"As Cats are Drawn to Cream": Expanding Debt Settlement Regulation to Traditionally-Exempt Entities

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Debt settlement companies — firms that purport to settle consumers' debts for severely reduced lump-sum payments — have existed since the mid-twentieth century. While state regulations initially appeared to have dealt with many of the industry's more harmful business practices, such as charging advanced fees or counseling their customers to stop paying their creditors, the 2008 recession provided the necessary fuel for these abuses to come back at full force and prey once again on consumers in debt. Although the federal government and several states reacted to these developments with new legislation and a series of lawsuits, ultimately these companies have been able to exploit a variety of statutory loopholes. This Note explores two such loopholes — the exemption for attorneys and the exemption for firms that do not hold money for their clients — and proposes statutory changes that will capture these firms within the existing rules by increasing liability for debt settlement companies purporting to act as attorneys and for other actors involved in the debt settlement industry who facilitate transactions but nonetheless escape regulation.

I. INTRODUCTION

The industry goes by many names: debt settlement, debt consolidation, debt pooling, debt management, debt relief, debt ad-

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justment, and budget planning among others.[1] These many aliases comprise the industry that the Federal Trade Commission (FTC) and the Better Business Bureau term the Debt Settlement Industry.[2] Debt settlement firms offer indebted consumers a simple promise: to help these individuals avoid bankruptcy and pay off their debt at a reduced rate, usually a lump sum payment amounting to a fraction of their total debt.[3] Unfortunately, these companies often fail to meet their stated goal of helping individuals to pay off their debt, frequently leaving them in a worse place than where they started. Instead of working their way out of debt, these consumers often find themselves being sued by their creditors or forced into bankruptcy.[4]

Debt settlement companies and other forms of debt relief have existed since the early twentieth century.[5] As opposed to the current practice of settling debts for a reduced lump-sum, settlement companies originated as small, local, for-profit companies that attempted to negotiate with consumers' creditors for reduced

1. *See, e.g.*, N.Y. GEN. BUS. Law § 455 (McKinney 2006); OKLA. STAT. tit. 24, § 16 (2012); WASH. REV. CODE § 18.28.010 (2012). *See also* FED. TRADE COMM'N, KNEE DEEP IN DEBT (2011); Fed. Trade Comm'n, *Coping with Debt* (Nov. 2008), http://www.ftc.gov/bcp/edu/pubs/consumer/credit/cre19.shtm.

2. FED. TRADE COMM'N, KNEE DEEP IN DEBT, *supra* note 1; Better Business Bureau, *BBB on Differences Between Debt Consolidation, Debt Negotiation and Debt Elimination Plans* (March 2, 2009), http://www.bbb.org/us/article/bbb-on-differences-between-debt-consolidation-debt-negotiation-and-debt-elimination-plans-9350.

3. *See* NEW YORK CITY BAR, PROFITEERING FROM FINANCIAL DISTRESS: AN EXAMINATION OF THE DEBT SETTLEMENT INDUSTRY (2012), *available at* http://www2.nycbar.org/pdf/report/uploads/DebtSettlementWhitePaperCivilCtConsumerAffairsReportFINAL5.11.12.pdf [hereinafter BAR REPORT]; U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-10-539T, DEBT SETTLEMENT: FRAUDULENT, ABUSIVE, AND DECEPTIVE PRACTICES POSE RISK TO CONSUMERS (2010), *available at* http://www.gao.gov/new.items/d10593t.pdf; Peter S. Goodman, *Peddling Relief, Firms Put Debtors in Deeper Hole*, N.Y. TIMES, June 18, 2010, at A1; Letter from The Nat'l Ass'n of Attorneys Gen. to the Fed. Trade Comm'n (Oct. 23, 2009), *available at* http://www.ftc.gov/sites/default/files/documents/public_comments/2009/10/543670-00192.pdf.

4. *See* BAR REPORT, *supra* note 3, at 120; U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 9–10. *See also* Complaint, Miles v. Legal Helpers Debt Resolution, No. 12-2-36083, 2012 WL 5871437 (Wash. Super. Ct. 2012); People v. Nationwide Asset Servs., Inc., 888 N.Y.S.2d 850, 868 (N.Y. Sup. Ct. 2009).

5. *See* UNIFORM DEBT-MANAGEMENT SERVICES ACT prefatory note (Nat'l Conference of Comm'rs on Unif. State Laws 2011), *available at* http://www.uniformlaws.org/shared/docs/debt_management_services/udmsa_final_2011.pdf [hereinafter U.D.M.S.A.]; Leslie E. Linfield, *Uniform Debt Management Services Act: Regulating Two Related — Yet Distinct — Industries*, 28-APR AM. BANKR. INST. J. 50, 51 (2009).

monthly payments in exchange for sizeable fees.[6] The original companies engaged in many harmful practices, still present in the industry today, such as making misrepresentations to consumers and charging advanced fees that reduced the total amount of funds available to pay creditors.[7] Moreover, these early debt settlement companies had a penchant for absconding with clients' funds.[8] Over the years, both the federal and state governments have identified the debt settlement industry as an area of concern and have attempted to regulate it through a variety of means.[9] From the 1950s through the 1970s, the states responded to the industry's abuses with strong legislation, with half of them outlawing the practices outright and about a third of them choosing to regulate the companies.[10]

As a majority of the states enacted legislation, pre-existing debt relief companies began to reorganize themselves to qualify for various exceptions within the state statutes. Most reincorporated as nonprofits, which were exempt from many of the outright bans on debt settlement.[11] Meanwhile, others converted into debt management firms, a business model that is similar to debt settlement in that the firm negotiates with consumers' creditors for reduced interest rates or lower monthly payments in exchange for a portion of all money that the consumer pays to the creditors, as it was not subject to the same restrictions as debt settlement.[12] Yet, as credit cards became more popular during the 1980s and 1990s, leading to an increase in unsecured debt, the older model of debt settlement returned.[13] Although these new debt settlement companies were nonprofits, they charged large fees and paid their executives large salaries relative to

6. *See* Linfield, *supra* note 5, at 51.

7. *See id.*

8. *See id.*

9. *See, e.g.*, 15 U.S.C. § 1679 (2012); N.Y. GEN. BUS. Law § 455 (McKinney 2006); OKLA. STAT. tit. 24, § 16 (2012); WASH. REV. CODE § 18.28.010 (2013).

10. *See* U.D.M.S.A., prefatory note. *See also, e.g.*, N.Y. GEN. BUS. LAW §§ 455–57 (prohibiting for-profit budget planning); WASH. REV. CODE § 18.28.080 (2013) (limiting the fees which debt adjustors may charge).

11. *See* U.D.M.S.A., prefatory note. *See also, e.g.*, N.Y. GEN. BUS. LAW §§ 455–457 (2006).

12. *See* FED. TRADE COMM'N, *supra* note 1; U.D.M.S.A., prefatory note.

13. U.D.M.S.A., prefatory note.

other nonprofits. In effect, they behaved as for-profit companies despite their nonprofit status.[14]

While debt settlement and other debt relief companies remained relatively few in number through the 1990s, the 2000s saw an exponential increase in the number of such firms, particularly for-profit debt settlement companies.[15] During the first decade of the 21st century, American consumers' total credit card debt reached record highs.[16] Despite their considerable debt, many of these consumers earned enough money to be ineligible for legitimate nonprofit credit counseling services. A study conducted by the FTC in 2008 found that the number of consumers contacting the nonprofit credit counseling agencies had increased by 33%, whereas the total number of people who met the income threshold for those services fell by 40%.[17] In short, there was a great demand for these nonprofit services coming from a class of consumers who were ineligible for their aid. As a result, for-profit debt settlement companies stepped in to fulfill this increased demand. Creditors reported that by 2007, the number of communications from firms attempting to settle consumers' debt increased by 700 percent.[18] Two recessions in 2001 and in 2008 contributed in large part to this increased indebtedness. They forced many consumers to default on their debt and to seek alternate means of reducing or eliminating their debt.[19] In particular, the "Great Recession" of 2008 has been credited with a major expansion in the debt settlement industry: in 2009 the debt settlement companies represented by the industries then two largest trade groups, the United States Organization of Bankruptcy Alternatives (USOBA) and the Association of Settlement Companies (TASC), had over 425,000 customers and $11.7 billion in credit card debt enrolled in their programs, split between some

14. *See* S. Rep. No. 109-55 (2005); I.R.S., CREDIT COUNSELING COMPLIANCE PROJECT SUMMARY OF RESULTS (2006), *available at* http://www.irs.gov/pub/irs-tege/cc_report.pdf (the I.R.S. examined 63 credit counseling companies, which together made up some 56% of industry revenues, and found that 41 of the 63, accounting for 41% of industry revenues, were not or may not be entitled to nonprofit status).

15. *See* FED. TRADE COMM'N, TRANSCRIPT OF THE CONSUMER PROTECTION AND DEBT SETTLEMENT INDUSTRY WORKSHOP 7 (2008), *available at* http://www.ftc.gov/sites/default/files/documents/one-stops/debt-relief-and-credit-repair-scams/officialtranscript.pdf.

16. *Id.* at 6.

17. *Id.*

18. *Id.* at 7.

