



TASC POSITION PAPER

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TASC History and Mission

The Association of Settlement Companies (“TASC”) was established in September 2005 in response to ambiguous debt management legislation passed in Texas—SB 1112. TASC was able to demonstrate to the Texas Finance Commission and the Texas Consumer Credit Commission charged with enforcement of SB 1112 that the bill originally aimed at nonprofit consumer credit counseling companies but inadvertently included for-profit debt settlement companies who do NOT hold the consumer’s funds in escrow. Accordingly, TASC was able to work with The Honorable Commissioner Leslie Pettijohn and her staff to develop language which was in keeping with the bill’s original intent but excluded certain models of debt settlement companies from the enforcement of said legislation. Subsequent to Texas, TASC broadened its focus to monitoring legislation in all fifty states because other states were passing or proposing legislation which dramatically hinders indebted consumers’ options for financial recovery. There is clearly a developing trend of debt management legislation which targeted nonprofit consumer credit counseling companies but contains language that unwittingly affects for-profit debt settlement companies, a completely different business model.

Debt settlement companies act on behalf of consumer debtors to help them resolve their debts. They do this by entering into direct negotiations with creditors in order to facilitate the repayment of debts. In return for their services, debt settlement companies are generally paid a fee based upon a combination of the total amount of the debt handled and the amount saved by the consumer debtor. Most debt settlement companies including all TASC members do not escrow, handle, manage, or otherwise control their client’s funds. This is a distinguishing factor between debt settlement companies and other debt management business models including the nonprofit consumer credit counseling companies.

TASC’s goals are to promote good business practice in the debt settlement industry, protect the interests of consumer debtors, and educate legislators and regulators at all levels of government with respect to the issues involved in the debt settlement industry. The mission of TASC is to encourage debt settlement companies to provide services in accordance with the highest professional and ethical standards, in order to retain the confidence of the public, the credit industry and local, state, and federal government. TASC is NOT anti-regulation. On the contrary, TASC fully supports legislation that is both fair and effective when applied to the debt settlement business model.

Debt Settlement Industry Background

The Debt Settlement Industry arose in response to the increase in revolving consumer credit debt in the United States. For a large portion of the American population, credit has become a way of life. According to the Federal Reserve Statistical Release dated February 7, 2006, American consumers dramatically increased their consumer debt obligation to over \$800 billion.¹ Consumer debt levels are significantly

United States Federal Reserve Statistical Release February 7, 2006¹

outpacing disposable income levels while at the same time personal savings are at an all time low. Consumers making only the minimum payment on their credits cards make hardly a dent in their overall debt balance. In 2005, personal bankruptcies rose 31.6 percent to a record level of two million filings.²

Over the years, several programs have been developed to address the issue of inability to make the minimum monthly payments on outstanding debts, which have had varying degrees of success. Bankruptcy is the most obvious option, but the recent amendments to the federal bankruptcy law have made obtaining bankruptcy relief significantly more difficult. Chapter 7 liquidation, which offers a complete “new start,” has been placed out of reach for many debtors. Chapter 13 filings impose on the debtor a full repayment plan covering an extended period of time and the stigma and long term adverse effects of bankruptcy filing exert a major deterrent effect. Moreover, the national rate of completion for confirmed Chapter 13 plans is only 33%³.

Another option involves credit counseling which is also known as debt consolidation. These services are often offered by “non-profit” consumer credit counseling companies which are in fact subsidized by the banking industry through “Fair Share” payments and other monetary support. Credit Counseling does not offer to the consumer any reduction in the principal amount of the debt owed, but only a reduction in interest and late fees over the life of an extended repayment plan. In addition, the rate of successful completion of credit counseling program is only 21% according to a study undertaken by the credit counseling industry itself.⁴ In other words, 79% of the people enrolled in a credit counseling program do not complete their plan as originally contemplated.

Debt settlement offers an alternative for both the debtor and the creditor. It provides a middle ground where the debtor and creditor can negotiate the outstanding financial obligation, including principal, to a mutually agreeable level. This permits debtors to make restitution on their financial obligation in a shorter time period and a more manageable monthly payment than that required through a credit counseling program.

Compared with credit counseling and bankruptcy, debt settlement is a relatively new industry with a significantly smaller number of participants. Therefore, there is no long term statistical evidence regarding expected completion rate for this type of program. (Although anecdotal evidence within the industry suggests that the rate exceeds that for Chapter 13 plans and significantly exceeds that for credit counseling). One factor which may explain the more favorable completion rate is that the consumer participates in determining the repayment terms. By comparison, in a Chapter 13 filing, the payment terms are determined by a Trustee while in a credit counseling program, the payment terms are dictated by the creditors. In the debt settlement model, the consumer debtor

² Chu, Kathy, *Managing Your Money*, USA Today, January, 11, 2006

³ Bankruptcy by the Numbers: Measuring Performance in Chapter 13,” by Gordon Bermant and Ed Flynn, Executive Office for the U.S. Trustees

⁴ Consumer Reports, *Pushed Off the Financial Cliff*, July 2001.

has significant input on the amount and terms of the repayment. The consumer debtor is in the best position to determine the feasibility and compliance thereof from any repayment plan. By empowering the debtor with this ability, there is a greater likelihood of completion with the debt settlement program. In addition, evidence within the industry suggests that consumers who complete debt settlement programs generally do so in shorter periods of time and for less money than would have been the case had they been involved in credit counseling.

This position paper provides statistics of which you may already be aware. The purpose is not to solve the greater issue of rising consumer debt in this country but to preserve options to consumers in your state attempting to recover from the destructive effects of excessive debt.

