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PROTECTING CONSUMERS FROM DECEPTIVE DEBT SETTLEMENT SCHEMES

FIELD HEARING

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

AUGUST 12, 2010

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ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

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PROTECTING CONSUMERS FROM DECEPTIVE DEBT SETTLEMENT SCHEMES

THURSDAY, AUGUST 12, 2010

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Kansas City, MO.

The Committee met, pursuant to notice, at 9:30 a.m. in Kansas City Public Library, Helzberg Auditorium, 14 West 10th Street, Kansas City, Missouri, Hon. Claire McCaskill, presiding.

OPENING STATEMENT OF HON. CLAIRE MCCASKILL, U.S. SENATOR FROM MISSOURI

Senator MCCASKILL [presiding]. I want to thank Crosby and the entire team here at the library. I grew up in a family that my mother was so smart that when we got in trouble, our punishment was she would say, "You cannot go to the library this week." So, I was brought up learning that the library was a reward for good behavior, and therefore we all loved going to the library. And what he has done and what his team have done with this location has really enhanced, not just the greater Kansas City region, but clearly downtown, and has made this a spot to be very proud of in the Kansas City landscape, and I congratulate you on that work. I told him when I got here, "This is a great fit for Crosby Kemper." He was a good banker, but there has always been a part of Crosby Kemper that was a renaissance man, as opposed to a numbers man. So, I think he has found a great fit for his skill set and Kansas City is the better for it.

I want to welcome everyone to this hearing. This is a hearing of the U.S. Senate Commerce Committee, and we are holding this hearing here in Kansas City because I think it's important for us to do hearing work outside of Washington. And, if we were in Washington, every seat in this room would be full. And the reason it would be full is because they would all be lobbyists. There is never a hearing at the Commerce Committee in Washington that isn't a full house, because so much of the work of the Commerce Committee deals with commerce, and therefore it has to do with money, and therefore a lot of lobbyists are involved in the work of the Commerce Committee when we're in D.C. How refreshing it is to look out and realize, I bet we don't have a lobbyist in the group, at all. So, that's another good reason to have field hearings for the Commerce Committee.

Let me briefly give an opening statement, and then I will introduce the witnesses that we have this morning, and we'll get into

their testimony and questions of them on this subject that we're going to deal with today.

This is a hearing that's going to examine the impact to consumers from the business of debt settlement companies. We're going to examine the debt settlement industry and the scheme it runs to take money from consumers, and the efforts that need to be made to combat these abuses.

The Commerce Committee in Washington held a similar hearing on this subject back in April, and since then I've introduced legislation, and the FTC—who is represented today—has issued a rule to address abuses in the debt settlement industry. I believe it's a great time to have an additional hearing, especially in light of the rule that has now been proposed by the FTC.

Consumers today in America are very vulnerable to the marketing techniques of debt settlement companies. People are having a difficult time paying their bills. Many people do not know where to turn for help. So when you hear that advertisement on the radio, or you see that advertisement on television that says, "Call us, and we can take care of your debts," that is a seductive call.

Many, many, many people in America have absolutely fallen victim to what these companies are doing. There are 2,000 debt settlement companies now operating in this country. They promise to get people out of debt by negotiating with the consumer's creditors. And there are a few companies that do it right. But most rarely deliver on the claims they make in their marketing.

They target the most vulnerable—those with low incomes, high debt, unemployed, fixed incomes, and seniors. They falsely advertise what they can do, and they give people false hope. They are on the lowest level of the food chain. Their sole goal is to take advantage of people who are hurting.

We have a victim, here, from Odessa who has a story to tell and who has bravely told her story to national news outlets, and what happened to her, and the fact that she was taken advantage of.

A lot of these debt settlement companies, in fact, are ponzi schemes. They say to someone who's in debt, "Give us your money up front, and we will help you." They promise to deliver a product at a later date, but they collect all of the money up front. They claim they're building capital to help with creditor negotiations. Instead, they usually sit on the money and do nothing for months. That's because they would rather have the consumers pay them, as opposed to going out immediately and beginning negotiating. Debts pile up, and the consumer is worse off than before. Credit card interest piles up, and one of the things that happens, that is probably most disillusioning, is that the consumers are told not to pay their credit cards. "Quit paying your credit cards and pay us instead." What people don't realize at that point in time, is that that doesn't stop the credit cards from trying to collect their money. And we'll hear about that from our witness here this morning.

The consumer often ends up owing more than they started out owing when this whole process began. In other words, they pay a company to help them, the company doesn't help them, and they end up more in debt than they were when they began the process.

Debt settlement uses false claims to lure people in. They claim that 40 to 70 percent of the debt is retired. They claim that it will

only take 12 to 36 months to get out of debt. In reality, most consumers drop out of the program, because they don't see results.

The industry's own trade association states that two-thirds of the enrollees drop out of the program. They admit that only two-thirds of the people that they are signing up see enough benefit to even continue in the program. And most everyone ends up owing more than they did when they started.

Along with Senator Chuck Schumer, I have introduced legislation, S. 3264, to address the abuses. It will ban the up-front fees, it will allow no collection of fees until the debt is settled, it will cap the overall amount that the company can collect, it will allow cancellation with full refund, it will increase disclosure requirements, and it gives the FTC and the States clear enforcement authority over these companies.

We asked that—the Government Accountability Office do an investigation; this is the large group of auditors that work on behalf of the U.S. Government, looking at programs and figuring out whether they work, and whether or not they're wasting money. The GAO did an undercover investigation, looked at 20 companies. They testified about those findings in April. They found that most companies charged up-front fees, most companies told consumers to stop paying their debts, and that most of them were making fraudulent claims.

The FTC is also represented at the hearing this morning. They have issued a final rule that institutes many of the same provisions that are contained in my legislation. The rule bans up-front fees, it says no collection of fees until debt is settled, it also requires more disclosure. It is clear that the industry is going to challenge this rule in court. That's why the FTC needs the full statutory authority that the legislation that I have offered provides.

In Missouri, there have been some great efforts by the Attorney General's Office. We have seen a tripling of the complaints, and the Attorney General has pending litigation alleging fraud by one debt settlement company, and are pursuing other cases. Forty-one Attorneys General across the State have supported the FTC rule.

The goals we have this morning are very simple. We want to expose the debt settlement industry for what it is, we want to talk about the ways to put the bad ones out of business, we want to discuss the proposals that are out there to protect consumers, and we want to talk about the combined efforts of State enforcement, FTC enforcement, and the work of the U.S. Senate in this regard.

Now, let me introduce the three witnesses we have today. First, I want to thank each of you for coming. Our first witness today is Linda Robertson. Linda Robertson just got off the night shift at her job and went home and cleaned up and came to the hearing. We really appreciate her making an effort to be here. She's a resident of Odessa, Missouri. Today, she's going to share her experiences that she had from a personal standpoint with a debt settlement company.

She has told her story before, in fact, her story was featured in a front-page article in *The New York Times* several months ago. Thank you very much, Linda, for being here today.

Dave Angle is also here. Mr. Angle is an Assistant Attorney General with the Missouri Attorney General's Office. He has been an

Attorney for 20 years, and has served as a Public Defender, a Civil Rights Advocate, and a Consumer Protection Advocate. He has worked extensively on recent debt settlement cases; he joined the Consumer Protection Division of the Attorney General's Office in 2007.

And, finally, we have Alice Hrdy. Ms. Hrdy is an Assistant Director of the Division of Financial Practices at the Federal Trade Commission in Washington, D.C. In her current position she supervises enforcement and policy matters relating to debt relief services and other financial products and services. She joined the FTC in 1994 as a Staff Attorney. She was in charge of the final rule that the FTC issued last month to crack down on the debt settlement industry.

I thank you for traveling here, Ms. Hrdy, all the way from Washington.

And, with that, I will ask the witnesses to begin their testimony. And we will begin with you, Ms. Robertson. Feel free to take all of the time that you need, and if there is any further testimony that any of you all would like to put into the hearing record, you certainly can submit that, anything in writing that you would like to be added to the record of this hearing.

Ms. Robertson?

STATEMENT OF LINDA ROBERTSON, CONSUMER, ODESSA, MISSOURI

Ms. ROBERTSON. Thank you, Senator McCaskill, for giving me the opportunity to share my experiences with debt settlement. I want to share my story so that others will learn about the debt settlement schemes that are out there. And I hope my testimony helps other people who are in the situation that I was in.

In 2008, I was working as a real estate appraiser in Phoenix, Arizona when the slow economy forced me to give up that work. At the same time, there was an illness in my family, so I began having a hard time keeping up with bills. When my credit card debt became too high, I turned to a debt settlement company. I had seen advertisements for debt settlement on television, which made promises about helping people settle their debt without declaring bankruptcy. So, it seemed like the right option.

In February of 2009, I signed up with a debt settlement company called Financial Freedom of America after seeing one of its television advertisements. I called their toll free number and their representative told me the company would get me out of debt within 3 years without taking bankruptcy. I was made to feel confident that they would handle my credit cards and settle for up to 50 percent of the original balance.

I sent every correspondence from the credit card companies to FFOA, as was instructed, and felt secure in the fact that they were handling these accounts. Their representative also informed me to stop paying my credit card bills, so I thought FFOA was taking care of it.

My monthly payment to Financial Freedom of America was $428.97 per month. It was automatically taken from my checking account. And that was a lot of money to me, while I was making

around $11.00 an hour at the time, but I wanted to avoid bankruptcy.

After making payments to FFOA for 10 months, I was served with court papers and informed that Capital One was suing me in court. I was surprised, because I thought FFOA was handling this for me. I immediately called them and was told I did not have enough money in my account to settle with Capital One. I had paid approximately $4,000 by this time, and was told I only had about $1,900 in my account. They stated that they had no control on what a credit card company could do and that I did not have enough money to settle this account.

I learned, at this time, that FFOA had taken over $2,000 in "up front" fees out of what I had paid. This did not make sense to me, as they didn't even know what the credit card companies would settle for. It did not make sense that would they take the money up front; they were making money off of me, even though they had done nothing to earn it, yet. I called back and canceled the account and was then told I only had $1,400 in my account. There were several phone conversations back and forth before I received a check for around $1,100. I was just sick about this. Once the New York Times interviewed me, FFOA decided to return another $1,200 to me. However, I still have not received all of my money back from them—I'm sorry, I lost my place. And companies like this are taking advantage of people who are desperate for help and trying to do the right thing. This is a scam and a rip-off, and I told them that.

And I thank you that I was able to testify on this today, and I hope that it helps other people.

[The prepared statement of Ms. Robertson follows:]

PREPARED STATEMENT OF LINDA ROBERTSON, CONSUMER, ODESSA, MISSOURI

Thank you, Senator McCaskill, for giving me the opportunity to share my experiences with debt settlement. I want to share my story so that others will learn about the debt settlement schemes that are out there. I hope my testimony helps other people who are in the situation I was in.

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My monthly payment to Financial Freedom of America was $428.97 per month. It was automatically taken from my checking account. That was a lot of money to me, while I was making around $11.00 an hour at the time, but I wanted to avoid bankruptcy.