19. BAR REPORT, *supra* note 3, at 2.

2,000 firms — a sharp increase from the group of a dozen or so firms which dominated the industry at the start of the decade.[20]

Existing regulations notwithstanding, these new, for-profit debt settlement companies managed to proliferate by exploiting various loopholes in state statutes. These loopholes became increasingly attractive as the Internal Revenue Service cracked down on debt settlement companies operating as nonprofits in name only.[21] As regulations and enforcement evolve, so to do the strategies that they exploit to avoid regulation, and this Note will focus on two of the loopholes *du jour* on which contemporary firms rely. Under the first strategy, debt settlement companies present themselves as law firms that negotiate settlements for their clients in exchange for a retainer agreement. This practice is acceptable under most federal and state statutes.[22] Under the second strategy, debt settlement companies avoid handling money directly, relying instead on third-party administrators to handle consumers' funds.[23] This strategy exempts the debt settlement companies from certain state regulations.[24]

This Note will provide an overview of the debt settlement industry and the applicable legal framework, focusing on the states' attempts to regulate the industry and the strategies that debt settlement firms adopted to circumvent these regulations. Part II provides an overview of the debt settlement industry, discussing its basic business model and the problems inherent in this system. Part III discusses attempts to regulate the debt settlement industry, including individual state laws, proposed uniform legislation, and federal regulation, as well as the limits of these efforts. Part IV discusses the two strategies mentioned above that debt settlement companies use to take advantage of state regulations: first, hiring attorneys to claim that the debt settlement firm is offering legal services, which the New York City Bar Asso-

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20. Goodman, *supra* note 3.

21. I.R.S., *supra* note 14; BAR REPORT, *supra* note 3, at 26.

22. *See, e.g.*, Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372 (E.D. Wash. 2011); *In re* Kinderknecht, 470 B.R. 149 (Bankr. D. Kan. 2012); FED. TRADE COMM'N, DEBT RELIEF SERVICES & THE TELEMARKETING SALES RULE: WHAT PEOPLE ARE ASKING (2010), *available at* http://business.ftc.gov/documents/bus73-debt-relief-services-telemarketing-sales-rule-what-people-are-asking.

23. *See* FED. TRADE COMM'N, TRANSCRIPT OF THE CONSUMER PROTECTION AND DEBT SETTLEMENT INDUSTRY WORKSHOP, *supra* note 15, at 226.

24. *Id*.

ciation labels the "purported attorney model"),[25] and second, contracting with third-party administrators to manage clients' accounts in exchange for exorbitant fees.[26] Finally, Part V recommends updating state statutes to remove exemptions for debt settlement companies acting as attorneys in name only and to impose greater liability on third-party account administrators to expand the pool of available defendants in civil suits and to pressure the debt settlement industry to reform some of its more-harmful practices.

II. OVERVIEW OF THE DEBT SETTLEMENT INDUSTRY

Debt settlement firms offer consumers a means to settle unsecured debt.[27] When a consumer enrolls in a debt settlement program, he or she generally ceases paying credit card debts and instead starts paying money to the debt settlement company. The company then puts the funds into an escrow account held by the consumer, the debt settlement company, or some third party.[28] Once that account reaches a certain threshold, the debt settlement company attempts to use that money to pay off one of the consumer's debts for a single lump sum, ideally less than the total amount that the consumer originally owed to that creditor.[29]

Unfortunately, this plan often fails.[30] This failure stems from the fact that, often, when consumers begin putting money into their debt settlement accounts, they stop paying their creditors.[31] Debt settlement companies generally deny playing any role in causing consumers to default, claiming that they only assist consumers who have already defaulted on their payments.[32] Nonetheless, there are numerous documented cases of non-payment

25. BAR REPORT, *supra* note 3, at 80.

26. *See, e.g.*, Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486, 491–92 (2011).

27. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 1.

28. *Id.* at 4; *Settling Credit Card Debt*, FED. TRADE COMM'N (Nov. 2012), http://www.consumer.ftc.gov/articles/0145-settling-credit-card-debt.

29. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 4; *Settling Credit Card Debt*, *supra* note 28.

30. *See, e.g.,* People v. Nationwide Asset Serv., Inc., 888 N.Y.S.2d 850 (N.Y. Sup. Ct. 2009); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 1.

31. U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 9.

32. FED. TRADE COMM'N, TRANSCRIPT OF THE CONSUMER PROTECTION AND DEBT SETTLEMENT INDUSTRY WORKSHOP, *supra* note 15, at 257.

occurring, sometimes at the express direction of the debt settlement companies.[33] Even if debt settlement companies do not expressly recommend that consumers stop paying their creditors, it makes intuitive sense that an indebted consumer who has trouble paying his creditors would be required to stop paying them in order to have enough cash on hand to put into a debt settlement account.[34] Further, the debt settlement companies' business model depends in part on consumers not making their payments in order to provide more leverage against the creditors when negotiating settlements.[35]

As the consumer's credit ratings falls, they become inundated with collection calls and often, they are sued by their creditors.[36] Moreover, their total debt may increase as creditors add late fees and interest to the original charges.[37] Consequently, some consumers who are sued may, in the end, be forced to pay a judgment in excess of what they owed before they began working with a debt settlement agency.[38] To make matters worse, the consumer's debt settlement account probably will not have reached a sufficient size to pay off the debt at this point, due in part to how slowly funds accumulate.[39] Thus, the consumer may not have funds on hand to pay the judgment and may be forced to make monthly payments to the creditor in addition to what she is already paying to the debt settlement company.[40] She may be forced to drop out of the program before being able to realize much bene-

33. *Id*. *See also, e.g.*, Complaint, Rajagopalan v. NoteWorld, LLC, No. 3:11CV05574, 2011 WL 9212378 (W.D. Wash. July 26, 2011); *Nationwide Asset Serv., Inc.*, 888 N.Y.S.2d at 855; Complaint, *Miles*, *supra* note 4; NAT'L CONSUMER LAW CTR., AN INVESTIGATION OF DEBT SETTLEMENT COMPANIES: AN UNSETTLING BUSINESS FOR CONSUMERS (Mar. 2005), *available at* http://www.nclc.org/images/pdf/debt_settlement/report_investigation_debt_settle_co.pdf.

34. *See* FED. TRADE COMM'N, TRANSCRIPT OF THE CONSUMER PROTECTION AND DEBT SETTLEMENT INDUSTRY WORKSHOP, *supra* note 15, at 167–68; 257.

35. Telemarketing Sales Rule, 74 Fed. Reg. 41988-01 (proposed Aug. 19, 2009) (to be codified at 16 C.F.R. § 310).

36. *See, e.g.*, Complaint, *Rajagopalan*, *supra* note 33; *Nationwide Asset Serv., Inc*., 888 N.Y.S.2d 867; Complaint, *Miles*, *supra* note 4.

37. Letter from the Nat'l Ass'n of Attorneys Gen, *supra* note 3.

38. *See, e.g.*, Complaint, Minnesota v. Debt RX USA, 2010 WL 581773 (Minn. Dist. Ct. 2010) (documenting that enrollees wages have been garnished and that they face additional fees and tax problems after being sued); Complaint, *Miles*, *supra* note 4 (plaintiff had $11,000 in debt, but after interest and arbitration fees paid $11,957 in damages).

39. *See* Complaint, *Debt RX USA*, *supra* note 38; Complaint, *Miles*, *supra* note 4.

40. *See* Complaint, *Debt RX USA*, *supra* note 38; Complaint, *Miles*, *supra* note 4.

fit, and is consequently left off worse than when she started.[41] This problem is exacerbated by the fact that some creditors refuse to negotiate with debt settlement companies and some debt settlement companies delay the negotiation process because funds accumulate so slowly in the consumer's account.[42] As a result, many consumers are forced to drop out of the program before being able to realize much benefit — either because they can no longer afford to make payments or because their debt was effectively settled through law suits — and are frequently left off worse than when they started.[43]

The number of consumers who drop out of debt settlement programs varies between companies, but tends to be substantial. According to a study released by the Colorado Attorney General's Office, over 50% of consumers enrolled in such programs dropped out between 2007 and 2009. In 2010, when the federal government announced new regulation for the industry, that number dropped to 43.3%,[44] and yet, only 1.71% of consumers successfully completed their programs.[45]

A variety of questionable business practices endemic to the debt-settlement industry escalate the harm to consumers beyond those associated with mere nonpayment of creditors. First, many debt settlement companies utilize fee structures that work against the ultimate goal of helping consumers save enough money to settle their debts. The most detrimental fee structure used by debt settlement companies involves charging fees upfront before the settlement of a single debt.[46] This practice reduces' both the incentive of debt settlement companies to settle accounts and the total amount of money in consumers' personal accounts, as fees are traditionally deducted from that pool.[47] Also, many

41. *See* BAR REPORT, *supra* note 3, at 68.

42. *See id.* at 64.

43. *See id.* at 68.

44. COLO. DEP'T OF LAW, 2010 ANNUAL REPORT — COLORADO DEBT-MANAGEMENT SERVICES PROVIDERS (2010), *available at* http://www.coloradoattorneygeneral.gov/sites/default/files/uploads/uccc/2010%20DMSA%20Annual%20Report.pdf.

45. *Id.*

46. Telemarketing Sales Rule, 74 Fed. Reg. 41988-01 (proposed Aug. 19, 2009) (to be codified at 16 C.F.R. § 310); BAR REPORT, *supra* note 3, at 2; U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 4.

