

MICRC

MARYLAND CONSUMER RIGHTS COALITION

Debt Settlement in Maryland

Compounding Problems, Deepening Debt

Marceline White
Maryland Consumer Rights Coalition

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The **Maryland Consumer Rights Coalition (MCRC)** is a nonprofit organization founded in 2000 that seeks to advance and protect the interests of Maryland consumers through education and advocacy, and works to ensure fairness and safety in the marketplace. MCRC educates individuals, organizations and public officials about consumer issues and consumer rights; advocates for consumer interests before the Maryland legislature and state agencies; studies issues of concern to consumers and serves as a resource to the community on those issues; and coordinates our efforts with national consumer organizations on issues of concern to Maryland consumers.

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I. EXECUTIVE SUMMARY

As households struggle financially in today's fragile economy, debt settlement companies are proliferating. Debt settlement companies claim they can relieve financial distress by negotiating with creditors to reduce a consumer's debt. More than 2,000 debt settlement companies exist in the United States today—triple the number that existed a few years ago¹.

Debt settlement companies have emerged as declining incomes and rising living costs have led consumers to see their debts increase. This includes the millions of American homeowners who borrowed against their home's equity to cover costs, and families who used credit cards to meet basic expenses, pay for necessary home repairs, unforeseen medical expenses, or to cover monthly expenses when a family member was out of work.

In Maryland, the cost of living has been increasing, while foreclosures and job losses mount. Maryland's unemployment rate doubled within 18 months—from 3.6 percent in December 2007, to 7.3 percent in October 2009². By the end of September 2009, at least 150,000 Maryland homeowners were at least one month behind in their payments, according to *The Baltimore Sun*³.

In the hopes of reducing expenses and obtaining some financial relief, many consumers in Maryland and elsewhere are turning to debt settlement services. Debt settlement services promise to halve a consumer's debt by negotiating lump-sum settlements for consumers.

However, unlike debt management plans, which are usually provided by nonprofit credit counseling agencies and negotiate better terms for consumers to pay creditors monthly, debt settlement agencies employ a different tactic and a different fee structure. Too often, these tactics result only in substantial fees for the debt settlement company but leave the consumer far worse off than he or she was before contracting with the company.

Debt settlement agencies tell consumers to quit paying their creditors altogether. Instead, consumers pay a monthly amount into a separate bank account that is often set up by the debt settlement firm, or to which the contract gives the debt settlement firm access. The firm promises that once a consumer has accrued enough money to negotiate a "lump-sum" settlement, the debt settlement firm will negotiate on the consumer's behalf a settlement for a lower amount than originally owed.

Debt settlement firms charge advance fees – well before any or all of the debt is settled. These fees are often between 14-20 percent of the full amount of the debt and must be

paid in full even if the consumer drops out of the program or the company is unsuccessful in negotiating the promised debt reduction. Under two of the common fee models, consumers pay in full well before the debt settlement program is completed. All fees to the firm must be paid (often within the first 4-6 months of the program) before any negotiations begin on the consumer's behalf. Not surprisingly, because debt settlement firms collect fees before performing any work, they often do not contact creditors or perform any other service for the consumers.

In another widespread fee structure, 14-20 percent of the total debt is due in a set-up fee of about 4 percent of the debt, with the rest of the fee spread over up to the first half of the contract. While the debt settlement industry calls this a prorated fee, it too results in the full fee being paid well before the consumer gets the result he or she has sought, which is the settlement of all debts.

Debt settlement, in short, is more often than not a vehicle for predatory companies to make money at the expense of consumers who have turned to them for help in putting their finances in order. Instead of getting the promised services, consumers typically end up with less money, more debt, a worse credit score, and dwindling options.

Problems with Debt Settlement Companies

Complaints about debt settlement companies have been increasing nationally in the past three years. This is certainly true in Maryland, where complaints about debt settlement firms increased by 144 percent in the past three years, according to the Maryland Attorney General's office. The industry as a whole has generated complaints, primarily dealing with the following issues:

Payment Before Services and Results

Debt settlement firms often require individuals to pay fees ranging from 14-20 percent of their total debt regardless of whether any or all of the debt has yet been settled. For example, a consumer with \$25,000 in debt would pay a fee ranging from \$3,500-\$5,000. This is particularly egregious because as previously noted, often no services are provided after this fee is paid. In some cases, services are offered but yield no reduction in debt for the consumer, yet the fee is still collected. Creditors are not contacted, debt increases due to late fees and penalties, and collection activities continue. Even if creditors are contacted, the size of the debts can continue to grow due to interest or penalties charged by the creditor, collection activities continue, and the consumer even can be sued on the debts while waiting for the settlement firm to act.

Deceptive Practices

Many debt settlement companies misrepresent their success rate, the amount by which they can reduce a consumer's debt, and the amount of time it will take to complete the program. Consumers are misled about the probability of settlement and the amount they may save. For example, the State of New York sued two debt settlement firms for deceptive practices and false ⁴advertising. One firm, Credit Solutions of America (CSA), promised a 60 percent reduction in consumers' debt but on average only 1 percent of CSA clients realized any savings⁵. In Maryland, the Frederick Law Firm claimed it could reduce consumers'⁶ debt by 70 percent but could not substantiate those claims.

Debt settlement advertising and marketing makes the process seem relatively risk-free. The firms rarely if ever communicate effectively to consumers that debt settlement may not stop collection activities, may damage a consumer's credit score and credit rating, and that any income saved may be taxable. Furthermore, claims of success or track record, such as a claim to save 40-60 cents on the dollar, are not adjusted to account for the fees that will reduce those savings. A claim that others saved 50 cents on the dollar is deceptive if the consumer is likely to achieve that result only on some, but not all, of the debts.

There is a significant drop-out rate among consumers contracting with debt settlement companies. Many consumers pay debt settlement firms a substantial advance fee yet are unable to save enough to negotiate a settlement and they drop out of the program. One reason for the high drop-out rate is the eligibility qualifications debt settlement firms often use. Often an individual must owe at least \$10,000 to several creditors to be eligible for debt settlement.

Individuals generally seek debt settlement services only when financial setbacks or life circumstances makes it increasingly difficult to pay monthly bills. In other words, debt settlement is often a last resort for low-to-moderate-income consumers. Due to their financial circumstances, these consumers are often the least likely to be able to save enough money to pay a debt settlement firm's advance fees and then accrue enough to pay any settlements that are reached with creditors. Yet, most debt settlement firms do not consider whether a consumer will be likely to make the required monthly payments when they contract with consumers. The suitability of debt settlement programs for individual consumers is not a consideration of most debt settlement firms.

