Options for Consumers in Crisis:

An Updated Economic Analysis of

The Debt Settlement Industry

(Data as of March 31, 2015)

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1. Executive Summary

Please refer to §2 for a Glossary of capitalized terms used in this report.

In 2012 the American Fair Credit Council commissioned the 2012 Report, the original study upon which this update is based, with the objective of performing the first-ever independent analysis of the economic consequences of participation by financially challenged consumers in debt settlement programs. The 2012 Report examined the outcomes of more than 1.0 million Accounts associated with approximately 170,000 individual Clients enrolled in debt settlement programs from January 1, 2006 through December 31, 2012.

Perhaps the most significant challenge faced in the 2012 Report was separately analyzing consumer outcomes from what are, essentially, two completely different business models: Version 1.0 (the "advance fee model," which was virtually universal prior to October 27, 2010) and Version 2.0 (the "no-advance fee model," which became the only legitimate operating model for debt settlement companies operating on and after October 27, 2010). Moreover, because Version 2.0 program enrollments occupied only 26 months of the 84-month study period, Version 2.0 programs were not only underrepresented in all segments of the Account population but not truly predictive due to a lack of program completion for any Version 2.0 vintage.

With this first update of the 2012 Report, the number of Version 2.0 Clients in the study population is now greater than the number of Version 1.0 Clients,[1] with the result that Version 2.0 trend lines may now be extrapolated with a much higher degree of confidence. Subsequent updates of the analysis presented here are expected to discontinue reference to Version 1.0, as it is largely irrelevant to the debt settlement industry today, and focus exclusively on Version 2.0 Clients and outcomes.

The analysis presented below addresses the outcomes of 1.9 million individual Accounts that were enrolled in debt settlement programs from January 1, 2006 through March 31, 2015. These Accounts were associated with approximately 297,000 individual Clients. As described in greater detail below, the following conclusions are evident:

- Across all Version 2.0 Client types, Debt Reduction is $2.94 for each $1.00 of Fees, which compares with $3.04 of Debt Reduction for each $1.00 of Fees for all Version 1.0 Client types. It is clear that, by transferring risk of success from the Clients to the providers, even with the increased fees associated with Version 2.0 programs

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[1] Although the pool of Version 1.0 Clients has remained static, as Version 1.0 has not been offered by any debt settlement company since October 27, 2010, the study population for this update includes an additional population of Version 1.0 Clients acquired by one or more of the study participants after December 31, 2012.

Version 2.0 is both producing significant consumer benefits and making those benefits available to more persons.

- Debt settlement Clients as a group (including all Active, Terminated or Completed Clients for both Version 1.0 and 2.0) have realized $2.99 in Debt Reduction for every $1.00 of Fees (*i.e.*, $1.99 of Savings). (see Charts 5.1, 5.7, 5.8, 5.9, 5.10, and 5.11).[2]

- The average rate of Debt Reduction is less than that shown in the 2012 Report (then $3.15 for each $1.00 of Fees). The reduction is principally due to:

    - An increased proportion of Version 2.0 Accounts, which, on average, realize lower Debt Reduction.

    - An expanded population of Version 1.0 Accounts included in the study. These Accounts were originated prior to the implementation of the FTC Rule by non-participating entities, and were not held or serviced by the participating entities at the time data was collected for the 2012 Report.

- At the time of the 2012 Report, only two years of data on Version 2.0 Accounts was available. The 2015 Report benefits from the more than four years of data now available on Version 2.0 Accounts (and nine years of data for Version 1.0 Accounts). The expanded data provides evidence supporting the following conclusions.

    - Version 2.0 Clients typically reach settlements earlier in the program than Version 1.0 Clients (see Charts 5.2 and 5.4), with the first settlement occurring, on-average, at 4.5 months versus 8.0 months, respectively.

    - Since Version 2.0 Clients do not pay Fees until a settlement is reached, these Clients have experienced, and will continue to experience, Savings irrespective of program tenure (see Chart 5.2). On average, Version 1.0 Clients required seven months of program tenure to realize Savings, whereas Version 2.0 Clients generally realize Savings on the first settlement.

