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Via E-mail/Confirmation by U.S. Mail

Alice Saker Hrdy
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Federal Trade Commission
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Re: Comments Submitted in Connection with the FTC Debt Settlement Workshop

Dear Ms. Hrdy:

On September 25, 2008 the Federal Trade Commission (“FTC”) hosted a workshop to examine the debt settlement industry. In addition, the FTC solicited comments on a number of topics of interest to the industry. On behalf of Morgan Drexen Integrated Legal Systems (“Morgan Drexen”), I write to express our concerns regarding one topic in particular, legal and regulatory issues facing the industry.

Since March 2007 Morgan Drexen has provided comprehensive administrative support services to attorneys and law firms that represent consumers in unsecured credit and other finance matters, including managing and conducting debt negotiation and debt settlements. Morgan Drexen seeks to reduce the administrative burden these attorneys face by, among other things, qualifying debtors for debt settlement services, overseeing statement processing, generating automated billing slip statements, managing communications with consumers, negotiating with creditors, and processing settlement documents and payments.

As an active participant in the debt settlement industry, Morgan Drexen is concerned about the patchwork of state laws that currently regulate the debt settlement industry. Morgan Drexen believes that debt settlement companies – for profit-companies that attempt to work with consumers and creditors to discharge consumer debt for less than the full amount owed – provide an important service for consumers whose hardship precludes paying off the entire debt; who wish to avoid declaring bankruptcy; and who are ineligible, or (for many valid reasons) do not want to work with credit counseling¹ services.

State laws vary significantly in their treatment of debt settlement companies. This variance in state laws significantly increases compliance costs for those involved in the industry, in some cases, limits consumers’ ability to select the credit-related service that best fits their needs, and in times of recession retards market-driven solutions to clearing unsecured debt that impairs the

¹ We use the definition of “credit counseling” supplied by the FTC in its request for comments: “[S]ervices offered by non-profit agencies that assist consumers in repaying their debts through budgeting, financial advice, or debt management plans.”



nation's economy. Accordingly, I believe that a federal law is the proper means by which to regulate debt settlement.

The National Conference of Commissioners on Uniform State Laws has drafted a Uniform Debt-Management Services Act ("Uniform Act") that attempts to establish some consistency in state laws' treatment of the debt settlement industry. While this attempts a step in the right direction, the value of the Uniform Act is only as great as the number of states that adopt it. Moreover, despite its name, the Uniform Act permits states to adopt different positions concerning a fundamental aspect of the industry—the ability of for-profit entities to engage in debt management services. *See* Uniform Debt-Management Services Act, Prefatory Note at 4 ("The Act is neutral on the question whether for-profit entities should be permitted to provide debt-management services. Each state must decide whether to permit for-profit entities to provide credit-counseling services, debt-settlement services, or both."). In this respect, the Uniform Act offers little improvement over the current state of the law. Moreover it addresses detrimental practices by those who would handle services for consumers. It does not address acts or actions by the suppliers of credit that exacerbate the hardship for consumers.

Navigating state laws presents a major obstacle for the success of many debt settlement companies. At one extreme, states like North Carolina have almost entirely banned debt settlement services. *See* N.C. Gen. Stat. § 14-424 (2008) ("If any person shall engage in, or offer to or attempt to, engage in the business or practice of debt adjusting, or if any person shall hereafter, offer to act, or attempt to act as a debt adjuster, he shall be guilty of a Class 2 misdemeanor."). North Carolina has established limited exceptions to its prohibition, most notably for attorneys and non-profit organizations, but these exceptions do not encompass many companies that assist consumers in addressing their problems related to debt.

Other states have adopted narrow definitions of debt settlement that, at best, create confusion, and, in other instances, leave segments of the industry unregulated. California's "prorater" law, for example, arguably extends only to those debt settlement companies that actually manage a trust account for consumers.² *See* Cal. Fin. Code § 12002.1 (2008) ("A prorater is 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.").

Still other states have complex regulatory schemes that mandate licensing requirements, the use of surety bonds, continuing professional education requirements, and mandatory disclosures. *See, e.g.* S.C. Code. Ann. § 37-7-101 (2008), *et seq.* In and of themselves, each of these requirements is useful in helping to protect vulnerable consumers from unscrupulous business

² There is some authority to suggest that California's prorater law is broader than the plain language suggests, *see Nationwide Asset Servs., Inc. v. DuFauchard*, 79 Cal. Rptr. 3d 844 (Cal. Ct. App. 2008), though neither the legislature nor the California Supreme Court has addressed the subject.



practices. Viewed against the backdrop of a complicated web of state laws, however, such detailed regulatory approaches inevitably increase compliance costs, which are most likely passed on to consumers, and can create pitfalls for unsuspecting companies unfamiliar with local practices.

Morgan Drexen takes as a given that well-managed debt settlement companies provide value to consumers and fill an important market-driven need with services for “near-bankrupt” consumers attempting to manage their debt. Unfortunately, the current regulatory environment imposes unnecessary costs and makes it difficult for legitimate industry providers to flourish without fear of idiosyncratic regulatory or enforcement initiatives. Debt settlement companies typically service clients from across the nation, and the costs of complying with the laws of each state can be prohibitive. Yet by its very nature, debt settlement tactics tend not to vary from state-to-state, which augurs for a national, not a state-to-state regulatory approach.

The most efficient way to regulate the industry for the benefit of consumers and debt settlement companies, and to partially address the unsecured debt crisis in the national economy, is for Congress to pass legislation that recognizes the debt settlement industry and establishes uniform standards that debt settlement companies must meet. Such standards might include: Annually audited financial documents confirming a **minimum capitalization** of at least \$250,000; a **fidelity bond** that covers every employee who has access to trust accounts in which a debtor’s funds may be held; an independent **annual audit** of trust accounts; an independent **accreditation of minimum business practices** including adequate infrastructure to service clients; a requirement for independent **screening of all employees** to assure no history of breaching fiduciary obligations; and independent **legal counsel review of all settlements** to assure a debtor’s rights are neither improperly nor insufficiently protected.

Morgan Drexen appreciates the FTC’s efforts to learn more about this industry. We hope these comments will be useful. Morgan Drexen also hopes that the FTC’s workshop is just the first step in a partnership with the industry to ensure that consumer’s debt settlement needs are being served honestly, efficiently, not-deceptively, and not unfairly. If Morgan Drexen can be of any further assistance, please do not hesitate to contact us.

Sincerely yours,

Walter Ledda
Chairman & C.E.O.