Financial Hardship/Difficulties Canceling Contract

Thus, consumers who enter these programs are often those who are least likely to benefit from this type of service since they are already facing financial distress. They are unlikely to be able to save as much as the program requires in order to settle their debts, and they drop out of these programs before achieving any settlement. Yet, by the time they leave the program, many have had their credit scores damaged, faced increased collection activity, and lost time and money dealing with the debt settlement company. Since a substantial portion of the fees paid is the nonrefundable set up fee and early high monthly fees, the consumer will have paid substantial sums – money that could have been used to pay down debts – and have little or nothing to show for months of savings after fees are deducted.

Federal and State Laws on Debt Settlement

To date there are no federal laws that specifically regulate the debt settlement industry. The Federal Trade Commission has proposed an amendment to its Telemarketing Sales Rule, which if adopted would explicitly address some of the problems with debt settlement industry sales made by phone. However, no part of the rule would apply if there was a face-to-face sales presentation, which is an important marketing tactic for debt settlement firms. Moreover, the rule does provide the right to cancel a contract or ban misrepresentations of successful results. States have adopted a range of approaches to address the debt settlement industry. Several states have banned debt settlement firms from operating within their state. Other states have set limits on the amount and percentage of fees a firm can collect, and they require certain disclosures and forbid certain practices.

Maryland Law and Debt Settlement

Maryland does not regulate debt settlement companies. In the absence of regulation, Maryland consumers have been and continue to be led down the proverbial primrose path, a path scattered with misleading promises by debt settlement companies, front-loaded fees and poor results. At the end of the process, Marylanders often are far worse off than if they had never entered into a contract with debt settlement companies. While Maryland has several laws that can be applied to attempt to provide restitution to consumers who have been taken advantage of by debt settlement firms, they fail to help consumers avoid deceptive and expensive debt settlement programs in the first instance. This mess can and should be changed through appropriate legislation that sets reasonable standards and enables consumers to understand, realistically, whether debt settlement is right for them.

Policy Recommendation

Maryland should pass legislation to specifically regulate the debt settlement industry.

Legislation should:

- ◆ employ a broad definition of debt settlement services and products;
- ◆ set reasonable fees of no more than 15 percent of the total savings achieved in completed paid settlements, with the savings measured by the difference between the amount of the original debt and the amount of a binding settlement of the debt;
- ◆ require payment only after results (settlements) are achieved;
- ◆ mandate disclosures of the material facts and negative consequences of debt settlement; and,
- ◆ ban claims of savings as inherently misleading because individual results vary so widely that historical results may not apply to many debts; at a minimum, require that claims of savings be based on savings net of fees paid.

II. ABOUT THE REPORT

This report draws from a literature review of debt settlement news articles; a review of relevant federal and state laws; consumer law treatises; Federal Trade Commission documents; consumer complaints and enforcement actions in Maryland; and stakeholder interviews with Maryland policymakers, regulators, and consumers who used debt settlement companies. The report employs a mix of qualitative and legal analysis. Where possible, quantitative analysis is used as well. However, data has been difficult to obtain from debt settlement companies and questions about the quality of the data remain. While state agencies receive and track consumer complaints, demographic information such as the sex, race, age, income level, location, and other information about the consumer is not collected.

Anecdotal evidence taken from consumer complaints, experiential research, and consumer testimony illustrates the types of deceptive practices that debt settlement companies engage in and the harm that befalls the consumers who contract with them.

The legal analysis surveys federal law, Maryland state law, and other state laws regarding debt settlement and highlights opportunities for legal action and enforcement as well as gaps and inconsistencies in current law. The report concludes with a series of policy recommendations to better protect consumer interests in Maryland.

III. INTRODUCTION

As low- and middle-income households continue to struggle in today's economy, debt settlement companies are proliferating—enticing consumers with promises to halve their debt and relieve their financial distress.

Debt settlement companies promise to reduce consumer debt by negotiating with credit card companies to reduce the total amount a consumer owes to creditors; but in reality, most firms only increase an individual's debt and damage his or her credit.

As many as 2,000 debt settlement companies operate in the United States, triple the number from a few years ago.⁷ The growth in the industry is the result of two converging forces: increased consumer indebtedness combined with a decreased ability to pay.

According to *Business Week*, the typical U.S. household has more than \$7,000 in outstanding balances, up 45 percent from five years ago⁸. A national study by Demos of low- and middle-income households found the average household had \$9,827 in credit card debt. Consumer debt has grown for a number of reasons. Some individuals bought more goods and services than they could afford. However, for many individuals, credit cards were used to make up the difference between stagnant wages and rising costs of living. Between 2000 and 2006, most households experienced stagnant wages while the cost of living rose by 27 percent.⁹

To cover this gap, households accumulated nearly \$900 billion in credit card debt¹⁰. Results from the Demos survey found that at least 37 percent of low- and moderate-income households relied on credit cards to cover their rent, mortgage, groceries, utilities, or insurance when they didn't have enough money in their checking or savings account to pay for these expenditures. These same households often increased their indebtedness to pay for a major home or car repair or to provide a safety net during a period of unemployment. Additionally, 52 percent of households stated that medical expenses contributed to their credit card debt.¹¹

As home values decline, job losses and underemployment continue, and credit markets tighten, consumers are falling behind on their mortgages and on their payments to creditors. More than 6 percent of households are more than 30 days late paying their credit card bills, an all-time high.¹² According to a recent *New York Times* article, the amount of consumer credit at risk of default is \$24.5 billion.¹³

In Maryland, the findings mirror national trends. In 2007, the median wage rose 2.5 percent from 2006, but remained only 4.4 above the 1999 level when adjusted for

inflation¹⁴. While Marylanders’ real income rose a scant 4 percent in the last decade, the cost of living was spiraling upwards—leaving many Marylanders with few options other than borrowing against their home equity or using credit cards to make up the difference between their incomes and expenses. Wages remained flat for high-, medium-, and low-income Maryland workers¹⁵. Nearly 18 percent of full-time workers in Maryland earn below-poverty wages¹⁶. Between 2007 and 2009, job losses skyrocketed and foreclosures increased precipitously. Maryland’s unemployment rate doubled within 18 months—from 3.6 percent in December 2007, to 4.5 percent in August 2008, to 7.2 percent in August 2009, to 7.3 percent in October 2009¹⁷. Preliminary estimates suggest that 215,216 people are unemployed in Maryland today—a 50 percent increase from last year. This figure doesn’t include the number of discouraged workers who are no longer seeking jobs or under-employed workers.

Job loss is contributing to rising foreclosure rates throughout the state as well. In November 2009, nearly one in every 10 prime borrowers—homeowners judged to be good credit risks—fell behind in their mortgage payments¹⁸. By the end of September 2009, nearly 150,000 Maryland homeowners were at least one month behind in their payments¹⁹. This represents a 70 percent increase in the number of delinquent payments by prime-borrowers since September 2008²⁰. Foreclosures in Maryland rose 130 percent between 2007 and 2008. In August 2009, foreclosures were up 70 percent from a year before.

In Maryland, as in other parts of the country, distraught consumers are turning to companies that promise to reduce their debt and improve their financial stability.

