RESPONSES PROVIDED FOR

Federal Trade Commission, Division of Financial Practices
Questions from Ms. Allison Brown dated December 18, 2009

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"Telemarketing Sales Rule - Debt Relief Rulemaking Forum"

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Abstract

We appreciate the opportunity to provide the Federal Trade Commission with additional operational details for DMB Financial, which we believe to be the largest *performance-based* debt settlement company in the country. We encourage continued dialogue about our complex and evolving industry in order to inform and guide reasoned regulation that benefits both consumer and free enterprise. For simplicity in reporting, all figures and statements are complete, current, and accurate to the best of our knowledge as of January 10th, 2010.

Questions

1. **Company Background**
    a. *How long have you been enrolling consumers in debt settlement programs?*
        i. **RESPONSE** – DMB Financial was organized as a Limited Liability Company in the state of Massachusetts on November 24, 2003 and began enrolling clients in early 2004. Please refer to the LLC Articles of Organization located here: http://corp.sec.state.ma.us/corp/corpsearch/CorpSearchSummary.asp?ReadFromDB=True&UpdateAllowed=&FEIN=300216576

    b. *Have you made significant changes in your programs since you began offering settlement programs?*
        i. **RESPONSE** – As with any growing company in an un-established industry, we've made quite a few operational changes but the Guardian Program has remained fundamentally the same since inception.

2. **Number of Accounts and Consumers** *("Enrolled" is defined as consumers who have made at least one payment. For each question, state the specific time period.)*
    a. How much total debt have consumers enrolled with the company?
        i. **RESPONSE** –DMB Financial has enrolled **$404 million** in consumer debt since inception.

    b. How many total consumers have enrolled with the company?
        i. **RESPONSE** – DMB Financial has enrolled **10,984 clients** since inception.

3. **Debt Reductions**
    a. What is the average percentage reduction of settled debt that consumers who completed your program received? Please calculate this percentage reduction using the amount owed at enrollment. "Completed" is defined as having had 95%-100% of the consumer's total amount of debt settled.
        i. **RESPONSE** – On average, our clients pay back just 55% of their "enrolled (original) balance" and just 45% of their "current balance" at the time of settlement. Clients of debt settlement are, by definition, unable to pay their debts off in full at the time of enrollment. As such, all options, including bankruptcy, credit counseling, and paying their credit card monthly minimums, incur costs – legal fees, interest, or other fees. For this reason, we feel that "current balance" is the more accurate determinant *of a negotiator's success and value delivered to the consumer*. The <u>difference</u> between "current balance" and "enrolled balance" is decided by *how quickly the consumer can accumulate the cash* necessary to pay off a reduced amount; the speed of client savings is not controlled or determined by the debt negotiator. Therefore, **"success" should be focused on what a debt settlement company can actually *control***, which is the percentage off the "current balance" at whatever time the client is able to provide the funds for a settlement. Success should not be determined by how slowly (or quickly) a consumer is able to accumulate those funds, which is primarily a function of the severity of their financial hardship and employment

status. Furthermore, if a client loses their job or stops making payments into a debt settlement savings program, those are not eflections of the debt settlement company's performance.

b. What is the average percentage reduction of settled debt that consumers who completed your program received? Please calculate this percentage reduction using the amount owed at settlement.
    i. **RESPONSE** – On average, our clients pay back just 45% of their "current balance" at the time of settlement. However, that is not the whole picture. As you can see from the data in the table below, settlements over a portfolio of debt will come back with a fairly wide variation of settlement performance.[1] This is driven by a number of factors, including:
        - **the creditor holding the debt at the time of settlement** – debt can change owners several times during a settlement program,
        - **the size of the debt being negotiated** – creditors may be more willing to negotiate on larger debts than they are on smaller debts,
        - **the age of the debt** – creditors are more willing to negotiate debts they perceive as falling irreparably behind, or
        - **the ability of the consumer to "lump sum" money** towards the settlement.

