AFSA Law Committee
Debt Settlement Working Group Report

1. Recent News

a. CFPB v. Freedom Debt Relief

On July 9, 2019, the Consumer Financial Protection Bureau settled its lawsuit against Freedom Debt Relief, LLC, the nation's largest debt-settlement services provider. Freedom agreed to pay $20 million in restitution to affected consumers and a $5 million civil money penalty. The CFPB lawsuit alleged that Freedom violated the Telemarketing Sales Rule (TSR) by charging advance fees and failing to inform consumers of their rights to funds they deposited with the company. The CFPB also alleged that Freedom violated the Consumer Financial Protection Act of 2010 by charging consumers without settling their debts as promised, charging consumers after having them negotiate their own settlements with creditors, and misleading consumers about the company's fees and its ability to negotiate directly with all of a consumer's creditors. The CFPB alleged that Freedom and its CEO violated the CFPA by engaging in the following conduct:

- Despite knowing there was a significant chance that it would be unable to negotiate directly with certain creditors, by touting its "negotiating power" when marketing its services, creating "the false net impression that Freedom itself would be able to negotiate directly with all creditors."
- Failing to disclose to consumers before they enrolled in Freedom Debt Relief's program that they might be required to negotiate with creditors on their own.
- Despite representing to consumers that it would not charge any fees for its services until it had settled a debt and the consumer had made a settlement payment to the creditor, charging fees in cases where Freedom Debt Relief had not settled the consumer's debt and no settlement payment was made.

The CFPB also alleged that Freedom Debt Relief and its CEO violated the TSR (and thereby also violated the CFPA) by engaging in the following conduct:

- Charging fees in the absence of a settlement.
- Failing to clearly and conspicuously disclose that the consumer owned the funds held in a dedicated account, could withdraw from the debt-relief service at any time, and would be entitled to all funds in the account other than fees earned by Freedom Debt Relief if the consumer withdrew.

The settlement requires Freedom to provide disclosures to consumers before enrollment regarding requests by Freedom for the consumer to negotiate directly with the creditor and the consumer's right to receive deposited funds upon withdrawal from Freedom's program. It also prohibits Freedom from charging a fee where it considers a debt to be resolved but where the debt had not been settled with the creditor ("non-settlement outcome"). Also, as part of the settlement, Freedom is enjoined from engaging in this conduct in the future. Freedom also agreed to a consent order with the Federal Deposit Insurance Corp (FDIC).

A copy of the amended complaint is available at:
https://files.consumerfinance.gov/f/documents/cfpb_freedom-debt-relief_first-amended-complaint_2019-07.pdf

A copy of the stipulated final judgment and order is available at:
https://files.consumerfinance.gov/f/documents/cfpb_freedom-debt-relief_stipulated-final-judgment-order_2019-07.pdf

b. Colorado Attorney General Lawsuit

On August 19, 2019, the Colorado Attorney General entered into a settlement agreement with Nationwide Debt Reduction Services and Sky Bridge Financial resolving allegations that the companies had violated Colorado consumer protection laws. Between 2017 and 2019 Sky Bridge Financial made loans supervised loans under Colorado's Uniform Consumer Credit Code (UCCC) to Nationwide's Colorado customers, despite both companies being wholly owned and operated by the same individuals. Under Colorado law, a debt management company and a lender with shared ownership cannot provide lending and debt management services to customers. The attorney general alleged this arrangement created a conflict of interest and was prohibited under Colorado law. The settlement requires Nationwide Debt Reduction Services to issue a $300 refund to each of the 315 Colorado customers impacted, totaling $94,500 and Sky Bridge must issue refunds to the 47 impacted borrowers, totaling $80,763. Additionally, both companies are barred from either lending or providing debt settlement services in the state. The Colorado Attorney General had previously taken action in 2013 against another debt management company for violations of the state's Uniform Debt Management Services Act by failing to provide required cancellation notices and consumer disclosures.

A copy of the press release is available at: https://coag.gov/press-releases/8-19-19/

c. CFPB Report of Consumer Credit Card Market

On August 27, 2019, the Consumer Financial Protection Bureau released its fourth biennial report on the state of the credit card market for the period 2017-2018. The Report includes a special discussion of credit card issuer experience with debt settlement company activity. First, the Report provides that issuers have internal policies that guide their specific settlement practices. Second, the Report provides some general debt settlement statistics related to credit card debt for 2017 and 2018. Finally, the Report includes tax implication information related to debt settlements, and that most companies disclose the potential of tax implications in a letter or telephone script.

Regarding settlements, the Report states "the volume of balances settled through DSCs grew proportionately faster than the growth in the issuers' overall account receivables and fresh charge-offs between 2017 and 2018. Pre-charge-off settlements grew 117 percent and post-charge-off settlements grew 104 percent between 2017 and 2018, compared to only 16 percent growth in accounts receivables and 12 percent growth in fresh charge-offs. Respondents reported nearly $2.2 billion in debt settled through DSCs within the two year survey period, $1.4 billion of which was settled post-charge-off, almost twice the volume of pre-charge-off settlements. Growth in pre-charge-off settlements accelerated more quickly than in post-charge-off settlements within the first half of the survey period before leveling off in 2018."

A copy of the 2019 Card Report is included in the materials.

d. Wall Street Journal Article

The Wall Street Journal published an article on August 10, 2019 titled "That Offer to Make you Debt-Free? It can Make You Worse Off." The article highlights the aggressive, marketing activities of debt settlement companies. The article seeks to expose "legal gray area" regarding the major credit bureau reporting agencies supplying consumer credit bureau data directly to debt settlement companies or indirectly to lenders affiliated with DSCs.

A copy of the article is included in the materials.

e. American Fair Credit Council 2019 Report

The American Fair Credit Council (AFCC), a trade association created and operated by the debt settlement industry, released a report in September 2019 entitled "2019 Economic Impact of the Debt Settlement Industry." This report is a biased, dangerous, and powerful piece of propaganda that was prepared by a former big tobacco economist from Brooklyn, New York named John Dunham of John Dunham & Associates. The press release which states that "debt settlement services contributed a total economic impact of $4.9 billion to the U.S. economy in 2018."