Issue: Uniform Debt-Management Services Act

With the admirable intentions of protecting vulnerable consumers from abusive and deceptive debt management companies, The National Conference of Commissioners on Uniform State Laws (“NCCUSL”) approved and recommended for enactment The Uniform Debt – Management Services Act (“UDMSA”). UDMSA was originally intended to regulate only credit counseling organizations; it was expanded to cover debt settlement companies substantially later in the drafting process. Because of this change, UDMSA now attempts to regulate both non-profit organizations and for profit organizations in the same model legislation.

One of the principal distinctions between the credit counseling organizations and the debt settlement companies is that the former generally receive, control, and disburse the debtor’s funds to the creditors while the latter do NOT. It is understandable that there is a need for increased scrutiny when an organization exercises control over a debtor’s money. However, most debt settlement companies (and TASC members) DO NOT RECEIVE, DISBURSE OR EXERCISE ANY FORM OF CONTROL over their client’s money. Accordingly, a different form and level of regulation is appropriate than those applied to organizations which control their clients’ money.

UDMSA also is based on the assumption that both the consumer counseling and debt settlement business models are competing for business on a level playing field. On the contrary, credit counseling companies receive funding, not only from their clients, but from creditors and banks which helps to subsidize their operations. Debt settlement companies, as unsubsidized, fully taxed, for-profit entities, must compete in the marketplace for investment capital.

Finally, UDMSA imposes restrictions and limitations which are quite onerous to debt settlement companies. If enacted in its entirety, UDMSA may preclude continued operation of debt settlement companies. The end result is severely limited debt management choices for your state’s indebted consumers.

TASC Summary of Position

TASC takes no official position on the applicability of UDMSA as it applies to the credit counseling companies. TASC does, however, oppose the applicability of UDMSA to debt settlement companies for several reasons.

Costs of Operation. The actual dollar costs of administering either a debt settlement or a credit counseling program will vary dependent on many factors, including but not limited to the costs of labor, space ownership or rental, operational efficiency...etc. While the actual costs vary from company to company, there is little disputing that the operational and overhead costs of administering a debt settlement company is higher than the costs of administering a credit counseling program.

* **Client Enrollment.** Creditors and recent bankruptcy reforms refer potential debtors to credit counseling programs; thus credit counseling companies have inherently lower marketing costs. On the other hand, debt settlement companies must engage in more active and costly marketing campaign to promote the option and benefits of the debt settlement programs. This results in higher costs to acquire and enroll a client.

* **Client Services.** Debt settlement companies provide varying levels of customer service support throughout the term of a debtor client's contract. The number of hours required to service, negotiate, and administer the accounts for the duration of the program far exceeds that needed by credit counseling companies. Debt settlement companies do not simply negotiate the debts at the beginning of the contract and then act as a repayment collection and disbursement vehicle to the creditors, as is the case with credit counseling companies. Debt settlement companies must negotiate and actively monitor each creditor's activities with respect to their client's accounts throughout the length of the program. Therefore, debt settlement companies must be allowed to collect reasonable fees in the beginning of the contract to maintain effective levels of ongoing client support.

* **Creditor Contacts.** Administering a debt settlement program normally requires numerous contacts with a creditor during the negotiation process. There exists the possibility of additional contacts regarding the client's account if the account is transferred from the original creditor to a third party collection agency. On the other hand, credit counseling companies typically have software that specifies the payment amount and interest rate required by each creditor. This ability simplifies the preparation of the debt management proposal ultimately sent to each creditor. Once the creditor accepts this proposal, the creditor contact is simply the mailing or electronic payment of the required monthly payment to said creditor for the duration of the program. The added time and expenses incurred by the debt settlement companies result in a higher number of active hours per account; hence, higher costs to the settlement company versus the credit counseling companies.

Sources of Funding. Debt settlement companies rely on compensation solely from the consumers without any outside assistance. Debt settlement companies do not

receive contributions or subsidies from outside sources such as creditors or banks. This ensures debt settlement companies act entirely on behalf of the debtor client and owes only this duty of loyalty to the debtor client. In essence, debt settlement companies act as a consumer advocate for clients in resolving their debt. Analogous to the relationship between debt settlement companies and their clients is the relationship between the collection agencies to their clients, banks and creditors.

TASC Proposed Action

TASC is in full support of legislation that protects consumers, addresses the concerns of the governmental entities and allows debt settlement companies to compete equally in a consumer driven marketplace.

TASC proposes registration for all debt settlement companies which will allow the governmental bodies a monitoring vehicle in their respective states. Additionally, a fee structure, that recognizes the distinctions between debt settlement companies and credit counseling companies, which allows the debt settlement companies to collect a reasonable portion of fee at the beginning of the contract rather than collection of all fees after the completion of the program. This will allow debt settlement companies to continue to provide services to the debtor consumer since a debt settlement program average proximately 36 months. Performance guarantees can be utilized in place of fee caps, thus allowing settlement companies the opportunity to compete in a free-market environment without the risk of over-charging the consumer. Finally, TASC supports standards for all its members that are independently verified by an outside third party agency.

The debt settlement industry recognizes and supports your state's desire to protect your consumers. Our industry embraces regulations that shut down dishonest and unscrupulous debt settlement operators. To achieve this goal, TASC has prepared draft legislation that would both achieve these goals and permit debt settlement companies to continue operation and to provide the vital "third option" that they offer to distressed consumers. Regulations that prohibit consumers from seeking multiple avenues in resolving their financial obligations will stifle reconciliation, recovery, and growth in the debt management industry. The consumer debtors and current debt settlement businesses in your state will ultimately suffer from the passage of UDMSA.

TASC respectfully requests an opportunity to meet with you and your staff to discuss this matter in greater specificity and detail.