    One of the issues under scrutiny by the FTC is how debt settlement companies advertise their success rates. We caution the FTC that debt portfolios will always perform across a wide spectrum of success as influenced by the issues stated above.

Category	Total Amount of Debt	Total Amount of Settlement	Total Settlements	%	Cumulative %
Accounts Settled for < $.40	$4,418,919	$1,291,186	465	25.4%	25.4%
Accounts Settled for $.40-$.50	$3,810,098	$1,711,307	550	30.1%	55.5%
Accounts Settled for $.50-$.60	$2,957,184	$1,541,252	464	25.4%	80.9%
Accounts Settled for $.60-$.70	$1,289,369	$812,048	163	8.9%	89.8%
Accounts Settled for $.70-$.80	$628,382	$461,105	110	6.0%	95.8%
Accounts Settled for > $.80	$589,930	$566,669	77	4.2%	100.0%
Total	**$13,693,882**	**$6,383,567**	**1829**	**100.0%**	

[1] Data set is from January 1, 2006 through May 10, 2009 for clients enrolled in the state of New York only.

4. Accretion

a. What is the average rate of increase in amounts that consumers owe to creditors between enrollment and settlement?
    i. **RESPONSE** – The average increase is approximately 20%, inclusive of interest, late fees and penalties. In stark contrast, a consumer with $20,000 of credit card debt **who makes only the minimum monthly payments to their creditor would pay back a whopping 388% increase over the original balance** in interest between Day 1 and their final payment.[2]

5. Fee structure

a. The comment states on pages 5-7 that DMB Financial offers two fee structures. The comment states that under the Guardian Program, you collect a set-up fee, a monthly fee and a settlement fee upon settlement.
b. Under the Guardian Program, over how many months is the fee collected?
    i. **RESPONSE** – Fee is collected during every month of the program, from the first month to the very last. In the Guardian Program, the first two monthly savings payments are collected as Enrollment Fees. The enrollment fee amount varies with the length of the program and amount of debt enrolled. Each month thereafter, $34.95 is charged as an Administration & Client Services fee. And, at the time of each settlement, 25% of the savings ("current balance" less the settled amount) to the consumer is charged as a Settlement Fee.

c. Under the Guardian Program, how many consumers have enrolled with DMB Financial?
    i. **RESPONSE** – 10,846 clients.

d. Has the Guardian Program's fee structure changed over time?
    i. **RESPONSE** – Not fundamentally. As we've added additional resources for our clients (more client service representatives, better educational materials, free enrollment in a discounted and free legal services network, etc.) the monthly Administration and Client Services Fee has risen from $29.95 to $34.95 (2009). Otherwise, the fee structure has remained constant.

e. The comment states that under the Freedom Program, you collect no set-up fee, but rather a monthly fee and a settlement fee only after DMB Financial has negotiated a settlement and the funds are sent to the creditor. You also state that the fee amount is 35% of the consumer's savings. When did the DMB Financial begin offering the Freedom Program?

    Technical clarification: *DMB Financial does not collect an Enrollment Fee under the Freedom Program, but we do collect a monthly Administration and Client Services Fee of $34.95 per month, starting at Month 1 and each month thereafter.*
    i. **RESPONSE** – DMB Financial began offering the Freedom Program in July 2008 on a limited basis.

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[2] Scenario assumes $20,000 of debt at 24.99% interest rate, making monthly payments of $420.00. It would take 19.36 years to pay off the debt in full and would pay $77,556.37 in interest in addition to any late fees or penalties levied by credit card companies. The interest alone represents an increase of 388% over the original balance.

f. Has the Freedom Program's fee structure changed over time?
    i. **RESPONSE** – Other than an increase in the monthly Administration and Client Services Fee from \$29.95 to \$34.95, no there have been no other substantive changes to the program.

