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PREPARED STATEMENT OF

THE FEDERAL TRADE COMMISSION

on

"Consumer Protection and the Credit Crisis"

Before the

SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

Washington, D.C.

February 26, 2009

I. Introduction

Chairman Rockefeller, Ranking Member Hutchison, and Members of the Committee, I am Pamela Jones Harbour, a Commissioner of the Federal Trade Commission ("FTC" or "Commission").[1] I appreciate the opportunity to appear before you today to discuss the Commission's efforts to help consumers in financial distress.

The Commission protects consumers from harmful acts and practices at every stage of the credit life-cycle, from when credit is first advertised to when debts are collected. At the early stages of the cycle, the FTC protects consumers from the unfair, deceptive, or otherwise unlawful acts and practices of brokers, lenders, and others who advertise or offer credit. The agency also protects consumers at the middle stages of the credit life-cycle from the unlawful conduct of creditors and servicers who collect payments from consumers who are current on their debts. At the later stages of the cycle, the Commission protects consumers who are delinquent or in default on their debts from the unlawful acts and practices of debt collectors, credit repair companies, debt settlement firms, and mortgage foreclosure scam artists.

Although the agency protects consumers throughout the credit life-cycle, the FTC recently has increased its focus on preventing harm to consumers who are already in debt. Consumer debt is now at historic levels.[2] Moreover, the recent economic downturn has made it

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[1] The views expressed in this statement represent the views of the Commission. My oral presentation and responses to any questions are my own, however, and do not necessarily reflect the views of the Commission or any other Commissioner.

[2] Between 1985 and 2007, outstanding household debt in the United States increased from approximately 60 percent of annual disposable income to more than 125 percent, a jump due mostly to increased mortgage debt. *See* Federal Trade Commission, "Collecting Consumer Debts: The Challenges of Change, A Report by the Federal Trade Commission," at 16 (Feb. 26, 2009). The ratio of household indebtedness to annual disposable income peaked at 126 percent in the third quarter of 2007. Since that time, the latest available data indicate that, as of the third

even more difficult for consumers with high debt levels to remain current on their mortgages, credit cards, and other types of debts.[3] In short, many American consumers are now in financial distress.

Consumers in financial distress are particularly vulnerable to unfair, deceptive, and otherwise unlawful business practices. Some debt collectors use unfair, deceptive, or abusive practices such as threats of imprisonment or harassing calls to try to compel consumers to pay their debts. Some debt settlement firms promise for a fee to negotiate settlements with creditors that will result in consumers owing less than the full amount of the balance on their credit cards, but in fact these firms do not negotiate the promised reductions. Some credit repair companies promise for a fee to be able to remove delinquencies, bankruptcies, and other negative information from the credit reports of consumers, but these companies cannot remove such information if it is truthful and accurate. Finally, some scam artists target consumers facing home foreclosure and promise that for a fee they will be able to negotiate a deal with lenders or servicers that will allow the consumers to stay in their homes. However, consumers later learn that no one has taken steps to save their homes from foreclosure, resulting in many consumers

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quarter of 2008, the ratio has declined slightly to 123 percent. This remains well above typical indebtedness levels in the past two decades. *See id.*

[3] For example, the percentage of borrowers who are 60 or more days past due on their mortgage loans increased for the seventh straight quarter in the third quarter of 2008, reaching a national average of 3.96 percent. Press Release, TransUnion, Mortgage Loan Delinquency Rates Rise for Seventh Straight Quarter (Dec. 8, 2008), *available at* http://newsroom.transunion.com/index.php?s=43&item=502. This figure is approximately 54 percent higher than the figure for the third quarter of 2007. *Id.* Similarly, in January 2009 late payments on credit cards in the United States topped record levels, and defaults rose sharply to just below all-time highs. Al Yoon, *US Credit Card Delinquencies at Record Highs – Fitch*, REUTERS, Feb. 4, 2009, *available at* http://www.reuters.com/articlePrint?articleId=USN0428871920090204.

losing both the fee and their homes.

The Commission has used all the tools at its disposal to increase its protection of consumers in the later stages of the credit life-cycle. The FTC has brought law enforcement actions against those who engage in unfair or deceptive acts and practices in violation of Section 5 of the FTC Act, as well as against those who violate specific credit statutes, such as the Fair Debt Collection Practices Act ("FDCPA") and the Credit Repair Organizations Act ("CROA"). The agency has created and distributed extensive consumer education materials about debt collection, debt relief services, credit repair, foreclosure rescue scams, and other financial services topics to assist consumers in financial distress in taking steps to protect themselves.[4] The Commission has conducted cutting-edge empirical research on how to improve mortgage disclosures and engaged in comprehensive policy development activities related to debt collection and debt settlement.

The FTC believes that its past efforts have provided important protections to American consumers in financial distress. The agency, however, also recognizes that it must do more. To allow the Commission to perform a greater and more effective role in protecting consumers in financial distress, the agency recommends the enactment of legislation that would:

- permit the FTC to employ notice and comment rulemaking procedures to declare acts and practices relating to financial services to be unfair or deceptive in violation of the FTC Act;

- authorize the FTC to obtain civil penalties for unfair or deceptive acts and practices related to financial services, and authorize the FTC to bring suit in federal court to obtain civil penalties;

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[4] The FTC also participates in the governmental Financial Literacy and Education Commission and has contributed its expertise to the production of *MyMoney.gov* and *Taking Ownership of the Future: The National Strategy for Financial Literacy.*

- authorize the FTC to promulgate rules to implement the FDCPA; and
- provide additional resources to assist the FTC in increasing its law enforcement activities related to consumer financial services and expanding its critical empirical work on the efficacy of disclosures.

