

United States Organizations for Bankruptcy Alternatives (USOBA)  
Statement before the NCCUSL Committee on the  
"Uniform Debt Management and Debt Settlement Act"  
October 8-10, 2004  
Chicago, Illinois

Chairman Hillman, Reporter Greenfield, Committee Members, my name is Robert Lemelin and I am here on behalf of the United States Organizations for Bankruptcy Alternatives. I would like to thank you for giving USOBA the opportunity to address this committee and provide a brief overview and insight into "Debt Settlement" and the debt negotiation industry. Because the Committee has chosen to refer to this particular bankruptcy alternative as "Debt Settlement" I will do the same in this presentation.

First, let me state that the membership of USOBA as well as many other industry participants commend this Committee for its hard work and welcome the long overdue need for regulation and uniformity in both the Consumer Credit and Consumer Debt Industries.

The concept of debt settlement is not new. In one form or another individuals have engaged in the settlement of third party debts since the inception of commerce. However, the current application of today's Debt Settlement Industry has only experienced significant growth within the past decade. This growth is a direct result of a consumer need that is not being met by traditional or established alternatives. This is not to say that these alternatives are not meeting consumer's needs, but rather that the market has grown tremendously which has allowed today's debt settlement companies to complement Credit Counseling, Debt Consolidation lending, and other programs.

It is important to note that while each of these bankruptcy alternatives operate in the same arena, the largest growth opportunity and expansion has been in the area of Debt Settlement. Therefore, it is important to understand how Debt Settlement works, how it differs from traditional Credit Counseling, "Debt Management Plans", and why it has become such an important choice for consumers who are faced with significant unsecured debt.

This Committee would like to define "Debt Settlement" in the proposed draft, and has even gone so far as to consider renaming the Act the "**Uniform Debt Management and Debt Settlement**

**Services Act**". While there are a number of similarities between Debt Management and Debt Settlement, there are also a number of significant differences. As a result of these differences, we feel it would be difficult to regulate each of these distinct programs under one unified law.

The Committee defines "Debt Settlement" in Section 2, paragraph 10 of the proposed Act as **"acting or negotiating on behalf of an individual for the purpose of securing the creditor's assent to receiving in full satisfaction of the debt owed to it an amount less than full principal of the debt "** adding , **"in fewer than four installments"**. This definition summarizes the core services offered by Debt Settlement companies. It is the application of these services, and the relationships of the participants involved, that more clearly define the differences between Debt Management and Debt Settlement.

Debt Settlement and Debt Settlement programs are Based, Rely on, and Operate under a for profit business model. Unlike traditional Credit Counseling Agencies which operate on a fundamental not for profit business model that includes fair share contributions from creditors: Debt Settlement Companies offer debt settlement programs to consumers based on a true principal- agent relationship that is market driven and does not have any financial participation or direct incentives by creditors. The relationship between a Debt Settlement Company and the creditor is one of an arms length transaction with the Debt Settlement Companies loyalty lying squarely with the consumer. These companies are subject to normal market pressure and competition; no different than any other for profit business in the marketplace today.

As such, there is no better incentive for a Debt Settlement Company to provide quality products and services to the consumer than the checks and balances of the competitive marketplace. This could be strengthened by responsible regulation that addresses the particular scope and nature of the Debt Settlement Industry rather than regulation that seeks to expand existing or proposed regulation to be all encompassing.

There are a number of reasons why we have seen an increase in the demand for Debt Settlement Services.

The first is an explosive growth in consumer credit and the ease with which today's consumer can qualify for unsecured debt. The Banking and Credit Card Industries have provided the consumer with a number of available options to obtain unsecured credit. As a result

of intense marketing and diverse products that encourage higher household debt, the potential for consumers to get into debt has grown drastically. The majority of consumers who seek out the services of Debt Settlement Companies are those consumers who have in excess of 5 credit cards issued directly by traditional credit card companies, Banks and other financial institutions as well as direct merchant store cards.

The average household debt, not including mortgages, has doubled in the past decade to an alarming \$19,000 with an average credit card balance per household nearing \$12,000. Despite these national statistics, most debt settlement companies see consumers enrolling in their programs with unsecured debt in excess of \$30,000.

*Note: \$19,000 and \$12,000 quotes from: Eileen Alt Powell, Consumer Debt More Than Doubles in Decade, Associated Press, January 6, 2004. See: [http://www.independentmedia.tv/item.cfm?media\\_id=4851&category\\_desc=Economy](http://www.independentmedia.tv/item.cfm?media_id=4851&category_desc=Economy).*

The second catalyst that is fueling the growth of debt settlement as a bankruptcy alternative is the fundamental differences between operating under the traditional business model used by Credit Counseling Agencies and that model used by Debt Settlement Companies.

As previously stated, debt settlement is rooted in a for profit business model. This model has been proven to help the growing number of consumers burdened with debt. These consumers have turned to debt settlement to help them overcome their personal and financial hardships in a Timely Manner, Avoid Bankruptcy and Achieve their Financial and Personal Goals of becoming Debt Free. In that debt settlement is performance based, so are the fees collected.

