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State Law Update

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2010 State Law Update: New Debt Settlement Laws Become Effective In Three States on July 1, 2010

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This summer three U.S. states will implement new laws governing debt settlement companies that operate within their borders or market to their residents. New statutes have been enacted in Indiana, Nevada and Tennessee, and all three will take effect on July 1, 2010.

Proposed new debt settlement legislation is under consideration in many other states including, notably, in Illinois, where H.B. 4781 was passed by the state legislature subject to approval by Governor Pat Quinn, and in California, where A.B. 350 continues to be scrutinized by the Senate Judiciary Committee.

Finally, Mississippi has re-approved its existing debt settlement law and will continue to enforce its provisions.

Indiana

Indiana's new law will require debt settlement companies to obtain a $25,000 surety bond, which must be filed with the state's attorney general, and make certain disclosures to consumers before doing business in the state or entering into contracts with state residents. *See* Indiana Code § 24-5-15-2 et. seq.

The new statute subjects debt settlement companies to the same requirements and restrictions that previously governed credit repair, loan modification and loan consolidation companies. The law redefines the term "credit services organization" to include a person or entity that sells, provides or performs debt settlement services for compensation on behalf of a buyer.

Before executing a contract or agreement with a buyer or receiving any money, the new law requires debt settlement providers to deliver a set of written disclosures, including a description of the nature and cost of the services to be provided, the consumers' right to proceed against the company's surety bond, and the consumer's right to review or obtain or dispute the completeness or accuracy of any file on the consumer maintained by a consumer reporting agency.

Significantly, the law does not include any restrictions on the timing or amount of fees that may be charged to consumers by debt settlement providers.

Nevada

Beginning on July 1, 2010, debt settlement companies operating in the state of Nevada and/or serving Nevada consumers will be governed by a new law that is based on the Uniform Debt Management Services Act (UDMSA). The statute requires debt settlement companies to register with the state's Commissioner of Financial Institutions, obtain a surety bond in the amount of $50,000 and obtain a $250,000 insurance policy. Among other requirements, debt settlement providers will also be required to make specific consumer disclosures, offer counseling services and provide a complete list of goods and services offered.

The new law includes limitations on the amount of fees that can be charged for debt settlement services as follows:

- **Set up fee:** the lesser of 4% of the enrolled debt or $400
- **Monthly fee:** no more than $10 per creditor, up to a maximum of $50
- **Settlement fee:**
  - **Flat fee:** no more than 17% of the consumer's enrolled debt that may be collected in equal installments over at least half the contract period; **or**
  - **Savings fee:** no more than 30% of the consumer's savings as of the time of the settlement up to a maximum of no more than 20% of the amount of the consumer's enrolled debt.

Tennessee

Effective July 1, 2010, Tennessee will impose new obligations on debt settlement providers, but will also allow them to charge higher fees for their services than in the past. *See* Tenn. Code § 47-18-5401 et. seq. The state has implemented new provisions that are consistent with the UDMSA, replacing the existing law, which was designed to regulate debt management companies that held and distributed consumer funds.

The new law requires debt settlement providers to register with the Division of Consumer Affairs and obtain a $50,000 surety bond and a $250,000 insurance policy. The law also requires specific contractual provisions and disclosures to consumers.

The new law expands the kinds and amounts of fees that may be charged by debt settlement providers, allowing the same set up, monthly and settlement fee structures as are described above for Nevada's UDMSA-based law.

Illinois

On May 6, 2010, the Illinois legislature passed the Debt Settlement Consumer Protection Act (H.B 4781), which will have a significant effect on debt settlement companies operating in the state if it is enacted. The proposed new legislation was submitted to the Governor on June 4, 2010, and would take effect immediately upon approval.

If enacted, the new law would prohibit upfront and monthly fees, allowing only a one-time initial fee of $50. After that, the only additional fees that could be charged to consumers would occur upon the settlement of a debt and would be limited to no more than 15 percent of the savings obtained for the consumer.

The proposed new law would require debt settlement companies to be licensed by and obtain a $100,000 surety bond. It would also require that certain disclosures be provided to consumers, prohibit debt settlement companies from telling consumers that they should stop payments to creditors and allow consumers to cancel their contracts at any time.

California

As of this date, the proposed Debt Settlement Service Act (A.B. 350) remains stalled before California's Senate Judiciary Committee. Author Theodore Lieu (D-Torrance) recently requested that the Committee postpone a scheduled hearing to reconsider the current proposal, and a legislative analysis published on June 30 recommended additional negotiations to try to resolve disputed issues between industry proponents and consumer advocates.

The current version of the bill provides for the licensing of debt settlement providers, as well as numerous other compliance requirements, but contains no limitations on the fees that may be charged to consumers. Consumer advocates have argued that the bill should be re-crafted to prohibit any upfront fees and to allow no more than a 15% of savings fee on settlements achieved for consumers. It is unclear as of this writing whether the proposed Act can be passed without a fee provision or whether a compromise on fees can be reached.

Mississippi

On March 17, 2010, Governor Haley Barbour signed a bill extending the Mississippi Debt Management Services Act, Miss. Code § 81-22-1 et. seq, which had been due to be repealed by its terms on July 1, 2010. The new legislation will continue the operation of the Act for another three years to July 2013.

Mississippi's debt settlement law applies to any entity that "act[s] or offer[s] to act as an intermediary between a consumer and one or more creditors of the consumer for the purpose if adjusting, compromising, negotiating,

settling, discharging or otherwise deferring, reducing or altering the terms of payment of the consumer's obligation." Miss. Code § 81-22-3 (a)(iv).

The Act requires debt settlement providers to obtain a license and a $50,000 bond. It also requires mandatory disclosure and contractual provisions in consumer agreements and limits fees that may be charged to consumers to no more than a $75 set up fee and a $30 monthly fee. Miss. Code §§ 81-22-5, 7, 11 and13. The law also requires licensees to provide notice to the Department of Banking and Consumer Finance if they will use a third-party payment processor to hold and/or distribute consumer funds. Miss. Code § 81-22-28.

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