations.[7] Although the vast majority of agencies now charge at least some fees for service, nearly every organization in the industry operates as a non-profit. It may be possible to overcome this hurdle by arguing that a non-profit is a for-profit business in

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[4] 15 U.S.C. §§1679-1679j. See National Consumer Law Center, Fair Credit Reporting ch. 15 (5th ed. 2002 and Supp.).

[5] 15 U.S.C. §1679a(3)(A).

[6] See National Consumer Law Center, Fair Credit Reporting Ch. 15 (5th ed. 2002 and Supp.) (discussion of state credit repair organization laws).

[7] 15 U.S.C. §1679a(3)(B)(i).

disguise either because it focuses entirely on selling DMPs or because of close connections to for-profit affiliates.

Many state laws specifically prohibit the business of debt pooling (also known as debt management plans, debt consolidation, budget planning, or debt prorating). With notable exceptions, these state laws are generally ineffective and/or under enforced. The majority do not specifically provide for private enforcement. In fact, many of the laws are contained in the state criminal codes. Where no specific private remedy is provided, violations should be state unfair and deceptive acts and practices (UDAP) violations.[8]

The state laws vary in scope. About half of the states require some type of licensing for agencies providing debt management services.[9] But nearly half of these states explicitly exempt most non-profits from the licensing requirements. A minority of states restricts debt management business in the state to non-profits and requires these non-profits to be licensed.

The stronger state laws provide regulation beyond licensing and/or regulation. The most common substantive regulations include fee limits, requirements that consumers be given written contracts and that agencies maintain consumer payments in separate trust accounts. In addition, most of the states that require licenses also require agencies to post bonds. With only a few exceptions, most of the states that have licensing requirements also limit the fees that licensed agencies are allowed to charge.

About twenty states take a different, generally less restrictive approach. Most of these states generally prohibit debt adjusting, but allow a long list of exceptions. Most important, nearly all of the states exempt non-profit organizations from the general prohibition. Other states do not require licensing, but still limit fees agencies can charge and/or other practices.[10]

In addition to these specific debt management laws, advocates should also consider state credit repair laws and UDAP laws. Unauthorized practice of law statutes and regulations[11] and state loan broker laws[12] may also apply.

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[8] As with the CROA and state credit repair laws, there may be issues in some states regarding whether the UDAP law applies to non-profit organizations. See National Consumer Law Center, Unfair and Deceptive Acts and Practices §2.3.5 (5th ed. 2001 and Supp.).

[9] For a complete listing of these state laws, see National Consumer Law Center, Fair Credit Reporting §13.7.10 (2004 Supp.). As of 2005, this section will be moved to NCLC's Unfair and Deceptive Acts and Practices manual.

[10] Id.

[11] See National Consumer Law Center, Unfair and Deceptive Acts and Practices §5.12.2.4 (5th ed. 2001 and Supp.).

[12] See Id. §5.1.11.1.

Advocates should also keep up to date with I.R.S. rulings and investigations with respect to agency non-profit status. Information is generally available on the I.R.S. web site at www.irs.ustreas.gov.[13] The Federal Trade Commission also has information on its web site about current lawsuits and information for consumers. (See www.ftc.gov.).

Useful Information and Web Sites

National Consumer Law Center Publications and Articles:

National Consumer Law Center and Consumer Federation of America, "Credit Counseling in Crisis", April 2003. Available at: http://www.nclc.org/initiatives/credit_counseling/content/creditcounselingreport.pdf.

National Consumer Law Center, Fair Credit Reporting §13.7.10 (2004 Supp.). As of 2005, this section will be moved from the Fair Credit Reporting manual to NCLC's Unfair and Deceptive Acts and Practices manual.

National Consumer Law Center, Guide to Surviving Debt (2002 ed).

Available in Fall 2005: NCLC will publish and distribute a workbook for consumers on various strategies, including credit counseling, to address problems with credit card debt. Information about this publication will be posted on the "Seniors Initiative" section of NCLC's web site, www.nclc.org.

Also see NCLC's Consumer Facts for Older Americans, "Tips on Choosing a Reputable Credit Counseling Agency."

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[13] See, e.g., Debra Cowen and Debra Kawecki, "Credit Counseling Organizations", CPE 2004-1 (January 9, 2003). As of August 2004, available at www.irs.ustreas.gov/pub/irs-tege/eotopica04.pdf.