

The Rapidly Changing Legal Landscape: Keeping It All in Perspective and What Every Debt Settlement Company Needs to Know

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Introduction

- Overview: The Laws that Apply to Debt Settlement Companies
- State Debt Adjusting Law Update
 - Uniform Debt-Management Services Act (UDMSA)
 - Pending State Debt Adjusting Statutes
- Law Firm Affiliations
- Unauthorized Practice of Law
- Federal Trade Commission Act and Enforcement
 - FTC Act / Mini-State FTC Acts
 - CROA
- Marketing / Advertising / Lead Generation
- Questions and Answers

Overview of Laws that Apply to Debt Settlement Companies

- State Debt Adjusting Statutes
- Check Seller/Bill Payer Laws
- Unauthorized Practice of Law Statutes
- Home Sales Solicitation Statutes
- FTC Act and State Unfair and Deceptive Acts/Practices Laws
- Federal Credit Repair Organizations Act and State Credit Services Organization Acts
- Others

The Legal Landscape for Debt Settlement Companies

Nearly *all* of the states regulate debt adjusting; few exempt tax-exempt 501(c)(3)s; only two states prohibit “debt adjusting” for compensation; only 2 states and DC do not regulate debt adjusting. Additionally, there are *a number of other state laws* debt settlement companies must navigate (*e.g.*, qualification to do business as foreign corporation, FTC Act, CROA, mini-FTC Acts, mini-Credit Repair Organization Acts, unauthorized practice of law restrictions, check seller/bill payer laws, etc.).

State Debt Adjusting Law Update

State Debt Adjusting Laws

48 States

Debt
Adjusting
Laws

Virtually all of
these laws apply
based on the
state of
residence of the
client.

Debt Adjusting Statutes

48 States

**Exemptions
and Exclusions**

A debt settlement company that services clients nationally in the U.S. must typically register and/or obtain licensure in approx. 30 different states before it starts to provide negotiation services to clients in these states.

Vary from state to state (in some cases, depends on whether debt settlement company touches or controls client funds destined for creditors.)

The Debt Adjusting Laws cover...

In California:

Prorater means a person who, for compensation, *engages in whole or in part in the business of receiving money or evidences thereof* for the purpose of distributing the money or evidences thereof among creditors in payment or partial payment of the obligations of the debtor.
(California Proraters Law)

In Delaware / Rhode Island / Utah:

“Debt-management services” means services as an intermediary between an individual and 1 or more creditors of the individual for the purpose of obtaining concessions, but does not include:

- (a) legal services provided in an attorney-client relationship by an attorney licensed or otherwise authorized to practice law in this state;
- (b) accounting services provided in an accountant-client relationship by a certified public accountant licensed to provide accounting services in this state; or
- (c) financial-planning services provided in a financial planner-client relationship by a member of a financial-planning profession whose members the administrator, by rule, determines are: (i) licensed by this state; (ii) subject to a disciplinary mechanism; (iii) subject to a code of professional responsibility; and (iv) subject to a continuing education requirement.