This testimony will provide an overview of the FTC's consumer protection authority related to financial services, describe how the Commission has used its consumer protection tools on behalf of consumers throughout the credit life-cycle, and recommend changes in the law and resources to enable the FTC to do more to protect consumers in financial distress.

II. Overview of Commission Authority

The Commission has law enforcement authority over a wide range of acts and practices related to financial services. The agency enforces Section 5 of the Federal Trade Commission Act,[5] which prohibits unfair or deceptive acts or practices in or affecting commerce. In addition, among other specific financial services statutes,[6] the FTC enforces the FDCPA,[7] which prohibits unfair, deceptive, or abusive debt collection practices by third-party debt collectors. It also enforces the CROA,[8] which prohibits credit repair firms from making false statements about their ability to improve the credit rating of consumers and from charging an advance fee before providing credit repair services. The FTC Act, as well as the FDCPA and CROA, provide the

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[5] 15 U.S.C. § 45(a).

[6] The FTC enforces numerous consumer protection statutes that govern financial services providers, including the Truth in Lending Act (15 U.S.C. §§ 1601-1666j), the Consumer Leasing Act (15 U.S.C. §§ 1667-1667f), the Fair Credit Reporting Act (15 U.S.C. §§ 1681-1681x) ("FCRA"), the Equal Credit Opportunity Act (15 U.S.C. §§ 1691-1691f), the Electronic Funds Transfer Act (15 U.S.C. 1693-1693r), and the privacy and pretexting provisions of the Gramm-Leach-Bliley Act (15 U.S.C. §§ 6801-6809).

[7] 15 U.S.C. §§ 1692-1692p.

[8] 15 U.S.C. §§ 1679-1679j.

fundamental authority that the Commission uses to take law enforcement action against those whose acts and practices harm consumers in the later stages of the credit life-cycle.

Although the Commission has the authority to take action against a wide array of acts and practices in the financial services arena, some financial service providers are exempt from the FTC's jurisdiction. Banks, thrifts, and federal credit unions are specifically exempt from the Commission's jurisdiction under the FTC Act.[9] The FTC's jurisdiction under the FTC Act extends only to non-bank financial companies, including non-bank mortgage companies, mortgage brokers, and finance companies. Similarly, under the FDCPA and CROA, the Commission has jurisdiction over non-bank entities covered by these statutes, including debt collectors and credit repair organizations, respectively.[10]

In conducting its law enforcement and other activities, the FTC often cooperates with other agencies, such as the federal agencies who have authority over banks, thrifts, and federal credit unions. Even more significant in the context of assisting consumers in financial distress, the FTC has a history of close cooperation with many state attorneys general and state banking departments on issues such as debt collection, foreclosure rescue scams, and credit repair.

III. The FTC's Protection of Consumers During the Credit Life-Cycle

A. Marketing and Advertising of Consumer Credit

A consumer's credit life-cycle begins when he or she initially shops for a mortgage, credit card, auto loan, or any other form of credit. In the area of marketing and advertising of credit, the FTC has brought numerous enforcement actions challenging deceptive or illegal

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[9] *See* 15 U.S.C. § 45(a)(2).

[10] *See* 15 U.S.C. § 1692a(4), (6); 15 U.S.C. § 1679b(4).

marketing by lenders, brokers, or other advertisers of consumer credit in violation of the FTC Act or the Truth in Lending Act.[11] In mortgage advertising, for example, the Commission has brought actions against mortgage lenders or brokers for deceptive marketing of loan costs[12] or other key loan terms, such as the existence of a prepayment penalty[13] or a large balloon payment due at the end of the loan.[14] Most recently, the Commission announced settlements with three mortgage lenders charged with using ads that touted low interest rates and low monthly payments, but failing to adequately disclose that the low rates and payment amounts would increase substantially after a limited period of time.[15]

The FTC has also brought enforcement actions against credit card marketers and advertisers. In June 2008, the FTC sued a credit card marketing company, CompuCredit Corporation, for allegedly deceptively marketing its credit cards to subprime consumers nationwide, primarily through solicitations that misrepresented the amount of available credit

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[11] *See, e.g.*, *FTC v. Mortgages Para Hispanos.Com Corp.,* No. 06-00019 (E.D. Tex. 2006); *FTC v. Ranney,* No. 04-1065 (D. Colo. 2004); *FTC v. Chase Fin. Funding,* No. 04-549 (C.D. Cal. 2004); *FTC v. Diamond*, No. 02-5078 (N.D. Ill. 2002); *United States v. Mercantile Mortgage Co.*, No. 02-5079 (N.D. Ill. 2002); *FTC v. Associates First Capital Corp.,* No. 01-00606 (N.D. Ga. 2001); *FTC v. First Alliance Mortgage Co.,* No. 00-964 (C.D. Cal. 2000).

[12] *See, e.g.*, *FTC v. Associates First Capital* Corp., No. 01-00606 (N.D. Ga. 2001); *FTC v. First Alliance Mortgage Co.*, No. 00-964 (C.D. Cal. 2000).

[13] *FTC v. Chase Fin. Funding*, No. 04-549 (C.D. Cal. 2004); *FTC v. Diamond*, No. 02-5078 (N.D. Ill. 2002).