The report claims to have examined a broad range of data to prove that the debt settlement industry has a positive impact on the United States economy by: (1) providing employment opportunities stating that the "debt settlement industry is responsible for 27,980 jobs and $1.9 billion in wages, along with "$659.6 million in federal, state and local taxes"; (2) allowing creditors to receive funds faster through affordable settlement and avoid risks associated with debtors filing for bankruptcy; and (3) allowing debtors to be active participants in their local economy because settlements allow debtors to save money and gradually reinvest those funds in the local economy through shopping and entertainment. The report also suggests that debt settlement services should be expanded to the states where debt settlement companies are not allowed. There is a restriction on debt settlement services in eighteen (18) states. However, the report argues that the data demonstrates that in 2018 debtors in every state engaged in debt settlement. During 2018, debt settlement companies settled around 55% of the debt owed, and the average settlement fee was about 22.2% of the debt.

A copy of the report can be found at:
https://impactreport.americanfaircreditcouncil.org/assets/files/AFCC_Impact_Report2019.pdf

2. Survey Data Needed

a. Tracking DSC activity, company losses due to DSC activity, increases in first payment defaults, time and $ spend on handling and responding to disputes.
b. Use this information to quantify harms and provide to regulators and legislators interested in understanding and supporting enforcement and regulation.

3. **Legislative and Regulatory Strategy**
    a. **Federal**
        i. Letter to CFPB Director and FTC Chairman requesting examination of regulatory framework for DSCs. Seeking congressional signatures and support.
        ii. Draft legislation and seek to gain congressional hearing.
    b. **State**
        i. Meeting with state regulators and attorneys generals to raise issue of DSC consumer harm and increase DSC activity.
        ii. Try to understand lack of enforcement in states with outright bans or significant restrictions where DSC activity remains strong and is growing.

4. **Developing Best Practices**
    a. Implement **policies and procedures** for handling DSC activity in company
    b. Create **borrower education** materials regarding DSC harm
    c. Send **customer communications**

5. **Other Initiatives**
    a. Engage support, resources, and technical knowledge of nonprofits:
        i. National Foundation of Credit Counseling (NFCC)
        ii. Center for Responsible Lending (CRL)

    b. Engage support of other trade associations:
        i. ABA Card Policy Institute
        ii. Bank Policy Institute
        iii. **CDIA** follow-up needed regarding special comment code for credit bureau reporting to differential DSC activity from participation in non-profit consumer credit counseling programs which present different risk profiles.

BUREAU OF CONSUMER FINANCIAL PROTECTION | AUGUST 2019

The Consumer Credit Card Market

7.4 Special topics in credit card collections

7.4.1 Debt settlement companies

Borrowers sometimes work with DSCs, which are typically for-profit entities with the primary objective of enrolling qualified borrowers in a debt settlement program.[258] These firms do not receive any compensation from issuers. Instead, they typically assess the borrower a fee based on the original debt balance and contingent upon completing the settlement with the creditor. Debt settlement programs involve redirecting payments that consumers would have made to creditors to a borrower-controlled fund, which is then used by the debt settlement company to pay negotiated settlements. Since enrolled consumers stop making payments to creditors, borrowers who work with the DSCs typically find that their accounts continue to grow in delinquency and are reported to the credit reporting agencies.[259] Issuers may also pursue legal collections on these accounts. DSCs also often advise consumers to send a cease and desist communication letter to creditors as part of the program. Those issuers who sell debt often sell charged-off debt for which they have received a cease and desist communication letter to debt buyers because such debts generally are more difficult to recover.

All of the surveyed issuers have established policies and procedures about how to manage accounts enrolled with DSCs. In most cases, issuers require a third-party authorization document signed or otherwise authorized by the consumer in order to communicate with the DSC about the account. Some issuers reported that they will not negotiate settlements with DSCs even after receiving third-party authorization from the consumer. Some issuers have policies that allow the accounts to move quickly to placement with special third-party agencies for potential litigation. Most issuers that work with DSCs reported that they apply the same

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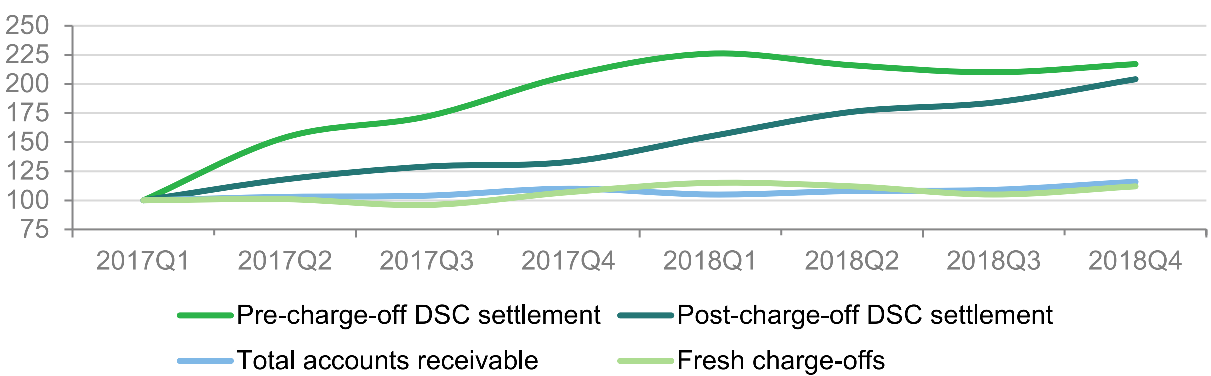
[258] *See* Greg J. Regan, *Options for Consumers in Crisis: An Updated Economic Analysis of The Debt Settlement Industry*, American Fair Credit Council, (Feb. 5, 2018), *available at* https://americanfaircreditcouncil.org/regan-reports/ (data as of Mar. 31, 2017).

[259] One RFI commenter claimed that consumers have "limited niche choices in debt relief assistance," while also lacking data necessary to make informed choices about debt relief products and services. The commenter advocated greater disclosure of performance data for non-profit and for-profit debt relief providers, including "success rate, the impact to future retirement savings, credit report/score impact, protection from legal action, and cost of the solution." *See* Steve Rhode Comment Letter, at 2.

settlement policies available to consumers who call the creditor directly to request settlements. However, a minority of issuers who work with DSCs have a set settlement rate specific to debt settlement companies, and these fixed rates forgive a smaller percentage of the balance owed than the floor settlement rates available to consumers who call the creditor directly and demonstrate financial hardship. In some cases, creditors have dedicated teams, either in-house or provided by third-parties, which specialize in engaging with DSCs.