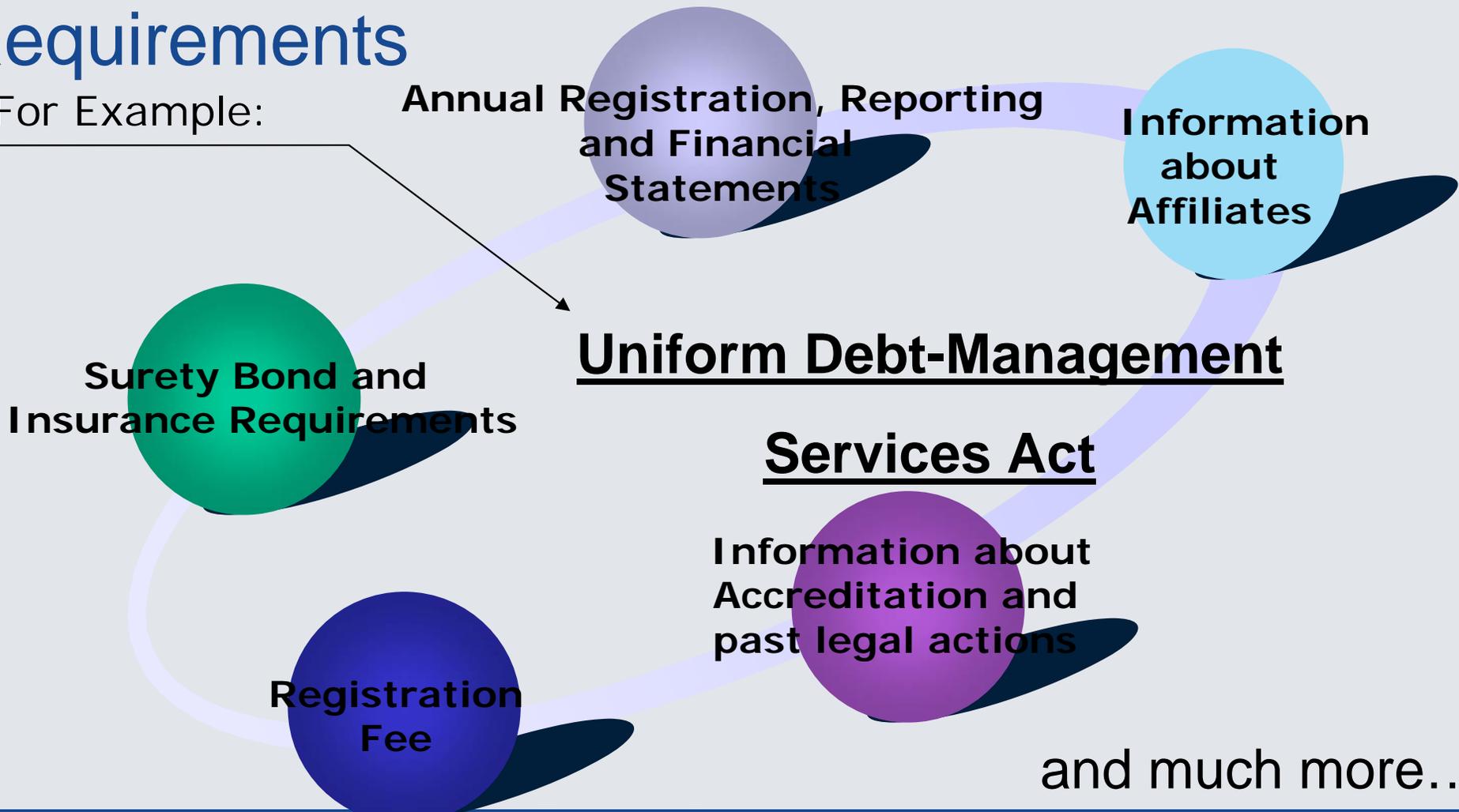
Texas:

Debt management service means:

- the receiving of money from a consumer for the purpose of distributing that money to or among one or more of the creditors of the consumer in full or partial payment of the consumer's obligations;
- arranging or assisting a consumer to arrange for the distribution of one or more payments to or among one or more creditors of the consumer in full or partial payment of the consumer's obligations; OR
- exercising control, directly or indirectly, or arranging for the exercise of control over funds of a consumer for the purpose of distributing payments to or among one or more creditors of the consumer in full or partial payment of the consumer's obligations.
- Regulation: The rules contained in this chapter of this title do not apply to business relationships or agreements that purport to assist consumers with their debts to the extent that consumers' funds are not deposited into an account under the control of the person or business entity who is assisting the consumers with their debts.

Typical State Debt Adjusting Registration Requirements

For Example:



Violations of State Debt Adjusting Statutes

- Common failures to adhere to specific statutory requirements include:
 1. Licensure/Registration, if applicable
 2. Fee Caps
- Using unfair or deceptive acts or practices or engaging in fraudulent conduct that creates a likelihood of confusion or misunderstanding.

Possibly Criminal Misdemeanor / Felony

State Debt Adjusting Statutes Fines and Penalties

Example - UDMSA



The law authorizes the imposition of restitution and penalties of up to \$10,000 per violation (or more). In addition, the law authorizes private remedies against debt settlement companies not registered under the Act (e.g., actual and punitive damages and attorneys fees). (Some violations of debt adjusting statutes carry criminal penalties.)