After making payments to FFOA for 10 months, I was served with court papers and informed that Capital One was suing me in court. I was surprised because I thought FFOA was handling this for me. I immediately called FFOA and was told I did not have enough money in my account to settle with Capital One. I had paid approximately $4,000 by this time and was told I only had about $1,900 in my ac-

count. They stated that they had no control on what a credit card company could do and that I did not have enough money to settle this account.

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Once the *New York Times* interviewed me, FFOA decided to return another $1,200 to me. However, I still have not received all of my money back from FFOA. Companies like this are taking advantage of people who are desperate for help and trying to do the right thing. This is a scam and rip-off.

I thank you for being able to testify about what has happened to me and hope it will help other people.

Senator MCCASKILL. Thank you very much, Linda. It's great that you've come and——

[Applause.]

Senator MCCASKILL.—and I think the hardest thing about this is when you're vulnerable, and you feel badly about the situation you're in and then to have someone take advantage of that is the worst. And you've done the right thing by coming forward and talking about it, even though I know it's an invasion of your privacy. We appreciate you being willing to allow us to take a peek into your personal life in regards to this, and it has been very helpful.

Mr. Angle?

STATEMENT OF DAVID ANGLE, ASSISTANT ATTORNEY GENERAL, OFFICE OF THE MISSOURI ATTORNEY GENERAL

Mr. ANGLE. Thank you, Senator. And thank you for bringing this hearing to Kansas City. It is a potential powerful partnership that we are discussing and engaging in, here, with Federal legislators, Federal regulators, and myself as a representative of the Missouri Attorney General's Office.

Attorneys General across the country have been addressing debt settlement issues for a number of years, now. It has been an ever-increasing problem. In our office, alone, we have had an ever-increasing number of complaints. In 2009, we experienced more than double the complaints that we had in 2008, and in 2010, we're on track to experience even more than that as compared to 2009.

Ms. Robertson's situation, unfortunately, is not unique. And if you listened to what she had to say, she mentioned that this debt settlement company had done nothing to earn the fees that they had appropriated from her. And, in our view, under this particular set-up, there's nothing that they can do to earn those fees because they're not earned, they're just taken.

The debt settlement structure is such that it is designed not to reduce consumer debt, but to drain fees from financially-vulnerable consumers, while the debt ever increases that they sought help from, and then the consumers are left out in the cold. The structure has been discussed ad nauseum. In your hearing in April, my colleague, Phil Lehman, from the North Carolina Attorney's General Office, I think, laid out quite ably what the problem is.

Debt settlers, not only will they instruct their "clients" to stop paying, but they also instruct them to stop communicating. That is a strategy that is designed, absolutely, to increase the fees, to in-

crease the interest rate, and indeed, as Ms. Robertson experienced, oftentimes it ends up getting the consumer sued on the very accounts that they thought they were getting help on. And the lack of communication not only flows from the consumer to their original creditors, but the debt settlers themselves are notorious for a lack of communication to their clients or to their creditors.

This is an inherently deceptive industry. It's inherently unfair, and it's structurally predatory because it's designed to do nothing other than drain fees from financially-vulnerable consumers.

Thank you very much for the opportunity to testify here and discuss some of these things. I thought, because we're in a policy-oriented environment, that it might be important to discuss some of the ways that this legislation adds, and could add, to the tool chest that the regulators and enforcers have in this industry.

State Attorneys General are responsible for enforcing laws that prohibit unfair acts and deception in the marketplace; the FTC is the primary Federal regulatory agency that exists on behalf of consumers to protect them from predatory conduct in the marketplace. Anything that increases the tools that we have available is a very welcome benefit to our office, to the FTC and to the consumer population, as a whole.

One of the things that hasn't necessarily been discussed or emphasized is, that there are third-parties out there who enable the debt settlement companies to accomplish the tasks that they accomplish. The primary debt settlement model involves not only the debt settlement entity, but payment processors to the debt settler's bank. Generally speaking, when a consumer signs up for a debt settlement program, they are introduced to a payment processing entity that is distinct from the debt settler, and the debt settler has his own bank account that the consumer's money goes into. This creates layers of obstruction that the consumers are unaware of when they enter into the program, and it allows the debt settlers, with a third-party entity, to automatically withdraw money from their primary bank account into a mysterious bank account that they had never heard of, that the debt settlement entity has equal, if not more, control over than the consumer does.

If the legislation you are considering could encompass those who materially aid the debt settlers, I think that would be a very valuable tool, not only for the Federal regulators, but for the State consumer protection officials, as well.

The FTC has issued a very strong rule: prohibition on advanced fees. If there is enough manpower out there to enforce it, we'll drive this business out of business. The additional tools that we could use would be those that would encompass those that materially aid the debt settlement entities, and your legislation currently has a very strong cap on fees: 5 percent will take these folks out of business, too. And they deserve to be out of business. They deserve the attention that this committee has paid to it, and we thank you for that. They deserve the attention that the FTC has paid to it, because they're predatory by their nature. I would urge you, Senator, to stay strong on the 5 percent cap, and to consider, also, widening the sweep so that we can get some of the other third parties into the scope of this regulatory and policymaking conduct, and that we'll just stamp these folks out, for good.

Thank you very much for your time.
[The prepared statement of Mr. Angle follows:]

PREPARED STATEMENT OF DAVID ANGLE, ASSISTANT ATTORNEY GENERAL, OFFICE OF THE MISSOURI ATTORNEY GENERAL

Chairman Rockefeller, Senator Hutchison, and members of the Committee, thank you for allowing me the opportunity to appear before the Committee and testify concerning the conduct of debt settlement industry participants and the impact this predatory industry has had on consumers in Missouri and across the country. I would also like to thank the Committee, and in particular Senator McCaskill, for bringing this hearing to Missouri. Although we are not alone in this regard, many Missourians have been deceptively lured into the debt settlement scheme. In my capacity as an Assistant Attorney General, I have responded to numerous complaints from Missourians who thought they had found a way to honorably reduce their debt burdens by enrolling in these so-called programs, only to find themselves in worse financial shape than before signing up for relief. I applaud your efforts to address the unfairness and deception inherent in this industry and am honored to share my thoughts and experiences today.

At the Committee's April 22, 2010 hearing, my colleague from the North Carolina Department of Justice, Phil Lehman, provided an excellent overview of the deception and unfairness inherent in the debt settlement industry. Additionally, 41 Attorneys General voiced their support for the FTC prohibition on the collection of advance fees by debt settlers. This was due in no small part to the efforts of our colleagues in the Illinois Attorney General's Office. Many additional consumer protection groups have also provided their valuable insights, including the Center for Responsible Lending and the National Consumer Law Center. As has been clearly demonstrated by the collective experience and wisdom of the consumer protection community, the debt settlement industry is a menace.

While many consumers can benefit from legitimate financial counseling, debt settlement practices are not aimed at reducing consumer debt. The objectives of debt settlers are to instill a false sense of hope in consumers mired in financial struggles while draining their limited resources.

The debt settlement scheme is fairly consistent. Advertisements reach consumers claiming a given entity can reduce that consumer's debt by 40–50 percent or more.[1] This message reaches consumers through television, radio, print, and Internet media. Stressed consumers are naturally drawn in by the possibility of living "debt free." Consumers' hopes are heightened upon making contact with the debt settler and being informed the settler has a special program, based on unique creditor relationships, that will allow debts to be magically reduced. The consumer is sent a package and signs up for this "program." In many instances, this includes setting up a stand-alone bank account, purportedly for the purpose of paying off reduced debt. What the consumer ultimately discovers is that this account is primarily a vehicle for payments to be made to the debt settler. In the process, the consumer is introduced to two additional entities—the payment processor and the debt settler's bank. As noted by Mr. Lehman in his April 22, 2010 testimony, numerous states enacted prohibitions on debt settlement conduct but in many states these prohibitions only apply if the debt settler directly receives consumer funds. The modern debt settlement scheme would likely not be as prevalent without the participation of these processing and banking parties.

Upon setting up the debt settlement bank account, automatic withdrawals from this account then take place. Payments are withdrawn first for the benefit of the debt settler. In my experience, any actual negotiation with creditors occurs, if at all, only after significant fees are extracted by the debt settler. In one recent example involving a Missouri consumer on a fixed income, the debt settlement company withdrew $1,278.84 as fees before any settlement activity took place. While these fees were being extracted, this consumer was sued on an account she thought was being negotiated. A judgment was lodged against this consumer and we are now working to obtain restitution on her behalf. Unfortunately, this is not an isolated instance. Complaints to the Missouri Attorney General's Office concerning debt settlement practices more than doubled from 2008 to 2009. Complaints in 2010 are on pace to more than triple the number from 2008.

The debt settlement "program" is premised on the debt settlers' claim that a consumer who ceases all payments on unsecured debt will be in a better negotiating

[1] See *e.g., www.creditsolutions.com* ("Put us to work for you and settle your unsecured debt by up to 50 percent.")

position with creditors.[2] The debt settler will also claim to have developed special relationships with creditors that facilitate reduction of debt. These claims are inherently deceptive. Indeed, many large creditors and/or the collection attorneys who work for them refuse to negotiate with debt settlement entities, a fact that is omitted from debt settlement advertisements.

Even where creditors may deal with a debt settler, the structure of the "program" operates to the detriment of the consumer. The approach of defaulting on unsecured debt and ceasing communication with creditors inevitably causes the debtor to incur additional charges that increase the consumer's debt load. These charges can be substantial, including late fees, higher interest rates, attorney fees, and other litigation costs. The debt settlement industry's claims of debt reduction, while deceptive from a macro level, are also unfounded when one looks at any debt they claim to have reduced. In making these claims, debt settlers include the additional, default-related charges incurred by a consumer in calculating the percentage of "reduction" purportedly achieved on behalf of a consumer. For example, a consumer may go into a debt settlement "program" with $5,000 in debt to a given creditor; cease payments and communication with this creditor; incur additional fees and charges of $2,500; and the debt settler would claim a 33 percent "reduction" by negotiating the consumer's debt to the original $5,000 balance but only after the consumer had paid the debt settler hundreds or thousands of dollars in fees. This practice is predatory and inherently deceptive.

Not surprisingly, and in spite of their claims to the contrary, debt settlement entities do not have track records of settling debts that even approach legitimacy. In one of the cases that illustrate this point, the FTC pursued the National Consumer Council for bogus claims regarding its claimed success rate in reducing consumer debt.[3] The court appointed receiver reported that only 1.4 percent of consumers actually completed the debt settlement "program."

Enforcement actions against debt settlement entities and principals are effective in dealing with the targeted entity. Unfortunately, where one entity's conduct is addressed by enforcement action, many others go unaddressed because enforcement offices do not learn of each entity operating within its jurisdiction; because resources do not allow for prosecution of every entity and/or its principals; and because the industry model is lucrative for its participants to the extent that the market is filled with new entrants.

One method of addressing the deceptive nature of this industry has been issued in the FTC's recently enacted rule prohibiting the collection of advance fees. The FTC has issued a strong rule in this regard. Additional protective action could include instituting a cap on the total amount of fees that may be collected when negotiating debts on behalf of consumers. Truly comprehensive measures would also address the participation of processing and banking entities. Debt settlement is an unfair and deceptive scheme, the perpetration of which is dependant on individuals and entities that are willing to process the transactions and deliver consumers' money to the scammers.