g. How many consumers have enrolled with DMB Financial under the Freedom Program? For clarification, "enrolled" is defined as consumers who have made at least one payment toward fees or settlement of debts.
    i. **RESPONSE** – 132 clients have been enrolled in the Freedom Program. 6 clients have been enrolled in our new **Independence Program**. The Independence Program was launched as a pilot test after the FTC Public Hearing on November 4, 2009. Officially, the Independence Program began on December 10, 2009 and is offered on a limited basis and geography. In the Independence Program, no fees are collected whatsoever prior to settlement—no enrollment fees and no monthly Administration and Client Services fees. The Independence Program charges 40% of the savings delivered to the client ("current balance" less settled amount at time of settlement) as its only fee. In light of potential regulatory changes, we felt it imperative to trial this new program immediately to gauge business risk, cash flow implications, and success. We have insufficient data so far to draw any conclusions about the long-term viability of the model but have spent many thousands of dollars in marketing, client services, and administration and are likely still 3-4 months away from realizing the very first dollar of revenue. **We approach the Independence Program with extreme caution** and have major concerns that clients who have "no skin in the game" are more likely to fudge qualification requirements in order to get into a debt settlement program, are more likely to terminate the program prior to completion as a result, and may attempt to renegotiate or default on the fees at the time of settlement.

h. Under the Freedom Program, does DMB Financial require consumers to save enough money to cover the settlement amount and the fee to DMB Financial before DMB Financial negotiates a settlement and sends funds to the creditor?
    i. **RESPONSE** – We would prefer that clients have saved both the total amount needed for settlement as well as our fee prior to settlements, but in practice we do not apply that standard except in the very last settlement of a client's portfolio. We've found that clients are happier (understandably) and more likely to stay in the program if we are able to get settlements earlier, which means collecting our fee over the period of several months. In addition, we've found that Term SIFs (settlement agreements that allow clients to pay off the settled amount over several months) keep clients depositing their savings towards settlements (and portions of our fee) over time; nobody wants to leave when they're paying off a great settlement. From a business perspective, it's important that we tether the two activities very closely together, lest we end up settling several accounts without collecting fee; by definition these clients have a history of accumulating debts they are unable to pay, so **"pay as you go"** is a critical piece of all our programs.

i. What is the total amount of fees paid by consumers who have completed the program?
   i. What is the total amount of fees paid by consumers who have completed the program under the Guardian Program?
      - **RESPONSE** – If this information is required, DMB would prefer to discuss this response by telephone with the FTC. In lieu of this response, for the Guardian Program, a typical client will pay approximately $6,760 in fee on $39,000 in debt.[3]

   ii. What is the total amount of fees paid by consumers who have completed the program under the Freedom Program?
      - **RESPONSE** – If this information is required, DMB would prefer to discuss this response by telephone with the FTC. In lieu of this response, for the Guardian Program, a typical client will pay approximately $6,760 in fee on $39,000 in debt.[4]

j. For consumers who have dropped out of the program before completion, what is the total amount of fees paid by them?
   i. What is the total amount of fees paid by consumers who have dropped out of the Guardian Program?
   ii. What is the total amount of fees paid by consumers who have dropped out of the Freedom Program?
      - **RESPONSE TO BOTH QUESTIONS**– If this information is required, we would prefer to discuss this response by telephone with the FTC. In lieu of a response, for both the Guardian and Freedom Programs, clients who “terminated” the program at DMB Financial almost always have at least some of their debts settled, e.g. a client with 7 accounts who settles 4 and then terminates the program to attempt to negotiate the remaining accounts themselves would be classified, under the definition you provided, as “terminated” although significant value has been delivered and earned. Over 66% of our “terminated” clients have had at least 1 debt or more settled. **It is important that the FTC <u>not</u> equate “fees paid by clients who terminated” to “fees paid by consumers who received no benefit”.** The difference is important.