[14] *FTC v. Diamond*, No. 02-5078 (N.D. Ill. 2002).

[15] *See, e.g, In the Matter of American Nationwide Mortgage Company, Inc.*, FTC Dkt. No. C-4249 (Feb.17, 2009); *In the Matter of Shiva Venture Group, Inc.*, FTC Dkt. No. C-4250 (Feb. 17, 2009); *In the Matter of Michael Gendrolis*, FTC Dkt. No. C-4248 (Feb. 17, 2009).

and failed to adequately disclose the cost of that credit.[16] Last December, CompuCredit agreed to settle this case for an estimated $114 million in credits as redress to consumers.[17]

The Commission believes the CompuCredit case provides valuable insight into consumers' experiences in procuring credit and going into debt. Deceptively marketing the costs of a credit product can have long-lasting consequences for many consumers. In this case, for instance, the deceptive marketing led many consumers to believe they would receive $300 in available credit, but instead they were charged $185 in fees and therefore initially received only $115 in credit. Many consumers were pushed over their credit limits almost immediately because they did not have as much credit as they thought they would have. These consumers were sent into a debt spiral from which they could not recover, and as a result, their debts were charged off by CompuCredit, in turn worsening their credit scores and further limiting their financial options.

The CompuCredit case also highlights what happens as more and more consumers face growing debt. Debt collectors are developing innovative approaches to collecting charged-off debt. CompuCredit and Jefferson Capital, its debt collection subsidiary, allegedly marketed a credit card specifically to consumers with charged-off debt. This type of program encourages

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[16] Although the credit cards were issued by various FDIC-regulated banks, CompuCredit created, designed, and distributed the credit card marketing materials that the Commission alleged were deceptive. As discussed above, the Commission does not have jurisdiction over banks, which issue nearly all credit cards in the United States. The FTC, however, does have jurisdiction over non-bank entities that market or advertise credit cards. The Commission worked closely on this case with the FDIC, which brought a parallel action challenging this deceptive conduct.

[17] *FTC v. CompuCredit Corp. and Jefferson Capital Systems, LLC*, No. 1:08-CV-1976-BBM-RGV (N.D. Ga. 2008).

consumers to enroll in a debt repayment plan in order to obtain a credit card. Once a consumer pays down a specific amount of his or her outstanding debt, the consumer is eligible for a credit card with a minimal amount of available credit. These debt repayment offers may be marketed to consumers whose debts were discharged in bankruptcy or whose debts are no longer reportable pursuant to the FCRA.[18] As a consequence, consumers who receive debt-transfer credit card offers may be induced to re-validate an old debt, for which collection action might not otherwise have been possible. Because of its impact on consumers in financial distress, the FTC will continue to monitor the marketplace for this type of debt collection practice.

B. Mortgage Servicing

In the mortgage market, servicers collect payments for lenders and other owners of mortgage loans. The FTC has challenged deceptive and unfair practices in the servicing of mortgage loans, addressing core issues such as failing to post payments upon receipt, charging unauthorized fees, and engaging in deceptive or abusive debt collection tactics. For example, in September 2008, the FTC settled charges that EMC Mortgage Corporation and its parent, The Bear Stearns Companies, LLC, violated Section 5 of the FTC Act, the FDCPA, and the FCRA in servicing consumers' mortgage loans, including debts that were in default when EMC obtained them.[19] Among other practices, the complaint alleged that the defendants: (1) misrepresented the amounts consumers owed; (2) assessed and collected unauthorized fees; and (3) misrepresented

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[18] 15 U.S.C. §§ 1681-1681x. Section 605(a)(4) of the FCRA prohibits credit reporting agencies from reporting charge-offs that are more than seven years old. 15 U.S.C. § 1681c.

[19] *FTC v. EMC Mortgage Corp.*, No. 4:08-cv-338 (E.D. Tex. Sept. 9, 2008). *See* Press Release, Federal Trade Commission, Bear Stearns and EMC Mortgage to Pay $28 Million to Settle FTC Charges of Unlawful Mortgage Servicing and Debt Collection Practices (Sept. 9, 2008), *available* at http://www2.ftc.gov/opa/2008/09/emc.shtm.

that they had a reasonable basis to substantiate their representations about consumers' mortgage loan debts. The complaint further alleged the defendants made harassing collection calls; falsely represented the character, amount, or legal status of consumers' debts; and used false representations and deceptive means to collect on mortgage loans.

The EMC settlement required the defendants to pay $28 million in consumer redress, barred them from future law violations, and imposed new restrictions on their business practices. In particular, it required EMC to establish and maintain a comprehensive data integrity program to ensure the accuracy and completeness of data and other information about consumers' loan accounts before servicing those accounts.

In addition to law enforcement, the Commission provides mortgage borrowers with tools to protect themselves. For example, the FTC distributes consumer education materials on mortgage servicing,[20] what to do if you are having trouble making your mortgage payments,[21] and how to manage your mortgage if your lender closes or files for bankruptcy.[22] The Commission also uses innovative approaches to reach out to consumers in other ways. This January, the FTC included a bookmark, "Numbers to Know & Places to Go," with contacts for more information about assistance with financial services along with the redress checks sent to over 86,000 consumers as a result of the Commission's settlement with EMC.

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[20] http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea10.shtm.

[21] http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea04.shtm.

[22] http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea12.shtm.

