Written Opposition Testimony on Senate Bill 112

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Chair Hackett, Vice Chair Hottinger, Ranking Member Craig, and members of the Ohio Insurance and Financial Institutions Committee, I am Danielle Fagre Arlowe, and I am Senior Vice President of the American Financial Services Association,[i] known as AFSA. I thank you sincerely on behalf of AFSA and its members for the opportunity to submit written testimony today regarding our significant concerns relating to SB 112.

We are specifically concerned about the exemption from Ohio fee limitations that would be afforded to debt adjusters, otherwise known as debt settlement companies. The proposed legislation inaccurately implies that debt adjusters are currently regulated at the federal level by the Telemarketing Sales Rule ("TSR") at 16 C.F.R. part 310. In fact, the TSR merely prohibits a debt adjuster from charging up-front fees and requires the disclosure of certain information to customers before signing them up for debt relief services. The TSR offers no regulatory framework and contains no limit on the fees charged to consumers. Without elements such as state licensing, regulation, and oversight of fees, the bill provides no framework to control debt adjusters and the fees they hope to charge distressed and potentially distressed borrowers. By contrast, many states have debt settlement fee caps on the amount that a for-profit debt settlement company can charge a customer. In fact, at least 40 states either have fee limits or an outright prohibition on for-profit debt settlement companies.

The Ohio Revised Code currently *does* authorize debt settlement in Ohio, as long as the debt adjuster does not charge a fee that "exceeds eight and one-half per cent of the amount paid by the debtor each month for distribution to the debtor's creditors or thirty dollars, whichever is greater."[ii] The proposed exemptions under SB 112, however, would open the floodgates in Ohio to for-profit debt adjusters by eliminating fee limits entirely. These companies thus would be able to charge any fees that they desire and to perform a service for consumers that creditors already provide for free.

Based on our experience, not only will consumers likely be charged exorbitant fees, but it is typical for debt adjusters to instruct borrowers to stop making payments to their creditors, harming consumers by making them delinquent on their credit obligations, and ruining their credit profile. Communication between creditors and their customers is critical; by their nature, for-profit debt settlement companies sever those valuable lines of communication.

Harm to Consumers

The debt settlement industry inundates consumers with ads promising relief from so-called "crushing" debt, but the debt settlement industry itself is more of a wolf in sheep's clothing, as it typically presents itself as a fiduciary of consumers, when in fact it often poses more harm than good. The process typically leaves borrowers, at the very least, no better off and often much worse off. The potential for harm is so great that the Consumer Financial Protection Bureau (CFPB) warns consumers directly on its website that "debt settlement companies may well leave you further in debt than when you started."[iii]

As referenced above, debt settlement companies disrupt the important relationship that exists between borrowers and creditors by inserting themselves into process and cutting off communication between the two. This disruption creates barriers to any resolution the borrower may already have at their disposal, namely, the ability to work directly with the creditor on a new debt reduction or payment plan without additional charge. Creditors are committed to working with distressed borrowers, as keeping accounts current is in everyone's best interest. Conversely, debt settlement companies advise borrowers to stop making payments on their accounts and cease communications with their creditors. This advice increasingly comes to borrowers who are current on their account and have not yet missed a payment.

Advising a borrower to stop making payments leads to significant harm for the consumer, who will now have a credit report reflecting missed payments and higher loan balances. This damage reduces their future options for credit and increases its cost, which says nothing of the late fees and increased interest they will face directly as a result of the missed payments. These costs are in addition to the fees the consumer pays directly to the debt settlement company itself. Accounting for late fees, the higher cost of future credit, fees charged by the settlement company, plus the taxes owed on any debt forgiven, it is easy for the consumer to come out of the process worse off, and it's clear why the CFPB warned of such an outcome.

The National Black Caucus of State Legislators, known as NBCSL, recently ratified a 2020 policy position on protecting minority communities from debt settlement companies. In it, NBCSL recognizes that stopping payments causes accounts to default and often leaves consumers in a worse-off position.

Steps Taken by Regulators

Debt settlement companies have faced recent scrutiny from federal and state regulators. Abuse is so rampant that the Federal Trade Commission (FTC) has a specific category of enforcement reserved for "Companies and People Banned from Debt Relief." This category includes hundreds of individuals and businesses that have harmed consumers in the process of offering debt settlement or debt resolution services. The CFPB recently settled with the largest debt settlement services provider in the country after the company was caught charging consumers without settling their debts, misleading consumers about the company's fees, and instructing borrowers to expressly mislead their creditors, among other damaging actions. The Colorado attorney general also recently took action against another debt settlement company that was making loans directly to its own debt settlement customers despite the state's law banning this practice, a clear conflict of interest.

When debt settlement companies prey on vulnerable consumers, the consumer and the lender both pay the economic price. In a 2010 study, the United States Government Accountability Office (GAO) found that "some debt settlement companies engage in fraudulent, deceptive, and abusive practices that pose a risk to consumers."[iv] Regarding consumer benefit, the GAO further noted FTC investigations that revealed less than 10 percent of consumers successfully complete programs through these settlement companies.[v]

Proposed Solutions

Debt settlement companies should be carefully regulated to ensure that the possible harm to consumers is minimized. Any regulatory structure should start with the requirement that such companies be fully licensed and examined by the state. Importantly, debt settlement companies should be prohibited from owning or being in any way financially affiliated with a creditor, or having any pecuniary interest in a creditor, because of the attendant and obvious conflicts of interest. Further, debt settlement companies should be prohibited from receiving any remuneration or referral fees for customers who seek out loans as part of the settlement process, as even informal arrangements could create a similar conflict. Finally, the state should create a formal mechanism for reporting bad industry actors. This mechanism would make it easier for borrowers, creditors, and other companies to root out abuses within the industry.

Conclusion

Debt settlement companies often present themselves as a necessary intermediary between creditors and consumers, claiming or implying they offer similar protections to delinquent debtors as those attorneys in bankruptcy proceedings provide. However, in the case of delinquent debt, working with intermediaries offers no advantage and significant disadvantages to working directly with creditors, with liability for additional fees being chief among these, particularly when one considers anything that a debt settlement company can negotiate with a creditor can be negotiated by the borrower themselves without additional cost.

It's important to remember that creditors, such as the members of AFSA, are invested in working directly with their borrowers, especially those in distress, to find a resolution that is mutually beneficial and acceptable to both parties. This is what allows creditors to maintain critical long-term client relationships and can, as far as possible, preserve the borrower's credit score.

It is very rare that regulators, watchdogs, and other businesses and associations across the spectrum which otherwise often disagree on aspects of credit provision, agree that a single industry is detrimental to consumers. That is what is happening with debt settlement companies. We urge you to join the opposition to these predatory, exploitative, and deeply problematic businesses, and we respectfully request that you oppose SB 112. Thank you again for the opportunity to submit AFSA's written testimony today.

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Protecting Credit Since 1916
American Financial Services Association

[i] Founded in 1916 and based in Washington DC, the American Financial Services Association (AFSA) is the primary trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including direct and indirect vehicle financing, traditional installment loans, mortgages, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans.

[ii] Ohio Revised Code Sec. 4710.02(B)(3)

[iii] https://www.consumerfinance.gov/ask-cfpb/what-are-debt-settlementdebt-relief-services-and-should-i-use-them-en-1457/

[iv] https://www.gao.gov/assets/130/124498.pdf [Though this study was carried out immediately before TSR took effect, we have seen no evidence that this characterization is no longer valid, and plenty of anecdotal evidence that it is]

[v] 74 Fed. Reg. 41988 (Aug. 19, 2009)