6. Completion Rate

a. (a) Of consumers who enrolled in the program at least 36 months ago, what percentage have completed it?
   i. **RESPONSE** – 40.32%.[5] However, we encourage the FTC to consider ***measuring “success” at the creditor level***, and not at the client level. In the case of a client who has 6 of 7 credit cards (creditors) successfully negotiated, it is inaccurate to deem the engagement “unsuccessful” for the consumer. Ostensibly, 85 percent of their debt burden may have been settled, marking a dramatic improvement in their financial posture. In contrast, credit counseling success must be measured at the client level because all creditors are lumped together under a single consolidated payment so default on one creditor is a default on all. This is not the case with debt settlement, where each account succeeds or

[3] Estimated fee calculated using typical client enrolled who successfully completes the Guardian program with $39,000 in debt in a 36 month program.
[4] Ibid.
[5] A total of 4,080 clients enrolled before January 1, 2007. Of those, 1,645 have completed the program as of January 10, 2010. 214 clients are still active as of this date, which means they continue to pay down their debts towards completion.

fails independent of the others.

b. Of consumers who enrolled in the program at least 36 months ago, what percentage are still active? If you can provide answers to these questions separately for the Guardian Program and the Freedom Program, please do so.
    i. **RESPONSE** – 5.25%. No clients in the Freedom or Independence Programs enrolled more than 36 months ago as of this publication date.

c. The comment states that DMB's completion rate for consumers in New York is 52%. If New York customers are representative of customers nationwide, please provide the basis for this statement.
    i. **RESPONSE** – As in any immature industry, best practices and information technology solutions are being written daily, and as such the data for historical customers (pre-2008) lies in an ever-improving state of fidelity. In May 2009, DMB Financial received an unannounced subpoena from the Attorney General of New York, requesting a variety of data. In compliance with the subpoena, DMB Financial did a major data cleanliness exercise and produced the results noted in this question. We feel these numbers are the most accurate data set we've analyzed; basically they're the best quality numbers we had at the time of the information request.

    We do, however, feel that the sample of New York clients is representative of our overall client base.

7. Number of Settlements

a. What percentage of consumers who enrolled in your program settled at least one debt in the first year after enrolling?
b. What percentage of consumers who enrolled in your program settled at least one debt in the first two years after enrolling?
c. How many consumers who have enrolled in your program have dropped out before settling any debts? If you can provide answers to these questions separately for the Guardian Program and the Freedom Program, please do so.
    i. **RESPONSE TO ALL** – The data is not readily available. Out of the 10,984 clients DMB Financial has enrolled, 6,298 have terminated. Out of those who terminated, 4,188 of those clients have completed at least one settlement prior to termination, with many of them doing 2, 3, or more settlements before terminating. Of those clients who have been enrolled for a full calendar year, we believe nearly 100 percent have reached at least their *first* settlement, although the structure of our information systems make that difficult to assert with absolute confidence, short of a tremendous (250+ hour) data analysis exercise.[6] We can say that it would be **extremely rare** for a client to enroll in our

[6] In operating a debt settlement company there is no daily/weekly/monthly need to run analysis of "how many clients are x% through their debt at time Y" at the aggregate level, in the manner requested by the FTC. The majority of our daily analysis is done at the individual client level and our information systems are not built to rapidly aggregate those kinds of statistics; although it *is* possible to find those answers, we assess that it would take several hundred hours of CRM restructuring, data cleanup, and analysis to produce these numbers for a single scenario, let alone for variable analysis (a different percentage or time value).

performance-based programs, make their monthly payments consistently for one year, and *not* reach a settlement within that first year.

8. Additional Questions

a. The comment has a chart comparing alternative debt relief options for a consumer with $39,000 in debt (page 3). Please explain in detail the assumptions underlying the stated savings rate for debt settlement. For example, did you assume that interest and fees stop accruing for a consumer enrolled in debt settlement?

   i. **RESPONSE** – Generally, all of the assumptions used were laid out on the footnotes; however, specifically to this question, when DMB Financial calculates the recommended monthly savings amount and program length to a client, we consider a number of factors.

      First and foremost is how much the client is able and willing to save each month. Then, we use a calculation based on 10,000+ client experiences that takes into consideration the **continued accumulation of interest and fees** on the original balance, the **monthly payment amount** and **desired program length**, and leaves a "safety factor" as well.