    - Version 2.0 Clients are more likely to obtain Savings than Version 1.0 Clients. More than 95% of Completed and Active Version 2.0 Clients realize Debt Reduction greater than their Fees (*i.e.*, a Savings, see Charts 5.2 and 5.3). Further, since Version 2.0 Clients can reject any offered settlement for any reason or no reason at all, it is very unlikely that a Version 2.0 Client will

[2] The charts and tables in this report are numbered by the section in which they appear and sequentially within those sections.

experience a lack of Savings in connection with any given settlement (see Chart 5.3).[3]

   - These findings support the conclusion that Version 2.0 Clients have a significantly greater probability of realizing Savings and therefore experience significantly less risk from participation in debt settlement programs than Version 1.0 Clients (see Chart 5.3). It is also the case, however, that Version 2.0 Clients pay increased Fees relative to Version 1.0 Clients in exchange for these benefits.

- Clients across all vintages are achieving substantial reductions to their account balances (see Charts 5.7, 5.8, 5.9, 5.10, and 5.11). Moreover, since Version 2.0 Clients only pay for settlements actually achieved, economic benefit should be measured on an account-by-account basis, not on a total-debt basis (in other words, Clients receive economic benefit from each settlement, irrespective of whether or not additional debts are settled). See §6 below, including Charts 6.3, 6.4, and 6.5.

- After approximately nine months (see Charts 6.1 and 6.2), accretion experienced by Clients on Enrolled Debt due to interest, fees, and penalties, falls below accretion that would otherwise occur if Accounts were to amortize at normal credit card rates of interest.

These findings indicate that, for all vintages (even the earliest), debt settlement is an effective debt relief option.

2. Glossary of Terms Used in this Report

As used in this report, unless the context otherwise requires, the following terms have the meanings given below.

2012 Report. The original study described in paragraph 1 of the Executive Summary.

Account. A record of an obligation owed by a Client to a creditor. An Account may have one of three different statuses: an "**Active Account**" is an Account that is currently enrolled in an active debt settlement program; a "**Settled Account**" is an Account that has been successfully settled; and a "**Terminated Account**" is an Account that has been withdrawn prior to settlement by a Client from a debt settlement program.

[3] Rarely, a settlement will occur that, when fees are included, aggregates more than 100% of the enrolled amount.

AFCC. The American Fair Credit Council. The American Fair Credit Council (formerly known as "TASC," the acronym for The Association of Settlement Companies), is the industry trade association representing virtually all of the national debt settlement companies operating in compliance with the FTC Rule.

Client. A consumer who has enrolled in a debt settlement program. A Client may be in one of three different statuses: an "**Active Client**" is a Client that is currently enrolled in an active debt settlement program; and a "**Terminated Client**" is a Client who has withdrawn from a debt settlement program prior to achieving "completed" status. The definition of "**Completed Client**" depends upon whether the Client is in a Version 1.0 or Version 2.0 program; refer to Section 4(c), below, for additional information on how "Completed Client" is defined for purposes of the analyses contained in this report.

Debt. An unsecured obligation, represented by an Account, owed by a Client to a creditor. An "**Enrolled Debt**" is a Debt that has been enrolled by a Client in a debt settlement program. Debts eligible for enrollment in a debt settlement program are predominately credit card obligations and other forms of unsecured indebtedness (including medical debt and non-Federally guaranteed student loan obligations); secured indebtedness is not eligible for debt settlement.

Debt Reduction. The difference between the amount owed by a Client to a creditor at the time of settlement and the amount for which that Debt is actually settled. By way of example, if a Client owes $10,000 at the time of settlement and the Debt is settled for $4,000, the Debt Reduction would be $6,000.[4]

Fees. The compensation charged by a debt settlement services provider. Note that fees charged by both debt settlement enterprises and credit counseling organizations are very different from each other and vary widely by state.

FTC. The Federal Trade Commission, the United States governmental agency responsible for oversight of certain aspects of the debt settlement industry.