C. Debt Collection

Consumer credit is a critical component of today's economy. Credit allows consumers to purchase goods and services for which they are unable or unwilling to pay the entire cost at the time of purchase. By extending credit, however, creditors take the risk that consumers will not repay all or part of the amount they owe. If consumers do not pay their debts, creditors may become less willing to lend money to consumers, or may increase the cost of borrowing money. Creditors typically use independent or third-party collectors to try to recover on debts to decrease the amount of their lost revenues. Debt collection thus helps keep credit available and its cost as low as possible.

Some debt collection activities, however, also may harm consumers. In 1977, Congress passed legislation to protect consumers from harmful debt collection practices and to protect ethical collectors from competitive disadvantage. The result was the landmark Fair Debt Collection Practices Act, which established specific standards of conduct for the collection industry. Consumer groups, labor groups, state and federal enforcement officials, and collection industry trade associations supported the law's passage. The Commission is the primary governmental enforcer of the FDCPA. Consumers also may file their own actions against debt collectors.

The FDCPA prohibits abusive, deceptive, and unfair debt collection practices, and specifies numerous practices that are barred. The FTC receives more complaints about debt collectors than any other industry.[23] The consumer complaints include demands for payments

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[23] *See* FEDERAL TRADE COMMISSION ANNUAL REPORT 2008: FAIR DEBT COLLECTION PRACTICES ACT at 4, *available at* http://www2.ftc.gov/os/2008/03/P084802fdcpareport.pdf. Note that, although the FDCPA generally does not cover the conduct of creditors collecting on their own debts, Section 5 of the FTC Act's prohibition on unfair and deceptive acts and practices does apply to such conduct.

that are not owed or larger than owed, harassment, false threats of legal or other action, impermissible calls to the consumer's place of employment, revealing debts to third parties, and other law violations.

Since 1999, the FTC has brought 21 lawsuits for illegal debt collection practices. In these cases, the Commission has obtained strong permanent injunctive and equitable relief, including substantial monetary judgments and, for some defendants, bans on collecting debts.[24] In addition, the FTC has held more individuals, rather than just companies, liable for unlawful debt collection practices. As an example of the FTC's current approach to law enforcement, in November 2008, Academy Collection Service, Inc. ("Academy") and its owner, Keith Dickstein, agreed to pay $2.25 million in civil penalties to settle charges that they violated the FDCPA and Section 5 of the FTC Act.[25] This is the largest civil penalty that the Commission has ever obtained in an FDCPA case.[26]

Although the Commission has provided effective protection for consumers within the current confines of the law, the FTC recognized that the law may need to be modified to provide consumers with even stronger protection against abusive debt collectors. In October 2007, the Commission therefore hosted a two-day workshop, entitled "Collecting Consumer Debts: The

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[24] *See, e.g., FTC v. Check Investors, Inc.*, 2005 U.S. Dist. LEXIS 37199 (D.N.J. July 18, 2005) (ban on debt collection and $10.2 million judgment), *aff'd,* 503 F.3d 159 (3d Cir. 2007), *petition for reh'g denied,* Nos. 05-3558, 05-3957 (3d Cir. Feb. 6, 2008).

[25] *United States v. Acad. Collection Serv., Inc.*, No. 2:08-CV-1576 (D. Nev. Nov. 18, 2008). *See* Press Release, Federal Trade Commission, Nationwide Debt Collector Will Pay $2.25 Million to Settle FTC Charges (Nov. 21, 2008), *available at* http://www.ftc.gov/opa/2008/11/academy.shtm.

[26] Previously, the highest civil penalty judgment in an FDCPA case was $1.375 million, entered in *United States v. LTD Financial Services*, No. H-07-3741 (S.D. Tex. Nov. 5, 2007).

Challenges of Change," to explore changes in the debt collection industry and examine their impact on consumers and businesses since the FDCPA was enacted in 1977.

The FTC is releasing its debt collection workshop report today. Based on the workshop record and its experience, the Commission concludes that debt collection law needs reform and modernization to reflect changes in consumer debt, the debt collection industry, and technology. The Report discusses these changes and sets forth the modifications to the law the FTC believes are needed to provide better consumer protection without unduly burdening debt collection.

Among other things, the Report concludes that major problems exist in the flow of information within the debt collection system. The law needs to be changed to require that debt collectors have better information, making it more likely their attempts to collect are for the right amount and are directed to the correct consumers. The Report also recommends that collectors be required to provide consumers with better information explaining their rights under the FDCPA.

The Commission also concludes that debt collection laws must be modernized to take account of changes in technology. The Report recognizes that the law generally should allow debt collectors to use all communication technologies, including new and emerging technologies, to contact consumers. However, it is important that the law be carefully crafted and applied to avoid collectors' use of communication technologies in a manner that causes consumers to incur charges, or otherwise subjects them to unfair, deceptive, or abusive acts and practices.

The workshop record also revealed that certain debt collection litigation and arbitration practices appear to raise substantial consumer protection concerns. Because the workshop record does not contain adequate information for the FTC to determine the nature and extent of these concerns, the Report announces that the agency will convene regional roundtables this year with state court judges and officials, debt collectors, collection attorneys, consumer advocates, arbitration firms, and other interested stakeholders to obtain more information about these concerns and develop possible solutions. The participation of state officials in these roundtables will be critical, because debt collection litigation and arbitration involve many issues of state as well as federal law.