      One cannot predict with extreme accuracy 3-4 years into the future what terms a creditor will accept on a settlement; creditors change their terms monthly and some creditors, like several major banks are doing currently, will announce publicly that they will do accept settlement offers while privately we continue to do settlements with them every day.[7] A safety factor is needed in part because there is a level of uncertainty about what terms will be available, when, and from which creditor. In addition, when a client reaches the end of a 36 month program, they never want to hear that there isn't enough money in their account and will have to continue saving for another 5 months to close out the last settlement. For that reason, we tend to be conservative in our estimates; we would much rather have a client enrolled in a 36 month program who completes the program in just 34 months. They feel great and are more likely to send referrals, which account for 10%-15% of our total business. In one study of our clients, we found that nearly 85% of the clients who graduate our programs, graduate *ahead* of the original schedule. The program calculator used by our Program Consultants to estimate monthly payment accounts for *all* of these unknowns.

b. What criteria does the company use to determine how much of his debt a consumer can afford to pay?

   i. **RESPONSE** – We work with the consumer to develop a budget application that lays out each of their monthly expenses and income amounts, as well as any long term savings or obligations, work situation, stress level, and lateness of their credit card payments. Normally, as a reference point, we try to target a number that is both lower than their current credit card minimum payments and still large enough to build a program that will

[7] To preserve the relationships with major creditors we need to effect good settlements, DMB Financial would prefer not to name the specific creditors publicly.

get them out of debt with the least likelihood of being sued by a creditor. We do not take clients into programs longer than 60 months and any program length longer than 48 months must be approved by an owner on a case by case basis; the risk of litigation is simply too strong for most prospects to allow them to stretch the program out that long.[8] Prospects who are unwilling to save sufficient money within a short period of time are not accepted into the program.

c. The comment states that most clients who terminate the debt settlement program do so because they file for bankruptcy or cannot afford to continue saving towards a settlement, not because of unhappiness with DMB Financial (page 11). What is the basis for this assertion?
    i. **RESPONSE** – This statement is based upon research conducted by Dr. Rick Briesch at SMU, and published in his second study on debt settlement (and paper submitted to the FTC around November 3, 2009).

d. The comment states that credit issuers debt settlement provides creditors with the highest expected return on the dollar: $.25-$.60, as compared to $.12-$.18 for litigation and $.06-$.25 for debt collection (page 13). What is the basis for the stated rates of return?
    i. **RESPONSE** –**Bankruptcy:** There are several reliable sources for this data, all confirmed by personal experience from the debt collectors and negotiators we have on staff. According to "The Anatomy of U.S. Personal Bankruptcy Under Chapter 13", a working paper written by representatives from the Federal Reserve Banks of Richmond and Philadelphia, *"The data suggests considerable variation in creditor recovery rates under Chapter 13, with a median recovery rate of 12 percent for both secured and unsecured debt."*[9]

    Debt Collection: The numbers vary considerably, firm to firm. Recovery rates in debt collection vary depending on the average dollar amount, the age, and if the debt is a first or second placement. However, a number of debt collection companies are public and report detailed statistics on their recovery rates to shareholders. One such company is Portfolio Recovery Associates. According to their 3rd Qtr Public Filings in 2009, Portfolio Recovery Associates purchased $1.75 billion of debt for $76.7 million (**a paltry 4.38% return on the debt to the original creditor**) and recorded $92.4 million in collections revenue (**a recovery rate of 5.28% against the original debt balance**, and a notional price to the aggregate consumer of $0.052/$1 at the portfolio level).[10] Other data suggest collection rates as low as 3-4 percent against original balance (see Figure 2). Debt purchase prices (the "recovery rate" for original creditor) are – *for any profitable collection firm* – by definition less than the collection company's recovery rates of 3-4 percent.