The success or failure of a Debt Settlement Program for a client is directly tied to the work performed by the Debt Settlement Company. In order for a Debt Settlement Company to succeed, it must perform **above** a minimum level or standard. We are confident that industry participants would support the proposed NCCUSL Act provided that regulations and standards are developed and adopted based on the Debt Settlement Business Model. Even a cursory review of the current draft seems to show that many of the Debt Management criteria are being incorrectly applied to the Debt Settlement Business Model.

The day-to-day functions of a Debt Settlement Company performing settlement services for its clients are different from that

of a tradition Credit Counseling Agency. They include but are not limited to:

1. Tracking client's unsecured creditors to locate the current creditor who is holding the specific debt. That creditor can be a first party issuer, internal recovery unit of the creditor or a third party collector. With multiple enrolled program debts this can be a tedious process.
2. Tracking the large volume of collection notices, legal documents, demands and correspondence issued too or from the client increases the work flow for the debt settlement company as well.

Additionally, there are also the on going negotiations with the Creditor, Agent, and Law Firm pursuing the client, addressing the ongoing calls and finalizing settlements on behalf of the client. The largest department and greatest consumer protection focus within a Debt Settlement Company is in the Customer Service Department.

The fees charged by Debt Settlement Companies are structured on a percentage based fee tied to either the amount of debt forgiven or the amount of debt enrolled in the program. In either event, there is a direct link between the amount of debt or number of debts, enrolled in the program, to the amount of work performed. One of the reasons why a Debt Settlement Program is more expensive than a traditional Debt Management Plan is that Debt Settlement Companies are not subsidized by the credit granting community by fair share or any other financial support. The greater the number of debts enrolled in the program, the more time and effort is spent. It therefore would be extremely difficult, if not impossible, to maintain the high level of service currently being provided by Debt Settlement Companies under the suggested Fee Structure and Fee Limit's proposed under this Act.

This Committee suggests that ***"a person providing debt-settlement services may not charge or receive compensation until the settlement of an individual's debt with a creditor"*** further adding ***"the amount of compensation of a debt-settlement services provider may not exceed the lesser of [\$600] or [15%] of the amount of the debt that each creditor forgives"***. This fee structure does not support any business model for debt settlement. (See Section 20 (g) of the Draft Act)

The overwhelming argument in support of allowing debt settlement fees to be market driven rather than pre determined is the fact that the successful completion of a debt settlement program results in

significant savings for the consumer. The majority of Debt Settlement Companies would confirm that consumers who stick to their Debt Settlement Program will pay less than the balance they owed at the start of their program including all fees. This is a material difference between Debt Settlement and other available options.

The need for regulation and oversight is recognized and embraced by the Debt Settlement Industry. However, the proposed Act seeks to overlay the much needed regulation of those companies directly involved in Debt Management on to those companies limited to providing Debt Settlement Services. As this Committee is aware, debt settlement does not receive monies from consumers for distribution to creditors. The overwhelming majority of Debt Settlement Companies use the services of Independent, Licensed and Regulated third party administrators to handle the client's monies. Those monies are controlled by and at all times remain under the Care, Custody and Control of the client. The Debt Settlement Company does not and should not have access to those funds. This does not cancel out the need for regulation and oversight, but rather lend itself to establishing requirements different from those set forth in the current proposed Act.

There are a number of organizations and companies that have sought to maintain the traditional Debt Management business model and to provide the level and caliber of education and service that is needed. It is our belief that these companies are not interested in exploring the Debt Settlement business model. They provide a needed service to a particular class of consumer and we applaud and support these organizations.

It is therefore important for this Committee to embrace the opportunity to clearly define the differences between those companies founded and operating under a Non Profit Business Model and those that operate in a competitive For Profit arena. By drafting and enacting Separate and Distinct regulatory standards for each industry you will ultimately be benefiting and protecting the consumer.

The Debt Management and Debt Settlement Industries are ever emerging and although there are a number of significant differences between the two, they do share some common traits. Both are founded on servicing the best interests of the consumer who finds themselves in debt. However, it is important that each of these industries be allowed to operate independently of each other and as such be subject to regulatory standards and requirements specific to

their individual business model and role in servicing their client base and niche. This should be our collective goal.

The membership of the United States Organizations of Bankruptcy Alternatives as well as many others within the Debt Settlement Industry welcome the opportunity to work with this Committee in Recognizing, Evaluating, Educating and Participating in the regulatory process. Our goal is to draft an Act that will establish Operational Standards and Guidelines to protect the Consumer, Service Provider and Industry as a whole.

Our clients come from very diverse backgrounds and all economic classes. But they all have one thing in common. They all have suffered some type of hardship such as Divorce, Loss of Income, Death or Severe Illness. The programs offered by Debt Settlement Companies vary depending on the type and needs of the client. But they all share one common goal.....**to protect the consumer and help them fulfill their financial obligations.**

I would like to thank Chairman Hillman and this Committee and its membership for allowing us the opportunity to address you today. We look forward to working with you.

Thank you for your consideration.