The debt settlement industry is deserving of the attention this Committee is paying to it. Any action by the Committee that supplements the tools and resources available for the Attorneys General, consumers, and society is welcome.

Senator MCCASKILL. Thank you very much, Mr. Angle.

Ms. Hrdy?

STATEMENT OF ALICE SAKER HRDY, ASSISTANT DIRECTOR, DIVISION OF FINANCIAL PRACTICES, FEDERAL TRADE COMMISSION

Ms. HRDY. Thank you, good morning. And thank you, Senator McCaskill, for holding this hearing and inviting the Federal Trade Commission to participate. I am honored to be here, in Kansas City. As a native Ohioan it's always wonderful to travel west from Washington. And you've brought us together today to discuss this critical issue facing Americans: credit card debt and the very problematic practices in the debt relief industry.

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[2] See *e.g., www.netdebt.com* ("When your accounts are past due, your creditors become very willing to accept significantly less than the balance owed and will settle the account.")

[3] *FTC* v. *National Consumer Council et al.*, case no. 04–0474, U.S. District Court, Central District of California.

The millions of Americans who are struggling with credit card debt, like Ms. Robertson, need realistic solutions that are tailored to their individual, particular situation. And, as you noted, there are some legitimate debt relief service providers who can provide valuable assistance. But, in far too many cases, consumers are paying large, up-front fees for nothing but empty promises.

The FTC is working on several fronts to stop these deceptive and abusive practices by this industry. First, of course, is enforcement. Over the last decade, the Commission, State Attorneys General, including the Missouri Attorney General, have brought a combined 259 actions against these types of firms and their principals to halt the illegal practices and, wherever possible, to return money to victims. But enforcement—case-by-case enforcement, alone, is not enough to address illegal practices that harm consumers.

And so, as you noted, 2 weeks ago, the Commission announced its final amendments to the Telemarketing Sales Rule. These new rules, which include an advance fee ban, will aid significantly in our efforts to tackle this industry's most harmful practices. And our education initiatives—for both businesses and consumers—will, of course, continue.

This burgeoning industry of debt settlement has come under particular scrutiny for good reason. Using dramatic claims, extensive advertising, and high-pressure sales tactics, many debt settlement services claim the company will negotiate with consumers' creditors to achieve deep reductions in their debt, and ultimately to eliminate consumers' debt. Relying heavily on telemarketing sales pitches, they convince consumers to enroll in their services.

Often we've seen that the companies track the latest headlines, and some of the worst actors lie—just outright lie—by claiming there's a government bailout for credit card debt. Or they simply claim they are the government.

Consumers who enroll must pay hundreds—or even thousands—in fees before the company even starts contacting their creditors. As a result, hard-pressed consumers face what is often an impossible task: paying the fees—which, often, the consumers don't even know they're paying to the debt settlement company—saving money for the settlements, and trying to pay their monthly bills for groceries and other things that they need. And not surprisingly, most consumers can not sustain this level of expenditures, and so they drop out before getting the savings that they were promised. After all, these are the consumers who were struggling to pay their bills in the first instance, before piling on the fees of the debt settlement company. And, in the cases that we've brought, and the State Attorneys General have brought, we've seen that those who do have to drop out forfeit almost all, if not all, of the fees that they've paid, unless they complain. And obviously, we know that it is so important for consumers to complain. Not only can it help to get the company to do right by the consumers, but it helps law enforcers to spot trends and to know which companies deserve a close look, or more.

So, these new rules under the Telemarketing Sales Rule set clear standards for the debt relief industry, and will make our enforcement efforts more effective. Through these rules, we've strengthened protections for consumers in three key ways. First, the ad-

vance-fee ban; it will prohibit debt relief companies from taking any money from consumers until they achieve results. This pay-for-performance model is intended to align incentives of both the industry and consumers, so that consumers are paying for actual results, not unfulfilled promises of results.

The second key protection afforded by the new rules are new disclosures specific to debt relief. Consumers must be told, clearly and conspicuously, before they pay for the service, and not in fine print after the fact.

The contracts will need to provide key information, including how long it will take to get the promised results, how much it will cost, and the negative consequences to your credit score that could result if you stop paying your creditors.

And third, the new rules prohibit specific misrepresentations that are common to debt settlement telemarketing, including deceptive claims about the amount of debt relief—that is, the debt reductions they can achieve.

Our statement of basis and purpose—which is very extensive, and accompanies the final rule, provides extensive guidance about the type of evidence these marketers must have before they make these dramatic claims of 40 to 60 percent reduction, or more. They have to have that evidence before they make claims that, in fact, most consumers are getting those results.

To assist industry members in their efforts to comply with the new rules, we've published this plain-English Business Education Guide, available online and by mail. We, of course, have other education materials geared to consumers on this topic, on the full range of debt issues, in English and in Spanish, online and in print.

And as we plan our future enforcement efforts of this rule, it's important to highlight the importance of continued joint FTC/State efforts. And to that end, we feel the TSR, in particular, is an excellent enforcement tool. The rule authorizes both the FTC and State Attorneys General to enforce its provisions in Federal court. You can be assured we'll be vigilant in our enforcement efforts to make sure that consumers across the country receive the benefits of these new rules.

Thank you, Senator, and I look forward to our discussion today.

[The prepared statement of Ms. Hrdy follows:]

PREPARED STATEMENT OF ALICE SAKER HRDY, ASSISTANT DIRECTOR, DIVISION OF FINANCIAL PRACTICES, FEDERAL TRADE COMMISSION

I. Introduction

Senator McCaskill and members of the Committee, I am Alice Saker Hrdy, Assistant Director in the Division of Financial Practices at the Federal Trade Commission ("FTC" or "Commission").[1] I appreciate the opportunity to appear before you today, and the Commission thanks this Committee for its interest in the work of the FTC to protect consumers from deception and abuse in the sale of debt relief services.

The Commission has a long history of protecting consumers of financial products and services offered by entities within the agency's jurisdiction. With Americans continuing to feel the effects of the economic downturn, the Commission has stepped

[1] The views expressed in this statement represent the views of the Commission. My oral presentation and responses to any questions you may have are my own, however, and do not necessarily reflect the views of the Commission or any Commissioner.

up its efforts to stop fraudulent financial schemes that exploit consumers who are particularly vulnerable as a result of financial distress.[2]

Stopping deceptive debt relief practices is one of our highest consumer protection priorities. Providers of debt relief services purport to help people who cannot pay their debts by negotiating on their behalf with creditors. Debt settlement companies, for example, market their ability to dramatically reduce consumers' debts, often by making claims to reduce debt by specific and substantial amounts, such as "save 40 to 60 percent off your credit card debt." In many instances, consumers pay hundreds or thousands of dollars for these services but get nothing in return.

The FTC utilizes its four principal tools to protect consumers of debt relief services: law enforcement, rulemaking, consumer education efforts, and research and policy development. To halt deceptive and abusive practices and return money to victimized consumers, the Commission has brought 23 lawsuits in the last 7 years against credit counseling firms, debt settlement services, and debt negotiators.[3] These cases have helped over 500,000 consumers harmed by deceptive and abusive practices.[4] The Commission continues to actively investigate debt relief companies and pursue aggressive enforcement in this arena. As the Commission's law enforcement experience has shown, victims of these schemes often end up *more* in debt than when they began. Especially in these difficult economic times, when so many consumers are struggling to keep their heads above water, this is unacceptable.

Over the past decade, the Commission and state enforcers have brought a combined 259 cases to stop deceptive and abusive practices by debt relief providers that have targeted consumers in financial distress. Despite these sustained efforts, consumer complaints continued to increase as did problematic advertising and telemarketing of these services. To strengthen the agency's ability to stop deception and abuse in the provision of debt relief services, the Commission proposed amendments to the Telemarketing Sales Rule ("TSR"). On July 29, 2010, after a thorough and careful review of the rulemaking record, the Commission announced its final amendments to the TSR. The Rule now bans debt relief providers from collecting fees in advance of performing promised services, prohibits them from making misrepresentations, and requires them to make several important up front disclosures.

This testimony provides an overview of the three common types of debt relief services, as well as the Commission's law enforcement efforts with respect to each. The testimony then describes the Commission's amendments to the TSR[5] and discusses the FTC's ongoing efforts to educate consumers about debt relief options and how to avoid scams.[6]

II. The Commission's Authority

The Commission enforces Section 5 of the FTC Act, which prohibits unfair or deceptive acts or practices in or affecting commerce,[7] as well as the Telemarketing and Consumer Fraud and Abuse Prevention Act ("Telemarketing Act")[8] and the associ-

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[2] Since the beginning of 2009, the FTC has brought more than 40 cases to stop scams that prey on consumers suffering from the financial downturn. *See, e.g.,* Press Release, FTC, *FTC Cracks Down on Con Artists Who Target Jobless Americans* (Feb. 17, 2010), available at *www.ftc.gov/opa/2010/02/bottomdollar.shtm*; Press Release, FTC, *FTC Cracks Down on Scammers Trying to Take Advantage of the Economic Downturn* (July 1, 2009), available at *www.ftc.gov/opa/2009/07/shortchange.shtm*.

[3] A list of the Commission's law enforcement actions against debt relief companies is attached as Appendix A.

[4] In addition to consumers who lost money to fraudulent debt relief companies, millions of consumers have been harassed by automated robocalls pitching services in violation of the Do Not Call provisions of the Telemarketing Sales Rule. The Commission has charged companies engaging in these robocalls with violations of the Rule. *See, e.g., FTC* v. *Asia Pac. Telecom, Inc.,* No. 10C3168 (N.D. Ill., preliminary injunction issued June 17, 2010); *FTC* v. *JPM Accelerated Servs. Inc.,* No. 09–CV–2021 (M.D. Fla., preliminary injunction issued Dec. 31, 2009); *FTC* v. *Econ. Relief Techs., LLC,* No. 09–CV–3347 (N.D. Ga., preliminary injunction issued Dec. 17, 2009).

[5] *Telemarketing Sales Rule; Final Rule*, 75 Fed. Reg. 48,458 (Aug. 10, 2010) (to be codified at 16 C.F.R. § 310).

[6] With respect to its research and policy development in this area, in September 2008, the Commission held a public workshop entitled "Consumer Protection and the Debt Settlement Industry," which brought together stakeholders to discuss consumer protection concerns associated with debt settlement services. Workshop participants also debated the merits of possible solutions to those concerns. An agenda and transcript of the Workshop are available at *www.ftc.gov/bcp/workshops/debtsettlement/index.shtm*. Public comments associated with the Workshop are available at *www.ftc.gov/os/comments/debtsettlementworkshop/index.shtm*.

[7] 15 U.S.C. § 45.