[8] Longer programs equate to lower monthly savings payments.
[9] *"The Anatomy of U.S. Personal Bankruptcy under Chapter 13"*, Working Paper # 07-05; Eraslan, Hulya (University of Pennsylvania), Li, Wenli (Federal Reserve Bank of Philadelphia), and Sarte, Pierre-Daniel (Federal Reserve Bank of Richmond); September 2007, p3.
[10] *"Portfolio Recovery Associates Reports Third Quarter 2009 Results",* Press Release, October 29, 2009. Accessed at http://phx.corporate-ir.net/phoenix.zhtml?c=135456&p=irol-newsArticle&ID=1348541&highlight= on January 18, 2010. An excellent table of debt purchases and collections by year can be found in their **2008 Annual Report**, page 6, accessible at http://phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9MzM4MTQ1fENoaWxkSUQ9MzIyOTczfFR5cGU9MQ ==&t=1 as of January 18, 2010. From this table, one can calculate recovery rates in a variety of ways.

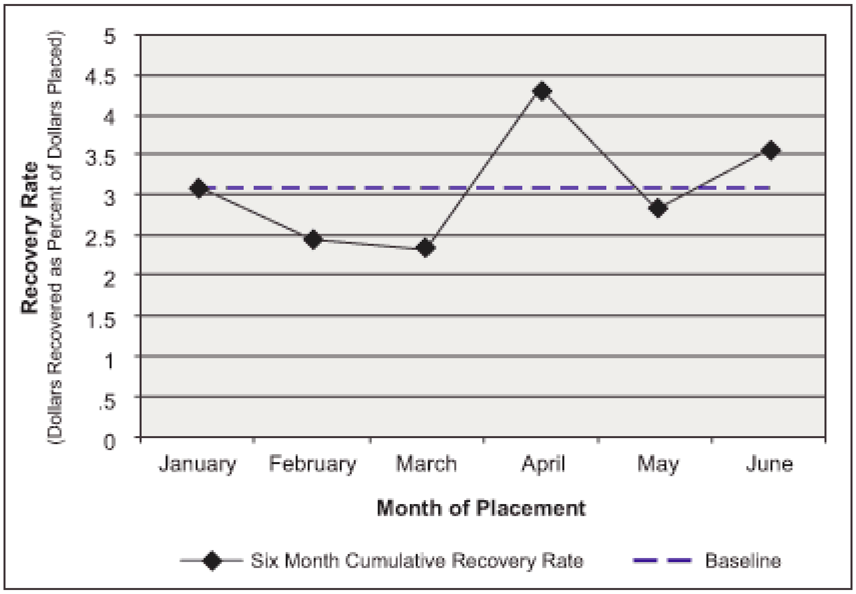

Figure 2: Baseline Six Month Cumulative Collection Recovery Rate[11]

Although these aggregate debt collection rates are reflective of the overall portfolio within a debt collection company, the numbers from a consumer's perspective tell a different story. ***Of those consumers who pay their debts through a debt collector***, many pay 6-25 percent of their original balance or more back in total. Some consumers pay back 100 percent of the owed debt and others pay only a small fraction of the debt—the collection company's portfolio reflects 3-5 percent *aggregate recovery rates*, but this includes both non-recovered debts and consumers paying back large percentages of their debts.

In addition, DMB Financial's founders and the majority of our debt settlement negotiators come from a debt collection background. They contributed their professional insight in interpreting the various data points to come to a combined, realistic range of debt collection recovery rates.

In assembling the data for the table in DMB Financial's FTC comments, we aggregated these factors and used an educated average. **We are confident that few debt collection companies would be so bold as to suggest an average collection rate above 25 percent.**

In both bankruptcy and debt collection, for the purposes of our FTC comments, we intentionally chose conservative estimates, giving the best possible light to bankruptcy and debt collection statistics and the least favorable light to debt settlement.

[11] Figure provided by Six Sigma Financial Services. Accessed at http://finance.isixsigma.com/library/content/c060222a.asp on January 18, 2010.