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Our Opinion: Put curbs on debt settlement companies

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In 2005, Illinois passed the Payday Loan Reform Act because lawmakers and consumer advocates believed some payday lending practices were landing borrowers in heavy debt.

Now lawmakers and consumer advocates are taking aim at another consumer finance industry, this one promising to get people out of debt.

The for-profit debt settlement industry, they say, entices consumers saddled with heavy credit card debt by offering to settle with creditors for amounts far less than those owed. What consumers often get, however, are heavy up-front fees, greater damage to their credit rating and, ultimately, even more debt.

The Illinois Debt Settlement Consumer Protection Act would do to the debt settlement industry in Illinois what the payday loan reforms did for that business. It wouldn't put them out of business, but it would impose restrictions and create safeguards that would, advocates hope, prevent consumers from unwittingly

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making their already heavy debt load even worse.

It passed in the Illinois House on March 25 by a 106-9 vote. It ought to be a slam dunk to pass in the Senate.

From our perspective, the for-profit debt settlement companies and practices targeted in the bill (HB 4781) are particularly troublesome for two reasons. First, their alluring TV and radio ads make unreasonable promises to appeal to the desperation of those facing huge debt. Second, whether it is intentional or not, these companies easily can be confused with legitimate, not-for-profit consumer credit counseling operations that really do help their clients get out of debt.

Typically, the schemes operate like this: A company promises to reduce a person's credit card debt by 40 percent to 50 percent. First, the consumer must pay a fee of 15 percent to 20 percent of his or her total debt. The companies target customers with heavy debt — usually $10,000 or more — so the initial fee is accordingly heavy.

"For the first few months, all they're doing is taking their fee. They're not actually doing any work to talk to your creditors and negotiate a settlement," says Attorney General Lisa Madigan. "In the meantime, they tell you to stop paying your creditors, to stop paying your credit card bills. By doing that, you have late fees tagged on, your interest rate often goes up because of that, and so you end up with more debt and they still haven't contacted your creditors."

It can get worse from there. Some creditors won't work with debt settlement companies, and will sue a person when they learn of the debt settlement arrangement. When that happens, consumers are on their own because debt settlement companies can't represent them in court. Meanwhile, creditors continue to hound debtors for payment. (Conversely, nonprofit consumer counselors work directly with creditors to arrange a payment plan, often with interest eliminated or reduced, and make the collection calls stop.)

"What we have learned is that 65 percent of people who initially enroll with debt settlement companies drop out before any communication (with creditors) has been made. Before any of their debt has been settled at all," says Madigan, whose office has seven lawsuits pending against debt settlement companies. "Those people don't get a refund. They don't give you your up-front fees back, they don't give you your ongoing fees back. You still owe them whatever you signed up for based on that contract."

Worse, 30 percent to 40 percent of those who enroll ultimately end up filing for bankruptcy, Madigan says.

We're not against companies making a profit filling a legitimate niche, just as we don't outright oppose the short-term lending offered by payday lenders. But the practices described by Madigan should not be allowed in Illinois.

The bill now before the Senate would eliminate up-front fees except for a $50 enrollment fee. It would require refunds to customers who drop out and would allow companies to charge fees based on what they save a customer, not what the customer owes to creditors. Settlement companies would have to be licensed by the Illinois Department of Financial and Professional Regulation. They wouldn't be allowed to offer the kind of blatantly bad advice they now give — like telling people to ignore their bills.

People saddled by heavy unsecured debt already are paying for their bad judgment. They shouldn't get hit again by those who promise to help.

Events scheduled to mark Money Smart Week

This week the Federal Reserve Bank of Chicago is sponsoring hundreds of events around the state to mark Money Smart Week.

Among them are two 90-minute sessions at 11:30 a.m. and 2 p.m. Monday that deal specifically with consumer debt issues.

"All about Credit and Debt Management" will feature Michael Hicks from Central Illinois Debt Management and Credit Education Inc. offering advice on how consumers can establish, maintain or restore their credit.

The session will be held at United Way of Springfield, 1999 Wabash Ave, Suite 107. It's free, open to the public and refreshments will be provided.

Consumers seeking help with debt can start by visiting Central Illinois Debt Management and Credit Education's Web site at www.cidmce.org or calling (888) 671-2227.

For a full schedule of Money Smart Week events in the Springfield area, visit the Federal Reserve Bank of Chicago's Web site at www.chicagofed.org. Select "education" then click "Illinois" under the Money Smart Week column. Click the "online calendar" link and you can search for events in Springfield and several other regions throughout the state.

Comments (2)

curiosity KTC *2 hours ago* Report Abuse

Wouldn't effort be better expended in not allowing people to get into such deep debt to begin with? And if that is considered too 'invasive' to any supposed freedoms, then so should 'rescuing' the numbskulls after the fact.
In other words, pass a limit on the amount of debt ANYONE can individually assume, or stay out of the affair entirely. Attacking any problem at the beginning rather than the end makes a heck of a lot more sense. The 'people' are being provided what they 'want', not what they need. The 'people' seldom want what they need, it doesn't taste as sweet nor fill all the empty shelves with STUFF. Government is again blaming the messenger, when the message should be the point of attack.

Conservative Democrat *2 hours ago* Report Abuse

This is a good start. Now they should go after trade schools charging large amounts for tuition to train for jobs that will never pay enough to cover all of the loans the student took out.

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