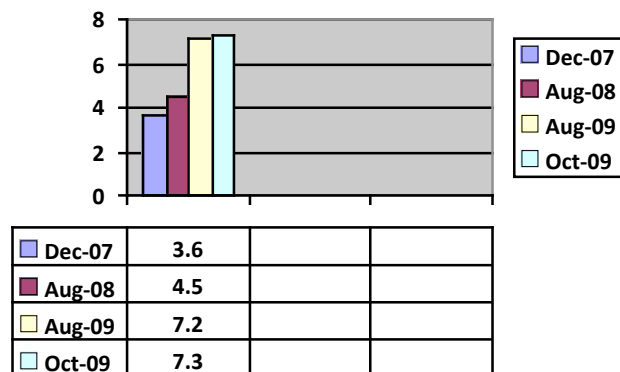


Table 1. Unemployment Rates in Maryland 2007-October 2009

Source: Bureau of Labor Statistics www.bls.gov

DEBT RELIEF

For many consumers, the terms “debt management,” and “debt settlement” may seem interchangeable, but each describes a very different program of promised debt relief. This report will focus on debt settlement. The debt management model is described below and in the chart for comparison.

Debt Management

Debt management plans (DMPs) are provided by for-profit and nonprofit credit counseling agencies. DMPs allow consumers to pay down debts through a monthly payment plan established with creditors. The DMP service provider will negotiate a reduction in interest rates, late fees, and minimum payments to lower consumers’ monthly payments. Many debt management plans also have creditors remove delinquencies from the consumer’s account, thereby improving the consumer’s credit score. Many also include community education, financial literacy, and budgeting workshops in addition to the DMP plans. Many of these plans include a fee for set-up and a monthly maintenance fee but the fees themselves are often fairly modest. The consumer’s monthly payment goes primarily to paying down the debt.

Debt Settlement

Debt settlement companies differ from debt management services in several critical ways. Unlike DMP programs in which consumers pay their creditors each month, debt settlement companies require or strongly suggest that consumers stop paying their creditors.

Rather than making a minimum payment to a credit card company or other creditor, the consumer makes payments directly to the debt settlement company or into a separate account arranged by the debt-settlement company, from which the debt settlement company directly withdraws its fees. Debt settlement firms argue that withholding payment will make a creditor more likely to agree to a lump sum settlement that is lower than what is owed. In theory, the consumer then saves enough of their own funds in these accounts to provide those lump-sum settlements to each creditor. Because multiple debts are often involved, this process may take several years. Settlement negotiations do not begin until the consumer has saved enough to negotiate and settle the first debt.

Most debt settlement firms will only work with consumers that have multiple debts and – unlike debt management companies -- debt settlement companies have a “floor” for the amount of unsecured debt that they are willing to handle- (i.e. a consumer must owe at least \$5,000 to two or more creditors).

To join a debt settlement program, an individual typically must pay a fee before any services are performed. These “front-end” fees require consumers to pay a large portion of the total fee within the first few months and the balance within a year to a year and a half—often before any negotiations take place, and well before all debt is expected to be settled. Other debt settlement firms charge a “flat fee” to set up a savings account and to enroll in the program. These programs have a 2-4 percent “set up” fee due on signing and often spread over the first three months, with overall fees totaling 14-20 percent of the full amount of the debt. Under this approach, the entire fee is collected out of the monthly savings by the end of the first half of the contract, whether or not any debt has been eliminated during that time.

Most debt settlement companies claim that they will contact creditors to explain that a consumer is not making their minimum monthly payment until a settlement is reached; however, in many cases, creditors are never contacted. Moreover, whether or not the creditor is contacted, the individual’s credit worthiness rapidly deteriorates because non-payment is noted on the consumer’s report. The amount due continually grows by the amount of late fees and penalties assessed for non-payment. Some credit card companies also hike their customers’ interest rates due to the perceived increased risk of non-payment, further inflating the amount due and burying the consumer deeper in debt.

Debt settlement firms settle a client’s debts one by one. If, for example, an individual owed three creditors \$5,000 each for a total of \$15,000, the debt settlement company would settle one \$5,000 debt first, then, once that debt was settled, move onto the next debt. However, the consumer would continue to accrue late fees and penalties from the debts that were not being settled—even as they saved up money to negotiate a lump-sum settlement.

The debt settlement company gets access to the account where the consumer savings are held and typically has a contractual provision allowing the firm to automatically debit a certain amount of money from the account each month. Some companies insist on a contractual provision giving the debt settlement firm a limited “power of attorney” providing access to the account.

Often debt settlement firms direct consumers to send all creditor information to the company so that the firm receives all notices of collection activities, penalties, and fees. This practice often hides from the consumers how bleak their deteriorating situation has become and leaves the consumers without adequate information to determine their best course of action.

Non-completion rates are very high and successful-settlement rates are very low.

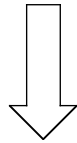
Debt Management vs. Debt Settlement

	Debt Management	Debt Settlement
Profit model	Nonprofit and for profit	For-profit
Program description	Pay down debt monthly to creditors through plans that reduce interest rates and late fees to lower individual's monthly payments.	Sets up or requires a separate account for individuals to save up funds to pay future settlements of debts. Does not pay creditors monthly and encourages individuals to stop paying creditors.
Fee structure	Set up and maintenance fees, generally modest, regulated in many states.	Advance fees to company; flat-fee ranging from 14-20 percent of total debt. Fees due in full by the end of the first half of the contract. Fees owed whether or not any debt is ever settled.
Completion rate	High	Low-some estimates as low as 1 percent, industry estimates at 25 percent for those who stick with it for three years.
Effect on credit	Works with creditors to pay off debt; does not harm credit.	Damages credit as individuals fail to pay creditors.
Regulation/Relevant state & federal law	Credit Repair Organization Act (CROA) FTC Telemarketing Rule 310 State Unfair and Deceptive Practices Acts (UDAP) State Debt Management laws Maryland Debt Management Law	Credit Repair Organization Act (CROA) FTC Telemarketing Rule 310 State Unfair and Deceptive Practices Acts (UDAP) State Debt Settlement Laws No law to regulate the debt settlement industry exists in Maryland

Debt Settlement Scenarios

IDEAL

Consumer contacts debt settlement company.
Debt settlement representative speaks to consumer and candidly explains that debt settlement will not stop collection activity or growth of the debt.



Consumer opens separate account to save for lump-sum settlement.
Debt settlement company contacts creditors.
Debt settlement company negotiates settlement for consumer at lower amount than owed.
Consumer saves up lump sum in account for negotiation of next settlement.
Debt settlement company gets paid a percentage of the savings from the original debt amount for each settlement achieved.

WHAT OFTEN HAPPENS

Consumer contacts debt settlement company or company contacts the consumer.
Company does not explain that collection activity will continue, debts will grow and credit score will be further damaged.



