

**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  
April 8, 2010

**DRAFT**

**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: March 31, 2010

On Wednesday, February 24, 2010, representatives of four consumer advocacy groups – Consumer Federation of America, Consumers Union, Consumer Action, and the National Consumer Law Center (collectively, “the advocates”) – met with FTC Chairman Leibowitz, his attorney advisors, and FTC staff members to discuss the proposed debt relief amendments to the Telemarketing Sales Rule (“TSR”).<sup>1</sup>

The advocates stated that the proposed debt relief amendments to the TSR are important, especially with so many consumers facing increasing amounts of debt. Of particular importance, the advocates stated, is the proposed prohibition against advance fees, without which none of the other proposed rule provisions will effectively stop debt settlement companies from harming consumers. They also said that, in implementing the advance fee ban, the FTC should require debt relief companies to provide consumers with a written contract from the creditor. The contract should state that the creditor will eliminate the consumer’s entire debt upon the consumer’s acceptance of the agreement and the creditor’s receipt of the settlement payment. Such a requirement would prevent debt relief companies from collecting a fee for a settlement offer that the consumer is unable to fund, the advocates asserted.

The advocates responded to the debt settlement industry’s claim that because debt settlement companies provide consumers with valuable services other than settlement before settlement occurs, advance fees should be permitted. The advocates asserted that there is minimal evidence to support this claim and thus, the FTC should include an advance fee ban in the Final Rule. The advocates analyzed data that industry members submitted to the rulemaking public comment record and argued that the industry’s own data makes a strong case that debt settlement companies are not providing services to consumers. For example, they noted that one industry study found that 60% of a sample of consumers who enrolled in one company’s debt settlement program cancelled the program before completion. They cited another industry survey, which found that 65.6% of consumers who enrolled in a debt settlement program still owed 25% or more of their original debt after three years in the settlement program. The advocates also summarized allegations by the Florida Attorney General in one case that a debt settlement company had a completion rate of less than 13.5%. They then reviewed results of a survey submitted by the Colorado Attorney General finding that fewer than 1% of consumers who enrolled in a debt settlement program in 2008 eliminated all of their debt that year. The

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<sup>1</sup> In attendance were: Susan Grant from Consumer Federation of America; Gail Hillebrand and Pamela Banks from Consumers Union; Andrew Pizor from National Consumer Law Center; and Ruth Susswein from Consumer Action.

advocates' analysis of the industry data and data from several states is attached to this memorandum as Attachment 1. The advocates also contested the accuracy of industry success claims, arguing that some industry success claims are based upon offers of settlement that consumers cannot afford to fund.

The advocates addressed the concern raised that the proposed rule covers only for-profit debt relief companies by asserting that the stringent requirements of Section 501(q) of the Internal Revenue Code adequately regulate nonprofit debt relief entities.<sup>2</sup> The advocates were confident that the amended TSR would cover any for-profit debt relief company, regardless of whether it claimed to be a nonprofit because the FTC Act and the TSR exempt only *bona fide* nonprofits.

The advocates expressed support for a performance-based fee model, arguing that this fee model is the only way to ensure that the industry has a real incentive to achieve settlements for consumers. They noted that some states, including Florida and Maine, have mandated success-based fees and urged the FTC to follow this approach.<sup>3</sup> They argued that the FTC should prescribe the circumstances and timing of when a debt relief company can charge a fee, and states should continue to limit the amount of fees a debt relief company can charge.

The advocates do not believe there are any alternatives to an advance fee ban that would curb abuses in the debt relief industry. They said that a very small enrollment fee, to cover costs such as consumer intake and initial creditor contacts, probably would not be problematic. However, they would be concerned by a monthly maintenance fee because it would drain the funds consumers need to accumulate for settlement, which would prevent consumers from successfully settling their debts.

In addition, the advocates expressed concern regarding the specific success claims used in advertising because not all companies calculate success rates in the same way and, thus, it is very difficult for consumers to compare these success claims. The advocates argued that, at the very least, debt relief companies should be required to deduct fees paid to the company from any savings claims. Finally, the advocates argued that the debt relief amendments to the TSR should prohibit debt settlement companies from encouraging consumers to cease communication with their creditors.

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<sup>2</sup> 26 USC 501(q).

<sup>3</sup> The advocates' calculation of the total fees that debt settlement providers could charge consumers under various fee models is attached to this memorandum as Attachment 2.

# ATTACHMENT 1

## RECENT DATA ON DEBT SETTLEMENT

### Most consumers drop out of debt settlement

- In a sample of 4,500 debt settlement customers of one company, **60% cancelled the debt settlement service, and the median time for cancellation was between five and six months after starting debt settlement.** R. Briesch, *Economic Factors and the Debt Management Industry*, August 6, 2009, posted at: <http://www.consumercreditchoice.org/files/ACCC-Dr.%20Briesch%20Study%20Report%20on%20Debt%20Management%20Industry.pdf>. This study was issued by a pro-industry group called Americans for Consumer Credit Choice.