[8] 15 U.S.C. §§ 6101–6108. Pursuant to the Telemarketing Act's directive, the Commission promulgated the original TSR in 1995 and amended it in 2003, 2008, and 2010.

ated TSR that prohibit certain deceptive and abusive telemarketing practices.[9] The Commission has used this authority to challenge debt relief providers within its jurisdiction [10] who have engaged in deceptive or abusive practices. In addition, the Commission works to protect consumers from a wide range of other unfair and deceptive practices in the marketplace, such as credit-related and government grant scams, mortgage loan modification scams, deceptive marketing of health care products, deceptive negative option marketing, and business opportunity and work-at-home schemes. The FTC works closely with many state attorneys general and state banking departments to leverage resources in consumer protection.[11]

III. Overview of Debt Relief Services and FTC Law Enforcement Efforts

Debt relief services have proliferated over the past few years as greater numbers of consumers struggle with debts they cannot pay. A range of nonprofit and for-profit entities—including credit counselors, debt settlement companies, and debt negotiation companies—offer to help consumers facing debt problems. As detailed below, consumers have complained of deceptive and abusive practices in all of these services, and in response, the FTC and state enforcement and regulatory bodies have brought numerous cases.[12]

A. Credit Counseling Agencies

Credit counseling agencies ("CCAs") historically were nonprofit organizations that worked as liaisons between consumers and creditors to negotiate "debt management plans" ("DMPs"). DMPs are monthly payment plans for the repayment of credit card and other unsecured debt that enable consumers to repay the full amount owed to their creditors but under renegotiated terms that make repayment less onerous.[13] Credit counselors typically also provide educational counseling to assist consumers in developing a manageable budget and avoiding debt problems in the future. Beginning in the late 1990s, however, some CCAs registered as nonprofit organizations with the Internal Revenue Service, but in reality were operating as for-profit companies and engaging in aggressive and illegal marketing practices. Other CCAs incorporated and openly operated as for-profit companies.

Since 2003, the Commission has filed six cases against credit counseling providers for deceptive and abusive practices.[14] In one of these cases, the FTC sued

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[9] The Commission also has law enforcement authority and, in some cases, regulatory powers under a number of other consumer protection statutes specifically related to financial services, including the Truth in Lending Act, 15 U.S.C. §§ 1601–1666j; the Consumer Leasing Act, 15 U.S.C. §§ 1667–1667f; the Fair Debt Collection Practices Act, 15 U.S.C. §§ 1692–1692o; the Fair Credit Reporting Act, 15 U.S.C. §§ 1681–1681x; the Equal Credit Opportunity Act, 15 U.S.C. §§ 1691–1691f; the Credit Repair Organizations Act, 15 U.S.C. §§ 1679–1679j; the Electronic Funds Transfer Act, 15 U.S.C.§§ 1693–1693r; the privacy provisions of the Gramm-Leach-Bliley Act, 15 U.S.C. §§ 6801–6809; and the Omnibus Appropriations Act of 2009, Pub. L. No. 111–8, § 626, 123 Stat. 524 (Mar. 11, 2009).

[10] The FTC Act exempts banks and other depository institutions and bona fide nonprofits, among others, from the Commission's jurisdiction. 15 U.S.C. §§ 44, 45(a)(2). These exemptions apply to the FTC's jurisdiction under the Telemarketing Act and the TSR as well.

[11] *See, e.g.,* FTC, Press Release, *Federal and State Agencies Target Mortgage Foreclosure Rescue and Loan Modification Scams* (July 15, 2009), available at *www.ftc.gov/opa/2009/07/loanlies.shtm* (announcing sweep targeting mortgage assistance relief scams, including *FTC* v. *US Foreclosure Relief Corp.*, No. SACV09–768 JVS (MGX) (C.D. Cal., final order March 11, 20 10) (State of Missouri, State of California, and FTC filed joint case alleging violations of FTC Act and TSR against defendants purporting to provide mortgage assistance relief services)); Press Release, FTC, *FTC Announces "Operation False Charity" Law Enforcement Sweep* (May 20, 2009), available at *www.ftc.gov/opa/2009/05/charityfraud.shtm* (including four cases brought by the Attorney General of Missouri).

[12] The Commission has addressed similar problems with respect to companies offering to resolve consumers' mortgage debts. The Commission has engaged in an aggressive, coordinated enforcement initiative to shut down companies falsely claiming the ability to obtain mortgage loan modifications or other relief for consumers facing foreclosure. In the past year alone, the FTC has brought 10 cases targeting foreclosure rescue and mortgage modification frauds, with other matters under active investigation. In addition, state enforcement agencies have brought more than 200 cases against such firms in recent years. Further, as directed by Congress under the Omnibus Appropriations Act of 2009, Pub. L. No. 111–8, the Commission has initiated a rulemaking proceeding addressing the for-profit companies in this industry. Under the proposed rule, companies could not receive payment until they have obtained for the consumer a documented offer from a mortgage lender or servicer that comports with any promises previously made. *Mortgage Assistance Relief Services*, 75 Fed. Reg. 10707 (Mar. 9, 2010).

[13] To be eligible for a DMP, a consumer generally must have sufficient income to repay the full amount of his or her debts, provided that the terms are adjusted to make such repayment possible.

[14] *See* Appendix A (items 15, 16, 17, 18, 20, and 21).

AmeriDebt, Inc., at the time one of the largest CCAs in the United States.[15] On the eve of trial, the FTC obtained a $35 million judgment as part of a settlement agreement. Thus far, the Commission has collected and distributed $12.7 million in redress to 287,000 consumers.[16] In AmeriDebt and other credit counseling cases, the FTC charged that the agencies engaged in deceptive conduct in violation of Section 5 of the FTC Act and the TSR, including:

- misrepresentations about the benefits and likelihood of success consumers could expect from the services, including the savings they would realize;[17]
- misrepresentations regarding fees, including false claims that the CCAs did not charge up-front fees;[18]
- deceptive statements regarding their purported nonprofit nature;[19] and
- violations of the TSR's provisions that require certain disclosures and prohibit misrepresentations, as well as the requirements of the TSR's Do Not Call provisions.[20]

In addition, over the last several years, in response to abuses such as these, the IRS has challenged a number of purportedly nonprofit CCAs—both through enforcement of existing statutes and new tax code provisions—resulting in the revocation, or proceedings to revoke, the nonprofit status of 41 CCAs.[21] In addition, state authorities have brought at least 21 cases against CCAs under their own statutes and rules.

B. Debt Settlement Services

Debt settlement companies purport to obtain from consumers' unsecured creditors lump sum settlements for significantly less than the full outstanding balance of the consumers' debts. Unlike a traditional DMP, the goal of a debt settlement plan is to enable the consumer to repay only a portion of the total debt owed. Debt settlement providers heavily market through Internet, television, radio, and print advertising. The advertisements typically make claims about the company's supposed ability to reduce consumers' debts to a fraction of the full amount owed, and then encourage consumers to call a toll-free number for more information.[22] During the calls, telemarketers repeat and embellish many of these claims.

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[15] *FTC* v. *AmeriDebt, Inc.*, No. PJM 03–3317 (D. Md., final order May 17, 2006).

[16] *See* Press Release, FTC, *FTC's AmeriDebt Lawsuit Resolved: Almost $13 Million Returned to 287, 000 Consumers Harmed by Debt Management Scam* (Sept. 10, 2008), *www.ftc.gov/opa/2008/09/ameridebt.shtm*. The FTC expects to make another distribution of consumer refunds this year.

[17] *See FTC* v. *Integrated Credit Solutions, Inc.*, No. 06–806–SCB–TGW (M.D. Fla., final order Oct. 16, 2006); *United States* v. *Credit Found. of Am.*, No. CV 06–3654 ABC(VBKx) (C.D. Cal., final order June 16, 2006); *FTC* v. *Debt Mgmt. Found. Servs., Inc.*, No. 04–1674–T–17–MSS (M.D. Fla., final order Mar. 30, 2005).

[18] *See FTC* v. *Leshin*, No. 06–cv–61851–WJZ (S.D. Fla., final order May 5, 2008); *FTC* v. *AmeriDebt, Inc.,* No. PJM 03–3317 (D. Md., final order May 17, 2006).

[19] *See FTC* v. *Leshin*, No. 06–cv–61851–WJZ (S.D. Fla., final order May 5, 2008); *FTC* v. *Integrated Credit Solutions, Inc.,* No. 06–806–SCB–TGW (M.D. Fla., final order Oct. 16, 2006); *United States* v. *Credit Found. of Am.*, No. CV 06–3654 ABC(VBKx) (C.D. Cal., final order June 16, 2006); *FTC* v. *AmeriDebt, Inc.*, No. PJM 03–3317 (D. Md., final order May 17, 2006); *FTC* v. *Debt Mgmt. Found. Servs., Inc.*, No. 04–1674–T–17–MSS (M.D. Fla., final order Mar. 30, 2005). Although the defendants in these cases had obtained IRS designation as nonprofits under Section 501(c)(3) of the Internal Revenue Code, they allegedly funneled revenues out of the CCAs and into the hands of affiliated for-profit companies and/or the principals of the operation. Thus, the FTC alleged that the defendants were "operating for their own profit or that of their members" and fell outside the nonprofit exemption in the FTC Act. 15 U.S.C.§ 44.

[20] *See FTC* v. *Leshin*, No. 06–cv–61851–WJZ (S.D. Fla., final order May 5, 2008); *United States* v. *Credit Found. of Am.*, No. CV 06–3654 ABC(VBKx) (C.D. Cal., final order June 16, 2006).

[21] Eileen Ambrose, *Credit Firms' Status Revoked; IRS Says 41 Debt Counselors Will Lose Tax-Exempt Standing*, BALTIMORE SUN, May 16, 2006. To enhance the IRS's ability to oversee CCAs, Congress amended the IRS Code in 2006, adding Section 501(q) to provide specific eligibility criteria for CCAs seeking tax-exempt status as well as criteria for retaining that status. See Pension Protection Act of 2006, Pub. L. No. 109–280, § 1220 (Aug. 2006) (codified at 26 U.S.C. § 501(q)). Among other things, Section 501(q) of the IRS Code prohibits tax-exempt CCAs from refusing to provide credit counseling services due to a consumer's inability to pay or a consumer's ineligibility or unwillingness to agree to enroll in a DMP; charging more than "reasonable fees" for services; and, unless allowed by state law, basing fees on a percentage of a client's debt, DMP payments, or savings from enrolling in a DMP. In addition, as a result of changes in the Federal bankruptcy code, 158 nonprofit CCAs, including the largest entities, have been subjected to rigorous screening by the Department of Justice's Executive Office of the U.S. Trustee. Finally, nonprofit credit counseling agencies must comply with state laws in 49 states, most of which specify particular fee limits.