Figure 10: INDEXED GROWTH IN PRE- AND POST-CHARGE-OFF DSC SETTLEMENT BALANCES, ACCOUNTS RECEIVABLE, AND FRESH CHARGE-OFFS (MMI)[260]



As shown in Figure 10, the volume of balances settled through DSCs grew proportionately faster than the growth in the issuers' overall account receivables and fresh charge-offs between 2017 and 2018. Pre-charge-off settlements grew 117 percent and post-charge-off settlements grew 104 percent between 2017 and 2018, compared to only 16 percent growth in accounts receivables and 12 percent growth in fresh charge-offs. Respondents reported nearly $2.2 billion in debt settled through DSCs within the two year survey period, $1.4 billion of which was settled post-charge-off, almost twice the volume of pre-charge-off settlements. Growth in pre-charge-off settlements accelerated more quickly than in post-charge-off settlements within the first half of the survey period before leveling off in 2018.

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[260] This graph represents changes in balances settled through for-profit DSCs, accounts receivables, or fresh charge-offs indexed to the values in the first quarter of 2017. These numbers do not include settlements for accounts where legal representation or other third parties were involved in settlement negotiations.

7.4.2 Cease communication

All issuers reported honoring cease communications requests, both verbal as well as written, from the consumers or their power-of-attorney, though only a minority of issuers reported tracking volumes of written requests separately from verbal requests. Issuers accommodated requests to cease all communications (phone calls, written communications, etc.) except to send legally required communications like monthly statements. They also accommodated special and limited cease communication requests (*e.g.*, "no phone calls only," "no calls to place of employment"). For accounts placed with third-party collectors, issuers generally recall those accounts with cease and desist requests and place them with attorney firms for further collections, including litigation. Those issuers who reported selling debt post-charge-off, regularly sold accounts with cease communication status. In 2018, 2.8 percent of the pre-charge-off balance inventory had cease and desist communication status, a 7 percent increase from 2017. Similarly, 4.7 percent of the post-charge-off balances had cease communication status representing a 10 percent increase compared to 2017. These increases may partly be due to the fact that more consumers are working with for-profit DSCs, who advise their clients to send cease communication requests to their creditors while waiting to negotiate settlements.

7.4.3 Consumer-level collections

When a consumer has multiple delinquent accounts, issuers may choose to collect debt at the consumer level by managing all the delinquent accounts together. Three-fourths of the surveyed issuers noted that they pursued some degree of consumer-level pre-charge-off collections for borrowers with multiple delinquent accounts, the same as in the Bureau's 2017 Report.[261] Respondents indicated that consumer-level collection strategies were more common for internal and first-party pre-charge-off collections than for third-party collections. Issuers who utilized a consumer-level strategy for pre-charge-off collections generally reported that the oldest delinquent account with the highest balance in the relationship was the lead account, and that all of a consumer's delinquent accounts were discussed during a single call to the consumer. The percentage of total pre-charge-off delinquent dollars belonging to consumers with multiple

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[261] 2017 Report, *supra* note 5, at 333.

accounts from the same issuer varied widely across issuers, ranging from 5.2 to 66 percent in 2018.

Most of the surveyed issuers did not have a consumer-level approach for recovering post-charge-off debt. For the minority of issuers that used a consumer-level recovery strategy post-charge-off, some issuers reported that they placed all of a consumer's charged-off accounts with the same third-party agency, while others reported that they used a litigation strategy involving assigning all of a consumer's charged-off accounts to the same law firm.

THE WALL STREET JOURNAL.

That Offer to Make You Debt-Free? It Can Make You Worse Off

Debt-settlement firms seek out struggling consumers to sell them plans that can leave them with high fees, damaged credit and a tax bill

By Jean Eaglesham and AnnaMaria Andriotis
Updated Aug. 10, 2019 7:58 am ET

Early this year, Phoebe Tu was rejected for a $30,000 loan to consolidate her credit-card debt. Within days, the gears were turning in a multibillion-dollar lending machine that enables consumers to borrow and, more recently, has tried to profit as they run into trouble.

The system is powered by the companies that compile credit reports based on consumers' borrowing histories. These credit-reporting companies typically sell the data to financial institutions offering loans, but as consumer debt has risen, another type of offer is being pitched to tens of millions of households.

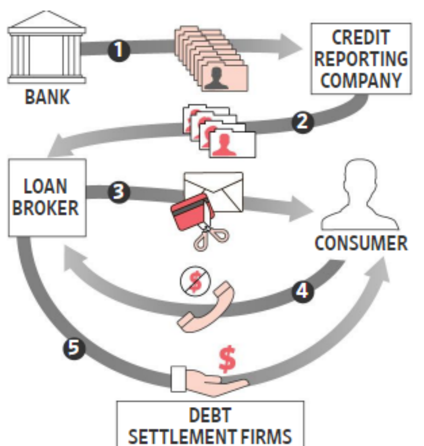
"You may be completely debt free in only 24-48 months," said a typical mailer from New York-based National Debt Relief, which added that the offer was based on a credit report.

Companies like National Debt Relief seek out heavily indebted consumers with a promise to help them get out from under it. But regulators say these debt-settlement programs can leave customers worse off, facing high fees, damaged credit scores and unexpected income-tax bills.

Steven Boms, an adviser to the American Fair Credit Council, the debt-settlement industry's trade body, said most people who enroll in debt-settlement programs already are behind on payments. "The only real alternative many of these consumers have to debt-settlement is bankruptcy," he said.

Selling Relief

How information from lenders has been used to sell debt-settlement services



1. Banks and other lenders sent information on consumers' debts to a credit-reporting company.

2. Credit-reporting company sold lists of consumers who appear to be getting deeper into debt to loan brokers.

3. Loan brokers mailed indebted consumers an offer for a loan, to consolidate their debts at a low interest rate.

4. Consumers called loan brokers and typically were refused a loan.

5. Instead, the loan brokers pitched a program from an affiliated debt-settlement firm. These programs can involve high fees and lead to damaged credit and unexpected tax bills.

Consumer debt, not counting mortgages, hit a record $4.02 trillion this year, a big reversal after Americans aggressively paid down what they owed and lenders wrote off unpaid debts following the financial crisis. As borrowers have fallen deeper into debt, the amount enrolled in debt-settlement programs has risen sevenfold, from $1.7 billion to $12 billion in the five years that ended in March 2017, according to a survey by the debt-settlement industry's trade group.