47. *See, e.g.*, Complaint, Duran v. The Hass Group, No. CV10-4538, 2010 WL 4236649 (E.D.N.Y. 2010); People v. Nationwide Asset Serv. 888 N.Y.S.2d 850, 855–56 (N.Y. Sup.

debt settlement companies require consumers to deposit their funds into third-party accounts, called "Special Purpose Accounts" or "Special Bank Accounts."[48] Under these arrangements, consumers pay a sizeable monthly management fee[49] and sign a limited power of attorney, which gives the debt settlement company complete control of the special purpose account, thereby allowing, including the withdrawal of funds as settlements are reached with the creditors.[50] As a result, the consumer's access to the money in the account is cut off for the duration of their enrollment.[51]

Second, debt settlement companies often resort to fraud or deceptive trade practices to entice consumers into their programs. Companies inundate consumers with advertisements promising prompt payment of their debts for a fraction of the cost of making their minimum monthly payments.[52] For instance, the defendant firms in *People v. Nationwide Asset Services Inc.* assured consumers that enrolling would save them, on average, between 25% and 40% of their total debt.[53] In reality, only 0.3% of their consumers realized savings of that magnitude.[54] Similarly, several firms mentioned in a U.S. Government Accountability Office study had assured consumers that their success rates fell in the neighborhood of 100%, when in reality only 10% of consumers, on average, successfully completed those programs.[55] Other common tactics include firms representing themselves to be government agen-

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Ct. 2009); Telemarketing Sales Rule, 74 Fed. Reg. 41988-01; U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 6; NAT'L ASS'N OF ATTORNEYS GEN, *supra* note 3, at 6.

48. *See, e.g.*, *Nationwide Asset Serv., Inc.*, 888 N.Y.S.2d 856; *Special Purpose Account Agreement*, GLOBAL CLIENT SOLUTIONS, http://www.globalclientsolutions.com/specialPurpose.html (last visited Jan. 20, 2013) (in its contract, one of the two largest account administrators in the country lists its monthly maintenance fee as $9.85).

49. *See, e.g.*, *Nationwide Asset Serv., Inc.*, 888 N.Y.S.2d 856 (the firm in this case charges $49 per month); *Special Purpose Account Agreement*, *supra* note 48.

50. *See, e.g.*, *In re* Kinderknecht, 470 B.R. 149, 162 (Bankr. D. Kan. 2012); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 14

51. *See In re Kinderknecht*, 470 B.R. at 162.

52. *See, e.g.*, Complaint, *Duran*, *supra* note 47 (promising that the program will "improve credit worthiness" and may "improve credit scores"); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3 at 16, 18 (documenting promises that "if you can't get out of debt in 24 hours we'll pay you $100," "Eliminate excessive credit card debt interest immediately").

53. *Nationwide Asset Serv., Inc.*, 888 N.Y.S.2d at 857.

54. *Id*.

55. U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3 at 8. *See also* Letter from the Nat'l Ass'n of Attorneys Gen, *supra* note 3, at 7.

cies[56] and advertising themselves as a superior alternative to bankruptcy because their plans will have a less-detrimental impact on consumers' credit scores.[57]

Third, many debt settlement firms provide questionable or fraudulent legal advice to consumers on how to deal with their creditors. Many firms counsel their consumers to ignore collection calls, claiming that there is no real danger in missing monthly payments, and provide "cease-and-desist letters" to forward to the debt collectors — a practice which rarely, if ever, stops the collection attempts.[58] When creditors sue their consumers, some debt settlement companies even give consumers ersatz advice on how to handle the trial, a tactic that may be counterproductive to reaching a beneficial solution for the consumers.[59]

Fourth, many debt settlement companies refuse to refund any money to consumers — an especially troubling trend given the number of consumers who ultimately drop out of the debt settlement programs.[60] A common pattern is that debt settlement companies may send consumers the funds remaining in their special purpose accounts, but keep the money collected as fees.[61] This practice is problematic misleading as the money in the special purpose accounts is held in escrow and belongs to the con-

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56. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3 at 16 (advertisement states "New Government Programs! New free and easy programs are available for those who are in debtright now! Take advantage while they're still available").

57. *See, e.g.*, Complaint, McPherson v. Financial Consulting Serv., LLC, No. 110-CV-02840, 2010 WL 3164327 (E.D.N.Y. 2010); *In re* Kinderknecht, 470 B.R. 149, 160 (Bankr. D. Kan. 2012); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 1; *Getting Debt Free*, FINANCIAL CONSULTING SERV., http://www.fcsdebt.com/getting-debt-free.html (last visited Jan. 20, 2013) (debt settlement firm advertises that "you can rebuild your credit quicker and easier than if you had declared bankruptcy."). As of the time of publication, Financial Consulting Services has removed that promise from its website, possibly in an effort to shield itself from liability. FINANCIAL CONSULTING SERV., http://www.fcsdebt.com (last visited Mar. 10, 2014)

58. U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 8.

59. *See, e.g.*, *In re Kinderknecht*, 470 B.R. at 159 (on-staff attorney advised client to appear *pro se*); Complaint, *Miles*, *supra* note 4 (debt settlement company told plaintiff that she just had to file a hardship letter with the court in lieu of an answer).

60. *See, e.g.*, Complaint, *Miles*, *supra* note 4; Complaint, *Duran*, *supra* note 47; Complaint, *McPherson*, *supra* note 57; Fed. Trade Comm'n v. Debt-Set, No. 07-cv-00558-RPM (D.Colo. 2008), *available at* http://www.ftc.gov/os/caselist/0623140/080422khanfinalorder.pdf. *See also* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 12.

61. *See, e.g.*, *In re Kinderknecht*, 470 B.R. at 164; Complaint, *Duran*, *supra* note 47; Complaint, *McPherson, supra* note 57.

sumer to begin with so it is not a refund in any sense.[62] If requesting a refund fails, consumers may either attempt to sue the debt settlement companies directly or file complaints with government agencies or consumer watch groups such as the Better Business Bureau.[63] However, many consumers find their suits barred by arbitration clauses in their contract with the debt settlement company.[64] Though some consumers are fortunate enough to have these arbitration clauses voided as unconscionable,[65] such cases are the minority. Unless consumers can demonstrate a statutory violation like fraud that can prompt the FTC or a state attorney general to sue, they are generally left with limited options.[66]

Of course, while there are numerous examples of abuse and failure in the debt settlement industry, there have been some successes.[67] It should be acknowledged that not every debt settlement company employs the abusive behavior documented in cases like *Cuomo*. As Jenna Keehnan, former executive director of USOBA, put it at a 2008 FTC workshop, "[W]hen I . . . describe an attorney to you, I don't go look at the disbarred attorneys list to tell you how to act as a good attorney."[68] At that same workshop, FTC Commissioner J. Thomas Rosch acknowledged that debt settlement, if provided at a fair price, could in some cases be a viable solution to unwieldy consumer debt.[69]

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62. *See, e.g.*, *In re Kinderknecht*, 470 B.R. at 164; Complaint, *Duran*, *supra* note 47.

63. Complaint, *McPherson, supra* note 57; People v. Nationwide Asset Serv. 888 N.Y.S.2d 850 (N.Y. Sup. Ct. 2009); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 12.

64. *See, e.g.*, Rajagopalan v. NoteWorld, No. C11-05574BHS, 2012 WL 727075 (W.D. Wash. Mar. 6, 2012); Willis v. Debt Care, USA, Inc., No. 3:11–CV–430–ST, 2011 WL 7121456 (D. Or. Oct. 24, 2011); Rex v. Credit Solutions of Am., Inc., 507 F. Supp.2d 788 (W.D. Mich. 2008).

65. *See, e.g.*, Newton v. Am. Debt Serv., Inc., 854 F. Supp.2d 712 (N.D. Cal. 2012); Carlsen v. Freedom Debt Relief, 2010 WL 1286616 (E.D. Wash. 2010).

66. *See Bar Report*, *supra* note 3, at 41. *See also, e.g.*, *Nationwide Asset Serv., Inc.,* 888 N.Y.S.2d 850.

67. *See, e.g.*, *Nationwide Asset Serv., Inc.* 888 N.Y.S.2d at 857 (while the firm overestimated the success rate, there were some clients for whom the firms settled their debts at a savings of over 25%). *See also* FED. TRADE COMM'N, *supra* note 15, at 75 (Scott Johnson, CEO of U.S. Debt Resolve, a debt settlement company, stated that he often sees consumers' finances improve after entering debt settlement programs).

68. FED. TRADE COMM'N, *supra* note 15, at 239. The USOBA is a debt settlement industry trade group.

69. *Id* at 14.

Proponents of debt settlement note that consumers in the United States had accumulated $795.8 billion in credit card debt as of the second quarter of 2012.[70] In 2011, credit card companies declared $45.3 billion in chargeoffs — indicating that the debt would likely not be collected — and did the same for another $17.1 billion in the first half of 2012 alone.[71] While some indebted individuals qualify for bankruptcy or nonprofit aid, many do not. For these unqualified debtors, advocates of debt settlement argue, debt settlement is one of the only viable options.[72] Along these lines, Keehnan pointed out that one of the necessary characteristics of an effective debt settlement company is a functioning screening process.[73] The firms have to be careful to enroll only those clients who are capable of completing the settlement program: those who have sufficient income to set aside the money necessary to settle their debts, and who are ineligible for alternatives like bankruptcy or credit counseling.[74] Most important, the firms must ensure that consumers are already behind on their payments and the firms must avoid counseling consumers to stop making payments since such practices prove to be the origin of many problems in the industry.[75] These individuals are already at an increased risk for being sued by their creditors, so if the debt settlement company can settle even a portion of their debt, they might benefit, as opposed to most cases one encounters where individuals are not vulnerable to suit prior to enrolling in the debt settlement program. With these safeguards in place, a debt settlement company can avoid harming consumers who might have better options available to them.[76]

70. *Q2 Main Findings 2012 Credit Card Debt Study*, CARDHUB, http://www.cardhub.com/edu/q2-2012-credit-card-debt-study/ (last visited Jan. 20, 2013).

