Comments on the National Conference of Commissioners on Uniform State Laws (NCCUSL) Uniform Debt Management Services Act

March 2006

The National Consumer Law Center, on behalf of its low-income consumer clients, and Consumer Federation of America oppose the NCCUSL Uniform Debt Management Services Act unless provisions regulating debt settlement services are removed or dramatically amended.

Our key concerns are:

1. The Act regulates debt settlement as a valid type of debt management service. We believe that this legitimizes a business that is very dangerous for consumers.

2. The Act gives states the option of allowing for-profit firms to offer debt management and debt settlement services, undermining recent steps by the I.R.S and some states to root out abuses in the credit counseling industry.

These concerns are described in greater detail below.

Debt Settlement

The regulatory framework for debt settlement in the NCCUSL Act is inappropriate and weak. Although there are many new requirements that would be imposed on debt settlement companies, it does not prohibit the most serious abuses in the debt settlement industry, such as charging excessive fees to settle debts or requiring or encouraging consumers to establish escrow accounts that settlement firms control or monitor. In short, the NCCUSL law legitimizes a business model that is dangerous for consumers.

Debt settlement can be a legitimate debt management tool for consumers who have funds to put toward settling debts. However, for-profit debt settlement businesses do not target these consumers. Instead, they focus on consumers who do not have funds to settle debts, requiring them to pay hefty fees while supposedly saving money to eventually pay off debts through agreements to be negotiated by the companies. While this process is going on, the consumers are not paying their debts and are generally facing collection, even lawsuits. In addition, interest and fees are accruing.

A summary of the main concerns with this business model can be found in a March 2005 investigative report by the National Consumer Law Center. The report is available on-line at http://www.nclc.org/action_agenda/credit_counseling/content/DebtSettleFINALREPORT.pdf.

In addition, the Federal Trade Commission and Attorneys General offices have brought several enforcement actions against debt settlement firms for unfair and deceptive practices in recent years.

Regulation of debt settlement companies should be separate from regulation of credit counselors/debt management providers. Including these two very different industries in the same statutory framework is confusing, complicated and ultimately difficult to administer. Throughout the NCCUSL process, consumer groups consistently recommended that the Committee adopt a different regulatory model for these separate industries. The Committee did not accept our recommendations even though the debt settlement industry has repeatedly refused to provide useful, public information about the track record and performance of their businesses.

Regulation should also prohibit abusive practices that are at the heart of the debt settlement business model, such as:

- Activities by non-attorneys that violate attorney licensing laws (unauthorized practice of law)
- Excessive fees
- Failing to provide an accounting of the services to be provided and the cost of such services
- Requiring consumers to delegate financial authority to the debt settlement companies, usually by signing powers of attorney
- False advertising or promises about the merits of debt settlement, including misleading information about how quickly debts can be paid off
- False or misleading comparisons between the cost of debt settlement plans and other types of debt relief

Non-Profit Limits

The NCCUSL Act allows states to decide whether to require that debt management and debt settlement companies be non-profit organizations. We urge states to choose the non-profit option. If states make this choice, passage of the NCCUSL Act with respect to traditional debt management will significantly improve consumer protections in most states. However, policymakers should understand that the law contemplates an extensive registration process that will be effective only as long as adequate resources are devoted to oversight and enforcement.

Limiting the industry to non-profit organizations is not about restricting competition, as many profit-oriented members of the industry argue. Instead, it is intended to ensure that credit counseling and debt relief services are truly educational and to prevent profiteering and poor-quality counseling. Only a true non-profit can be counted on to provide quality counseling and educational services and to act in the best interests of consumers.

Industry representatives claim that non-profit status has become meaningless due to abuses. This statement is both ironic, given that this abuse has been propagated in some cases by some of the same firms that are now promoting for-profit counseling, and untrue. While there has been widespread abuse of non-profit status, the I.R.S. is now taking this problem very seriously and is cracking down on offenders. Aggressive enforcement of non-profit laws and regulations is beginning to filter out the unscrupulous agencies.

Non-profit status is not a guarantee that an agency will provide holistic, consumer-centered, quality services, but it is a critical prerequisite that, along with careful oversight of various counseling and business practices, will go a long way toward protecting consumers.