D. Debt Relief Services and Credit Repair

1. Foreclosure Rescue Scams

With the rapid increase in mortgage delinquencies and foreclosures, the FTC has intensified its efforts to protect consumers from mortgage foreclosure rescue scams.[27] There are many varieties of mortgage foreclosure rescue fraud, but in most cases the perpetrator makes misleading promises that a consumer's home will be saved from foreclosure and that the consumer's loan can be modified. These scams share at least two common characteristics. First, the fraudulent schemes target consumers who are facing foreclosure or delinquency on their mortgage and who have limited time and resources to save their homes. Second, these schemes falsely promise that they can save consumers' homes from foreclosure or obtain a loan workout or modification chiefly by negotiating directly with the mortgage lender or servicer. Many consumers, however, ultimately lose both their homes and the money they paid to scammers.

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[27] On February 13, 2008 the FTC testified before the Senate Special Committee on Aging about foreclosure rescue fraud. The FTC's testimony is *available at* http://www.ftc.gov/os/testimony/P064814foreclosure.pdf.

In the past year, the Commission has brought six cases targeting mortgage foreclosure rescue scams,[28] including a case announced earlier this month.[29] In these cases, the Commission alleged that the defendants promise to stop foreclosure in exchange for an up-front consumer payment, ranging from $500 to $1,200. After a consumer makes the payment, the defendants do little or nothing to stop the foreclosure. This fraud deprives consumers not only of much-needed funds but also of the opportunity to explore realistic options to avoid foreclosure, including with the assistance of a non-profit housing counselor. In one case, the Commission alleged that the defendants enticed consumers into a second mortgage or home equity line of credit on very unfavorable terms without fully disclosing the costs, risks, and consequences of doing so.[30]

In tandem with its recent law enforcement actions against alleged foreclosure rescue scams, the Commission initiated a stepped-up outreach initiative on foreclosure rescue fraud. The FTC is involved in federal, state, and local task forces in several regions where foreclosures are most prevalent both to coordinate enforcement and develop consumer outreach strategies. In addition, to warn consumers about the red flags for scams and inform them about the legitimate resources available to them, the Commission has undertaken a variety of other outreach initiatives. The FTC submitted a series of radio public service announcements, in

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[28] *FTC v. United Home Savers, LLP,* No. 8:08-cv-01735-VMC-TBM (M.D. Fla. Sept. 3, 2008); *FTC v. Foreclosure Solutions, LLC, and Timothy A. Buckley*, No. 1:08-cv-01075 (N.D. Ohio April 28, 2008); *FTC v. Mortgage Foreclosure Solutions, Inc.,* No. 8:08-cv-388-T-23EAJ (M.D. Fla. Feb. 26, 2008); *FTC v. National Hometeam Solutions, Inc.,* No. 4:08-cv-067 (E.D. Tex. Feb. 26, 2008).

[29] *FTC v. National Foreclosure Relief, Inc.*, No. SACV09-117 (C.D. Cal. Feb. 2, 2009) (temporary restraining order issued pending hearing on FTC's motion for preliminary injunction).

[30] *FTC v. Safe Harbour Foundation,* No. 08 C 1185 (N.D. Ill. Feb. 25, 2008).

English and Spanish, to stations in cities hardest hit by mortgage foreclosures. The Commission also distributed an article adapted from its mortgage foreclosure scam consumer education brochure to a national syndicated news service, which in turn, sent it to more than 10,000 community newspapers across the nation for inclusion in their publications.

2. Debt Settlement

With historically high levels of consumer credit card debt, many consumers are looking for ways to manage or reduce their debt. For decades, credit card debt relief was almost exclusively the province of non-profit credit counseling agencies ("CCAs"). Beginning in the mid-1960s, creditor banks initiated the current model of non-profit credit counseling to reduce personal bankruptcy filings. Under this model, CCAs work with consumers and creditors to negotiate a repayment plan of principally credit card debt (a "debt management plan" or "DMP") and also assist the consumer in developing a manageable budget and educational tools to avoid debt problems in the future.[31] If the consumer cannot afford a repayment plan, the credit counselor explores other options, including referral to a bankruptcy attorney.

The historic levels of consumer debt necessarily have affected the services CCAs can provide. Non-profit credit counselors have told the Commission that the number of consumers contacting them about debt has increased by over a third. However, they also have said that the

[31] To negotiate a DMP, the credit counselor first obtains the consumer's full financial profile. Then, the credit counselor contacts each of the consumer's creditors. Based principally on the consumer's debt load and available income, the creditor then determines what, if any, repayment options to offer the consumer. Repayment options, or concessions, include reductions of the interest rate on the credit card and elimination of late or over-limit fees. After negotiations with all of the consumer's creditors, the credit counselor calculates a consolidated and reduced monthly payment to enable the consumer to repay the balance in full over a period of years, typically three to five years. The consumer sends the payment to the credit counselor, which then distributes payments to each of the consumer's creditors.

number of consumers who meet the income requirements to enroll in debt management plans has decreased substantially, which means that there are more consumers in debt who are looking for relief but cannot obtain that relief from non-profit credit counseling services. These reports from credit counselors are consistent with what the Commission has observed in the marketplace as part of its law enforcement activities related to debt settlement.[32]

The increased demand for debt relief options resulted in the recent growth of *for-profit* debt settlement companies. The term "debt settlement" refers to services for-profit companies market that promise to obtain lump sum settlements of consumers' unsecured debt – principally, credit card debt. These companies typically promise that they will negotiate with creditors to obtain settlements in amounts less than the full balance owed by the consumer. The for-profit debt settlement business model typically encourages consumers, even those who are current on their payments, to become delinquent on credit card debt to encourage creditors to accept less than full payment of principal as a form of loss mitigation. Unlike DMPs, debt settlement companies do not consolidate credit card debt or arrange a monthly payment plan to pay off the debt over a period of years. Rather, the goal of debt settlement is to save enough cash, while not paying creditors, so that the creditors will offer to take a fraction of the balance owed as settlement in lieu of the full debt.