71. *Id*.

72. *See, e.g.*, Derek S. White, *The Bear Hug that is Crushing Debt-Burdened Americans: Why Overzealous Regulation of the Debt Settlement Industry Ultimately Harms the Consumers it Means to Protect*, 14 TEX. REV. L. & POL. 277 (2010).

73. FED. TRADE COMM'N, *supra* note 15, at 239.

74. *Id.*

75. *Id. See, e.g.*, Complaint, *Miles*, *supra* note 4.

76. FED. TRADE COMM'N, *supra* note 15, at 239.

III. Regulation of the Debt Settlement Industry

A. Federal Regulation

1. *Credit Repair Organizations Act*

The Credit Repair Organizations Act (CROA) is designed to regulate what the FTC defines as "credit repair organizations": any person who purports to offer services for the purpose of "improving any consumer's credit record, credit history, or credit rating."[77] As discussed, many debt settlement companies claim to be able to improve consumers' credit rating; they would therefore fall under this statute.[78] Of particular relevance to debt settlement companies, the statute bars credit repair organizations from making any false or misleading statements to consumers. In another notable provision, CROA bans credit repair organizations from charging any advanced fees.[79] Given that the debt settlement business model generally has a negative effect on consumers' credit ratings, the firms that claim to be able to repair consumers' credit scores can CROA by making false representations.[80] These firms tend to structure their advertising campaigns without explicitly promising to improve consumers' credit ratings, thereby falling outside the scope of the statute.[81]

2. *Telemarketing Sales Rule*

In 2010, the FTC amended its Telemarketing Sales Rule (TSR) to prohibit any organization engaged in debt relief services from charging any fees until the organization has "renegotiated, settled, reduced, or otherwise altered the terms of at least one debt pursuant to a settlement agreement."[82] Further, once an organization begins to settle the consumer's debt, its ability to charge the consumer is limited — it can charge either (1) a portion of the

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77. 15 U.S.C. § 1679a (2012).
78. *See, e.g.*, Complaint, *Duran*, *supra* note 47.
79. 15 U.S.C. § 1679b(b) (2012).
80. *See, e.g.*, Complaint, *Miles*, *supra* note 4; Complaint, *Rajagopalan*, *supra* note 33; People v. Nationwide Asset Servs., Inc., 888 N.Y.S.2d 850, 868 (N.Y. Sup. Ct. 2009).
81. *See, e.g.*, Pavlov v. Debt Resolvers USA, Inc., 907 N.Y.S.2d 978, 805 (N.Y. Civ. Ct. 2010).
82. 16 C.F.R. § 310.4 (2013).

total fee based on what percentage of the total debt was settled or (2) a percentage of the total amount saved through the settlement.[83] The TSR specifically mentions settlement in the definition of debt relief service, so in contrast to the CROA, all debt settlement companies that fall under this rule's jurisdiction are covered.[84]

In addition to limiting the times at which the firm may be paid, the TSR sets disclosure requirements. Debt relief service providers must disclose (1) the amount of time the entire program will take and the amount of time before the company will actually send out the settlement offers; (2) the amount of money that must accumulate in the account, as a percentage of the total debt, before the company can make settlement offers; (3) the fact that the consumer's credit score may be adversely affected and the fact that the consumer may end up further in debt with the addition of interest and late fees; and (4) that the consumer is entitled to whatever funds remain in their special purpose account should they withdraw from the program.[85] It further prohibits making misrepresentations to consumers.

The TSR has been hailed as a major advancement in the regulation of the debt settlement industry and has enabled the FTC to prosecute some of the more common abuses beyond what the CROA allowed.[86] Unfortunately, the rule has proven easy to circumvent.[87] The combined membership for the industry's two largest trade groups, the USOBA and the American Fair Credit Council (AFCC), a precursor to TASC, plummeted in the year after the amendments to the TSR were adopted, dropping from over 400 to less than 70 firms, yet industry experts estimate that the

83. *Id.*

84. *Id.* § 310.2 (2013).

85. *Id.* § 310.3 (2013).

86. *See, e.g.*, John L. Robiaquet & Jason B. Hirsch, *The 2010 Amendments to the Telemarketing Sales Rule: Expanding FTC Regulatory Oversight to Debt Relief Services,* 64 CONSUMER FIN. L.Q. REP. 382 (2010); Edward Wyatt, *New Restrictions Placed on Debt Settlement Companies*, N.Y. TIMES, June 18, 2010, at B2. *See also* FTC v. Golembiewski, No. 2:12cv893 (S.D. Ohio 2012), *available at* http://ftc.gov////.pdf (order resulting from FTC enforcement action brought under the TSR against 17 related debt settlement companies, ordering monetary damages and enjoining the defendants from providing debt relief services).

87. BAR REPORT, *supra* note 3, at 95.

number of firms in the industry has remained constant.[88] The decline can be attributed to the fact that the trade groups require their members to abide by the provisions of the TSR, and many debt settlement companies have chosen to go around the rule.[89] Due to the nature of the rule, the TSR's jurisdiction is limited to sales made over the telephone in connection with telemarketing, which applies (1) when the seller contacts the buyer over the telephone or (2) when the buyer contacts the seller via telephone in response to general media advertisements.[90] The rule therefore exempts instances where the final sale is made after a face-to-face meeting, even if an agreement is made over the telephone.[91] However, the face-to-face meeting must be more than perfunctory.[92] Merely meeting with consumers after they have chosen to enroll in the program but before they formally enroll will not suffice — the buyer and the seller have to meet in person to discuss the terms of the contract before either party agrees to the transaction.[93]

Unfortunately, the face-to-face exemption has made the rule difficult to enforce.[94] Debt settlement companies have several avenues for circumventing the rule. First, some debt settlement companies simply refuse to make transactions over the telephone, requiring consumers to meet in person in order to discuss the plan and the possibility of consumer's enrollment.[95] Second, certain national debt settlement companies maintain local, inde-

88. Elizabeth Ody, *Debt Firms Play "Whack-a-Mole" Using Lawyers to Skirt Fee Ban*, BLOOMBERG (Sep. 30, 2011), *available at* http://www.bloomberg.com/news/2011-09-30/debt-firms-play-whack-a-mole-to-skirt-fee-ban.html.

89. *Id.*

90. Telemarketing Sales Rule, 74 Fed. Reg. 48458-01 (Aug. 10, 2010) (to be codified at 16 C.F.R. § 310).

91. 16 C.F.R. § 310.06 (2013), FEDERAL TRADE COMM'N, COMPLYING WITH THE TELEMARKETING SALES RULE (2011), *available at* http://business.ftc.gov/documents/bus27-complying-telemarketing-sales-rule#facetoface.

92. FEDERAL TRADE COMM'N, DEBT RELIEF SERVICES & THE TELEMARKETING SALES RULE: WHAT PEOPLE ARE ASKING (2010), *available at* http://www.business.ftc.gov/sites/default/files/pdf/bus73-debt-relief-services-telemarketing-sales-rule-what-people-are-asking.pdf,

93. *Id.*

94. *See* Jonathan L. Voigt, *A False Light in the Darkness: Protecting Consumers and Creditors from the Debt Settlement Industry,* 87 N.D. L. REV. 273, 289 (2011).

95. Press Release, N.Y.C. Dep't of Consumer Affairs, Department of Consumer Affairs (DCA) Launches Investigation into Debt Settlement Companies (Aug. 9, 2011), *available at* http://www.nyc.gov/html/dca/html/pr2011/pr_080911.shtml.

pendent contractors who meet with the consumers.[96] Third, some debt settlement companies rely on third parties with ongoing relationships with the consumers, such as law firms or mortgage modification companies, to refer and to pitch the debt settlement company's services to consumers who show interest.[97] Beyond taking advantage of the face-to-face exception, some debt settlement firms circumvent the TSR's jurisdiction by ensuring that none of the telephone calls are interstate.[98] Some national debt settlement firms set up offices, similar to those used by independent contractor's in the strategy discussed above, in each state where the firms do business.[99] Thus, consumers only contact the office in the state wherein which they reside, and the firms avoid both interstate calls and the TSR's jurisdiction.[100]

B. STATE REGULATION

1. *General Consumer Protection Statutes*

Most states have some manner of generic consumer protection statute that bars fraud and deceptive trade practices.[101] Under these statutes, state attorneys general and private plaintiffs have been able to bring suit against debt settlement companies that make misrepresentations to their clients through advertisements or otherwise.[102] While these statutes allow states and consumers

96. *See, e.g.*, *In re* Kinderknecht, 470 B.R. 149, 159 (Bankr. D. Kan. 2012); (national company employs independent contractors in each state which meet with consumers prior to enrollment); Comments from Able Debt Settlement, Inc., to Federal Trade Comm'n, (Oct. 21, 2009), *available at* http://www.ftc.gov/policy/public-comments/comment-543670-00314 (firm provides debt settlement services on behalf of a number of independent contractors including attorneys, accountants, and financial analysts).