Data from credit-reporting companies has been used by some debt-settlement firms to solicit consumers as their debt is rising and when many are trying to sort out their financial situation. Other firms flood mailboxes with offers of loans, but when consumers call, the pitch can be very different.

‘Get the client’s guard down’

Ms. Tu, a 33-year-old business development manager in the San Francisco Bay Area, said that after she was rejected for the personal loan, a mailing from GreenLink Financial LLC arrived offering a loan of about $60,000—twice what she wanted—and at a surprisingly low interest rate. But when she called the firm, it turned her down for the loan and pitched her a debt-settlement program instead, she said.

“They said, ‘It’s to help you get by because you’re in a financial crisis.’ I’m not in a financial crisis, just trying for a low interest rate,” she told The Wall Street Journal.

Former GreenLink employees said only a small number of people who responded to the company’s mailings were offered loans. Instead, they were pitched a debt-settlement program that GreenLink sells on behalf of San Mateo, Calif.-based Freedom Debt Relief, the former employees said.

GreenLink’s salespeople were taught to “get the client’s guard down,” according to a GreenLink telephone sales script reviewed by the Journal. The Journal couldn’t determine the date of the script.

Most people who responded to GreenLink mailers were told they would be called back after loan-underwriting checks had been made, the former employees said. On that second call, the salespeople were told to say, “I couldn’t stop thinking about your file” and to pledge, “I am going to make YOU my top priority today,” according to the script.

Then, the consultants were told to break it to the caller that he or she didn’t qualify for the loan offer the company mailed, the script said.

“But this actually turned out to be GREAT NEWS!” the salespeople were instructed to say, according to the script, before pitching the debt-settlement program that offers “a payment which fits perfectly within your budget.”

Responding to an online complaint on Yelp by Ms. Tu, GreenLink wrote in May that its agent had “handled the call with utmost respect.” It added that Ms. Tu did “not meet the minimum requirements needed to get approved for any loan with our funding source.”

In response to a complaint on the Better Business Bureau website, GreenLink wrote that debt-settlement “is only an option for clients that we can’t qualify for a loan.”

The company didn’t respond to requests for further comment.

GreenLink, of Santa Ana, Calif., sent about 27 million mailers last year, according to estimates from data-provider Competiscan, up from about 1.2 million in 2015, the first calendar year after the company was formed.

Freedom Debt Relief in July agreed to pay $25 million to settle a civil lawsuit filed by the federal Consumer Financial Protection Bureau that claimed it charged consumers without settling their debts as promised, and misled them about fees. Freedom didn’t admit or deny the allegations.

A representative of Freedom Debt Relief, which describes itself as the nation’s biggest debt-settlement company, didn’t respond to requests to comment. National Debt Relief also didn’t respond.

Consumers who sign up for these programs are often told to stop paying their credit-card bills and other debts and instead put the payments in a special bank account, regulators say. Then the debt-settlement company negotiates with creditors to try to get them to reduce the consumer’s debt.

Halting payments, though, can trigger big penalties and potentially lawsuits by creditors and can hurt a person’s credit score. Even if the company persuades a creditor to reduce the debt—and there is no guarantee of this—the customer may owe income taxes on the amount of debt forgiven.

Taxes combined with fees these firms charge of as much as 25% of enrolled debt could wipe out any savings from a reduced debt balance. And a lower credit score that the strategy can trigger could make future borrowing more expensive.

The trade group's Mr. Boms said companies marketing loans often discover information during the loan-underwriting process, such as additional debts, that wasn't known when a mailer was sent. The group said last year that a survey of its members found debt-settlement plans reduced consumers' debts by an average of $2.64 for every dollar they paid the firms in fees.

Alternatives to debt-settlement companies include nonprofit credit counseling services, which attempt to work with the borrower and creditors to agree on a debt-management plan. These plans usually don't reduce the amounts owed; instead, creditors may agree to lower interest rates or waive fees. Credit counselors may charge fees for some of their services.

Legal gray area

At least some debt-settlement firms have used information from credit-reporting companies to pounce on troubled borrowers. The federal Fair Credit Reporting Act allows the companies, including TransUnion, TRU -1.05% Equifax Inc. EFX -1.23% and Experian EXPGY -0.13% PLC, to sell the data from credit reports only for certain uses, such as firm offers of credit. Debt settlement isn't specified in the law as a permitted use of this sensitive financial information to solicit consumers, and some experts consider it a gray area.

Some firms use the data to pitch debt-settlement plans, according to mailings reviewed by the Journal and lawsuits filed by consumers. The lawsuits reviewed by the Journal all were settled confidentially by the firms.

Other firms first offer loans and then shift their sales pitches to debt settlement, according to former employees of the companies and telephone sales scripts reviewed by the Journal.

Jeff Sovern, a law professor at St. John's University in New York, said that, based on his reading of the Fair Credit Reporting Act, it isn't legal to use consumer-credit reports for debt-settlement solicitations since "that's not a firm offer of credit." He added that the law requires credit-reporting companies to obtain certification from the entities with which they share such information that it will be used for a lawful purpose.

Credit-reporting companies that sell data used to solicit debt-settlement services "bear some responsibility" for the practices of some in that industry because they should be vetting the firms they sell the information to and how those firms use it, said Chi Chi Wu, staff attorney at the National Consumer Law Center, a nonprofit consumer-advocacy group.

TransUnion told the Journal it no longer supplies credit-report data to the debt-settlement industry. A spokesman said the company "historically…has sold prescreen data" to some debt-settlement companies, adding that this complied with federal law because these firms allowed consumers to delay payments for their services—which TransUnion said was a form of credit—or because they actually offered loans.

An Equifax spokeswoman said the company "does not, as a matter of policy, provide consumer-report information to companies who it knows to be charging advance fees for debt or mortgage-assistance relief." The spokeswoman didn't respond to questions about whether Equifax sells information to debt-settlement companies that don't charge advance fees, a group that includes the biggest players in the industry. By law, for-profit companies that sell debt-settlement services over the phone are barred from charging advance fees.

Experian said it has never sold information from credit reports to the debt-settlement industry for solicitation purposes.

CreditAssociates LLC, a Dallas-based debt-settlement company, said it stopped receiving data from TransUnion last year, but sent offers to consumers based on the company's information as recently as last month.

"You are preapproved for a debt relief program that can save you thousands of dollars," said a mailer sent earlier this year by CreditAssociates. "This 'pre-screened' offer of credit is based on information in your credit report."