No creditors are contacted by debt settlement firm.
Collection activities by creditors continues.
Credit rating falls, interest rates and penalties increase for consumer.



Consumer struggles to pay monthly fee and to save for settlement
Consumer receives no help from company, tries to cancel contract but finds it difficult to do so. Unsettled debts are higher than when debt settlement began.
Consumer has paid significant fees, and is still left with significant debts.

IV. DEBT SETTLEMENT INDUSTRY

Overview

The debt settlement industry has been the subject of numerous consumer complaints. Nationally, the number of complaints that states have received against debt relief companies, particularly debt settlement companies, has more than doubled²¹. Since 2007, debt settlement and debt negotiation companies have generated the most complaints received by the Better Business Bureau²².

Maryland's record is even worse than the national trend. In Maryland, the number of consumer complaints received by the Office of the Attorney General (OAG) between 2008-2009 has more than tripled. In 2007, the OAG received 15 complaints; in 2008, the number doubled to 30 complaints; and in 2009, the number rose to 104 complaints—a 144 percent increase in just three years.

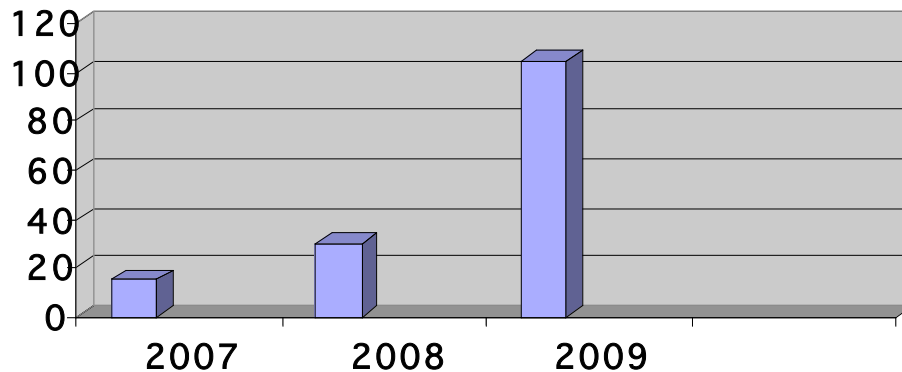


Table 2. Number of debt settlement complaints received in the Office of the Attorney General in Maryland.

Source: Office of the Attorney General. Email correspondence, November 2009.

As unemployment rises and homeowners fall behind on mortgage payments, more individuals may turn to debt settlement as a last-ditch effort to reduce their debts. The rise in complaints against the industry may reflect the growth in the industry and the increase in the number of Marylanders turning to these companies for relief during these challenging economic times.

Yet, rather than bringing relief, debt settlement companies too often engage in deceptive practices and provide irresponsible advice that only compounds an individual's financial problems.

The debt settlement industry is unregulated in Maryland. Although state and federal laws exist that may help consumers after they have been taken advantage of by debt settlement companies, few people in such financial distress can find attorneys willing to fight for them. Maryland should proactively regulate debt settlement companies so that the worst abuses can be prevented *before* they happen.

Problems with Debt Settlement Companies

1. Payment Before Services

Debt settlement firms often require individuals to pay fees ranging from 14-20 percent of their total debt before beginning to negotiate with their creditors. For example, a consumer with \$25,000 in debt would pay a fee ranging from \$3,500-\$5,000. At the same time, consumers are told to stop paying creditors. Not surprisingly, their debt grows thanks to late fees and higher interest rates. Their creditworthiness deteriorates as consumers follow the advice to ignore creditors in order to save funds to pay a debt settlement firms fees and accrue enough to possibly negotiate a "lump-sum" settlement of their debts.

The business model calls for consumers to pay 40 percent or more of the fees within the first 3-4 months and 65 percent within the first six months "without any results at that point."²³ The flat fee model works in the same way; about a quarter of the full fee is due up front as payment for setting up the account, and the balance of the fee is collected over the first half of the enrollment period.

It is important to note these high fees are being charged to financially distressed consumers. Many consumers pay debt settlement firms a substantial advance fee yet are unable to save enough to negotiate a settlement and eventually end up dropping out of the

program. Most debt settlement firms require that clients have a minimum amount of debt (often between \$5000-\$10,000) and owe multiple creditors. These consumers are financially strapped and often cannot afford to pay the high advance fees that debt settlement firms charge and also save enough money to negotiate a settlement of their debt. This is one reason that so many consumers drop out of debt settlement programs. Consequently, many low-and-moderate income consumers have paid debt settlement firms their fees, yet their debts have not been settled and they have lost a substantial amount of money that is difficult if not impossible to recoup.

Not surprisingly, if fees are collected before any services are delivered, many firms do not actually do any work. The Federal Trade Commission has noted that debt settlement companies frequently fail to provide any services once they have collected their fee²⁴. Creditors are not contacted, settlements are not negotiated, and the consumer has lost both money and time in the process. While some debt settlement companies assert that the service they provide is encouragement to save, consumers are signing up for debt settlement to get rid of their debts, and debt settlement does not eliminate all of the debt for the large majority of consumers who sign up for it.

2. Deceptive practices

Debt settlement companies claim that they can substantially reduce a consumer's debt and they tout high success rates. Unfortunately, many of these claims cannot be substantiated. To induce consumers to contract with their firms, many debt settlement companies misrepresent their success rate, the amount by which they can reduce a consumer's debt, and the amount of time it will take to complete the program. Other firms claim to have helped thousands of consumers settle debts but have not backed up those claims with meaningful documentation.

A. Misrepresentation of Potential Savings

In Maryland, the Law Offices of Richard Brennan could not verify its claim that it could reduce consumers' debts by as much as 70 percent²⁵. In New York, two debt settlement firms were sued for deceptive practices and false advertising. Credit Solutions of America (CSA), one of the firms being sued, promised a 60 percent reduction in consumers' debt but on average, only 1 percent of CSA clients realized any savings. CSA collected nearly \$17 million in fees from New Yorkers. Similarly, Nationwide Asset Services, Inc. (NAS) promised New Yorkers that the firm could reduce their outstanding debt by between 25-40 percent yet the New York Attorney General's office found that only one third of 1 percent of consumers reduced their debt by using NAS' services²⁶.

Debt settlement promises of “lower monthly payments” obscure the fact that there can be no fair comparison between a payment to a creditor and a payment to a debt settlement firm that goes toward fees and to savings for future debt payment.

B. Misrepresentation of Completion Rates

Although firms claim to have helped thousands of consumers attain debt relief, these statements are not borne out.

A January 2008 preliminary study from The Association of Settlement Companies (TASC), an industry trade group, claims completion rates ranging between 35-60 percent²⁷. However, many questions remain concerning the study’s methodology and reliability, apart from the self-interested sponsor of the report. Specifically, the study was a preliminary one, but no final study has been forthcoming as of December 2009. It remains unclear how the survey was conducted, how many members participated in the survey, and how the study measured and defined completion rates.