97. *See, e.g.*, Complaint, Morgan Drexen v. Visser and Assocs. 2010 WL 3266602 (W.D. Mich. Apr. 20, 2010) (firm employs lead generators that contact law firms and have them refer consumers who are potential candidates for debt settlement).

98. 16 C.F.R. § 310.2 (2013) ("Telemarketing means a plan, program, or campaign which is conducted to induce the purchase of goods or services or a charitable contribution, by use of one or more telephones and which involves more than one interstate telephone call").

99. *See, e.g. In re Kinderknecht*, 70 B.R. at 159.

100. *See, e.g.*, *id.*

101. *See, e.g.*, N.Y. GEN. BUS. LAW § 349 (2013) (barring deceptive trade practices); WASH. REV. CODE 19.86.093 (2013) (civil action for unfair or deceptive acts or practices).

102. *See, e.g.*, People v. Nationwide Asset Serv., Inc., 888 N.Y.S.2d 850 (N.Y. Sup. Ct. 2009); Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486 (2011); Ameet Sachdev, *Chicago Law: Debt-Settlement Firm to Wind Down Business*, CHI. TRIB., July 27, 2012,

to recover large sums in restitution, their power is limited in that the statutes require the commission of some deceptive act or practice.[103] Though such deceptive acts are common in the debt settlement industry and account for much of the harm that consumers face, these statutes cannot regulate the full scope of harm.[104] Firms that tell consumers the truth but nonetheless counsel consumers to stop paying creditors, charge advanced fees, or engage in other similar practices fall outside their purview.[105]

2. *Uniform Debt Management Services Act*

The National Conference of Commissioners on Uniform State Laws introduced the Uniform Debt Management Services Act (UDMSA) in 2005 in an attempt to create greater uniformity in regulation of the debt settlement industry and to ensure a minimum level of regulation.[106] Thus far, only six states have chosen to enact the statute, though it has been introduced in other state legislatures.[107] Most of the six states have enacted altered versions, creating several classes of debt management service providers.[108] The UDMSA defines debt management as any service that acts as "an intermediary between an individual and one or more creditors of the individual for the purpose of obtaining concessions," and thus includes debt settlement companies.[109] The Act's main vehicle for regulation is licensing.[110] In order to obtain a license, debt management companies must comply with a number of requirements, including the requirement that the firm

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http://articles.chicagotribune.com/2012-07-27/business/ct-biz-0727-chicago-law--20120727_1_debt-settlement-legal-helpers-debt-resolution-debt-settlement-firm (Illinois Attorney General reached a $2.1 million settlement with Legal Helpers Debt Resolution).

103. *See, e.g.*, N.Y. GEN. BUS. LAW § 349 (2013).

104. *See Nationwide Asset Serv., Inc.*, 888 N.Y.S.2d at 869; U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 3, at 5.

105. *See, e.g.*, N.Y. GEN. BUS. LAW § 349.

106. *See* U.D.M.S.A., prefatory note (Nat'l Conference of Comm'rs on Unif. State Laws 2011).

107. *See Welcome to UDMSA.org,* UNIFORM DEBT MANAGEMENT SERVICES ACT, OFFICIAL INFORMATION WEBSITE, http://www.udmsa.org (last visited Jan. 20, 2013). *See also* COLO. REV. STAT. §§ 12-14.5-201–242 (2012); DEL. CODE ANN. tit. 6, § 2401a–2439a (2012); NEV. REV. STAT. § 676A.010–780 (2011); R.I. GEN. LAWS § 19-14.8-1–43 (2012); TENN. CODE ANN. § 47-18-5501–5541 (2012); UTAH CODE ANN. § 13-42-101–141 (2011).

108. *See Welcome to UDMSA.org*, *supra* note 107.

109. U.D.M.S.A., § 2.

110. *Id.* § 4.

carry insurance and post a bond to ensure that the firm can satisfy any judgments against it, the requirement that employees to become certified credit counselors, and requirement that firms offer full refunds of their fees should a consumer withdraw from the program.[111] The Act also imposes fee caps on services[112] and prohibits debt management companies from making misrepresentations to consumers.[113] In terms of enforcement, it allows both state and private actors to bring suit for violations.[114]

The model statute has many advantages, and broader adoption the UDMSA would serve to strengthen regulation of the debt settlement industry in several ways. First, unlike many current state statutes, the act's definition of debt management services does not require the company to have any control of the money, and removes a loophole that debt settlement companies often exploit to avoid regulation.[115] Second, unlike many state and federal statutes, by ensuring that the firms are insured and that they post a bond, the UDMSA addresses the problem of debt management companies not having enough capital on hand to satisfy judgments.[116]

However, the UDMSA is not a perfect piece of legislation. Certain consumer groups feel that licensure is an inappropriate means of regulating the debt settlement industry because it confers legitimacy to the industry — perhaps more than warranted, given the potential harm to consumers.[117] Also, the Act does not fully address certain problematic practices such as charging fees in advance of settling any debts and excessive fees.[118] In addition, the Act does not prohibit for-profit debt settlement, which certain experts in the field believe to be an inherently problematic business model.[119] Finally, there is some concern that the Act at-

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111. *Id* § 5.
112. *Id* § 23.
113. *Id*. § 28.
114. *Id*. §§ 33, 35.
115. *Compare id.* § 2, *with* FTC, *supra* note 15, at 226.
116. U.D.M.S.A., § 5.
117. NATIONAL CONSUMER LAW CENTER, COMMENTS ON THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS UNIFORM DEBT MANAGEMENT SERVICES ACT 1 (2006), *available at* http://www.nclc.org/images/pdf/credit_counseling/comments_nccusl_2006.pdf.
118. *Id.*
119. *Id*. *See also* Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486, 502 (Wash. 2011) (Chambers, J. Concurring).

tempts to regulate two similar yet distinct industries — for-profit debt settlement and nonprofit credit counseling — and that the debt settlement industry may be better served by a statute tailored to its specific needs and practices.[120]

3. *Other State Statutes*

While only six states have adopted the UDSMA thus far, most states have some manner of statute or regulation dealing with the debt settlement industry, the intricacies of which cannot be fully addressed in this Note. Thirty-one states require licensure or registration, including the six states that have enacted the UDSMA.[121] Six states ban for-profit debt settlement[122], while four states ban the practice outright.[123] Thirty-five states impose caps or bans on certain types of fees.[124] Five make violating the statute a potential felony[125], while seventeen make it a misdemeanor.[126] Only two states do not regulate the industry: Alaska does not have an applicable statute,[127] and the Commonwealth Court of Pennsylvania struck down Pennsylvania's statute, which gave the state's Department of Banking the authority to establish a licensing procedure and set fee caps, as an unconstitutional delegation of power.[128]

While the states appear to have a relatively comprehensive regulatory system in place, in practice it does not capture the entire industry. For instance, state statutes use a variety of names to describe debt settlement. This leads to confusion and forces courts to examine each company's business model on a case-by-case basis to determine whether the company is covered.[129] Also,

120. *See* Leslie E. Linfield, *Uniform Debt Management Services Act: Regulating Two Related — Yet Distinct — Industries*, 28 APR AM. BANKR. INST. J. 50, 61 (2009); NATIONAL CONSUMER LAW CENTER, *supra* note 117, at 2.

121. *See* BAR REPORT, *supra* note 3, at 171–84.

122. *Id.*

123. *Id.*

124. *Id.*

125. *Id.*

126. *Id.*

127. *Id.* at 171.

128. U.S. Organization of Bankruptcy Alternatives v. Department of Banking, 991 A.2d 370, 373 (Pa. Commw. Ct. 2010).

129. *See, e.g.*, Pavlov v. Debt Resolvers USA, Inc., 907 N.Y.S.2d 798 (N.Y. Civ. Ct. 2010) (on whether debt settlement companies are "budget planners") (citing N.Y. GEN. BUS. LAW § 455 (2013)); Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486 (2011)

many state statutes have not kept pace with the industry. For example, they define debt relief companies as firms that receive and distribute funds directly from and on behalf of the consumer. As noted, these days most debt settlement companies do not touch the money.[130] Moreover, debt settlement companies have historically avoided state bans on for-profit debt settlement by registering as nonprofits while continuing to charge exorbitant fees and paying their executives large salaries comparable to the for-profit sector, and otherwise behaving as for-profit companies.[131] However, this particular model has been in decline as of late[132] Thus, while there are forty-eight different enforceable state statutes, they do not cover and regulate a lot of potentially harmful activity perpetrated by this industry. This activity will be discussed at length in Part IV.

IV. Modern Problems in Enforcement

A. Purported Attorney Model

States that regulate the debt settlement industry often include exemptions for attorneys. In such states, it is legal for an attorney, in exchange for a retainer, to negotiate a settlement with a creditor who may potentially sue a consumer.[133] Likewise, while federal legislation does not explicitly exempt attorneys, they likely fall outside the CROA — unlike debt settlement companies, ethical duties would bar an attorney from advising a client that debt settlement can improve the client's credit rating. Also, the FTC has suggested that attorneys would likely fall into the face-

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(on whether debt settlement companies are "debt adjusters" under WASH. REV. CODE § 18.28.010 (2013)).