[22] *See, e.g., FTC* v. *Connelly*, No. SA CV 06–701 DOC (RNBx) (C.D. Cal., final order Oct. 2, 2008); *FTC* v. *Edge Solutions, Inc.*, No. CV–07–4087 (E.D.N.Y., final order Aug. 29, 2008); *FTC*

Most debt settlement companies charge consumers hundreds, or even thousands, of dollars in up-front fees, in many cases with the entire amount of fees due within the first few months of enrollment and before any debts are settled. An increasing number of providers spread their fees over a longer period—for example, 12 to 18 months—but consumers generally still pay a substantial portion of the fees before any of their payments are used to pay down their debt. Most consumers drop out of these programs before completion, and they typically forfeit all of the money they paid to the debt settlement company, regardless of whether they received any settlements from their creditors.[23]

Since 2004, the Commission has brought nine actions against debt settlement providers, alleging that they deceived consumers about key aspects of their programs.[24] The defendants' misrepresentations included claims that:

- the provider will, or is highly likely to, obtain large reductions in debt for enrollees, *e.g.,* a 50 percent reduction or elimination of debt in 12 to 36 months;[25]
- the provider will stop harassing calls from debt collectors as well as collection lawsuits;[26]
- the provider has special relationships with creditors and is expert in inducing creditors to grant concessions;[27]
- the consumer will not have to pay substantial up-front fees,[28] and
- the consumer will be able to obtain a refund if the provider is unsuccessful.[29]

The Commission also has alleged that debt settlement companies encouraged or instructed consumers to stop paying their creditors, while not disclosing that failing to make payments to creditors may actually increase the amount owed (because of accumulating fees and interest) and would harm their credit rating.[30] In addition to the FTC cases, state attorneys general and regulators have filed over 125 law enforcement actions against debt settlement providers under state statutes that, among other things, ban unfair or deceptive practices.[31]

C. Debt Negotiation

Debt negotiation companies assert that they can obtain interest rate reductions or other concessions from creditors to lower consumers' monthly payments. Such companies often market debt negotiation services through so-called automated "robocalls." Like debt settlement companies, many debt negotiation providers charge significant up-front fees and promise specific results, such as a particular interest rate reduction or amount of savings.[32] In some cases, the telemarketers of debt ne-

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v. *Debt-Set, Inc.,* No. 1: 07–cv–00558–RPM (D. Colo., final order Apr. 11, 2008); *FTC* v. *Jubilee Fin. Servs., Inc.*, No. 02–6468 ABC (Ex) (C.D. Cal., final order Dec. 12, 2004).

[23] *Telemarketing Sales Rule; Final Rule*, 75 Fed. Reg. at 48471–72 (citing commenters).

[24] *See* Appendix A (items 2, 6, 11, 12, 13, 19, 20, 22, and 23).

[25] *See, e.g., FTC* v. *Edge Solutions, Inc.,* No. CV–07–4087 (E.D.N.Y. , final order Aug. 29, 2008); *FTC* v. *Innovative Sys. Tech., Inc.*, No. CV04–0728 GAF JTLx (C.D. Cal., final order July 13, 2005).

[26] *See, e.g., FTC* v. *Debt-Set, Inc.*, No. 1:07–cv–00558–RPM (D. Colo., final order Apr. 11, 2008); *FTC* v. *Better Budget Fin. Servs., Inc.*, No. 04–12326 (WG4) (D. Mass., final order Mar. 28, 2005); *FTC* v. Jubilee Fin. Servs., Inc., No. 02–6468 ABC (Ex) (C.D. Cal., final order Dec. 12, 2004).

[27] *See, e.g., FTC* v. *Debt-Set, Inc.,* No. 1:07–cv–00558–RPM (D. Colo., final order Apr. 11, 2008); *FTC* v. *Better Budget Fin. Servs., Inc.*, No. 04–12326 (WG4) (D. Mass. 2005). Some providers are also misrepresenting that their service is part of a government program through the use of such terms as "government bailout" or "stimulus money." *See, e.g., FTC* v. *Dominant Leads, LLC,* No. 1:10-cv–00997 (D.D.C., preliminary injunction issued July 8, 2010).

[28] *See, e.g., FTC* v. *Debt-Set,* No. 1:07–cv–00558–RPM (D. Colo., final order Apr. 11, 2008).

[29] *See, e.g., FTC* v. *Innovative Sys. Tech., Inc.*, No. CV04–0728 GAF JTLx (C.D. Cal., final order July 13, 2005).

[30] *See, e.g., FTC* v. *Connelly,* No. SA CV 06–701 DOC (RNBx) (C.D. Cal., final order Oct. 2, 2008); *FTC* v. *Jubilee Fin. Servs., Inc.,* No. 02–6468 ABC (Ex) (C.D. Cal., final order Dec. 12, 2004).

[31] *See, e.g., Minnesota* v. *American Debt Settlement Solutions, Inc.*, No. 70–CV–10–4478 (Minn., 4th Dist., filed Feb. 18, 2010); *Illinois* v. *Clear Your Debt, LLC*, No. 2010–CH–00167 (Ill. 7th Cir., filed Feb. 10, 2010); Press Release, Colorado Attorney General, *Eleven Companies Settle with the State Under New Debt-Management and Credit Counseling Regulations* (Mar. 12, 2009), available at *www.ago.state.co.us/press_detail.cfmpressID=957.html*; *Texas* v. *CSA-Credit Solutions of Am., Inc.,* No. 09–000417 (Dist. Travis Cty, filed Mar. 26, 2009); *Florida* v. *Boyd*, No. 2008–CA–002909 (Cir. Ct. 4th Cir. Duval Cty, filed Mar. 5, 2008).

[32] *See FTC* v. *Asia Pac. Telecom, Inc.*, No. 10 C 3168 (N.D. Ill., preliminary injunction issued June 17, 2010); *FTC* v. *JPM Accelerated Servs. Inc.*, No. 09–CV–2021 (M.D. Fla., preliminary injunction issued Dec. 31, 2009); *FTC* v. *Econ. Relief Techs*., LLC, No. 09–CV–3347 (N.D. Ga., preliminary injunction issued Dec. 17, 2009); *FTC* v. *2145183 Ontario, Inc.*, No. 09–CV–7423

Continued

gotiation services refer to themselves as "card services" or a "customer service department" during calls with consumers in order to mislead them into believing that the telemarketers are associated with the consumer's credit card company.[33]

The FTC has brought nine actions against defendants alleging deceptive debt negotiation practices.[34] In each case, the Commission alleged that defendants: (1) misrepresented that they could reduce consumers' interest payments by specific percentages or minimum amounts, (2) falsely purported to be affiliated, or have close relationships, with consumers' creditors,[35] and (3) violated the TSR's Do Not Call provisions, among other TSR violations.[36]

Our law enforcement colleagues at the state level also have focused attention on bogus debt negotiation companies. The states have brought at least 14 cases against such firms, and the FTC will continue to work closely with our state partners on these and related issues.

IV. The Commission's Amendments to the Telemarketing Sales Rule

On July 29, 2010, the Commission announced final amendments to the TSR governing providers of debt relief services ("Final Rule"), based on its determination that such revisions to the TSR are necessary to protect consumers from deceptive and abusive practices in the telemarketing of debt relief services.[37] The Commission developed the Final Rule after considering an extensive rulemaking record, including over 300 public comments,[38] and information gathered during a November 2009 public forum. At that forum, representatives of all the major stakeholders discussed the key consumer protection issues and problems that are present in the debt relief industry and possible solutions for them.[39] The Final Rule:

- prohibits any telemarketer or seller of debt relief services from requesting or receiving payment until it produces the promised services and provides proof documenting this fact to the consumer;
- mandates certain additional disclosures and prohibits misrepresentations in the telemarketing of debt relief services; and
- extends the existing protections of the TSR to inbound debt relief calls, *i.e.,* those where consumers call a telemarketer in response to a general media or direct mail advertisement.[40]

As to its scope, the Final Rule covers telemarketers of for-profit debt relief services, including credit counseling, debt settlement, and debt negotiation services. Because the FTC Act exempts nonprofit entities from the agency's jurisdiction under that Act, and the Telemarketing Act incorporates the FTC Act exemptions, the TSR generally does not apply to such entities. However, companies falsely claiming nonprofit status are subject to both the FTC Act and the TSR.

The Final Rule specifies that fees for debt relief services may not be collected until:

- the debt relief provider successfully renegotiates, settles, reduces, or otherwise changes the terms of at least one of the consumer's debts;

(N.D. Ill., preliminary injunction issued Dec. 17, 2009); *FTC* v. *Select Pers. Mgmt.,* No. 07–0529 (N.D. Ill., final order May 15, 2009); *FTC* v. *Group One Networks, Inc.,* No. 8:09–cv–352–T–26–MAP (M.D. Fla., final order March 19, 2009); *FTC* v. *Debt Solutions, Inc.,* No. 06–0298 JLR (W.D. Wash., final order June 18, 2007).

[33] *See* cases cited *supra*, note 32.

[34] *See* Appendix A (items 1, 3, 4, 5, 7, 8, 9, 10, and 14).

[35] *See* cases cited *supra*, note 32.

[36] *See* cases cited *supra,* note 32.

[37] Press Release, FTC, *FTC Issues Final Rule to Protect Consumers in Credit Card Debt* (July 29, 2010), available at *www.ftc.gov/opa/2010/07/tsr.shtm*. Commissioner Rosch dissented from the Commission decision.

[38] Comments were submitted by: 35 industry representatives, 10 industry trade associations and groups, 26 consumer groups and legal services offices, six law enforcement organizations, three professors, two labor unions, the Uniform Law Commission, the Responsible Debt Relief Institute, the Better Business Bureau, and 236 individual consumers. The public comments are available at *www.ftc.gov/os/comments/tsrdebtrelief/index.shtm*.

[39] A transcript of the forum is available at *www.ftc.gov/bcp/rulemaking/tsr/tsr-debtrelief/index.shtm*. After the forum, Commission staff sent letters to industry trade associations and individual debt relief providers that had submitted public comments, soliciting follow-up information in connection with certain issues that arose at the forum. The letters are posted at *www.ftc.gov/os/comments/tsrdebtrelief/index.shtm*. Sixteen organizations responded and provided data.

[40] Outbound calls to solicit the purchase of debt relief services are already subject to the TSR.

- there is a written settlement agreement, debt management plan, or other agreement between the consumer and the creditor, and the consumer has agreed to it; and
- the consumer has made at least one payment to the creditor or debt collector as a result of the agreement negotiated by the debt relief provider.

To ensure that debt relief providers do not front-load their fees if a consumer has enrolled multiple debts in one debt relief program, the Final Rule specifies how debt relief providers may collect the fee for each settled debt. First, the provider's fee for a single debt must be in proportion to the total fee that would be charged if all of the debts had been settled. Alternatively, if the provider bases its fee on the percentage of what the consumer saves as result of using its services, the percentage charged must be the same for each of the consumer's debts.

Another new provision of the Final Rule will allow debt relief companies to require that consumers set aside their fees and savings for payment to creditors in a "dedicated account." However, providers may only require a dedicated account as long as five conditions are met:

- the dedicated account is maintained at an insured financial institution;
- the consumer owns the funds (including any interest accrued);
- the consumer can withdraw the funds at any time without penalty;
- the provider does not own or control or have any affiliation with the company administering the account, and
- the provider does not exchange any referral fees with the company administering the account.

In addition, the Final Rule requires that providers must make several disclosures when telemarketing their services to consumers. Before the consumer signs up for any debt relief service, providers must disclose how long it will take for consumers to obtain results, how much it will cost, the negative consequences that could result from using debt relief services, and key information about dedicated accounts if they choose to require them. In addition, the TSR mandates general disclosures for all telemarketers, including the total cost and any material restrictions or limitations of the service.

The Final Rule also prohibits misrepresentations about any debt relief service, including savings rates and whether the provider is a nonprofit entity. The Commission's Statement of Basis and Purpose, which accompanies the Final Rule, provides extensive guidance about the evidence providers must possess before they make specific claims about the amount of debt reduction they will obtain for consumers. First, providers must account for the additional debt and costs consumers incur as a result of interest, late fees, and other charges imposed by the creditors or debt collectors during the course of the program. Second, providers must account for the fees consumers pay to the provider in calculating the savings. Third, providers must include in their calculation of savings those consumers who dropped out or were otherwise unable to complete the program. Finally, providers must account for individual accounts that were not settled successfully. Thus, providers may not exclude debts that they have failed to settle—including those associated with consumers who dropped out of the program—from their calculations of the average savings percentage or amount of consumers' debt reduction.