Although industry findings of 35-60 percent completion rates are unremarkable, findings from State Attorney Generals present much a much grimmer picture. In Florida, the Attorney General sued Nationwide Assets Services, Inc. and others alleging that 227 Floridians had enrolled over six years, but only 30 of those consumers completed the program, which is a completion rate of less than 13.5 percent²⁸. A complaint by the New York Attorney General alleged that of 1,981 consumers who signed up over three years, only 64 completed the program, at rate of just over 3 percent. In Colorado, the Attorney General analyzed information from annual reports by debt settlement companies in October 2009 and found that for Colorado consumers using debt settlement in 2008, less than 1 percent of consumers had all debt eliminated by debt settlement [0.84%]²⁹.

C. Failure to Communicate Consequences of Debt Settlement Process

Through advertising, web-based marketing, and telemarketing, debt settlement companies lead consumers to believe debt settlement is a relatively risk-free process with few negative consequences. Debt settlement employees rarely if ever effectively communicate to consumers that contracting with their firm will not prevent creditors from pursuing debt collection actions, that their credit score will worsen, that late fees and penalties will continue to be assessed, that any savings realized may be considered taxable income, and that their debt balance increases when payments are not being made. These mischaracterizations and omissions serve to make the process seem more appealing to financially stressed consumers.

D. Marketing and Market Segmentation Increase Consumer Confusion

Many debt settlement firms also choose names that closely resemble nonprofit credit counseling agencies. This serves only to create confusion among consumers who may be trying to contact a reputable nonprofit credit-counseling agency and fail to distinguish the subtle difference in the name of the organization. For example, a Maryland woman contacted Consumer Credit Counseling of America (CCCA) online but thought she was speaking with Consumer Credit Counseling Services (the nonprofit agency)³⁰. The CCA representative did not reveal that the firm was for-profit debt settlement company affiliated with attorney Richard Brennan until after the consumer had signed and faxed a contract back to them.

Another problem with debt settlement companies is that they often seem a many-headed Hydra—a parent company may divide each aspect of the debt settlement process—from marketing and solicitation, to contract origination and closing, payment collection and actual debt negotiation—among different companies. Other firms may reincorporate under different names, further confusing unwitting consumers and making their activities more difficult to monitor and regulate.³¹

For example, CareOne Services of Columbia, Maryland is linked with Persels and Associates as well as Amerix under the Ascend parent company. Richard A. Brennan operated under a variety of names including: the Law Office of Richard A. Brennan; the Frederick Law Group; and Consumer Credit Counseling of America. For consumers trying to track the progress of their debt settlement or an agency trying to enforce compliance, this segmentation or titular name change creates a morass of confusion. In addition to changing their names, firms have changed their office location, phone and fax numbers, which makes it difficult for consumers to lodge complaints, determine what is happening with their account, or cancel their contract.

As the industry adapts to market changes and undergoes increased scrutiny, some firms are developing new products to sell to desperate consumers seeking financial relief. Several firms have developed “debt-settlement kits” that a consumer can purchase with prices ranging from \$279 to \$2,000. Any regulation of debt settlement services should define the industry broadly to encompass the development of new products and services.

E. Confusing Contracts and Terms and Conditions of Service

The the process of contracting with a debt settlement company is problematic. Several companies no longer send consumers paper contracts to sign and fax back to the company. Instead, if a consumer is interested in finding out more about debt

settlement they will speak with a “financial advisor” at the firm. The “financial advisor” will ask the client to sign an online contract that the advisor will go through with them as they sit on the phone together. The consumer can then log into an intranet computer system, type in their credit card account numbers and debt amounts, and sign the e-contract after reading through the terms and conditions online with the debt settlement advisor. This process gives consumers no time to seek outside advice or to review the terms and conditions in a deliberate manner.

In Maryland, most consumer contracts available to MCRC stated the monthly payment and the number of months in the contract. The contracts, however, did not provide a description of what services the debt settlement firm would provide and the expected date by which a firm would contact a creditor. The contracts did not indicate how much money the consumer would have to save to pay the firm’s fees and accrue enough to negotiate a settlement.

Finally, consumers are asked to sign a limited power of attorney or a provision is included in contracts that allows debt settlement firms access to the consumer’s account so that the firm can automatically debit the monthly fee each month. This removes any choice from the consumer about paying that fee each month rather than making other spending choices.

3. Financial Hardship and Contractual Problems

Consumers who contract with debt settlement firms often find themselves increasingly frustrated with the company’s services. Because so many of the firms require fees in advance of starting negotiations, clients can often be paying for 4-6 months before any negotiations may begin with creditors. Not surprisingly, when a debt settlement firm receives all or a good chunk of their fee before providing any service, there is a disincentive to actually negotiate with creditors and fulfill its end of the bargain. Many consumers have complained that the debt settlement firm that they contracted with in fact did not contact creditors. Consequently, consumers paid a substantial amount to a debt settlement company without receiving any service from the firm.

Consumers who enter these programs are often those who are least likely to benefit from this type of service. They are already facing financial distress and they are unlikely to be able to save as much as the program requires in order to settle their debts (if in fact the firm does contact creditors). Many consumers drop out of these programs before any settlement is achieved. Yet, by the time they leave the program, many have had their

credit scores damaged, faced increased collection activity, and lost time and money contracting with the debt settlement company. For example, in a sample of 4,500 debt settlement customers of one company, 60 percent cancelled the debt settlement service, and the median time for cancellation was between five and six months after starting debt settlement³². In fact, the services these firms provide are often unnecessary. At a Federal Trade Commission forum in 2008, both the American Bankers Association and American Express noted that most consumers could settle their debts on their own by contacting their credit card companies directly³³.

When consumers try to extricate themselves from their contracts, they often discover cancellation fees, and have trouble recouping lost funds. For example, one South Dakota consumer contracted with a debt settlement company in Maryland to help settle debts. She paid the company \$3,490 in fees and received a refund of \$1,144 when she terminated the contract. In the end, the company gained \$2,346 and rendered no services at all. In order to receive the partial refund, the consumer had to sign a release that waived any rights to pursue legal action³⁴.

Complaints to the Maryland Attorney General's office exemplify the problems and costs consumers face when ending their contracts with debt settlement services.

One Maryland consumer explained that the debt settlement firm she contracted with has offered a 30 percent refund, saying they have performed work on the account. Regardless of whether the settlement firm worked on her account, their efforts did not lead to any settlements with her creditors, which is the service she paid them for. Consumers do not pay a home contractor for *starting* to fix a leak in their roof; they pay a contractor for *fixing* it. Yet, debt settlement companies demand payment for their activities regardless of whether they complete the job they were hired to do³⁵. Another Maryland consumer noted that when she cancelled her contract, the firm would not refund money because they charged \$2,300 per contract regardless of whether or not the contract was cancelled, which was not what the consumer had understood when signing up for the debt settlement services³⁶. Other Maryland consumers have stated that companies simply ignore their email and phone inquiries when they attempt to obtain a refund³⁷.