Uniform Debt-Management Services Act

Uniform Debt-Management Services Act

- Effective July 1, 2007 in Utah (amends provisions of UT CSOA); Effective March 31, 2007 in Rhode Island; Effective January 17, 2007 in Delaware.
- In 2007, introduced in Colorado, Hawaii, Maine, Missouri, and other states.
- Study Committee in Wisconsin (vote pending)
- Roadmap for other states to either adopt/amend and/or interpret existing debt adjusting statute

Uniform Debt-Management Services Act

- Regulates debt-management companies by requiring them to register with the state.
- To obtain a certificate of registration, a provider must supply information about itself, obtain insurance against employee dishonesty, and post a surety bond to safeguard any money that it receives from individuals for payment to creditors.

Uniform Debt-Management Services Act

- Regulates interaction with consumers, including steps to be taken before entering into an agreement with an individual, the content of an agreement (including limitations on the fees that may be charged), and provisions concerning the performance and termination of agreements.
- Includes broad prohibitions applicable to debt settlement companies.
- Enforcement both by a state agency and by private individuals, including rule-making authority on the part of the administrator and recovery of minimum, actual and, in appropriate cases, punitive damages in private enforcement actions (e.g., class actions).

UDMSA: Advertising

- The UDMSA requires providers to make certain disclosures when advertising. The required disclosures include the impact of debt-management services on credit ratings and the likelihood of collection efforts in an easily comprehensible manner. ***Under the UDMSA, a third party advertiser on behalf of a provider is viewed as an agent, and the provider can be liable if the advertisement fails to comply with these requirements.***

UDMSA: Liability for the Acts of Third Parties

- The provisions of the UDMSA impose duties and obligations on providers and on independent contractors, if they fall under the definition of provider, or as a person that caused the provider to violate the UDMSA.

Pending State Legislation and Activity

Pending State Legislation and Activity

- Colorado (UDMSA and UDSSA)
- Hawaii (UDMSA)
- Maine (UDMSA)
- Maryland (amendment to current Debt Management Services Act)
- Michigan
- Missouri (UDMSA and HB 329)
- North Carolina (Extend Current Law)
- Rhode Island (corrections)
- Wisconsin UDMSA Study Committee
- Rule Making: Delaware, Rhode Island and Utah

Law Firm Affiliations

Attorney Exemption from State Debt Adjusting Laws – Fact or Fiction?

In general, the attorney exemption in state debt adjusting laws are only available to attorneys who are licensed to practice in a particular state; the exception recognizes that a duly licensed attorney is frequently called upon to negotiate debts on behalf of clients in connection with the practice of law. In such instances, further licensure (beyond the state bar license to practice law) is not required.

* * * * *

Example: UDMSA exempts only legal services provided within an attorney-client relationship by an attorney licensed within the state to practice law.

Unauthorized Practice of Law

Unauthorized Practice of Law (cont'd)

- UPL is regulated by the States. Definitions Vary.
- Some factors that give rise to UPL (e.g., West Virginia):
 - evaluating the consumer's financial circumstances to determine whether debt settlement is an advisable plan for a particular consumer,
 - negotiating with creditors on behalf of consumers to achieve account settlements, and
 - charging a contingency fee based upon a percentage of the amount allegedly saved in a settlement

Unauthorized Practice of Law (cont'd)

- Steps to Minimize the Risk of UPL (when debt settlement is not considered inherently UPL):
 - Refrain from exercising the consumer's FDCPA rights
 - Avoid Threatened Legal Action
 - Limited Power of Attorney-in-Fact
 - Bankruptcy? Do you discuss it?
 - "We are not lawyers. Consult an attorney"
 - Adopt Rules, Procedures, and Safeguards

Federal Trade Commission Act

Federal Trade Commission Act

- The FTC Act [15 U.S.C. §§ 41 *et seq.*] is a statute of more general application than the Credit Repair Organizations Act. It prohibits “unfair or deceptive acts or practices in or affecting commerce.” This general proscription applies to the operations of both credit repair companies and debt settlement companies.
- Credit counseling, debt settlement, credit repair organizations, and debt collectors have all come under the FTC Act enforcement umbrella.