The amendments become effective on September 27, 2010, except for the advance fee ban, which becomes effective on October 27, 2010. To help businesses comply with the new debt relief rules, the FTC staff issued a compliance guide describing the key changes to the TSR affecting debt relief services.[41]

V. Efforts to Educate Consumers

To complement its law enforcement and rulemaking, the Commission has made significant efforts to educate consumers about debt relief services and alert them to possible deceptive practices. This past spring, the agency released a brochure entitled "Settling Your Credit Card Debts," which offers struggling consumers tips on seeking assistance with their debts and spotting red flags for potential scams.[42] This

[41] The guide is available at *www.ftc.gov/bcp/edu/pubs/business/marketing/bus72.pdf*.

[42] The brochure is available at *www.ftc.gov/bcp/edu/pubs/consumer/credit/cre02.shtm*. Since its release in March 2010, the agency has distributed 20,400 print copies, and consumers have accessed it on the Internet over 13,700 times.

brochure, along with additional educational materials on debt relief,[43] is available at an FTC web page, *www.ftc.gov/MoneyMatters*.[44]

In addition, the Commission has conducted numerous educational campaigns designed to help consumers manage their financial resources, avoid deceptive and unfair practices, and become aware of emerging scams. For example, the FTC has undertaken a major consumer education initiative related to mortgage loan modification and foreclosure rescue scams, including the release of a suite of mortgage-related resources for homeowners.[45] Moreover, the agency has focused outreach efforts on a number of other issues faced by people in economic distress, including stimulus scams, rental scams, church "opportunity" scams, offers for bogus auto warranties, and solicitations for phony charities that exploit the public's concern for the welfare of our troops and public safety personnel in a time of crisis.

The Commission encourages wide circulation of all of its educational resources and makes bulk orders available free of charge, including shipping. We provide FTC materials to state attorneys general and other local law enforcement entities, consumer groups, and nonprofit organizations, who in turn distribute them directly to consumers. In addition, media outlets—online, print, and broadcast—routinely cite our materials and point to our guidance when covering debt-related news stories.

VI. Conclusion

The FTC appreciates the opportunity to describe its work to protect consumers from deceptive and abusive conduct in the marketing of debt relief services. Stopping the marketers of debt relief services who prey on consumers facing financial hardship is among the FTC's highest priorities, and we will continue our aggressive law enforcement and educational programs in this area.

APPENDIX A

FTC Law Enforcement Actions Against Debt Relief Companies

1. *FTC* v. *MCS Programs, LLC*, No. 09–CV–5380 (W.D. Wash., final order July 19, 2010) (debt negotiation), available at *www.ftc.gov/os/caselist/0823216/index.shtm*

2. *FTC* v. *Dominant Leads, LLC*, No. 1:10–cv–00997 (D.D.C., preliminary injunction issued July 8, 2010) (debt settlement and mortgage assistance relief services), available at *www.ftc.gov/os/caselist/1023152/index.shtm*

3. *FTC* v. *Asia Pac. Telecom, Inc.*, No. 10–C–3168 (N.D. Ill., preliminary injunction issued June 17, 2010) (debt negotiation), available at *www.ftc.gov/os/caselist/1023060/index.shtm*

4. *FTC* v. *Advanced Mgmt. Servs*. NW, LLC, No. 10–148–LRS (E.D. Wash. filed May 10, 2010) (debt negotiation), available at *www.ftc.gov/os/caselist/0923187/index.shtm*

5. *FTC* v. *Group One Networks, Inc.*, No. 09–CV–00352 (M.D. Fla., final order March 19, 2010) (debt negotiation), available at *www.ftc.gov/os/caselist/0723230/index.shtm*

6. *FTC* v. *Credit Restoration Brokers, LLC*, No. 2:10–cv–0030–CEH–SPC (M.D. Fla., final order Mar. 11, 2010) (debt settlement and credit repair), available at *www.ftc.gov/os/caselist/0823001/index.shtm*

7. *FTC* v. *JPM Accelerated Servs., Inc.*, No. 09–CV–2021 (M.D. Fla., preliminary injunction issued Dec. 31, 2009) (debt negotiation), available at *www.ftc.gov/os/caselist/0923190/index.shtm*

8. *FTC* v. *2145183 Ontario, Inc.,* No. 09–CV–7423 (N.D. Ill., preliminary injunction issued Dec. 17, 2009) (debt negotiation), available at *www.ftc.gov/os/caselist/0923183/index.shtm*

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[43] *Fiscal Fitness: Choosing a Credit Counselor* (2005), available at *www.ftc.gov/bcp/edu/pubs/consumer/credit/cre26.shtm*; *For People on Debt Management Plans: A Must-Do List* (2005), available at *www.ftc.gov/bcp/edu/pubs/consumer/credit/cre38.shtm*; *Knee Deep in Debt* (2005), available at *www.ftc.gov/bcp/edu/pubs/consumer/credit/cre19.shtm*. In the last 2 years, the FTC has distributed more than 271,000 print versions of these three publications combined, and consumers have accessed them online more than one million times.

[44] Over the last 6 months, the Money Matters website has received approximately 60,000 hits per month.

[45] NeighborWorks America, the Homeowners Preservation Foundation (a nonprofit member of the HOPE NOW Alliance of mortgage industry members and U.S. Department of Housing and Urban Development-certified counseling agencies), and other groups distribute FTC materials directly to homeowners.

9. *FTC* v. *Econ. Relief Techs., LLC*, No. 09–CV–3347 (N.D. Ga., preliminary injunction issued Dec. 14, 2009) (debt negotiation), available at *www.ftc.gov/os/caselist/0923118/index.shtm*
10. *FTC* v. Select Pers. Mgmt., Inc., No. 07–CV–0529 (N.D. Ill., final order May 15, 2009) (debt negotiation), available at *www.ftc.gov/os/caselist/0623215/0623215.shtm*
11. *FTC* v. *Connelly*, No. SA CV 06–701 DOC (RNBx) (C.D. Cal., final order Oct. 2, 2008) (debt settlement), available at *www.ftc.gov/os/caselist/0523091/0523091.shtm*
12. *FTC* v. *Edge Solutions, Inc.,* No. CV 07–4087–JG–AKT (E.D.N.Y., final order Aug. 29, 2008) (debt settlement), available at *www.ftc.gov/os/caselist/0723025/index.shtm*
13. *FTC* v. *Debt-Set,* No. 1:07–cv–00558–RPM (D. Colo., final order Apr. 11, 2008) (debt settlement), available at *www.ftc.gov/os/caselist/0623140/index.shtm*
14. *FTC* v. *Debt Solutions, Inc.*, No. CV06–0298 (W.D. Wash., final order June 18, 2007) (debt negotiation), available at *www.ftc.gov/os/caselist/0523002/0523002.shtm*
15. *FTC* v. *Leshin*, No. 0:06–CV–61851–WJZ (S.D. Fla., final order May 5, 2007) (credit counseling), available at *www.ftc.gov/os/caselist/0523146/index.shtm*
16. *FTC* v. *Integrated Credit Solutions, Inc.*, No. 8:06–CV–00806–SCB–TGW (M.D. Fla., final order Oct. 16, 2006) (credit counseling), available at *www.ftc.gov/os/caselist/0323244/0323244.shtm*
17. *United States* v. *Credit Found. of Am.*, No. CV06–3654 ABC (VBKx) (C.D. Cal., final order June 16, 2006) (credit counseling), available at *www.ftc.gov/os/caselist/0423044/0423044.shtm*
18. *FTC* v. *AmeriDebt, Inc.*, No. PJM 03–3317 (D. Md., final order May 17, 2006) (credit counseling), available at *www.ftc.gov/os/caselist/0223171/0223171ameridebt.shtm*
19. *FTC* v. *Innovative Sys. Tech., Inc.,* No. CV04–0728 (C.D. Cal., final order July 13, 2005) (debt settlement), available at *www.ftc.gov/os/caselist/0323006/0323006.shtm*
20. *FTC* v. *Nat'l Consumer Council, Inc.*, No. ACV04–0474CJC (JWJX) (C.D. Cal., final order Apr. 1, 2005) (credit counseling and debt settlement), available at *www.ftc.gov/os/caselist/0323185/0323185.shtm*
21. *FTC* v. *Debt Mgmt. Found. Servs., Inc*., No. 8:04–CV–1674–T–17MSS (M.D. Fla., final order Mar. 30, 2005) (credit counseling), available at *www.ftc.gov/os/caselist/0423029/0423029.shtm*
22. *FTC* v. *Better Budget Fin. Servs., Inc.*, No. 04–12326 (WG4) (D. Mass., final order Mar. 28, 2005) (debt settlement), available at *www.ftc.gov/os/caselist/0412326/0412326.shtm*
23. *FTC* v. *Jubilee Fin. Servs., Inc.*, No. 02–6468 ABC(Ex) (C.D. Cal., final order Dec. 12, 2004) (debt settlement), available at *www.ftc.gov/os/caselist/jubilee/jubilee.shtm*

Senator MCCASKILL. Thank you very much.

Thank you to all of the witnesses.

Let's talk a little bit about some of the details on this. When you were finally sued, Ms. Robertson, by Capital One, did Financial Freedom of America offer you any assistance, whatsoever, at the point in time that you received the lawsuit?

Ms. ROBERTSON. They said that, like, you know, Capital One would win the lawsuit and say I had to pay them $100 a month, well, they'd deduct that off their payment. Well, that's, how do I want to say—contradicting what I was trying to do.

Senator MCCASKILL. Right.

Ms. ROBERTSON. And they just said, "Well, we can't help that they sued, we don't have any control over the credit card companies." And I was—I sent all of the paperwork, they knew what was going on. And I just felt, this is where I should have done my due diligence, and checked this company out before I ever went with them.

Senator MCCASKILL. Was there anything at all that the company accomplished on your behalf?

Ms. ROBERTSON. Nothing, nothing.

Senator MCCASKILL. And it cost you—even with you complaining and being on the front page of *The New York Times,* it still cost you a net—how much are you out-of-pocket for what happened to you, total?

Ms. ROBERTSON. I paid them almost $4,000 and I believe I've gotten around $2,200 back from them.

Senator MCCASKILL. OK.

Ms. ROBERTSON. And I wouldn't have got the last back if they didn't know I was being interviewed by *The New York Times*.

Senator MCCASKILL. Let's talk about how big a problem this is. I know, Ms. Hrdy, that the FTC has brought numerous separate actions against debt settlement companies over the past 2 years, and it's my understanding, Mr. Angle, that you have a current lawsuit that you all are actually pursuing.

First, to you, Mr. Angle, do you have more than one lawsuit, currently, against debt settlement companies in Missouri, and if not, are there others that are pending? Have you seen an increase in the complaints? How big a problem is this?

Mr. ANGLE. It's a big problem. The landscape is changing with the enactment of the FTC rule and with your efforts. So, hopefully, the landscape will be changing in the other direction.