### Even the industry's own statistics show that debt settlement does not regularly eliminate all of the debt for most consumers

- An industry trade association survey shows **most consumers do not eliminate all of their debt** in debt settlement.
- Only 34.4% of consumers who started debt settlement three years earlier had either "substantially completed" their debt settlement plans or were still actively saving for settlements. Only 24.6% had eliminated at least 75% of their debt; while 9.8% were still trying to get rid of their debts through settlement three years after starting debt settlement.
- The industry's own statistics showed that 65.6% of consumers still owed 25% or more of their original debts three years after starting debt settlement. Some of those consumers must have owed much more, because the industry survey also showed that for those consumers whose debt settlement plans were terminated without being completed, only 34.8% of the terminating consumers had even one debt settled before termination.

Source: The Association of Settlement Companies (TASC), October 26, 2009, comments to the FTC on the proposed amendments to the Telemarketing Sales Rule on the marketing of debt relief services, p. 9-11. <http://www.ftc.gov/os/comments/tsrdebtrelief/543670-00202.pdf>

### Debt settlement does not regularly eliminate all of the debt for most consumers

- The Florida Attorney General sued Nationwide Asset Services, Inc., and others, in the Fall of 2009, 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%**. The same case cited a complaint by the New York Attorney General alleging that of 1981 who signed up over three years, only 64 completed the program, at rate of just over 3%.

- The Colorado Attorney General analyzed information from annual reports to it by debt settlement companies in October 2009, and found that for Colorado consumers using debt settlement in 2008, less than 1% of consumers had all debt eliminated by debt settlement [0.84%].
- This is the first independent evidence about the actual completed settlement results for all consumers for *all* of the debt that they bring into a debt settlement program. These numbers appear to include people who started debt settlement in 2008 and those who had been in debt settlement for one, two, or three years. [Source: Colorado Attorney General, Oct. 23, 2009, comments to the FTC proposed amendments to the Telemarketing Sales Rule on the marketing of debt relief services <http://www.ftc.gov/os/comments/tsrdebtrelief/543670-00189.pdf>]

### **Debt settlement doesn't deliver on its promises**

Over the past five years, 21 states have brought 128 enforcement actions against 84 debt relief companies for unfair or deceptive trade practices. Most of these cases have been about debt settlement. States enforcement actions have alleged:

- Unsubstantiated claims of consumer savings.
- Deceptive representations about the length of time needed to complete a debt relief program.
- Misleading or failing to adequately inform consumers about the risk of debt collection efforts, lawsuits and increased debt balances while enrolled in debt relief programs.
- Deceptive disparagement of credit counseling and bankruptcy as alternatives for debtors.
- Failure to conduct individualized financial analyses to determine whether the debt relief is suitable for the consumer.
- Collection of substantial up-front fees even when the debt relief company fails to provide services to the consumer.
- Basing savings claims and settlement fees on the debt including the amount by which the debt has grown during debt settlement, rather than on the original debt amount that the consumer had upon entering the program.

Source: National Association of Attorneys General (NAAG) comments to the FTC on proposed amendments to the Telemarketing Sales Rule on the marketing of debt relief services, October 23, 2009, <http://www.ftc.gov/os/comments/tsrdebtrelief/543670-00192.pdf>

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# ATTACHMENT 2

## Amounts consumers could be charged for debt settlement under various proposals

An August 2009 study showed that 60% of consumers enrolled in debt settlement in a large one-company sample dropped out at a median time of 5-6 months after signing up. The average debt these consumers enrolled for debt settlement was \$24,000, with most consumers having 4 or more accounts.

	Maine statute	ACCORD	USOBA
<b>1.A Fees that could be charged to a consumer dropping out at 6 months with no settlements</b>	\$75 plus 15% of savings	50% of savings	5% set up, total 20% of debt over 1 <sup>st</sup> half of contract  \$1,920
<b>1.B Total fees plus remaining debt at drop out at six months with no settlements</b>	\$24,075	\$24,000	\$25,920
<b>2.A Fees that could be charged to a consumer staying in debt settlement for three years if half the debt was settled for half of the original amount</b>	\$975	\$3,000 (50% of savings represented by a 50% reduction in 50% of the debts)	\$4,800 (20% of the original debt)
<b>2.B Total fees plus settlements plus remaining debt after three years if half the debt was settled for half the original amount</b>	\$18,975	\$21,000	\$22,800
<b>3.A Total of fees after three years if two thirds of the debt was settled for half the original amount</b>	\$1,275	\$4,000	\$4,800
<b>3.B Total of fees plus settlements plus remaining debt after three years if two thirds of the debt was settled for half the original amount</b>	\$17,275	\$20,000	\$20,800