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[32] Federal Trade Commission, Debt Settlement Workshop (Sept. 25, 2008), Transcript at 6 (remarks of Lydia B. Parnes, then-Director of the Bureau of Consumer Protection), *available at* http://www.ftc.gov/bcp/workshops/debt settlement/OfficialTranscript.pdf.

Since 2001, the Commission has brought 14 cases against both sham non-profit credit counseling agencies and for-profit debt settlement companies.[33] In these cases, defendants allegedly deceive consumers who are seeking workout options for credit card debt into paying large upfront fees for debt relief services which, for many consumers, are nonexistent. Other allegations include deceptive promises that debt collectors will stop trying to collect from consumers enrolled in their programs and that stopping payments to creditors under their program will not hurt consumers' creditworthiness.

Earlier this month, the Commission brought a contempt action against an alleged sham non-profit credit counseling company and its principal for violations of an order a federal court entered against them in 2008.[34] The defendants, Express Consolidation and Randall Leshin, misrepresented their non-profit status, charged hidden fees, and misled consumers about the benefits of enrolling in a debt management plan, according to the Commission's underlying action.[35] The 2008 order prohibited them from the illegal conduct and from operating in states where they were not qualified to do business. Notwithstanding being subject to a federal court

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[33] *FTC v. Debt-Set,* No. 07-558 (D. Colo. 2007); *FTC v. Select Personnel Mgmt., Inc.*, No. 07-0529 (N.D. Ill. 2007); *FTC v. Dennis Connelly,* No. 06-701 (C.D. Cal. 2006); *FTC v. Express Consolidation,* No. 06-61851 (S.D. Fla. 2006); *United States v. Credit Found. of Am.,* No. 06-3654 (C.D. Cal. 2006); *FTC v. Debt Solutions, Inc.,* No. 06-0298 (W.D. Wash. 2006); *FTC v. Debt Mgmt. Found. Servs., Inc.*, No. 04-1674 (M.D. Fla. 2004); *FTC v. Integrated Credit Solutions, Inc.*, No. 06-00806 (M.D. Fla. 2006); *FTC v. National Consumer Council, Inc.,* No. 04-0474 (C.D. Cal. 2004); *FTC v. Better Budget Fin. Servs., Inc.,* No. 04-12326 (D. Mass. 2004); *FTC v. Innovative Sys. Tech., Inc., d/b/a Briggs & Baker*, No. 04-0728 (C.D. Cal. 2004); *FTC v. AmeriDebt, Inc.*, No. 03-3317 (D. Md. 2003); *FTC v. Jubilee Fin. Servs., Inc.*, No. 02-6468 (C.D. Cal. 2002).

[34] *FTC v. Randall L. Leshin d/b/a Express Consolidation*, No. 0:06-CV-61851-WJZ (S.D. Fla. 2008).

[35] *FTC v. Express Consolidation*, No. 06-CV-61851 (S.D. Fla. Dec.11, 2006).

order, the defendants continued to do business in states where they were unqualified and to collect fees from consumers who had cancelled their debt management plans. On February 17, 2009, the court found the defendants in contempt based on this conduct. The Commission currently is seeking an order reimbursing consumers for any fees collected in violation of the 2008 order.

As part of its research and policy development initiatives, the Commission convened a public workshop in September 2008 to examine the debt settlement industry, including the role of creditors, and the consumer protection issues that the for-profit business model raises. As a result of this workshop and the FTC's law enforcement experience, the Commission is considering what initiatives, in addition to continued aggressive enforcement, are needed to further protect consumers from deceptive and unfair practices by purported debt relief companies.

3. Credit Repair

Another consumer protection challenge exacerbated by the economic downturn is the effect of delinquencies, bankruptcy, or other negative credit information on a consumer's credit report. Fraudulent credit repair companies falsely promise to be able to remove for a fee accurate, negative information from consumers' credit reports. This false promise particularly appeals to consumers with poor credit histories who are seeking a job, a car loan, or a mortgage.

Consistent with its efforts to combat other types of financial fraud, the Commission has acted aggressively against such "credit repair" scams. Since 1999, the FTC has brought 42 cases against defendants that allegedly misrepresented the credit-related services they would provide. Most recently, in October 2008, the Commission and 24 state agencies announced a crackdown on 33 credit repair operations – entities that deceptively claimed they could remove negative information from consumers' credit reports, even if that information was accurate and timely.[36] The law enforcement sweep included ten FTC actions charging companies with violating the FTC Act and the CROA by making false and misleading statements, such as claiming they could substantially improve consumers' credit reports by removing accurate, negative information from credit reports. The agency also alleged that the defendants violated the CROA by charging an advance fee for credit repair services. The sweep included 26 state actions alleging violations of state laws and the CROA. Our partnerships with state authorities have increased significantly the reach of the Commission's law enforcement efforts to promote broader compliance with the law.