130. *See* BAR REPORT, *supra* note 3, at 27. *See, e.g.*, MICH. COMP. LAWS § 451.412 (2013) (requiring "the receipt of money from the debtor for distribution to a creditor in payment or partial payment of the debtor's obligations"); NEB. REV. STAT. § 69-1201 (2013) (requiring "the receiving therefrom of money or evidences thereof for the purpose of distributing the same to his or her creditors in payment or partial payment of his or her obligations"); OKLA. STAT. tit. 24, § 16 (2013) ("debtor agrees to pay a sum or sums of money periodically to the person engaged in the debt pooling who shall distribute the same among certain specified creditors").

131. *See* S. Rep. No. 109-55 (2005); I.R.S., *supra* note 14, at 1.

132. *See id.*

133. *See, e.g.*, CAL. FIN. CODE § 12100 (2013); 225 ILL. COMP. STAT. ANN. 429/10 (2013); U.D.M.S.A., § 2 (Nat'l Conference of Comm'rs on Unif. State Laws 2011).

to-face exemption of the TSR.[134] Because of this legal gap, many debt settlement firms choose to reinvent themselves as law firms in order to escape regulation.[135] In fact, since 2010 when the TSR, there was amended, there has been a sharp increase in the number of debt settlement firms working with or as attorneys.[136]

Debt settlement firms operating under this purported attorney model exhibit a wide variety of business practices, but not all of them are successful in circumventing regulation. Persels & Associates, LLC, was the subject of two cases, *In re Kinderknecht* and *Bronzich v. Persels & Associates, LLC*, and illustrates one such approach.[137] Persels acquired customers through referrals from legitimate debt management companies of consumers who were ineligible for debt management programs.[138] Persels offered consumers assistance in settling their debt and charged fees in advance of completing any settlements. Under the plan, the first eighteen months' worth of payments went towards legal fees, rather than debt settlement.[139] In both cases, the debt management company completed the bulk of the settlement work for a weekly fee that covered the cost of collecting and storing client data, communicating with the clients and their creditors, and negotiating settlements.[140]

At some point, one of Persels' attorneys reviewed each client's file to ensure that the client was eligible.[141] Because none of Persels' attorneys were licensed to practice in Kansas or Washington, the states in question, once one of Persels' attorneys had examined the file, it was handed over to a field attorney, an independent contractor licensed to practice in whichever state the client resided.[142] However, the field attorney provided no real legal services to the clients — they merely reviewed each client's

134. Telemarketing Sales Rule, 74 Fed. Reg. 48458-01 (Aug. 10, 2010) (to be codified at 16 C.F.R. § 310).

135. Ody, *supra* note 88.

136. BAR REPORT, *supra* note 3, at 78 (in a study of 64 complaints against debt settlement companies by state attorneys general, the FTC, and private plaintiffs 43 attorneys were implicated in the suits).

137. Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372 (E.D. Wash. May 27, 2011); *In re* Kinderknecht, 470 B.R. 149 (Bankr. D. Kan. 2012).

138. *In re Kinderknecht*, 470 B.R. at 157.

139. *Id.* at 158.

140. *Id.*, *Bronzich*, 2011 WL 2119372, at *4.

141. *Bronzich*, 2011 WL 2119372, at *4; *In re Kinderknecht*, 470 B.R. at 159.

142. *Bronzich*, 2011 WL 2119372, at *6; *In re Kinderknecht*, 470 B.R. at 159.

file every month, update's the company's database as need be and, in the event that the client was sued by a creditor, assisted the client in representing himself *pro se*.[143]

The United States Bankruptcy Court for the District of Kansas found that Persels constituted a debt settlement company and held it in violation of Kansas's Credit Services Organization Act, stating that "[i]f it walks like a duck and swims like a duck and quacks like a duck, it is a duck."[144] More specifically, the court found that Persels could not fall into the attorney exemption because none of Persels' attorneys were licensed to practice law in Kansas.[145] The Court went on to hold that the fact that the independent field attorney was licensed in Kansas was not enough to qualify Persels for the safe harbor because that attorney never provided any legal advice and never contacted or engaged in any negotiations with creditors.[146] The Court further held that the exemption did not apply because the consumer's contract was with Persels, not with the field attorney, and that contract was finalized before the client was ever assigned to the field attorney.[147] The United States District Court for the Eastern District of Washington agreed.[148]

While the *Bronzich* court similarly held that an attorney must be licensed to practice in the state in order to fall into the exemption it went one step further.[149] Unlike the Kansas statute, which exempts any "individual licensed to practice law in this state acting within the course and scope of such individual's practice as an attorney,"[150] the Washington statute exempts "[a]ttorneys-at-law, escrow agents, accountants, broker-dealers in securities, or investment advisors in securities, while performing services solely incidental to the practice of their professions."[151] The *Bronzich* court found that, under the Washington statute, an attorney

143. *In re Kinderknecht*, 470 B.R. at 159.
144. *Id.* at 185.
145. *Id*. KAN. STAT ANN. § 50-1116 (2012) ("Any individual licensed to practice law in this state acting within the course and scope of such individual's practice as an attorney, and such individual's law firm, shall be exempt from the provisions of this act.").
146. *In re Kinderknecht,* 470 B.R. at 167–68.
147. *Id.* at 167.
148. *Bronzich*, 2011 WL 2119372, at *6.
149. *Id.*
150. KAN. STAT ANN. § 50-1116 (2012).
151. WASH. REV. CODE § 18.28.010 (2013).

whose sole area of practice was debt settlement could not fall into the attorney exemption. Here, debt settlement is not incidental to the firm's practice of law; it is the firm's exclusive practice of law.[152]

The difference between the holdings in these two cases highlights the importance of limiting the attorney exemption to allowing consumers to recover under debt settlement statutes. At present, at least ten states use language similar to Washington's statute requiring the debt settlement to be incidental to the practice of law.[153] Other states have broader exemptions, including blanket exemptions for attorneys,[154] attorneys providing services in an attorney-client relationship,[155] or attorneys who are engaged in the practice of law.[156] Considering the example of Persels, the firm's home state of Maryland exempts "an attorney at law who is admitted to the Maryland Bar while the attorney at law is providing professional legal services in an attorney-client relationship."[157] Thus Persels, which still actively offers its services to consumers,[158] would at the least be able to operate in Maryland, where its attorneys are licensed, so long as it has enough contact with consumers and gives some modicum of legal advice sufficient to establish an attorney-client relationship.[159]

Persels may be an extreme case of attorneys trying to game the system. As both the *Kinderknecht* and the *Bonzich* courts pointed out, the attorneys did not personally provide the debt settlement services.[160] If every debt settlement law firm attempting

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152. *Bronzich*, 2011 WL 2119372, at *6.

153. ARIZ. REV. STAT. § 6-702 (2012) (effective 1968); CONN. GEN. STAT. § 36a-663 (2012) (effective 1958, amended effective 2009), § 36a-655 (2012); IDAHO CODE ANN. § 26-2239 (2012) (effective 1970, amended effective Jul. 1, 2008); IOWA CODE § 533A.2 (2012) (effective Jul. 1, 1967); LA. REV. STAT. ANN. § 14:331 (2011) (effective 1972); MISS. CODE ANN. § 81-22-3 (2011) (effective Jul. 1, 2003, amended effective Jul. 1. 2008); OR. REV. STAT. § 697.612 (2012) (effective 1983, amended effective Jan. 1, 2010); S.D. CODIFIED LAWS § 37-34-1 (2012); WASH. REV. CODE § 18.28.010 (2013).

154. *See, e.g.*, NEB. REV. STAT. § 69-1202 (2013).

155. *See, e.g.*, U.D.M.S.A., § 2(9)(A) (Nat'l Conference of Comm'rs on Unif. State Laws 2011).

156. *See, e.g.*, 225 ILL. COMP. STAT. 429/10 (2013).

157. MD. CODE ANN., FIN. INST. § 12-1003 (2012).

158. PERSELS & ASSOCIATES, http://www.perselsandassociates.com/how_persels_can_help.html (last visited Jan. 20, 2013).

159. MD. CODE ANN., FIN. INST. § 12-1003 (2012).

160. Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372, at *8 (E.D. Wash. May 27, 2011); *In re* Kinderknecht, 470 B.R. 149, 177 (Bankr. D. Kan. 2012).

to find safe harbor operated similarly, the purported attorney model would not be problematic.[161] Indeed, there are multiple documented cases of debt settlement firms failing to earn the debt settlement exception because, like Persels, the firms' attorneys neither provided legal services nor personally negotiate clients' debts.[162] However, other firms have been successful in exploiting the attorney exemption. Take Bay View Law Group, P.C., for example, a California law firm which was the subject of *Tanksley v. Bay View Law Group, P.C*.[163] In that case, the firm provided legal advice on whether a client would be better served by bankruptcy or debt settlement and the firm agreed to represent the client in negotiating a settlement should they be sued.[164] California exempts from its debt settlement regulatory statute "[t]he services of a person licensed to practice law in this state, when the person renders services in the course of his or her practice as an attorney-at-law."[165] The ultimate fate of Bay View is unknown as the contract contained an arbitration clause that the firm successfully moved to enforce.[166] However, because its attorneys were licensed to practice law in California and, according to the plaintiff's brief, did provide some manner of legal services, Bay View may well have operated as a debt settlement firm that could fall into a statutory attorney exemption.[167]