Richard Brennan & Brennan Law Firm

Richard Brennan & the Brennan Law Firm may be the most infamous example of the problems with the debt settlement industry. Brennan is the only debt settlement firm to be prosecuted in Maryland to date. Brennan was found in violation of the Maryland Debt Management Services Act (MDMSA), which at the time restricted for-profit companies from providing debt management services. Brennan was providing services he was not legally able to provide. The Consumer Protection Division of the Attorney General's office also charged that the firm misrepresented the experience of its staff and the amount consumers would save through debt settlement³⁸. Finally, Brennan was found to have promised services that he did not render.

In October 2007, Maryland Attorney General Doug Gansler announced that his office's Consumer Protection Division had reached a settlement with Richard Brennan, the Law Offices of Richard Brennan, LLC, and a related company called American Telecommunications Solutions LLC (collectively referred to as the Brennan Law Firm) in connection with their debt management and debt settlement services.

The suit charged that the Brennan Law Group failed to send consumers' payments to their creditors. Approximately \$240,000 from consumers was used to pay the firm's own debts. The firm promised to return all payments to consumers that were not forwarded to creditors as well as pay costs and a civil penalty. Brennan also promised to stop selling debt settlement services unless he posted a \$50,000 performance bond with the Consumer Protection Division of the Attorney General's office.

In January 2009, Brennan was disbarred from practicing law in the State of Maryland by the Court of Appeals. Despite agreeing to the settlement, Brennan never paid the penalties, costs and restitution, and continued to illegally sell debt settlement services to consumers. As a result, the Attorney General sued Brennan in the Circuit Court and in January 2009, the Court entered a judgment against him and his law firm and ordered him to cease selling debt settlement services to consumers and to pay restitution to the Division. After Brennan ignored that Order and continued to sell debt settlement services, the Division commenced its contempt action³⁹ and Brennan was jailed for contempt of court on July 31, 2009.

The basic facts of Brennan's case fail to convey the experiences of Maryland consumers who entrusted his firm, and others like it, to settle their debts and provide them with financial relief.

V. MARYLANDERS AFFECTED BY DEBT SETTLEMENT

Gloria Snowden of Baltimore is a claims specialist for the Department of Labor, Licensing and Regulation. Some bad spending decisions, coupled with not understanding that making the minimum payments on credit cards will do next to nothing to reduce the balance, caused her to build up a debt in excess of \$30,000 that she was having trouble repaying. She turned to the Consumer Credit Counseling of America and was thrilled to immediately feel a weight lifted from her shoulders.

“They told me I didn’t have to worry about anything anymore and that I should send them my money and then they would send it the creditors,” she said. “I felt as though the place was a legitimate business.”

Ms. Snowden, 65, was under the impression that the firm would work with her creditors to lower her interest rates and begin paying her debts immediately – the debt management model. What she did not realize was that the nearly \$400 per month that she was paying to the firm, which transferred her account to Richard Brennan’s Frederick Law Group, was actually going toward the firm’s fees and, once they were paid off, into an account to build up a lump sum to pay her creditors.

When Ms. Snowden’s creditors continued to call her at work and at home, she started trying to get answers from the Frederick Law Group about why they had not contacted the creditors or started paying off her debt. After getting the run-around on numerous occasions, she finally called the Office of the Attorney General of Maryland and discovered that the office was all too familiar with the Frederick Law Group.

“Because of this situation I ended up filing for bankruptcy. Because of Richard Brennan I got into even more debt. These people, because they are greedy, prey on innocent people,” she said. “I almost had a nervous breakdown – I couldn’t eat, I couldn’t sleep. There should be a law passed to stop predators.”

-- Interview with MCRC, Dec. 2, 2009

Lee Tarver, a 74-year-old retired steelworker in Baltimore, had built up about \$40,000 in credit card debt. He'd seen many commercials on television touting debt-reduction plans. Then one day he got a phone call from someone at a company called H.H. Unlimited Inc. of Florida who said he could lower Mr. Tarver's interest rates. The man asked, "Would you rather pay a 13 percent interest rate or 6 percent?"

"Of course you want to pay the lower rate," Mr. Tarver said. "So I gave them my credit card number."

Mr. Tarver began to contact H.H. frequently asking for status updates. When answers weren't forthcoming, he called the Maryland Attorney General's Office of Consumer Protection.

"They said they would write a letter, and that was the end of that," he said.

He's out the \$1,200 he paid H.H. Unlimited and now he's further in debt.

"I wasn't really being harassed by creditors before [dealing with H.H], but I am now," he said. "It seems like they're a bunch of crooks and they just keep changing their names. I think there should be more regulation. It seems like they can just pack up and go, or sell to someone else."

-- Interview with MCRC, Dec. 3, 2009

VI. FEDERAL LAW ON DEBT SETTLEMENT

To date, there is no single state or federal law designed to protect consumers against the deceptive practices, predatory fees, and failure to provide services that characterize so many debt settlement firms. While some provisions in federal and state statutes can be applied to the debt settlement industry, the result is a patchwork approach to protecting consumers. To protect Marylanders, legislation tailored to the challenges presented by the debt settlement industry is needed.

The Credit Repair Organization Act (CROA)

The federal Credit Repair Organization Act (CROA) applies to agencies that offer credit repair services. CROA may be applied to debt settlement companies if the company states that the payment of a debt will improve a consumer's credit rating or if the firm performs any work related to credit repair.

CROA requires organizations to make certain disclosures to consumers and includes a number of consumer protections such as a three-day right to cancel. Violations of CROA can entitle consumers to actual damages, punitive damages, and attorneys fees. Moreover, any contract that violates CROA is nullified. Debt settlement companies may fit within the CROA definition and can be found to be violating CROA through misrepresenting their services, success rate, or impact on a consumer's credit scores. However, many debt settlement companies operating in Maryland are keenly aware of CROA provisions and carefully avoid regulation by that statute. Thus, CROA does not adequately protect Marylanders.

Federal Trade Commission Act (15 U.S.C. 41 et seq)

The Federal Trade Commission has actively brought administrative action against debt settlement companies based on misrepresentations and deceptive practices. The FTC Act sets out the administrative processes to investigate, enforce the law, or sue those that violate consumers' rights, including persons that mislead consumers by misrepresenting facts or engaging in other deceptive practices. The Act states that the FTC can launch a civil action against any person or corporation that engages in unfair and deceptive practices. To provide redress to consumers affected, the court may decide to rescind a contract, award damages, restore lost funds, or return lost property.

