

**16 C.F.R. Part 310: Telemarketing Sales Rule  
Notice of Proposed Rulemaking To Amend the Rule  
To Address the Sale of Debt Relief Services,  
and Announcement of Public Forum  
Summary of Communications Pursuant to Commission Rule 1.26(b)(5)**

Donald S. Clark  
Secretary  
January 13, 2010

## MEMORANDUM

To: Don Clark  
From: Stephanie Rosenthal, Attorney, Division of Financial Practices  
Re: Telemarketing Sales Rule – Debt Relief Amendments, Comments to Be Placed on the Public Record  
Date: December 18, 2009

On Thursday November 5, 2009, representatives of debt settlement company Credit Solutions of America met with FTC Chairman Leibowitz, his attorney advisors, and FTC staff members to discuss the proposed debt relief amendments to the Telemarketing Sales Rule.<sup>1</sup>

The representatives stated that debt settlement is a legitimate industry and raised several concerns they had with the proposed rule. The representatives also said that an article from the November 2, 2009 Washington Independent suggested that debt settlement was more trustworthy than credit counseling because credit counseling organizations receive funds from creditors. The article is attached to this memorandum.

The representatives asserted that debt settlement companies need to be able to recover costs as they provide services, as other legitimate companies do. They stated that if the FTC bans advance fees in the debt settlement industry, it would be saying that the debt settlement industry is fundamentally fraudulent and the equivalent of recovery room scams, advance fee loans, and credit repair. The representatives argued that the FTC could use existing tools to challenge fraud, and it does not need an advance fee ban.

The representatives stated that debt settlement companies employ different fee models, and they acknowledged that charging all fees up-front would be problematic. Specifically, Credit Solutions charges a fee of 15% of the consumer's debt, collected over the first half of the debt settlement program. The representatives stated that in a debt settlement program, a first settlement can happen at any point from 3 months to 18 months after the consumer begins the program, and throughout that time the debt settlement company is providing services to help consumers save and prevent them from using additional credit. Credit Solutions has one employee for every two active customers and has two employees working on settlements for every one employee in the sales department. The representatives were unable to provide information about how often the company collects the full fee before any of the consumer's debts are settled. The representatives explained that although the company has a written refund policy, it determines refunds on an individual basis, in proportion to how much work had been done on the consumer's account. Credit Solutions asserted that it also has a video disclosure that explains its refund policy in detail. By prohibiting the collection of advance fees, according to the representatives, the consumers who cancel before settlement but get something of value would be subsidized by those consumers who complete the program.

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<sup>1</sup>In attendance from Credit Solutions were: Michael Frazier, Pendulum Strategies, LLC; Andrew Smith, Morrison & Foerster; Heather Carmichael, Vice President of Legislative Affairs for Credit Solutions; and Nicholas Cowling, Director of Operations for Credit Solutions.

The representatives stated that the Uniform Debt Management Services Act, adopted in various forms in several states, allows a 4% enrollment fee (up to \$400) and caps fees at 17% of the consumer's total debt. The representatives stated that the uniform act is a better model for fee limitations than the FTC's proposed advance fee ban. They stated that the FTC needs to permit debt relief companies to charge fees as they provide services because otherwise those consumers who complete a program will end up subsidizing those consumers who terminate before payment is due.

In addition, the representatives stated that the FTC needs to take more time to understand the debt settlement industry and give the industry more time to provide the requested data. They understand that it might be months or years before it could provide the FTC with complete data. They stated, however, that the FTC should wait until all the data is available to proceed with the rulemaking. The representatives also indicated that some of the data they collect would have to be submitted confidentially because it would reveal information about their business model, which they consider a trade secret.

The representatives explained that there is a long-standing commercial rivalry between the nonprofit credit counseling industry and the debt settlement industry. If the FTC enacts the proposed amendments, which do not regulate nonprofit entities, they claimed that it would appear that the FTC was choosing sides in the rivalry in favor of the nonprofit credit counseling industry. The representatives stated that although the IRS is doing a better job policing tax-exempt entities, not all tax-exempt entities are truly nonprofit.

Finally, the representatives argued that the remedy the FTC is proposing is drastic and could put a lot of debt settlement companies out of business, and the proposed rule sets up an uneven playing field between those companies who will try to follow the rule and the bad actors who will disregard it. They asserted that the advance fee ban would not be effective in stopping the fraudulent companies, while at the same time driving the legitimate companies out of business.

The Washington Independent, Nov. 2, 2009

<http://washingtonindependent.com/66103/ties-run-deep-between-subprime-lenders-financial-literacy-groups>

## **Ties Run Deep Between Subprime Lenders, Financial Literacy Groups**

### **Credit Crunch Increases Need for Education**

By Mary Kane 11/2/09 2:00 PM



Flickr: Stallio

As a credit squeeze continues, calls to beef up financial literacy among America's consumers are taking on a new urgency.

In Massachusetts, Democratic Senate candidate Stephen Pagliuca is pushing for a national financial literacy campaign, saying it would help avoid a repeat of the financial system collapse last fall. In Miami, which recently introduced citywide financial literacy programs, a top official called financial literacy “the new civil-rights problem of our century.” In the blogosphere, basketball superstar Magic Johnson is under fire for doing national commercials for Rent-A-Center, a leading firm in the costly rent to own business, and Jackson Hewitt, which offers high-rate tax refund anticipation loans. Critics contend Johnson is endorsing products that exploit a lack of financial sophistication among some low-income consumers.