B. THIRD-PARTY ACCOUNT ADMINISTRATOR MODEL

The second major enforcement loophole is the third-party account administrator model.[168] Under this model, third parties manage consumers' special purpose accounts and charge various fees to the consumer for doing so, including monthly maintenance

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161. *Bronzich*, 2011 WL 2119372, at *6; *In re Kinderknecht*, 470 B.R. at 167.
162. *See, e.g.*, *In re* Allegro Law LLC, No. 10-30631-WRS, 2010 WL 2712256, (M.D. Ala. July 6, 2010) (court found that an attorney was essentially licensing his name and his status as an attorney to a debt settlement company which did not employ attorneys).
163. Tanksley v. Bay View Law f, 2012 WL 5193680 (D. Kan. Oct. 15, 2012).
164. Complaint, *Tanksley*, 2012 WL 4990292 (D. Kan. Apr. 20, 2012).
165. CAL.FIN.CODE § 12100 (2013).
166. *Tanksley*, 2012 WL 5193680, at *1
167. *See* Complaint, *Tanksley, supra* note 164; Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372, at *6 (E.D. Wash. May 27, 2011); *In re* Kinderknecht, 470 B.R. 149, 167 (Bankr. D. Kan. 2012).
168. *See, e.g.*, Carlsen v. Global Client Solutions, LLC,171 Wash. 2d 486, 492 (2011).

charges or wire transfer fees.[169] The majority of cases involving third-party administrators cite two firms: Global Client Solutions LLC,[170] often in conjunction with Rocky Mountain Bank and Trust,[171] and NoteWorld LLC.[172] These administrators organized the accounts such that the consumers theoretically control their accounts — maintaining the right to withdraw money or terminate the accounts — but as part of their debt settlement contract they generally hand control over to the third party, authorizing in advance monthly transfers from their private accounts into the special purpose account for the duration of the program, and transfers from the special purpose account to creditors when appropriate.[173] Third parties are legally separate from the debt settlement companies they work with, do not directly advertise to consumers, do not negotiate with creditors on behalf of consumers, and are generally fall outside of states' definitions of debt settlement companies.[174]

Third party firms do not engage in many of the abuses common to the debt settlement industry. They do not directly deceive consumers and do not charge all of their fees in advance of rendering an actual service.[175] Nonetheless, their role in the debt settlement scheme is harmful to consumers. First, their monthly fees reduce the amount of money that ultimately ends up in the consumer's account, thus delaying the time when the account is large enough to reach a potential settlement and making it more likely that the consumer will be sued by creditors.[176] Second,

169. *Id.*

170. *See, e.g.*, Estrella v. Freedom Financial Network, LLC, No. CV 09-03156 SI, 2012 WL 4645012 (N.D. Cal. Oct. 1, 2012); Guidotti v. Legal Helpers Debt Resolution, LLC, 866 F. Supp.2d 315 (D.N.J. 2011); Complaint, People v. Nationwide Asset Servs., Inc., 888 N.Y.S.2d 850 (N.Y. Sup. Ct. 2009); Pavlov v. Debt Resolvers USA, Inc., 907 N.Y.S.2d 798 (N.Y. Civ. Ct. 2010); *Carlsen,* 171 Wash. 2d 486.

171. *See, e.g.*, *Estrella*, 2012 WL 4645012, at *2; *Carlsen*,171 Wash. 2d at 490.

172. *See, e.g.*, Morefield v. Noteworld, LLC, Nos. 1:10–CV–00117, 1:11–CV–00029, 2012 WL 1355573 (S.D. Ga. Apr. 18, 2012); Wheeler v. Noteworld, LLC, No. CV–10–0202–LRS, 2012 WL 3061489 (E.D. Wash. July 26, 2012); Complaint, *Rajagopalan*, *supra* note 33.

173. *See Guidotti*, 866 F. Supp.2d at 326 *Carlsen*, 171 Wash. 2d at 491–92.

174. *See, e.g.*, WASH. REV. CODE § 18.28.010 (2013); U.D.M.S.A., § 22 cmt. 5 (Nat'l Conference of Comm'rs on Unif. State Laws 2011). .

175. *See Nationwide Asset Servs.*, Inc., 888 N.Y.S.2d 850, 856 (N.Y. Sup. Ct. 2009) (charging monthly fees rather than advanced fees, without directly contacting the consumer); BAR REPORT, *supra* note 3, at 39.

176. *See, e.g.*, *Nationwide Asset Servs., Inc*., 888 N.Y.S.2d at 868 (N.Y. Sup. Ct. 2009); Complaint, *Miles*, *supra* note 4; BAR REPORT, *supra* note 3, at 38.

third-party accounts often do not pay interest, which, given the presence of fees in excess of a typical savings account, raises the question of whether the services convey any actual benefit to consumers.[177] Third, as discussed, third-party account administrators can aid debt settlement companies in evading regulations that require the debt settlement companies to handle funds themselves.[178]

Third-party account administrators are already partially regulated. The TSR requires that any debt settlement firm that mandates consumer funds to be placed in a special purpose account must ensure that (1) the funds are held in a FDIC-insured bank; (2) the consumer receives whatever interest the account accrues; (3) the entity controlling the account is not related to or controlled by the debt settlement company; (4) the third party does not give or accept money for referrals to debt settlement services; and (5) the funds can be withdrawn at any time, without penalty.[179] Likewise, the UDSMA imposes certain fiduciary duties on debt settlement companies who require consumers to put money into special purpose accounts regardless of whether those accounts are administered by third parties.[180] Under the UDSMA, debt settlement companies may contract with third-party administrators to have the administrators take on the fiduciary duties.[181]

Finally, states have enacted legislation targeting third-party administrators. Most recently, Washington amended its debt settlement statute to include a definition of the term "third-party account administrator."[182] Like the UDSMA, the Washington statute places liability for the third party's actions on the debt settlement company, counting any fees charged by the third party towards the total fee which the debt adjuster is allowed to charge

177. *See*, *e.g.*, Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486, 492 (2011).

178. *See* FTC, *supra* note 15, at 226.

179. 16 C.F.R. § 310.4 (2013).

180. U.D.M.S.A., § 22 (Nat'l Conference of Comm'rs on Unif. State Laws 2011) (Requiring the provider to hold all funds in trust, to ensure that the total amount of funds held is equal to the total amount of funds in each individual's account, and to refund consumers' accounts should they exit the program).

181. *Id.* at § 22, cmts. 1, 5. While there is no case law explicitly describing the nature of this fiduciary duty, the comments indicate that it mainly involves following the requirements of § 22. *Id*. cmt. 1,

182. WASH. REV. CODE § 18.28.010 (2013).

— 15% of the total debt listed on the contract.[183] Unlike UDSMA, this act goes a step further and attaches some liability to third parties.[184] Specifically, it requires third parties to be licensed money transmitters, imposes various requirements analogous to those found in the TSR, and requires that they maintain certain records.[185] This statute overturns, in part, the state Supreme Court's decision in *Carlsen v. Global Client Solutions LLC* , which held that the administrator was subject to the state's debt settlement statute as an accomplice[186] by exempting said administrators from the definition of debt adjuster.[187] Thus far, Washington's new statute contains the most extensive regulation of third parties of any state. However, other states do impose lesser limits on the types of activities in which these third parties may engage.[188]

Notwithstanding regulations that specifically address third-party account administrators, some plaintiffs have successfully brought suit against such administrators as accomplices to acts that were committed by debt settlement companies.[189] As discussed, the *Carlsen* court found that third parties could be held liable as accomplices under Washington's debt adjustor statute, but that decision was, of course, overturned by the amended statute.[190] However, other states have found that third parties could be held liable as accomplices under the states' deceptive trade practice statutes.[191]

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183. *Id.* § 18.28.080 (2013).

184. *Id.* § 19.230 (2013).

185. *Id.*

186. 171 Wash. 2d 486, 500 (2011).

187. WASH. REV. CODE § 18.28.010 (2013).

188. *See, e.g.*, 225 ILL. COMP. STAT. 429/125 (2010) (prohibiting debt settlement companies from charging monthly maintenance fees). It is unclear if it applies to fees charged by third parties.

189. *See, e.g.*, Estrella v. Freedom Financial Network, LLC, No. CV 09-03156 SI, 2012 WL 4645012 (N.D. Cal. Oct. 1, 2012); Guidotti v. Legal Helpers Debt Resolution, LLC, 866 F. Supp.2d 315 (D.N.J. 2011).

190. *See* Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486, 500 (2011).

191. *See, e.g.*, *Estrella*, 2012 WL 4645012 (Global Client Solutions and Rocky Mountain Bank and Trust settled a suit for $500,000 dollars); *Guidotti*, 866 F. Supp.2d 315 (declining to dismiss a suit against Global Client Solutions and Rocky Mountain Bank and Trust, holding that plaintiff pled sufficient facts to find them liable under New Jersey's debt settlement statute).