The FTC Act was amended to include the Telemarketing Sales Rule (16, CFR, Part 310), which was designed to protect consumers from telemarketing fraud by restricting when telemarketers could call consumers as well as proscribing that the sales person must

disclose the purpose of the call as well as the nature and price of the goods and services offered. Any violation of these terms would be treated as a violation of the FTC Act regarding unfair or deceptive acts or practices. States Attorneys General are able to pursue civil action on behalf of their states' residents to enforce compliance with the Act, obtain damages, restitution, or other compensation. The Act also allows for a private right of action if the suit is filed within three years of the violation.

However, the framework of the Telemarketing Sales Rule does not apply to contracts signed in a face-to-face sales presentation, creating a large potential loophole. Strong state law protections that regulate debt settlement companies, who prey on the most vulnerable, are essential.

Update on Telemarketing Rule

On August 19, 2009, the FTC issued a notice in the Federal Register calling for comments on revising the Telemarketing Sales Rule to apply to the debt settlement industry. Under the proposed revisions, the Telemarketing Rule would be extended to include debt relief services (including debt settlement) in its definition. As revised, *section 310.3 Deceptive telemarketing acts or practices*, would require debt settlement firms to disclose the amount of time necessary to achieve results; the specific time by which a debt settlement firm would make an offer with each creditor; as well as the percentage of each debt (or amount of money) that a consumer would have to accumulate before an offer would be made. The rule would also require debt settlement firms to disclose that this process may harm a consumer's creditworthiness, may not stop collection activities, and that any savings may be considered taxable income.

The FTC has collected comments from hundreds of consumer groups, debt settlement firms, debt settlement associations, and individuals. The comments are currently under review and the FTC is preparing a recommendation.

VII. STATE REGULATION OF DEBT SETTLEMENT

States have deployed a variety of approaches to regulate the debt settlement industry. Some states have used CROA and state “Unfair and Deceptive Practices” laws to prosecute debt settlement firms. Although many states have passed debt management laws, the majority of these do not apply to debt settlement companies. States that are in the process of developing debt management laws are often including debt settlement agencies within these new laws. If the definitions in the state debt management law are sufficiently broad, many debt settlement firms would be found in violation of the law in a number of ways including charging fees in excess to the limits set in debt management law.

Unfair and Deceptive Acts and Practices (UDAP)

Most states have at least one law protecting consumers from deceptive practices. These statutes are often referred to as “Consumer Protection Acts” or “Unfair and Deceptive Acts and Practices” laws. They typically prohibit unfair or deceptive practices by debt collectors. These statutes often cover both creditors as well as collectors and often include remedies such as tripling the amount the damages, statutory damages and attorneys’ fees.

States’ Debt Settlement Laws

As complaints against the debt settlement industry have mounted, states have passed a variety of laws to regulate the industry and protect consumers—from outright bans on the industry to restrictions on fees to requiring certain disclosures. Some states have written their debt management laws broadly enough that the debt settlement industry is also covered under the legislation.

States are becoming increasingly proactive in regulating the debt settlement industry since many of the remedies available to consumers arise only *after* consumers have been harmed. It is far more efficient and effective to address the problem at the front end, through sensible regulation that prohibits the worst abuses and helps consumers evaluate whether debt settlement is something from which can actually benefit.

Ban on Debt Settlement Firms

Several states including Arkansas (Ark. Code Ann. 5-63-301 et seq), Hawaii (Haw.Rev. Stat. 446-1 et seq), Kentucky (KY Rev.Stat. 380.010), New Mexico (N.M. Stat. Ann. 56-2-1), and Wyoming (Wyo Stat. Ann. 33-14-101) have banned debt settlement companies entirely.

Restrictions on Debt Settlement Firms

Other States are choosing to allow debt settlement companies to operate but are restricting the fees they can charge or requiring other restrictions and disclosures.

⁴⁰*Florida*-sets fee limits (e.g. \$50 for initial fee).

Idaho-establishes a licensing requirement for debt settlement firms (exempts attorneys but not nonprofits) and sets fee limits of no more than 15 percent of the amount received by the agency at any one time from or on behalf of the debtor.

Kansas- establishes a licensing requirement but exempts attorneys. Provisions include mandatory education, an initial fee of no more than \$50, monthly fee limits of the lesser of \$20 per month or \$5 per creditor.

Virginia—establishes a licensing provision and fee limits of \$75 set up, monthly fee of no more than 15 percent of total amount discussed but no more than \$60 per month.

State Litigation

On May 19, 2009, New York Attorney General Andrew Cuomo filed suit against two debt settlement companies under the state's UDAP statute for fraudulent business practices and false advertising.

On October 15, Attorney General Cuomo won the lawsuit against one of the firms, Nationwide Asset Services (NAS). The New York Supreme Court issued a decision barring NAS from operating in New York State unless it filed a \$500,000 performance bond to protect consumers. Cuomo's office also obtained a civil penalty of \$198,100 after the court determined that 1,981 consumers were defrauded by NAS.

The court also ordered NAS to compute restitution for 180 consumers who completed the program but paid more in fees and settlements than the amount due on their debts. NAS has been ordered to compute the amount owed to each consumer and the amount will be verified by the Attorney General's office.

As part of his broad investigation into the debt settlement industry, Cuomo has subpoenaed multiple debt settlement companies and affiliated businesses to uncover how the companies structure their fees, how many people benefit from their services, and what kinds of relief companies are actually providing.

Since Cuomo announced his suits last May, other Attorneys General have initiated similar litigation. On October 1, 2009, Illinois Attorney General Lisa Madigan filed suit against Credit Solutions of America for deceptive practices and failure to provide services⁴¹. Madigan is seeking to bar Credit Solutions from operating in Illinois. Madigan is also asking that Credit Solutions pay restitution to its clients, pay a \$50,000 fine for violating the State's Consumer Fraud Act and pay additional fines of \$50,000 for each instance of fraud. This is the third suit Madigan has filed against debt settlement companies this year. Her office has seen an increase in the number of complaints against debt settlement companies during the recession.

Maryland Law Regulating Debt Settlement

The debt settlement industry is unregulated in Maryland. Maryland consumers can seek restitution under existing laws but there are no laws to codify the terms and conditions under which the debt settlement industry can operate within the state. Today, laws can only help consumers after they have been harmed by the debt settlement industry rather than protecting consumers from harm at the outset.

Maryland Consumer Protection Act (CPA)

Maryland's CPA has strong provisions against unfair and deceptive practices. The Attorney General's office has been able to prosecute some debt settlement firms under this law. However, CPA is a remedial statute—it can be used to redress problems after they occur. It cannot be used to license, regulate, or promote disclosures within an industry—only to address consumers' concerns after a firm has engaged in unfair and deceptive practices.

Maryland Code Comm. Law 13-301 (14)(iii) makes the violation of the state debt collection law a CPA violation. Another part of the statute, Maryland Code Com. Law 13-303(4) provides that a person may not engage in any unfair or deceptive trade practice in the collection of consumer debts. However, debt settlement firms are not covered under the definition of debt collectors.

Maryland Debt Management Services Act

This law sets out licensing requirements and fees for debt management services, requires a surety bond to operate, and proscribes a series of consumer disclosures and protections necessary to operate in the state.