Those consumers have much greater need these days for financial literacy, given that credit is becoming harder and more expensive to get. The Wall Street Journal last month declared the end of the “democratization of credit” that occurred over the last decade, detailing the woes of a low-income 28-year-old woman drowning in \$36,000 worth of credit card and student loan debt, with little access to the easy credit she once tapped in recent years.

But despite that obvious need, most of the nation’s financial literacy efforts aren’t exactly up to the job. As credit expanded in past years, corporations threw money at financial literacy programs even as they continued marketing higher-rate credit cards and loans. Consumer credit and debt counseling agencies expanded into a \$7 billion industry that now includes everything from legitimate organizations that help a consumer fix his finances to flim-flam outfits that charge high fees and leave a borrower in worse shape than before. Subprime lenders created “consumer advocacy” organizations and offered financial literacy advice.

The situation has become so troubled that some credit experts no longer believe many financial literacy efforts are even effective. Between complicated credit card agreements that trip up even law students to payday lenders providing financial education, they say, most of the attempts to educate consumers on their finances are either hopelessly tainted or simply don’t make a difference.

“If you’re a consumer in financial distress, there’s really no trustworthy guide for pointing you to the right solution – almost everyone has a stake in the game,” said Adam Levitin, a Georgetown University law school professor who specializes in bankruptcy and credit. “The problem goes deeper, though, as all sorts of consumer credit counseling organizations are funded indirectly by various credit industry players. I’m frankly more comfortable with openly for-profit debt settlement agencies (they negotiate debt reductions in exchange for taking a percentage for themselves) than with the faux not-for-profit players.”

Irene Leech, former president of the Consumer Federation of America and a Virginia Tech University professor who focuses on consumer issues, agreed. “All education offered by the businesses that sell the product they’re educating on is subject to bias,” she said. “These companies don’t dare hit the points that need to be hit hard enough – or they’d lose business – so their efforts are at best disingenuous and at worst, fraud.”

As TWI has reported, the nation’s leading financial literacy effort, the JumpStart Coalition for Personal Financial Literacy, includes as one of its corporate partners CompuCredit, a subprime lender that offers high-rate credit cards and payday loans. Last year, CompuCredit reached a \$114 million settlement with the Federal Deposit Insurance Corporation and the Federal Trade

Commission, which had [charged](#) CompuCredit and two partner banks with deceiving hundreds of thousands of customers by failing to properly disclose upfront fees and credit limits on their cards.

In addition, JumpStart's Southeast Regional Director, William Cheeks, a paid consultant, also does consulting work for CompuCredit. JumpStart Executive Director Laura Levine told TWI that no one had previously brought these issues to JumpStart's attention, and that the organization's staff would investigate them. Last week, Levine said the organization plans to introduce a conflict of interest policy for staff and for consultants, in the wake of the story. The coalition's governance committee also "is going to look further into CompuCredit in particular," she said, and "we're going to continue to deal with issues regarding the suitability of partners on a case by case basis."

Like CompuCredit, other subprime lenders also aligned themselves in recent years with financial literacy efforts, or moved to portray themselves as good corporate citizens, by [donating](#) to local minority groups or [sponsoring](#) events in minority communities. In a campaign that particularly irked Leech, payday lenders ran an advertising campaign on Washington metro system, touting payday loans as a sound financial alternative.

Other high-rate lenders also are using similar tactics.

[Ray Forgue](#), a retired University of Kentucky professor who taught personal finance, and who has [written](#) personal finance books and a textbook, now lives in South Carolina. Car title lenders "are everywhere," he said, featuring advertisements that show consumers being allegedly financially savvy by taking out car title loans to pay for dental care. Car title lenders make loans using a borrower's car as collateral, with interest rates that can approach 400 percent. Borrowers who can't keep up with the high payments lose their cars, and then, in many cases, their jobs as well.

These kinds of tactics present a huge challenge for financial literacy efforts, Forgue said. Any financial literacy program has to both battle the saturation of subprime products that have made their way into the mainstream, and help consumers understand newer and more complex financial issues, from insurance to retirement planning.

"The products are far more complicated, both on the consumer credit and the investment side," Forgue said. "Financial literacy definitely is much more important than it ever has been before." Leech, for her part, said the problem with financial literacy in recent years has been that funding for unbiased, professional counselors has been replaced by corporate dollars. One fix might be for the government to reinvest in the nation's [Cooperative Extension System](#), a national educational network supported by the U.S. Department of Agriculture that [provides](#) consumers with experts and research on many topics, including financial literacy. The cooperative system was [created](#) by Congress in 1914, and uses the resources of land grant colleges and universities to offer its non-formal, non-credit programs to the public. The system has offices in every state and a [website](#) with financial research and information, from budgeting during lean times to an "ask an expert" feature, with questions like how much allowance a child should get at a certain age.

Leech also supports the [America Saves](#) campaign, a nationwide effort run by the Consumer Federation of America to encourage low and moderate income households to change their financial behaviors, build up savings, and pay down debt. The campaign, the nation's largest savings initiative, also sponsors an annual ["America Saves Week"](#) that encourages people to review their finances and improve their savings habits.

And the human resources departments of corporations and businesses are increasingly getting involved in financial literacy efforts, Leech added, since employees with financial troubles can be distracted or forced to miss work due to legal battles over debts.

But any financial literacy attempt faces an uphill fight. The attorneys general of 40 states recently [asked](#) the Federal Trade Commission to tighten regulation of companies offering debt relief services to consumers, saying the firms require customers to pay thousands of dollars in upfront fees, and then fail to renegotiate payments with creditors. The FTC will hear testimony this week on proposals for reform, as the battle over consumers and their money decisions continues, and the credit squeeze tightens further.