Rick Burton, a co-founder of CreditAssociates, said its debt-settlement offer in the mailer qualified as credit because clients can pay the fees it charges in installments, rather than a lump sum. This approach was approved by TransUnion compliance personnel, he said.

A TransUnion spokesman said it doesn't provide legal or compliance advice to its customers and doesn't approve customers' mailers.

Prof. Sovern called the practice of letting customers pay fees in installments a "quite imaginative" way of using the fair-credit law's provision allowing the use of credit-report data for loan offers "for a completely different purpose of debt-settlement offers."

Concern about credit score

In some cases, sales pitches for debt-settlement programs appear to minimize the risk to a consumer's credit score. Amanda Ricchio, a 34-year-old accounting student in Racine, Wis., was mailed offers for loans after she put a few thousand dollars of college costs on her credit cards. The offers said they were based on credit reports.

Ms. Ricchio called Simple Path Financial LLC, of Irvine, Calif., but was refused the 4.99% loan she had been pitched. Instead, she said she was offered a debt-settlement program, which she was told would cause only a "slight hit at first" to her credit score.

Ms. Ricchio, who had worked for a credit union where her father was chairman, said she didn't believe the claim. "I know this kind of program would actually cause serious damage to my credit score," Ms. Ricchio said.

Mr. Boms, the adviser to the debt-settlement industry trade group, said the credit scores of the "vast majority" of people who enroll in the programs would fall due to their existing financial problems, whether or not they go this route.

Simple Path was founded in 2016 by Bradley Smith and Branden Millstone and sells debt-settlement plans from another firm founded by the two men, public records show. Mr. Millstone in an interview said a "very large number of people" who respond to Simple Path mailers are offered a loan, adding that he didn't have the exact numbers.

People who do qualify for a loan may choose debt-settlement as a better option than "putting a Band-Aid on their situation" by taking on more debt, he added.

—Lisa Schwartz
contributed to this article.
https://www.wsj.com/articles/that-offer-to-make-you-debt-free-it-can-make-you-worse-off-11565409601

September ___, 2019

BY ELECTRONIC MAIL

Hon. Kathleen Kraninger
Director
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Hon. Joseph J. Simons
Chairman
Federal Trade Commission
600 Pennsylvania Avenue NW
Washington, DC 20580

Dear Director Kraninger and Chairman Simons:

We write to request that your agencies coordinate to thoroughly examine the legal and regulatory frameworks governing the so-called debt settlement company (DSC) industry. Having reviewed the July 9 consent order between the Consumer Financial Protection Bureau (CFPB) and Freedom Debt Relief—a DSC that allegedly helps consumers by charging them high fees and encouraging them to default on unsecured loans with the promise of settling them for cents-on-the-dollar—we are deeply concerned that regulation of DSCs is lacking in meaningful consumer protections. This lack of regulation decreases access to, and increases the costs of, consumer loans.

The debt settlement industry has grown over the last decade despite a healthy economy, relatively high consumer confidence metrics, and slowing consumer default rates. One reason for this unexpected growth is that DSCs have expanded their customer base beyond consumers in default to those who are current in their loan repayments. Based on information we have reviewed, we believe the DSC business model today operates as follows:

1. DSCs purchase credit information from credit reporting agencies to identify consumers who have unsecured trade lines on their credit report. These lines include credit card debt, installment loans, and other types of unsecured credit. In addition to aggressive television and radio advertisements effectively guaranteeing the DSC's ability to reduce amounts owed to creditors, DSCs directly market their services to consumers based on these credit reports—including to consumers who are current in their loan repayments. DSCs have also engaged in partnerships with lenders purporting to offer debt consolidation loans; in actuality these lenders make a minimal number of loans to consumers and instead act as conduits to funnel consumers to DSC programs. The use of consumer credit reporting agency data and lender partnership activity was recently highlighted in the Wall Street Journal.[1]
2. Once a consumer engages a DSC, the DSC instructs the consumer to sign a power of attorney in favor of the DSC. The DSC then instructs creditors and debt collectors to cease contact with the borrower, which the creditors must then do under the Telemarketing Sales Rule (TSR), the Telephone Consumer Protection Act, the Fair Debt

[1] Wall Street Journal, August 10, 2019, "That Offer to Make You Debt-Free? It Can Make You Worse Off"

Collection Practices Act, and other federal and state statutes and regulations. The DSC instructs the borrower to stop repaying all covered debts.

3. Having stopped payment, the consumer defaults on his or her loans, causing the borrower's credit score to plummet, often resulting in a 60-100 point reductions in FICO scores.
4. Instead of making payments to the lender, the DSC instructs the borrower to make monthly payments to the DSC, which are escrowed for a period of at least a few months. Once the escrow account is sufficiently large, the DSC attempts to negotiate a settlement plan with the borrower's creditors.
5. Under the TSR, the DSC may not collect fees unless at least one creditor accepts settlement. If one creditor agrees to a debt settlement, the DSC immediately charges fees, often many and high, which are debited from the escrow account.
6. Recently, DSCs have begun engaging in lending activity through bank partnerships, expediting payment of agreed upon settlements while amortizing payment of their fees and ensnaring at-risk consumers in additional debt.

We believe that this practice of structuring consumer defaults ultimately harms consumers more than it helps them.[2] The siphoning off of family income into an escrow account makes consumers, some of whom may be struggling to pay bills, even more cash-poor while seriously damaging their credit score and potentially driving them out of the mainstream financial system. DSCs are ultimately unable to help many consumers even reach the payment plan stage; approximately 50% of consumers who do reach the repayment plan stage do not complete the payment plan.

Moreover, a DSC's interference in the relationship between a creditor and a borrower creates an artificial externality on credit underwriting. An increase in the number of purposeful defaults by borrowers with a current repayment status (and the corresponding decrease in collection efficiency) forces lenders to try to develop mechanisms to screen for and deny more consumers loans. Furthermore, lenders may have to consider raising rates on future borrowers to cover the increase in defaults. Decreased access to loans offered at higher rates is an undesirable consumer financial services outcome.

While your agencies have actively pursued debt settlement agencies through enforcement actions, we encourage you to do more to prevent the harm that consumers face from DSCs. To that end, we request that your transmit to us by November 1, 2019: (i) a summary of existing federal authorities on which your agencies do or could rely on to regulate, supervise, or enforce conduct by DSCs; (ii) your views on whether there are any gaps in such authorities that inhibit your ability to regulate DSCs; and (iii) your views on what additional authorities your agencies need to ensure that consumers are not harmed by potentially predatory DSC activity.