Dissecting Common Advertising Claims

- Claim #1: Debt Settlement Company can cancel debt by using “secret programs.”
- Claim #2: Debt Settlement Company works with credit-card issuers to cancel outstanding debts.
- Claim #3: Debt Settlement Company can cancel up to _____% (e.g., 60%, sometimes greater, or a range) of outstanding credit-card debt.
- Claim #4: We can stop your creditors from calling.
- Claim #5: Your credit will improve when finished with the program...

Claim #1: Debt Settlement Company can cancel debt by using “secret programs.”

- Puffery?
- Proprietary Method?
- Readily known to the routine consumer?

Claim #2: Debt Settlement Company works with credit-card issuers to cancel outstanding debts.

- Does debt settlement “cancel” outstanding debts?
- Is this a promise that the debt settlement company can keep?

Claim #3: Debt Settlement Company “can eliminate *up to* ___% of your credit card debt”

- The use of the phrase “up to” does not grant an advertiser license to promise only its most dramatic results.
- An “up to” claim should reflect the performance or result that can typically be achieved.
- Not solely based on just the creditors that settle but the totality of the client’s experience.

Claim #4: We can stop your creditors from calling.....we end harassing phone calls!

- Who has the FDCPA rights?
- Make a distinction between creditors and collection companies.
- Substantiation

Claim #5: Your credit will improve when finished with the program...

- Disclose the negative credit consequences
- Can a debt settlement company disclose the negative consequences of credit but then describe the benefits a consumer will have when they complete the program?
- What about CROA?

Avoiding an Investigation from the FTC / State Attorney General (or BBB/NAD)

•It is very important that marketing / advertisements / enrollment materials for debt settlement are:

- Truthful;
 - Accurate; and
 - Reasonable.
- Do not over-promise the services offered or the results that can be delivered.
- Make the appropriate affirmative disclosures (*e.g.*, costs, risk of suit, impact on credit score, consumer's obligations, income taxes, creditor participation etc.).

Credit Repair Organizations Act

Credit Repair Organizations Act

The Credit Repair Organizations Act became effective on April 1, 1997, and is directed to the credit repair industry.

The term "credit repair organization"—

- (A) means any person who uses any instrumentality of interstate commerce or the mails to sell, provide, or perform (or represent that such person can or will sell, provide, or perform) any service, in return for the payment of money or other valuable consideration, for the express or implied purpose of—
- (i) improving any consumer's credit record, credit history, or credit rating;
or
 - (ii) providing advice or assistance to any consumer with regard to any activity or service described in clause (i).

CROA and Debt Settlement Companies?

- In *Plattner v. Edge Solutions, Inc.*, 422 F.Supp.2d 969, 2006 WL 763651 (N.D. Ill. March 22, 2006) the court recognized, that "[w]hether [an apparent debt settlement] company is a credit repair organization under the CROA depends on the representations made [to consumers]." *Plattner*, 2006 WL 763651 at *4.
- *In re National Credit Mgt. Group, LLC*, 21 F.Supp. 2d 424 (D.N.J. 1998), the court, in a case brought by the FTC, agreed with the FTC's position that certain educational and credit monitoring programs of a type offered by the credit counseling agency were governed by the CROA.

State Credit Services Organization Acts (CSOAs)

- $\frac{3}{4}$ of all states have CSOAs
- Broader Applicability
- Bonds
- Few Exemptions
- May have requirement inconsistent with typical debt settlement company business models
- Prohibition on advance payments
- Registration

CROA: REQUIREMENTS

- CROA requires full disclosure regarding consumer rights before any contract for credit repair services is executed. A written statement must be provided and signed by all prospective customers, and must be retained by the credit repair organization for at least two years after the statement is signed.
- Written Contract
- Accepting Payment in full until services are completely rendered
- They have the right to cancel a contract with any credit repair organization for any reason within three business days from the date it was signed.

CROA: Penalties

- CROA includes civil penalties for violations and procedures for administrative enforcement by both the FTC and the states.
- CROA includes a private right of action.

CROA: Waiver of Rights

A consumer cannot waive his rights under the CROA.

- Any waiver of any protection afforded by the CROA is treated as void, and contracts that are not in compliance with the Act's provisions may not be enforced by any federal or state court.

Sales / Marketing / Lead Generation

Questions and Answers: Keeping it All In Perspective

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