IV. Enhancing FTC Consumer Protection Efforts

As described above, the FTC has used a vigorous program of law enforcement, consumer education, and research and policy development to protect consumers of financial services. The current economic crisis, however, demonstrates that more needs to be done. As the nation's consumer protection agency, the Commission is well-positioned to provide the additional protection that is needed. The FTC can provide greater protection to consumers in financial distress through enhanced and streamlined authority to promulgate rules, including rules to implement the FDCPA, increased monitoring and oversight to assess compliance with the law, expanded authority to obtain civil penalties against those who violate the law, and increased policy-oriented research on financial services subjects. To exercise these responsibilities in the

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[36] *See* Press Release, FTC's Operation "Clean Sweep" Targets "Credit Repair" Companies, *available at* http://www.ftc.gov/opa/2008/10/cleansweep.shtm.

robust manner necessary to confer greater consumer protection, the Commission will need substantial additional authority and resources.

A. Rulemaking Authority

The Commission would be able to be develop rules concerning financial services more quickly and effectively if the procedures required for issuing such rules were streamlined; that is, if the FTC were permitted to use standard government-wide notice and comment rulemaking procedures under Section 553 of the Administrative Procedures Act ("APA")[37] to declare acts and practices to be unfair or deceptive. The FTC currently must use the burdensome, complicated, and time-consuming procedures of Section 18 of the FTC Act ("Magnuson-Moss rulemaking procedures") to promulgate such rules.[38] Commission rulemakings subject to Magnuson-Moss rulemaking procedure requirements typically take anywhere from three to ten years to complete. For example, the proceeding to promulgate the FTC's Credit Practices Rule[39] took almost ten years.

The cumbersome requirements of Section 18 of the FTC Act do not apply to other federal agencies when they promulgate rules to protect consumers of financial services from unfair and deceptive acts and practices. Most significantly, under the FTC Act itself, the Board of

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[37] 5 U.S.C. § 553.

[38] Section 18, for example, includes requirements that the FTC must publish an advance notice of proposed rulemaking and seek public comment before publishing its notice of proposed rulemaking; it must provide an opportunity for a hearing before a presiding officer at which interested persons are accorded certain cross-examination rights; and, where there are numerous interested parties, the FTC must determine which have similar interests, have each group of persons with similar interests choose a representative, and make further determinations about representation for those interests in the cross-examination process. 15 U.S.C. § 57a(b).

[39] FTC Credit Practices Rule, 16 C.F.R. § 444.

Governors of the Federal Reserve System ("FRB"), the Office of Thrift Supervision ("OTS"), and the National Credit Union Administration ("NCUA") may use notice and comment rulemaking to promulgate such rules for banks, thrifts, and federal credit unions, respectively.[40] The FTC, by contrast, must use the onerous and lengthy Magnuson-Moss rulemaking procedures to address the exact same unfair and deceptive acts and practices by financial entities within the Commission's jurisdiction. Changing the law to allow the Commission to use the same process under the FTC Act as used by the federal banking agencies would promote expedition and consistency in the promulgation of rules to protect consumers of financial services.

Similarly, expeditiously promulgating rules to address the acts and practices of debt collectors would be very beneficial in protecting consumers in financial distress. Section 814 of the FDCPA specifically prohibits the FTC from promulgating rules concerning the collection of debts by debt collectors.[41] In the debt collection workshop report that the Commission is issuing today, the agency concluded that the debt collection legal framework should be changed to enable the FTC to issue rules to implement the FDCPA to respond better to changes in technology and the marketplace. As with the rules under the FTC Act that address unfair and deceptive acts and practices related to financial services, the Commission would be able to issue rules to implement the FDCPA quickly and effectively if the agency were able to use notice and comment rulemaking procedures under the APA to promulgate them.

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[40] *See* 15 U.S.C. § 57a(f).

[41] *See* 15 U.S.C. § 1692l(d).

B. Expand FTC Ability to Obtain Civil Penalties for Law Violations

Civil penalties and other forms of monetary relief are vital to the effectiveness of the Commission's law enforcement program, because they punish noncompliance and deter future violations. The FTC, however, does not have the authority to seek civil penalties for violations of some of the laws that it enforces, most notably, the FTC Act.[42] Even in circumstances in which civil penalties are available to the FTC, the agency may not bring an action in federal court seeking penalties without first referring it to the Department of Justice (DOJ) to file on behalf of the Commission.[43]

First, in the context of financial services, enhanced civil penalty authority would increase deterrence of would-be violators within the FTC's jurisdiction.[44] Equitable monetary remedies, such as redress and disgorgement, may not be appropriate or sufficient in certain cases, and the availability of civil penalties against the wrongdoers would likely achieve greater deterrence.

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[42] Currently, the FTC may seek civil penalties against any entity that knowingly violates a trade regulation rule promulgated by the FTC or that violates an FTC cease and desist order. *See* 15 U.S.C. §§ 45(l) and (m)(1)(A). In addition, recognizing the importance of civil penalties, Congress has specifically authorized the FTC to seek civil penalties for violations of certain statutes, *e.g.*, the FDCPA.

[43] 15 U.S.C. § 56.

[44] If the Commission brings an action in federal court seeking civil penalties for violations of the laws it enforces, the agency should be permitted to obtain injunctive relief in such an action. In instances where there is a need to bring ongoing unlawful conduct by a financial services provider to a swift halt to protect consumers, and where both equitable relief and civil penalties are appropriate, the FTC should have the option of directly filing an action in federal court seeking both equitable relief and civil penalties.