If you have any questions, please do not hesitate to reach out to any of us directly.

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[2] Though anecdotal, the CFPB's Consumer Complaint Database is replete with narratives from consumers who allege that the DSC business model is inherently fraudulent.

Debt Settlement Companies

What's Hiding in Your Portfolio?

Austin Clancy, Vice President/Director
Government Relations

1

Debt Settlement Companies (DSC)

DSC Industry Overview

- DSCs are **for-profit companies** that work with indebted consumers and attempt to settle their debts for less than the amount owed. DSCs advise and instruct consumers to cease contact and stop making payments to their creditors.
- The **strategic default** that consumers are encouraged to engage in has a **detrimental effect on consumer credit profiles** and the financial stability of consumers.
- During the negotiation phase consumers are instructed to pay money into a trust account with the hope of affecting a settlement with those funds in the future.
- The average time to reach a settlement under the DSC plan is **3 to 6 months**[1]; the average DSC program is 36 months[2].
- With no reporting structure, creditors are often first informed of DSC involvement when the **power of attorney and "cease and desist" letter** are received.
- Creditors are left with few options to contact consumers engaged with DSCs and are often unable to communicate other forms of remediation for customers that may be available.
- While DSC activity has been associated with delinquent consumers in the past, the industry is now shifting its marketing to attract **current consumers**.

1. OneMain Internal Data
2. Federal Trade Commission. Debt Settlement Companies. https://www.consumer.ftc.gov/articles/0145-settling-credit-card-debt

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2

Debt Settlement Companies (DSC)

Largest Market Participants

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3

Debt Settlement Companies (DSC)

Largest Market Participants

Over **$10.6 billion** settled for over **805,000** customers; **$8.4 billion** of consumer debt under management

Over **$1 Billion** in settled debt with over **180,000 Customers**

Over **$1 Billion** in settled debt with over **180,000 customers**

Over **$450 million** in settled debt with over **200,000 customers**

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4

Debt Settlement Companies (DSC)

DSC Marketing – Customer Acquisitions

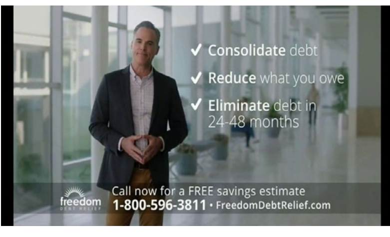
- Between 2012 and 2017, the amount of debt enrolled with DSCs grew from **$1.7 billion to $12 billion**[1]
- It is currently estimated **5 – 7 million consumers** are engaged with DSCs.
- DSCs employ high SEO presence on Google and other platforms that pushes negative information down in search results
- **Targeted advertisement on social media** (Facebook, Instagram, etc.) with limited interaction or outside comments
- Marketing materials through the mail specifically targeting consumers with high amounts of debt
- **Trigger Leads** – Large balance increase on an unsecured tradeline triggers offer for DSC services
- Loan brokers that offer debt consolidation loans are being used to funnel customers to DSC program. Very few consumers are actually offered loans and are instead offered DSC services.[1]

5   1. Wall Street Journal, August 10, 2019, "That Offer to Make You Debt-Free? It Can Make You Worse Off"   OneMain Financial

5

Debt Settlement Companies (DSC)

DSC Marketing – Television



6   1. Kevin Harrington, Accredited Debt Relief   OneMain Financial

6

Debt Settlement Companies (DSC)

DSC Marketing – Radio

- "Are you struggling with debt…"
- "Call today for the secret the credit card companies don't want you to know…"
- Various marketing campaigns are using ethnic accents and speech patterns to target listener demographics for particular radio stations
- Increased frequency during daytime radio designed to target working consumers

Debt Settlement Companies (DSC)

DSC Marketing – Mail Solicitation (National Debt Relief)

Congratulations! You've been pre-qualified for a very special credit offer from National Debt Relief for its popular debt-resolution program. That means you may be completely debt free in only 24-48 months, you don't have to pay any fees until your debt is resolved, and because you're pre-qualified, once your debt is resolved we'll allow you to defer payment of your program fees.*

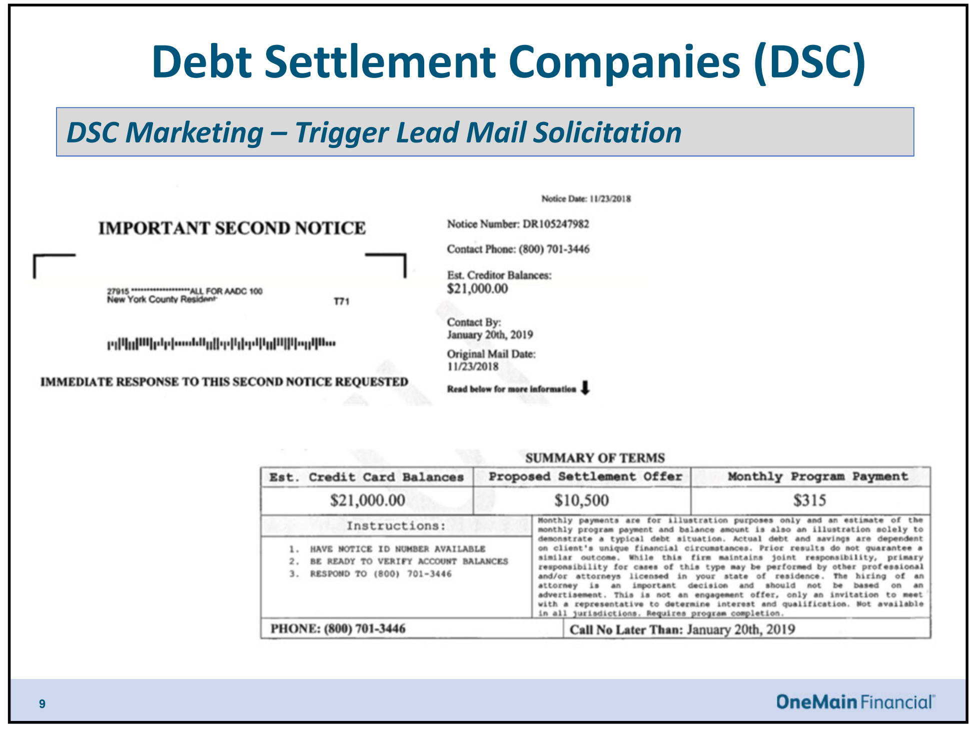
AFCC American Fair Credit Council | Top Consumer Reviews.com 2019 5 Star rating | BBB ACCREDITED BUSINESS A+