Although some debt settlement companies also providing debt management services might be covered under this law, the majority of debt settlement firms would not be covered because they do not provide debt management plans and services, which is what

the law regulates. The majority of debt settlement firms would remain unregulated in Maryland if policymakers relied on this law to regulate firms at the outset.

Gaps in Maryland Law

Although a few debt settlement firms may be regulated under current Maryland law and others might be prosecuted after consumers have lost money to predatory firms, a more targeted policy is needed to regulate the industry from the outset. Legislation is needed to set the terms and conditions under which debt settlement firms may operate within the state. If such a statute were passed, in combination with Maryland's CPA and FTC regulations, legitimate debt settlement firms would be able to operate in Maryland to serve those consumers who could genuinely benefit from their services. More importantly, disreputable firms would no longer prey upon Marylanders who are trying to reduce their debts and regain financial stability.

VIII. CONCLUSION

Consumers used credit cards with their easy introductory terms to both purchase unnecessary items as well as to meet their basic needs when their wages couldn't keep up with rising costs of living. As consumers tried to dig out of the debt that they had accrued, some turned to debt settlement companies that promised to reduce their debts and help them regain financial stability. Instead, most found themselves in a deeper hole, with mounting debts, reduced credit scores, and pursued by collection agents. Just as Maryland regulates drivers to protect the physical safety of our citizens by requiring that certain standards be met, so too should Maryland protect the financial interests of its citizens by ensuring that debt settlement firms meet certain standards to operate within the state.

IX. POLICY RECOMMENDATIONS

The State of Maryland should pass legislation to regulate the debt settlement industry in the state. Key provisions within the legislations should include:

Reasonable Fees for Service, due only upon results

- ◆ Debt settlement firms' consultation or set up fees should not exceed \$50.
- ◆ A debt settlement firm should be paid *after* results are achieved. The fee should not exceed 15 percent of the total amount of the savings from the consumer's original debt.
- ◆ Before contracting with a consumer, debt settlement companies should be required to present consumers, at no charge, with a realistic projection of fees, costs and benefits.
- ◆ Firms should not be allowed to charge fees for rescinding a debt settlement agreement.

Full Disclosure of Terms and Conditions of Services

- ◆ A debt settlement company shall provide a signed and dated agreement between the provider and the consumer that states the following:
- ◆ The name, address, and phone number of the consumer and debt settlement provider;
- ◆ A description of the debt settlement services to be provided;
- ◆ The name of the financial institution in which the consumer's funds will be held;
- ◆ A disclosure that debt settlement may not stop collection efforts by the consumer's creditors and may impact the consumer's credit rating and credit scores;
- ◆ A disclosure that any savings from debt reduction may be considered taxable income;
- ◆ A schedule of expected payments and fees;
- ◆ A description of how much the consumer will have to save to settle debts.

Prohibitions on Certain Practices

A debt settlement company should be prohibited from the following;

- ◆ Taking any control over, direct debit from, or right to information about the consumer's bank account;
- ◆ Representing success rates, track records, or any other figure that suggests that a consumer's debt could be settled for a specific amount or reduced by a specific percentage or range of percentages;
- ◆ Encouraging or advising a consumer to stop paying his/her creditors.

Include “Product” in scope of definition

- ◆ Any new policy aimed at regulating the debt settlement industry should define debt settlement as both a “service” and a “product.” As debt settlement servicers adapt to the changing regulatory environment, several have begun offering “debt settlement kits” for low-income consumers. To ensure that the policy applies broadly to those companies engaged in debt settlement, the definition should be as encompassing as possible.

Suitability Analysis

- ◆ Debt settlement firms should have to conduct a “suitability” analysis to determine whether debt settlement is appropriate for a consumer given his or her income, expenses, and debts, which is shared with the prospective consumer prior to signing the contract.
- ◆ Debt settlement firms must also make a determination as a result of the “suitability” analysis that the consumer is reasonably likely to be able to make the savings payments.

X. CONSUMER ADVICE

If You Are in Debt

If you are in debt and cannot meet your current financial obligations, consider the following:

- 1) Try to negotiate with creditors on your own behalf before working with a firm.
- 2) A wise first step to help resolve an outstanding account is to speak directly to the credit card issuer or other creditor.
- 3) Choose which debts to pay first; pay high-priority bills first
 - Pay for family necessities first—food, utilities, any medical bills that require pre-payment
 - Pay for household bills—pay your mortgage or rent. Pay your real estate taxes and insurance (unless included in your monthly payment)
 - Pay the minimum required to keep utilities on
 - Pay car loans and car insurance if you need an automobile
 - Pay any child support debt you may owe
 - Pay your income taxes and file your state and federal income tax returns.
- 4) After paying off high priority items, pay off lower-priority loans when possible. These include credit cards and loans for household goods.
- 5) Government student loans are a medium priority.

Tips on Dealing with Debt Settlement Companies

As noted in this report, most consumers are able to negotiate with creditors without relying on a debt settlement agency. Many consumers who contract with debt settlement firms do not reduce their debts and have increased debt due to penalties, interest rate charges, and late fees. Debt settlement does not stop collection activities.

If you do choose to work with a firm:

First consult a nonprofit credit counseling agency to see if you would qualify for debt management services. These services are typically provided at lower fees, do not harm your credit, and are often coupled with financial and consumer education. To find a nonprofit credit counseling agency, visit the Maryland Attorney General's website <http://www.oag.state.md.us/consumer/tip4.htm>.

If you do not qualify for a debt management plan, keep the following in mind if you are considering signing on with a debt settlement plan:

- Be wary of debt settlement companies that promise to obtain settlements for much less money than consumers owe. Many debt settlement companies misrepresent their typical results and their success rates.
- Avoid debt settlement companies that require payment in advance of obtaining the promised settlement.
- Avoid companies that do not send you a paper contract that is signed by both parties with clear contact information in the contract. The contract should lay out the fees, time expected to pay off the debts, the date when the first creditor will be contacted, and more.
- Keep in mind that debt settlement plans may not stop creditors from charging interest, late fees, or other penalties on outstanding debts, and do not prevent creditors from bringing collection lawsuits. In addition, failure to make required payments on your debts will negatively affect your credit score.
- Creditors are under no legal obligation to accept a settlement offer for less than the outstanding balance owed.
- Only a small number of consumers who enroll in debt settlement plans are able to complete them. Usually, consumers drop out after having paid service fees to the companies without receiving any benefit from their enrollment. If you sign up with a company who takes fees out of your savings before it gets you any settlements, you could end up deeper in debt.
- Enrollment in a debt settlement plan premised on stopping payments to creditors will likely lead to more frequent and aggressive creditor collection efforts and may result in judgments, wage garnishments, and freezing of bank accounts.
- Check with the Better Business Bureau to obtain a Reliability Report on a particular debt settlement company and its rating.

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