We have one case pending against Credit Solutions of America——

Senator MCCASKILL. There is not going to be a movie.

[Laughter.]

Mr. ANGLE. I didn't bring a Power Point presentation.

We have one case pending in St. Louis City Court against Credit Solutions of America. We have, probably, a dozen more investigative files that have been elevated to the enforcement level because of the groundswell of complaints. We've seen a doubling of complaints each year regarding consumers who were taken in and it's natural that they're taken in, because these claims are hitting them, as you said, when they're most vulnerable; they're looking for a way to honestly reduce their debts. And we see, probably, a minor percentage of the consumers in Missouri who are actually impacted by this because if it—and I have no reason to believe it doesn't—if it correlates with other consumer complaint activity, we only get a small percentage of folks to actually complain to our office.

Senator MCCASKILL. And so, one of the things we should talk about in this hearing today is making sure that consumers know that if they have signed up with a debt settlement company, they need to call the Attorney General's Office.

Mr. ANGLE. Yes, ma'am.

Senator MCCASKILL. The more people that call the Attorney General's Office, and there's a hotline number that is available at the Attorney General's Office for consumer complaints and we should certainly encourage consumers to do that. Because I think a lot of people are embarrassed, and don't know that there's strength in numbers—the more we know about, the more we can take action to try to help them.

What about from your perspective throughout the whole country? Are there any regions of the country that have fallen more victim

to this than others? And how big is—I know we were up to 2,000 companies, now. How big a problem is it?

Ms. HRDY. Based on the advertising, the pervasiveness of the advertising and the consumer complaints that we get, and that we get from the Better Business Bureaus, I think that this is a growth industry. We've just seen a real explosion in the advertising and increasing complaints as have the Attorney Generals.

And, in terms of whether it's more local or national—generally speaking, these are nationwide telemarketers that are saturating, I think, the airwaves across the country with ads, and getting consumers to sign up across the country.

In the mortgage foreclosure relief area, we've seen consumers principally in California, Florida, Arizona, Nevada—where we've seen the very worst of the market crash in the mortgage market really hit those consumers. So, I would project that where the foreclosure crisis is really hitting hardest is also where consumers are also being targeted for these credit card relief services.

Senator MCCASKILL. Let's talk about the claims that they make. I know that there's a principal and consumer law called substantiation. That is the notion that if you're, you know, it's like, "Buy this product, it will make you rich, famous, and thin," those kind of outlandish claims that are made, there are actually laws against that—making claims that cannot be substantiated.

The debt settlement industry often makes representations about their success. Tell us what the reality is of those claims that they're making, Ms. Hrdy, and what can be done to shut them down in terms of the false claims that they're using to trick people, like Ms. Robertson, into giving them their money?

Ms. HRDY. Yes, Senator. I think we all are very troubled by these, just, unqualified blanket claims, "We'll reduce your debt by 40 to 60 percent, or more." And, they're not qualifying them in the broadcast ads, and so they're leaving it all to the telemarketers to explain, "What does that mean?" A reasonable consumer is going to think, "OK, if I owe $10,000 now, and they're saying they're going to reduce it by 50 percent, I'm only going to have to pay $5,000 when it's all over." But we know from stories like Ms. Robertson's and other consumers that we've interviewed, that they're not counting the fees and penalties that the credit card companies will charge you as the program goes on, and especially if you're not paying on the debt, and the fees that the debt settlement company will charge you. So, it's not a 50 percent reduction; it's often far less.

And the debt settlement companies will often say that they're not taking that reduction based on the amount of debt you owed when you signed up, they're waiting until that debt balloons and saying, "Oh, no, but if you could see, the 50 percent reduction is after, you know, you've paid all of these—you have all of these fees and charges," and the debt has actually increased. So again, that's a smaller percentage.

Senator MCCASKILL. Well, and isn't it true that oftentimes these companies are not counting the people who dropped out?

Ms. HRDY. Oh, yes. And that's exactly right, Senator. So, when a consumer hears a claim, "We will reduce your debts by 50 percent," the law says, most consumers have to get that result. The

average consumer has to get that result in order for that claim to be true and substantiated. And so when, as you cited, the industry data itself says that only a third of consumers get results based on that one data sample, you can't say—make that blanket claim. That's a false claim.

Senator MCCASKILL. Up-front fees. I think that in the hearing in April some of the industry representatives said that banning up-front fees would decimate the industry, and I said, "That—well, that's a good thing. Nothing wrong with that." The ban is very important and does the industry model work? Can these companies even be profitable if we are successful in doing away with the up-front fees?

Ms. HRDY. Well, it's interesting, Senator, during our rulemaking proceeding, we did hear from a small—very small minority—but there were, there are for-profit debt settlement companies who say they are operating under what would be this advance-fee ban model. Whether they can make it——

Senator MCCASKILL. There are companies out there who are not charging up-front fees?

Ms. HRDY. Yes, a handful. I mean, not many.

Senator MCCASKILL. A handful out of 2,000?

Ms. HRDY. Exactly. That have come forward, and told us that they are trying to do this model. I mean, they have to capitalize, like any other business, in order to stay in business. But, that's what companies have to do.

The problem is, they're marketing these services like, you know, "Just go to your grocer's freezers and pull out your debt settlement." They're not engaging in what, we think, is the stringent, suitability requirement before they sign consumers up. Because for most—for many consumers, this is probably not possible. That's why they have these overwhelming dropout rates.

So, if they want to try to screen consumers and enroll consumers who, for whatever reason, can save for settlement—and save for fees, because, you know, if they do get a settlement then they should be able to get a fee—then there should be some companies who should be able to follow that model.

But, if the whole model is built on just on-boarding every consumer and just taking the fees up front, regardless of what happens afterwards, you know, we don't see that as a model that should succeed.

Senator MCCASKILL. Hasn't Missouri, Mr. Angle, already banned up-front fees by companies who assist with mortgage foreclosure?

Mr. ANGLE. Yes, that's true and there is also a statute on Missouri's books that deals with debt adjusters. And it, in some ways, is a permissive statute with regard to up-front fees, but as my colleague, Mr. Lehman, noted in the hearing in April, Missouri, like many States that have such statutes, they carve out the most prominent debt settler model, and basically the Missouri statute—which is in Chapter 425—says that you're not a debt adjuster unless you directly receive the money from the consumer.

So, we have an up-front ban that could be looked to in the mortgage modification industry, but we also have this other statute that's sort of a relic of times past in terms of what the modern debt settlement model is.

Senator MCCASKILL. I see.

Mr. ANGLE. Which is part of why I think it's important to look at the other actors who enable the debt settlement companies.

Senator MCCASKILL. Yes. And we're going to get to the third-parties in a minute, because I'm interested in that.

This notion that they're telling consumers to stop paying their bills. Now, the industry group, the association which is called The Association of Settlement Companies, TASC, their member companies supposedly are told they cannot direct potential or current clients to quit paying their bills. Obviously, there's a good reason you shouldn't encourage people to quit paying their bills. But, according to the testimony we heard—and I need both of you to comment on this—that's just not happening. That, in fact, I mean, Ms. Robertson, you were told to quit paying your bills, correct?

Ms. ROBERTSON. Yes, ma'am.

Senator MCCASKILL. That was the advice that you were given by the company you thought you had hired, was the best thing to do was to quit paying them and start paying Financial Freedom of America?

Ms. ROBERTSON. Well, I couldn't pay both.

Senator MCCASKILL. Right.

Ms. ROBERTSON. So, you know, I just thought that this was the way that I could get out of debt.

Senator MCCASKILL. And you assumed they were doing something——

Ms. ROBERTSON. Yes, I did.

Senator MCCASKILL.—with your creditors, and your creditors knew that you were in the process of working things out and that somehow they were going to hold in abeyance any efforts to collect the money that you owed to them.

Ms. ROBERTSON. Yes, but now listening to the other witnesses talk, with the fees going up, with the credit card and the late charges and all of that, how can they guarantee that your debt will be paid off in 3 years, because the estimations they made are not going to be the same?

Senator MCCASKILL. Right.

Ms. ROBERTSON. The credit cards are going to be more.

Senator MCCASKILL. Right.

Ms. ROBERTSON. So——

Senator MCCASKILL. It's like—it's like trying to get out of a hole and you keep digging deeper.

Ms. ROBERTSON. So, after 3 years, I can just hear them telling me, "Oh, we need a couple of more thousand dollars to settle this."

Senator MCCASKILL. Right, right.

Third-party processors—I'm trying to understand exactly how this works. The third-party processors are the people, is the institution that holds, "holds" the customer's money. Now, are these financially—are these financial institutions insured? Are these chartered financial institutions? Are these entities that are made up by the debt settlement companies for the purposes of holding, "holding" this money?

Ms. HRDY. The major player in this space is a company called Global Client Solutions, and they commented during our rulemaking. We understand about 80 percent of debt settlement com-

panies use Global Client Solutions. Global is not a bank. It has an account—it's called a Special Purpose Account—at an FDIC-insured institution—probably more than one. And what Global does is it's the account—it holds the Special Purpose Account, and then has all of these sub-accounts where it holds money for each consumer enrolled in a debt settlement company.

So, the good news is, that consumers that are putting their money into this account with Global Client—the account is FDIC-insured. So that—consumers' money is protected.

The less good news, and the concerns that we've had, is that Global Client Solutions is a third-party provider to the debt settlement company. And so, when the debt settlement company wants to get paid, it turns to Global and says, "See my contract with the consumer, I should get paid, now. And so the consumer, again, given our concerns about the prevalence of the deceptive advertising about the fees, they don't know that Global Client is sending money to the debt settlement company, because they don't even know that that money isn't being saved for settlement, it's being taken by this up-front fee.

So, some of the benefits of using the Telemarketing Sales Rule is that it has assisting and facilitating liability. So, these third-party providers, such as Global, if they are found to have knowledge of the violations that a debt settlement company is engaging in, they can be held liable under the Telemarketing Sales Rule. And, we intend to visit with Global, and any of the other major third-party providers and give them a copy of our compliance guide, and make sure that they understand what their responsibilities are under the law.

Senator MCCASKILL. Well, what is the purpose of Global?

Ms. HRDY. The purpose of Global is——

Senator MCCASKILL. I mean, because, why don't these companies just open——

Ms. HRDY.—bank accounts——

Senator MCCASKILL.—open bank accounts directly in an FDIC-insured financial institution? Why is this layer in here?

Ms. HRDY. Well, we—there are some, we think, who do directly open those FDIC-insured bank accounts. But, as we've seen in our cases, part of the telemarketing sales pitch is, "Don't worry, we're not going to hold your money," we, the debt settlement company. "We have this third-party, it's an arms' length transaction, your money's in an FDIC-insured bank account," true, "you can look at your account online," true, "don't worry, it's all taken care of. We're not taking your money." So, it fits within this whole idea that, "Don't worry, consumer, this is a good way to go, and we've got this third-party who will take care of your money, and it will sit there and grow, and so it won't be in your account, it won't be in our account, it'll be somewhere safe, saving for settlement."

Senator MCCASKILL. But, I guess, the advantage to the debt settlement companies is it's easier for them to pull the money out?

Ms. HRDY. Yes.

Senator MCCASKILL. Because there are not as many hoops to jump through as there would be if they put the money directly in a bank.