V. RECOMMENDATIONS

A. LIMITING THE PURPORTED ATTORNEY MODEL

The Washington debt settlement statute's language exempting attorneys only when the debt settlement is incidental to their practice of law provides the best statutory language available to close the attorney loophole and should be adopted by other states.[192] This statute has two main strengths. First, as seen in *Bronzich*, the statute does not apply to debt settlement companies who purport to be attorneys in name only — those whose business model is clearly that of a debt settlement company, and not a law firm.[193] This language ensures that firms operating as debt settlement companies are subject to the regulations to which the state legislature intended them to be subject, and that consumers are protected from harmful practices, regardless of what label the firm gives itself.[194] Second, the statutory language provides some protection for attorneys which many other states have determined to be an important part of the regulatory model.[195] It is easy to conceive of a situation where an attorney is hired to negotiate with a client's creditor when said creditor is threatening to sue the client. If the attorney is able to negotiate a settlement in their role as attorney, they should be subject to the state laws intended to govern attorneys, not those meant for debt settlement companies.[196]

At present, debt settlement attorneys that succeed in using this exemption are only governed by attorney's ethical rules, which does not provide sufficient protection for consumers.[197] Some industry watchdogs, such as the New York City Bar Association, believe that ethical rules are sufficient for controlling

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192. WASH. REV. CODE § 18.28.010 (2013).

193. Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372, at *6 (E.D. Wash. May 27, 2011).

194. *Id.*

195. *See, e.g.*, CAL. FIN. CODE § 12100 (2013); 225 ILL. COMP. STAT. ANN. 429/10 (2013); U.D.M.S.A., § 2 (Nat'l Conference of Comm'rs on Unif. State Laws 2011).

196. *See Bronzich*, 2011 WL 2119372, at *7 (holding that an attorney who's broader legal practice may, in some small way, resemble debt settlement should not be liable under the state's debt settlement statute).

197. BAR REPORT, *supra* note 3, at 94.

debt settlement companies using the purported attorney model.[198] Indeed, a firm like Bay View that operates as a debt settlement company would conceivably be in violation of several ethics rules. One may argue that offering debt settlement services in and of itself might constitute a breach of the duty of competence[199] or diligence.[200] Likewise, an attorney that charges fees that render it impossible for a client to accumulate enough funds within the timeframe for payment to creditors might be in violation of the ban on unreasonable fees.[201]

However, the penalties to attorneys under ethics rules are not sufficient given the severity of punishment for non-attorneys in the debt settlement area. In *Cleveland Bar Association v. Nosan*, the Ohio Supreme Court suspended an attorney for six months for operating a debt settlement business, sharing profits with non-attorneys, and allowing non-attorneys to counsel his clients — a suspension which would be stayed if the defendant repaid any unearned fees.[202] Presumably, an attorney proven to have violated ethics rules could also be open to malpractice suits from clients. If the attorney were prosecuted under the state's debt settlement statute, he could be found guilty of a misdemeanor and would be liable to the state for fines or jail time.[203] Furthermore, rather than forcing clients to sue in a series of individual malpractice suits or a class action, a debt settlement statute would allow the state attorney general to seek restitution for consumers in addition to the criminal penalty. This would reduce the number of follow-on suits and ensure that each of the wronged consumers receives some prorated amount of whatever funds are available.[204] Additionally, the lawyer would likely be found to have breached Ohio's rules of professional conduct for "committing an illegal act that reflects adversely on the lawyer's honesty or trustworthiness."[205] The penalty under the debt settlement statute would be significantly more severe than a six-

198. *Id.*
199. MODEL R. OF PROF'L CONDUCT R. 1.1 (2013).
200. *Id.* R. 1.3.
201. *Id.* R. 1.5.
202. 840 N.E.2d 1073 (Ohio 2006).
203. OHIO REV. CODE ANN. § 4710.99 (West 2012).
204. *Id.* § 4710.04.
205. OHIO ST. R. PROF'L CONDUCT R. 8.4. *See also Nosan*, 840 N.E.2d 1073.

month suspension and would limit the number of suits seeking restitution, thus reducing the strain on the courts.

The *Nosan* case is a parable of bad legislative drafting. Under Ohio law, Nosan could have faced a misdemeanor sentence, rather than potential suspension from the practice of law — this is what the state legislature determined to be an appropriate deterrent.[206] Unfortunately, the relevant Ohio statute exempts "[d]ebt [settling] incurred in the practice of law"[207] and the Ohio Supreme Court and the Cleveland Bar Association both acknowledged that Nosan was engaged in practicing law while operating the debt settlement business.[208] Nonetheless, the state had good reason to include the attorney exemption. As discussed, it is conceivable that an attorney may, at some point, need to negotiate a settlement between a client and one of their creditors. Yet in these situations, the Washington rule requiring that the provision of debt settlement services be incidental to the practice of law proves to be superior.[209] Under the Washington standard, an attorney operating a legitimate practice who finds himself having to settle a debt would still be exempt, while attorneys operating full-blown debt settlement companies using their *juris doctor* as a shield would be held liable. This would apply what the state legislature believed to be the necessary deterrent and punishment to those cases.[210] Thus, the Washington standard proves to be the superior means for balancing these competing legislative interests.

B. REGULATING THIRD-PARTY ADMINISTRATORS

Regulation of third-party administrators needs to be strengthened by increasing liability and subjecting administrators to the same penalties as debt settlement companies. Though currently

206. *See* OHIO REV. CODE ANN. § 4710.99 (West 2004).
207. *Id.* § 4710.03.
208. *Nosan* 840 N.E.2d 1073, 1075, 1077. *Compare id., with In re* Allegro Law LLC, No. 10-30631-WRS, 2010 WL 2712256 (M.D. Ala. July 6, 2010); *In re* Nelms, ASB No. 08-247(A), ASB No. 09-1481(A), CSP No. 09-1684(A) (Nelms was an attorney operating Allegro Law, a debt settlement company. He was found liable under both the state rules of professional responsibility and the state debt settlement statute).
209. WASH. REV. CODE § 18.28.010 (2013). *See also* Bronzich v. Persels & Assocs., No. CV-10-0364-EFS, 2011 WL 2119372, at *6 (E.D. Wash. May 27, 2011).
210. *See id.*

limited, the present regulation of third-party account administrators on the state and federal levels is a step in the right direction. Regulation could be improved by stripping the undeserved liability shield that administrators currently enjoy. As discussed, most debt settlement firms are affiliated with either Global Client Solutions LLC[211] or NoteWorld LLC.[212] Global Client Solutions and NoteWorld wield considerable market power — each manages accounts for hundreds of independent debt settlement companies.[213] While debt settlement companies may be thinly capitalized and unable to pay damages, these firms wield considerable capital and have been able to stay in business despite settling multiple class action suits.[214] Given their market power, these firms hold sway over the smaller debt settlement companies who work with them and need their services in order to function. Likewise, the firms clearly have the funds needed to make consumers whole if injured by debt settlement companies. Thus, while Washington State was correct in perceiving the need to specifically regulate third-party payment processors and in counting their fees towards the total fee charged by the debt settlement companies, the state was wrong to exempt them from regulation of the debt settlement industry.[215]

Giant account administrators have the power to privately reinforce state regulation among the hundreds of debt settlement firms they work with. Administrators ought to be incentivized to do so by being held liable when their partner debt settlement firms violate state or federal regulations. Of course, the present system does hold third parties liable in some cases, but it forces consumers to litigate the issue of third party liability under the state statutes, thereby increasing litigation costs for consumers who are already in dire financial straits due to their massive

211. *See, e.g.*, Estrella v. Freedom Financial Network, LLC, No. CV 09-03156 SI, 2012 WL 4645012 (N.D. Cal. Oct. 1, 2012); Guidotti v. Legal Helpers Debt Resolution, LLC, 866 F. Supp.2d 315 (D. N.J. 2011); Complaint, People v. Nationwide Asset Servs., Inc., 888 N.Y.S.2d 850 (N.Y. Sup. Ct. 2009); Pavlov v. Debt Resolvers USA, Inc., 907 N.Y.S.2d 798 (N.Y. Civ. Ct. 2010); Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486 (2011).

212. *See, e.g.*, Morefield v. Noteworld, LLC, 2012 WL 1355573 (S.D. Ga. 2012); Wheeler v. Noteworld, LLC, 2012 WL 3061489 (E.D. Wash. 2012); Complaint, Rajagopalan, *supra* note 33.

213. *Guidotti*, 866 F. Supp.2d 315 at 323.

214. *See, e.g.*, *Estrella*, 2012 WL 4645012; *Morefield*, 2012 WL 1355573.

215. WASH. REV. CODE § 18.28.010 (2013).

debt.[216] This may deter litigation and effective enforcement. Thus, the federal and state governments ought to amend their regulations to define debt settlement services as a complete package including the services provided by third parties. Further, states should define debt settlement companies as including any entities that provide services as part of that package, rendering third party firms vulnerable to the full range of enforcement.

VI. CONCLUSION

An attorney for Consumers' Union once described regulating the debt settlement industry as a game of whack-a-mole: as soon as a statute is enacted to strike down one business model, another business model pops up.[217] Justice Tom Chambers of the Washington Supreme Court has agreed, writing that "[a]s cats are drawn to cream, many for-profit debt adjusters will be attracted to the most unsophisticated of consumers."[218] Over half a century of regulation shows that the debt settlement industry is adept at evolving in order to circumvent regulations and stay in business. The latest evolution has brought two new models to prominence: the purported attorney and the third-party account administrator. While these models have not always been successful in avoiding liability, they have caused severe damage to consumers. The federal and state governments must once again examine their statutes pertaining to the industry and amend them as necessary to prevent these new abuses.

216. *See, e.g.*, *Estrella*, 2010 WL 2231790.
217. Ody, *supra* note 88.
218. Carlsen v. Global Client Solutions, LLC, 171 Wash. 2d 486, 502 (2011) (Chambers, J. Concurring).