The Commission's recent settlements with mortgage advertisers discussed above,[45] for example, contained no monetary relief. The FTC did not seek redress or disgorgement because of the difficulty in quantifying and proving consumer injury attributable to the particular ads challenged in those cases. Deterrence of unlawful conduct likely would be increased in these types of cases if civil penalties were available as a remedy.

In addition to authorizing civil penalties for violations of all consumer protection laws related to financial services, changes to the process required to obtain those penalties would make law enforcement more effective. Giving the FTC independent litigating authority when it seeks civil penalties would allow the Commission – the agency with the greatest expertise in enforcing the FTC Act – to litigate some of its own civil penalty cases, while retaining the option of referring appropriate matters to DOJ.[46] Conferring this authority on the Commission also would increase efficiency. Currently, if DOJ declines to participate in the name of the United States or otherwise fails to act within 45 days on such a referral, the Commission may file the case in its own name. This process requires extra time and delay, even under the best of circumstances. Moreover, once DOJ accepts a referral, the FTC normally assigns one or more of its staff attorneys, at DOJ's request, to assist in litigating the case. Despite excellent relations and coordination, the use of personnel at two agencies inevitably creates delay and inefficiencies. This is particularly true in cases where the FTC is simply referring to DOJ a civil penalty settlement to be filed in federal court.

[45] See cases cited *supra*, n. 15.

[46] Other independent federal agencies, such as the Securities and Exchange Commission and the Commodity Futures Trading Commission, are able to maximize the benefits of their own expertise by independently bringing administrative or judicial actions for civil penalties.

The FTC Act therefore should be amended to expand the agency's independent litigating authority to allow the FTC to bring actions for civil penalties in federal court "in its own name by any of its attorneys," without mandating that DOJ have the option to litigate on the FTC's behalf, as is currently required in most cases.

C. Increase Vital Empirical Research

One of the most challenging current policy issues in consumer protection is under what circumstances the disclosure of information allows consumers to make adequately informed decisions about products, including financial goods and services. The FTC has long recognized that the disclosure of information often can empower consumers, but that such disclosures may not be effective in some circumstances. In particular, the agency has recognized the challenges of conveying information about complex products and topics via disclosures. This challenge is an especially important one to address in the financial services area, because mortgage and credit products have become much more complex in recent years.

Statutory and regulatory schemes related to financial services include a host of requirements mandating that information be disclosed to consumers. Some have questioned whether these disclosures provide consumers with the information they need to properly understand the financial services they are purchasing. Specifically, some have argued that current disclosure requirements are inadequate in light of the advent and expansion of new financial services, such as alternative mortgages.

The Commission has a long history of conducting empirical tests of the efficacy of disclosures in a wide variety of commercial contexts.[47] Most recently, in 2007, the FTC's Bureau of Economics published a seminal research report concluding that the current mortgage disclosure requirements do not work and that alternative disclosures should be considered and tested.[48] As policymakers assess the utility of disclosures for financial products and services, the FTC has an opportunity to play a pivotal role in the debate. The Commission has the experience needed to conduct reliable studies of disclosures and report the results of these studies to policymakers and the public to better inform the debate. Focusing more attention on and devoting more resources to such vital empirical work is needed so that the FTC can foster the development of sound consumer protection policy.

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[47] In 2004, for example, the FTC released a study showing that broker compensation disclosures that the Department of Housing and Urban Development had proposed confused consumers, leading many of them to choose loans that were more expensive. *See* Federal Trade Commission, Bureau of Economics Staff Report, *The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment* (February 2004).

[48] *See* Federal Trade Commission, Bureau of Economics Staff Report, *Improving Consumer Mortgage Disclosures: An Empirical Assessment of Current and Prototype Disclosure Forms* (June 2007), *available at* http://www.ftc.gov/os/2007/06/P025505mortgagedisclosurereport.pdf. In this empirical study, the FTC staff tested currently required mortgage cost disclosure documents, as well as developed and tested a prototype mortgage cost disclosure document. The FTC staff study concluded that the current document "failed to convey key mortgage costs to many consumers," while the prototype document "significantly improved consumer recognition of mortgage costs, demonstrating that better disclosures are feasible." *Id.* at ES-1 and ES-5. Following up on this research, in 2008 the FTC's Bureau of Economics convened a conference to evaluate how mortgage disclosures could be improved. *See* Federal Trade Commission, "May 15, 2008 Mortgage Disclosure Conference," *available at* http://www2.ftc.gov/opa/2008/05/mortgage.shtm.

D. Increase in Resources

The FTC has a broad consumer protection mission that extends far beyond the financial services area, protecting consumers from identity theft, false advertising, malware, business opportunity frauds, telemarketing fraud, and more. Over the past few years, the Commission has responded to the need for more financial services enforcement by shifting consumer protection resources to the financial services area to the fullest extent possible. There is a great deal more that the FTC can accomplish in protecting consumers of financial services and we are prepared to do more. To accomplish this goal, the FTC needs significant additional professional staff.

V. Conclusion

The Commission is committed to protecting consumers throughout the credit life-cycle, including preventing harm to the many American consumers who struggle with mortgage, credit card, and other debt. The agency has used its traditional consumer protection tools of law enforcement, broad-based research and policy development, and consumer and business outreach to provide important protections for consumers of financial services. However, the Commission must do more. To enable the FTC to perform a greater and more effective role protecting consumers in financial distress, it recommends changes in the law and resources to enhance its authority to promulgate needed rules and prosecute cases against law violators. The Commission appreciates the opportunity to appear before you today to discuss the FTC's work and your consideration of its views.