Ms. HRDY. Well, obviously, if the debt settlement company is the account holder, that's the easiest way to take the money, but it sort of raises a level of suspicion with the consumer if they're just giving all of this money into the debt settlement account.

Senator MCCASKILL. Right.

Ms. HRDY. So, in our—consumers that we've interviewed have said they felt very comforted by this representation that, "Oh, this Global Client Solutions, they're going to hold my money, and it's going to be safe."

Senator MCCASKILL. OK, here's the $64-dollar question—how much is Global Client Solutions making on this?

Ms. HRDY. That is a very good question and I don't think they told us what their revenues were in their public comment. I can check it, and let you know. But, they represent that they are holding millions and millions of dollars in these Special Purpose Accounts.

Senator MCCASKILL. And so, do we know what the debt settlement companies are paying—there has never been any information that you all are aware of, of what the debt settlement companies are paying Global Client Solutions for this?

Ms. HRDY. I don't think we know how much the debt settlement company is paying Global. We do know—and we've seen it in the consumer contracts—that the consumers are paying to use Global Client Solutions. It can be anywhere between $10 or $20 a month. Again, if this is a 36-month program, that monthly fee will add up. So, the consumers are paying to use Global Client Solutions.

Senator MCCASKILL. Well, does Global Client Solutions do anything else?

Ms. HRDY. No. That's it. They have a proprietary——

Senator MCCASKILL. This is it?

Ms. HRDY. This is it. As far as we know.

Senator MCCASKILL. Do you know who owns it?

Ms. HRDY. Yes. And we've interviewed them as part of the rulemaking process——

Senator MCCASKILL. Are they a debt settlement business?

Ms. HRDY. They were.

Senator MCCASKILL. Ah.

Ms. HRDY. And then they realized that——

Senator MCCASKILL. Somehow that doesn't surprise me.

Ms. HRDY.—there was a business model—yes. And they developed this proprietary software that is, basically houses these Special Purpose Accounts so that it splices out all of these consumer accounts. And as part of our rulemaking, we did reach out to the FDIC, because they have examined both the FDIC-insured banks that are holding this money, and they've been onsite at Global, to ensure that—and again, the good news is that, consumers who are putting their money into these FDIC-insured accounts, the money is insured.

Senator MCCASKILL. The problem is, it's not insured against the debt settlement company taking it.

Ms. HRDY. Exactly. Which is where the TSR comes in.

Senator MCCASKILL. They're insured against the problem that if the bank had some kind of structural issue in terms of solvency,

but they're not protected, because the debt settlement companies can get access to as much of it——

Ms. HRDY. Right.

Senator MCCASKILL.—as they want, essentially, at any time.

Ms. HRDY. Right.

Senator MCCASKILL. OK. So, we probably need to look at the legislation as it's currently drafted and see if we've gone far enough to get at the aiding and assisting to get a company like Global Client that clearly has been created for the purpose of assisting in the marketing of debt settlement product——

Mr. ANGLE. And the facilitation of taking the consumer's money, that—the consumer will often see an automatic—a line item on their primary bank account statement, that an automatic withdrawal has taken place, and it says Global Client Solutions on it. That, to us, is also another level of deception that the consumer has to punch through, it's just another actor in this scheme.

Senator MCCASKILL. I think we also ought to reach out as a committee and ask some specific questions of Global Client, and get their responses for the record. Because I think we need to at least find out whether they're willing to talk to us.

You know, one of the interesting things is, I asked this—getting information from these companies, it is ridiculously difficult to get these companies to tell us things. In fact, the representative of the industry at the April hearing actually said, on the record, that they would provide to me a list of their members. And they were supposed to have done that by August 1. We have not received that. Have you all had any more success than the Commerce Committee has had in actually getting important information in terms of profitability, ownership, you know, how many clients they actually have—do you all feel that you have, either at the State level or at the Federal level, as people who are trying to enforce the law, that you've been able to get information that you need from these companies?

Mr. ANGLE. No. We'll get it, though. Thus far, in our investigative and enforcement activities, the first line of defense is to delay. But we'll get it. We won't just stand on non-responsive or obstructive answers. So, the process is sometimes slow of enforcing our investigatory subpoenas, or going through the discovery process, and seeking a motion to compel information that we've asked for. And oftentimes, industry will hide behind this model and say, "Well, we don't hold any money, so we can't tell you how much we've taken from X or Y consumer," well, that's baloney. So, we have to punch through that.

Senator MCCASKILL. Isn't the information—don't they market that it's available online?

Mr. ANGLE. Yes. We have to—it's a circle of deception that you just have to keep punching through as an enforcement officer.

Senator MCCASKILL. Right.

Ms. Hrdy?

Ms. HRDY. We've had the same enforcement experience as Mr. Angle, in terms of getting information in specific investigations and litigation, but we will pursue and get it. And there are—in terms of the rulemaking, it was a real challenge to get them to provide us the information that we needed to asses the business model.

And our requests go back to September of 2008, when the Commission held a public hearing, and we put out questions to the industry, "Tell us, what is your model like, what are your success rates? How do you substantiate your advertising claims?" And we got nothing in response; very little. And—nothing meaningful. And it wasn't until we issued the Notice of Proposed Rulemaking that we started to get a little something more. But, the best of their data shows that two-thirds of these consumers who enroll, drop out.

Senator MCCASKILL. The FTC rule, I know, you've used your authority under the telemarketing statutes. Which is terrific, and I think it's great that you all did the rule. As I said before, many things in the rule mirror the legislation. We go a little farther, in terms of capping the fees. The other thing that the legislation does that you can't do—you can only get at the telemarketing. And, I'm assuming that since this marketing model has been so successful, and since we've seen this as such a growth industry, preying on vulnerable people, I'm assuming that some of this is being marketed directly over the Internet?

Ms. HRDY. Yes, I think there is some of that. I mean, we're going to be watching that very carefully because the channel is really critical. And I think we'll—I would project that the Commission will be very vigilant and very aggressive in pursuing cases where it's clear that they're trying to get around the telemarketing aspect of it.

Senator MCCASKILL. Marketing rule.

Ms. HRDY. We always have Section 5, if they are completely not using phones. And if they——

Senator MCCASKILL. Why don't you explain what Section 5 is?

Ms. HRDY. Thank you. Section 5 of the FTC Act prohibits unfair, deceptive acts or practices. Very broad grant of authority—it's channel-neutral. No matter how you market, if you make a deceptive claim or engage in an unfair practice, you've violated Section 5. Under the TSR, telemarketing does have to be involved. So, if they move away from that model, that will be a concern. And, although we do have Section 5, that's definitely an area where your legislation would fill in.

Senator MCCASKILL. The GAO investigation, I want to put in the record some of the specifics of the investigation that was done. The GAO investigators called 20 well-known debt settlement companies and posed as consumers. The GAO did this so we could learn what the industry was actually doing. It is these undercover investigations where you really expose what is happening to people like Ms. Robertson.

Here's what happened when these auditors posed as consumers. Of the 20 companies GAO called, 17 of them collected up-front fees before ever making any attempt to settle any debt. Nearly all of the companies advised the consumers to stop paying their credit card bills, including their accounts that were current. So, they not only were telling them to quit paying the ones they're behind on, we're going to instruct you to get behind on every account. In other words, give us all the money you have for as long as we can get it from you, and then we'll leave you to deal with the wreckage left behind. That's, essentially, the model that GAO found.

The GAO also found that they made fraudulent and deceptive claims about their success rates, and some made claims, as you indicated earlier that they were linked to government programs, like we're, "This is a government program, we can help bail you out." And, do you think that with the findings that GAO found, is that actually in sync with what FTC has found, and with what you have seen on the State level?

Ms. HRDY. Yes.

Senator MCCASKILL. And, Mr. Angle?

Mr. ANGLE. It certainly is. Our consumer complaints which are our primary vehicle for learning what consumers are told by these entities are very consistent along that line. "Quit paying, quit communicating," that's a very important piece of it, too. Because the creditor—this is an industry that abuses debtors as well as creditors. That's a pretty unique combination. And, when you quit paying, there are consequences, and when you quit communicating, those consequences are enhanced. And the deceptive things that are told to consumers, as reflected in our complaints, include the litany of what was listed in the GAO investigation, too. "We'll improve your credit score," well, that's not true. "We'll get you out of debt in 3 years," that's not true. "All of the major creditors work with us." That's a key piece of material information that is omitted from their advertisements and communications frequently, is there are a number of major creditors who just won't deal with these people. And if they were told that up front, consumers would say, "Well, wait a minute, all of my credit card accounts are with creditors who won't deal with you, so I'm not going to sign up with you." The layers of deception are very consistent, the model itself, regardless of the debt settlement entity is generally the same, and that's reflected in our complaint information.

Senator MCCASKILL. You know, in the Commerce Committee we have—and I know in your every day work—both of your work, your life's work now is looking after consumers. And there are so many places that consumers are taken advantage of—so many places where they have deceptive marketing techniques that are used on them. But there really is a special place in hell for people who prey on the most vulnerable. Who have found a business model that takes advantage of people when they are at their most desperate state, in terms of trying to pay their bills, keep food on the table, and provide for their families. I know that the industry thinks that they're going to be able to somehow wiggle through the efforts that are ongoing to clamp down on these practices. This hearing just reaffirms, in my mind, that we've got to be tenacious about this. And we should not be afraid of their claims that we are going to "put them out of business." Well, that would probably be a good day's work. If we could put them out of business. Because there are ways that you can help people who are in financial trouble. There are credit counseling agencies that work, in good faith, on a model that is not front-loaded with the consumers' money. I can imagine that the credit card companies can't stand these guys, because all of the money they're collecting is, in fact, the very money that could be used to begin to pay down on significant debt that so many Americans now are facing.

I want to thank all of you. Is there anything else that you want to add to the record that I have not asked today, or anything else that we need to add to the record before we conclude the hearing?

Ms. ROBERTSON. No, I don't have anything.

Senator MCCASKILL. Anything else that needs to be added?

Mr. ANGLE. Just thank you very much, Senator, for your attention to this issue. It is a very powerful moment when State, and Federal agencies and legislative bodies can get together. Thank you.

Senator MCCASKILL. It is a special moment when we can have a Federal hearing at a local level with the Federal Government and the State Government both represented, with everyone on the same page, with everyone trying to accomplish the same goal. And I have a feeling, if we stay focused on this—because these are bad guys, and we need to clean this up—I think that we're going to be able to get it done.

We will keep the record of this hearing open. We will reach out to the third-party entities that are a player in this that, clearly, I don't think, maybe have gotten the scrutiny they deserve. I thank you for that suggestion, Mr. Angle, and we'll look at the legislation to see if we need to add any provisions in the legislation to deal with these third-party entities. And, I'm optimistic about the passage of this legislation. Probably not during the silly season—we are now in the silly season where we can't even agree on motherhood and apple pie in Washington at this point, but once we get past the elections, we'll get back down to work, hopefully, and we'll quit playing political games that seem to be ongoing right now. And I think that there's a chance that we can add this legislation to a number of different legislative vehicles that will be moving through the Senate.

So, thank you all for being here today, and the hearing is concluded.

[Whereupon, at 11 a.m., the hearing was adjourned.]

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