YOUR CURRENT DEBT BALANCE**:
$84,000

NATIONAL DEBT RELIEF COULD SAVE YOU**:
$25,200

YOUR MONTHLY PAYMENT AS LOW AS**:
$1,225.00

PRESCREEN & OPT OUT NOTICE: *This "prescreened" offer of credit is based on information in your credit report indicating that you meet certain criteria. This offer is not guaranteed if, after responding, it is determined that you no longer meet these criteria. If you do not want to receive prescreened offers of credit from this and other companies, call TransUnion at 1-888-567-8688 or visit the website at www.optoutprescreen.com; or write TransUnion Opt Out Request PO Box 505, Woodlyn, PA 19094-0505.*



Debt Settlement Companies (DSC)

DSC Marketing – Trigger Lead Mail Solicitation

Notice Date: 11/23/2018

IMPORTANT SECOND NOTICE

27915 ******************ALL FOR AADC 100
New York County Resident
T71

IMMEDIATE RESPONSE TO THIS SECOND NOTICE REQUESTED

Notice Number: DR105247982

Contact Phone: (800) 701-3446

Est. Creditor Balances:
$21,000.00

Contact By:
January 20th, 2019

Original Mail Date:
11/23/2018

Read below for more information

SUMMARY OF TERMS

Est. Credit Card Balances	Proposed Settlement Offer	Monthly Program Payment
$21,000.00	$10,500	$315

Instructions:

1. HAVE NOTICE ID NUMBER AVAILABLE
2. BE READY TO VERIFY ACCOUNT BALANCES
3. RESPOND TO (800) 701-3446

Monthly payments are for illustration purposes only and an estimate of the monthly program payment and balance amount is also an illustration solely to demonstrate a typical debt situation. Actual debt and savings are dependent on client's unique financial circumstances. Prior results do not guarantee a similar outcome. While this firm maintains joint responsibility, primary responsibility for cases of this type may be performed by other professional and/or attorneys licensed in your state of residence. The hiring of an attorney is an important decision and should not be based on an advertisement. This is not an engagement offer, only an invitation to meet with a representative to determine interest and qualification. Not available in all jurisdictions. Requires program completion.

PHONE: (800) 701-3446

Call No Later Than: January 20th, 2019

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Debt Settlement Companies (DSC)

DSC Marketing – General Marketing Claims

- “Creditors take us seriously because we’ve been negotiating with them for over a decade”
- “Unlike some companies that charge fees before debts are settled, Freedom Debt Relief never charges a fee until we’ve done our work and negotiated a settlement.”
- “Compared to bankruptcy, our program has a manageable effect on your credit score and won't cause long-lasting secondary problems.”
- “During the entire process, you'll be protected from harassing phone calls, insistent emails, in-person visits and other high-pressure tactics that creditors and collections agencies use to force payment.”

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Debt Settlement Companies (DSC)

DSC Plan Characteristics

- Most debt settlement companies require a minimum debt threshold to allow consumers to enter into the plan, normally between $5,000 - $20,000 depending on the size of the company, with some larger companies targeting $30,000 - $50,000 debt loads.
- The average number of accounts enrolled in a debt settlement plan is **5 – 7 accounts per consumer**
- The ability to negotiate a settlement is predicated on the consumer's ability to pay into the trust account; the larger the payments, the sooner the settlement offer
- Online customer acquisition is largely employed by these companies as a way to skirt state level fee caps, currently the **average fee is 20-25%[1] of the enrolled debt with some as high as 35%[2],** which includes handling fees, transactional fees, and tax consequences for forgiven debt are factored.
- Settlement offers are made on individual accounts but also on bundled accounts, where DSCs make multiple offers for a portfolio of consumers

1. Center for Responsible Lending: State of Lending, http://www.responsiblelending.org/state-of-lending/reports/12-Debt-Settlement.pdf
2. National Foundation of Credit Counseling. Evaluating Debt Settlement Companies. https://www.nfcc.org/tools-and-education/money-management-tips/consumer-protection/evaluating-debt-settlement-companies/

Debt Settlement Companies (DSC)

DSC Lending Activities

- DSCs have now begun direct lending activities, utilizing bank partnerships through invitation-only loans.
- Freedom Debt Relief offers these loans through Consolidation Plus, a subsidiary.
- Consumers enrolled with DSCs that have made consistent payments into the escrow account both before and after settlements have been reached are offered the loan.
- The rate is determined through risk based pricing with average term of 24-72 months and a 4.9% origination fee.
- The loans are originated through a New Jersey state bank and then assigned back to Freedom or an affiliate for servicing.
- The loans ensure that Freedom receives their fees and enables the customer to pay their settlement off with their creditors immediately, while shifting the obligation to Freedom.

Debt Settlement Companies (DSC)

DSC Consumer Harms

- During the settlement negotiation period, the reported late payment activity causes the credit score to drop an average of 60-100 points for those engaged with DSCs.[1]
- Not all creditors work with DSCs, leaving some debts outside of the proposed plan
- The negative payment activity also exposes consumers to unnecessary accrual of interest, late fees, and penalties depending on the credit product, as well as increased exposure to collection suits and instances of bankruptcy.
- DSC program efficacy is problematic with only 50% of accounts being successfully negotiated to settlement[2]; and of those where settlement is reached, only 50-55% of consumers successfully completing the DSC program.[1]
- Consumers that fail to complete the program are left in a worse position than before they engaged the companies due to fees paid and compounded damage to their credit profile.
- Consumers are not able to engage in traditional credit counseling or debt management because they lack the necessary liquidity due to fees paid to DSCs or funds abandoned under the DSC plan.

13

1. Center for Responsible Lending. State of Lending: Debt Settlement. http://www.responsiblelending.org/state-of-lending/reports/12-Debt-Settlement.pdf
2. OneMain Internal Data

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13

Debt Settlement Companies (DSC)

DSC Consumer Motivations – OneMain Survey Results[1]

- Customers that are engaging with DSCs are desperate and due to the limited research and data available, many customers go with the first DSC that they find with many choosing a DSC due to online and traditional marketing avenues.
- Most customers do not care how much the DSC will make in fees, only in the amount that they pay.
- Traditional outreach to customers experiencing hardship often comes too late to intervene prior to DSC engagement; this has caused OneMain to reevaluate hardship outreach. This is also problematic for current customers that engage DSCs.
- Bankruptcy is not viewed as an option because many customers do not qualify or are concerned with the repercussions.
- Most of those surveyed did not feel prepared to make large scale financial decisions due to desperation and the DSCs were perceived as an easier resolution.
- Customer satisfaction was largely dependent on the success of the program, which when compared to DSC program success rates shows that consumers who engage with DSCs are typically not satisfied with the program.

14

1. OneMain Internal Data

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14

Debt Settlement Companies (DSC)

DSCs Targeting Installment Lenders – Why Now?

- DSC industry has seen market erosion from larger banks and credit card companies refusing to participate as evidenced in the recent CFPB action against Freedom Debt Relief
- The odds of negotiating a lump sum settlement is less likely than a monthly payment plan given the limited funds from consumers.
- Payment plans are not preferred for credit card companies due to scrutiny regarding deferred losses or possible masking of poor initial credit risk selection practices.
- Under the 2010 revisions of the FTC's Telemarketing Sales Rule "advance fee ban", DSCs must effect a settlement and make a payment to a creditor prior charging any fees.
- Installment lenders are usually more likely to allow for a structured settlement given the industry's palate and understanding of the risk profile of our customers.
- By targeting installment lenders, DSCs ensure that they are able to adhere to the "advance fee ban" while gaining access to the trust account funds during the pendency of negotiating other accounts.

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Debt Settlement Companies (DSC)

DSC State Regulation and Enforcement

- Many states currently regulate DSCs under debt management and consumer credit counseling statutes, with only 5 states having dedicated DSC statutes.
- Debt management and consumer credit counseling statutes are not designed to regulate and enforce for the level of risk of consumer harm associated with DSC activity.
- Due to the online presence, many DSCs avoid licensure at the state level by which they are able to skirt fee caps placed on debt management or consumer credit counseling services. Many larger companies selectively license in various states to lend accreditation to their business activities, while ignoring licensing in less favorable states.
- Several states regulate these companies through agencies that are not financial regulators, instead monitoring these companies through license administration rather than true regulation and enforcement leaving consumers exposed.
- The majority of state statutes lack sufficient protections for consumers including limited bonding and insurance requirements, no specific marketing prohibitions, no service requirements, limited disclosures that fail to fully apprise the consumer of possible harms, and no educational requirements for licensees.

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Debt Settlement Companies (DSC)

DSC State Legislative Action

- The DSC industry is actively working to adjust or remove fee caps and regulation at the state level.
- Recent legislative action by the DSC industry includes:
  - **Ohio HB 131/SB 112** – Removal of fee caps for debt adjusting (Currently in Hearings)
  - **Tennessee HB 1182/SB 1013** – Establishes a new license for debt resolution services, removing those activities from debt management statutes and creating a licensing structure with limited disclosures and consumer protections (Held over for next session)
  - **Virginia HB 2196** – Establishes an additional license for debt settlement activities, establishes a different fee structure from debt management services (In Committee)
  - **Mississippi HB 792 (2018)** – Removed for-profit debt management services from the fee structure of non-profit debt management service providers. (Enacted)
  - **Pennsylvania (2014) – SB 612** – Removed prohibition against debt settlement activities, established licensing requirement, disclosures, and mild fee caps

Debt Settlement Companies (DSC)

DSC Federal Regulation and Enforcement

- Federal level regulation has been limited largely to regulation by enforcement actions by the CFPB and FTC.
- The only federal law that currently applies directly to DSC activity is the 2010 addition to the FTC's Telemarketing Sales Rule which prohibits advance fees until services have been rendered. While the rule was effective at stopping some advance fee abuses, it only requires a DSC to settle a single debt or have an agreed upon payment plan with a creditor to charge fees.
- The recent CFPB action against Freedom Debt Relief exposed troubling business practices such as violation of TSR, deceptive marketing, and lack of transparency.
- There is currently no agency engaging in preemptive regulation of the DSC industry which places the larger part of the burden of regulation on the states.
- Congress has not addressed the growth and possible harms of industry through legislation and this industry has benefited from its low profile.

What's Hiding in Your Portfolio?

10%

of Total Charge Off
In 2018
Attributed to DSC Activity

19

Debt Settlement Companies (DSC)

OneMain DSC Statistics

- OneMain receives notices averaging roughly 3500 accounts per month that have been engaged with DSCs.
- Majority of these engagements had no signs or warnings of a hardship situation, contact with the customer simply stops and then a DSC enrollment notice is received
- Since July 2018, greater than 50% of new DSC enrollments at OneMain have been only 0-2 payments behind, but there has been a large increase in consumers that are current on their payments engaging DSCs.
- As of September 2019, ___ % of new enrollments are currently paid customers
- Roughly 50-55% of those enrolled with a DSC finish the payment plan to completion.
- UPDATE SLIDE WITH RECENT STATS FROM ANALYTICS

1. Center for Responsible Lending: State of Lending, http://www.responsiblelending.org/state-of-lending/reports/12-Debt-Settlement.pdf
2. National Foundation of Credit Counseling. Evaluating Debt Settlement Companies. https://www.nfcc.org/tools-and-education/money-management-tips/consumer-protection/evaluating-debt-settlement-companies/

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20

15%

of Total Charge Off
Year to Date for 2019
Attributed to DSC Activity

21

Debt Settlement Companies (DSC)

What Can You Do?

- Develop and implement internal tracking for DSC activity and share your data with AFSA so we can appropriately gauge DSC activity
- Institute training, policy and procedure to effectively identify and respond to DSC activity for your organization
- Speak with your state associations and lobbyists to make them aware of the expansion of DSC activity and to monitor state and federal bills that expand DSC activity
- Speak with state and federal regulators regarding complaints from customers about DSC activity and encourage action to protect consumers and licensees
- Speak with your state and federal representatives to educate them on the danger to consumers posed by DSCs and the negative impact DSCs have on the credit markets that will ultimately lead to increasing the cost of credit
- Work with your customers to educate them on internal remediation and hardship programs that your organization offers
- CLEAR COMMUNICATION WITH OUR CUSTOMERS IS THE BEST TOOL FOR LIMITING DSC HARMS!

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22

Austin Clancy, Director/Vice President, Government Relations

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23