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[4] The FTC Rule mandates that, for marketing purposes, "savings" must be measured as the difference between the amount paid and the original (i.e., enrolled) balance of a Debt. However, using the original balance as a baseline for calculating savings distorts the economic benefit realized by a Client because, by ignoring accretion, actual savings is understated. Accordingly, for analytic purposes, the economic analyses presented in this report generally use actual savings, meaning savings measured against the amount owed at time of settlement.

FTC Rule. The Amended Telemarketing Sales Rules (16 C.F.R. Part 310 et seq.), as issued by the FTC on July 29, 2010, which rule implemented the "advance fee" ban, effective as of October 27, 2010.

Savings. The net economic value of a settlement to a Client. "Savings" represents Debt Reduction minus Fees. By way of example, the settlement of a $10,000 Debt for $4,000 with a 20% Fee yields Savings of $4,000 ($6,000 of Debt Reduction minus the $2,000 Fee).

Version 1.0/Version 2.0. The terms used to denote pre- and post-FTC Rule debt settlement programs, respectively. "Version 1.0" programs are debt settlement programs that were entered into on or prior to October 26, 2010; "Version 2.0" programs are debt settlement programs that were entered into on or after October 27, 2010, the effective date of the FTC Rule.

3. Introduction and Background

a. Debt Settlement

Debt settlement is the process by which a service provider, working on behalf of a Client (a financially distressed consumer enrolled in the service provider's debt settlement program), negotiates the settlement and discharge of the Client's unsecured indebtedness. Debt settlement generally serves those who cannot qualify for or afford other debt relief options, such as consumer credit counseling, or who are unable to satisfy the means test required as a prerequisite to personal bankruptcy.

Although the debt settlement process involves functioning as the intermediary between the debtor and the creditor, debt settlement service providers do not provide legal representation, nor do they provide tax or bankruptcy advice or counseling services. Similarly, debt settlement service providers do not provide assistance with secured indebtedness, such as mortgages or any other type of secured indebtedness (a creditor holding secured debt has no incentive to negotiate, or reason to accept, a settlement of less than the value of the underlying security).

Debt settlement has been available to commercial enterprises for many years, although it only became widely available as an option for consumers in 2003 and took off, as an industry, following the passage of the Bankruptcy Reform Act of 2005. The Bankruptcy Reform Act of 2005 made it much more difficult and expensive for consumers to seek discharge of their debts, particularly credit card-related debts.[5]

[5] Federal Reserve Bank of Boston, *Forgive and Forget: Who Gets Credit After Bankruptcy and Why?*, Working Paper No. QAU09-2, July 23, 2009, p.9.

b. The American Fair Credit Council

The AFCC's predecessor, TASC, was formed in 2005 for the purposes of articulating clear and fair operating standards for the debt settlement industry and promoting strong legislation that protects consumers from both real and perceived abusive practices.[6] TASC changed its name to the American Fair Credit Council following the October 2010 adoption of the FTC's advance-fee ban, discussed below, to reflect a new and expanded mission.

The AFCC's standards, along with industry "best practices" and the association's mission statement, may be found on its website at www.americanfaircreditcouncil.org.

c. The FTC & the Evolution of the Debt Settlement Business Model

Historically, a majority of the debt settlement industry charged fees based on a percentage of the amount of Debt a Client enrolled into the program (commonly around 15% of enrolled debt).[7] Fees were collected in installments over the first half of a program's term, often with the result that a Client paid a substantial amount of fees in advance of receiving settlements. This business model became known as the "advance fee" model and is referred to in this study as the Version 1.0 model.

Although AFCC members have historically delivered Debt Reduction substantially in excess of Fees, the experience of some consumers who paid Fees but received little or no Debt Reduction colored the public perception of the industry. In October 2008, in response to this perception, the FTC opened an inquiry into the business practices of the debt settlement industry, focusing specifically on the advance fee model. In July 2009 the FTC issued a draft rule that prohibited the advance-fee model. The FTC Rule took effect in October 2010.

d. A Paradigm Shift: The Client-Side Risks of Debt Settlement Have Been Absorbed by the Service Providers

The FTC Rule set in place the Version 2.0 model, a pay-for-performance requirement for those debt settlement service providers that are subject to FTC jurisdiction.[8] The Version

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6 See http://www.americanfaircreditcouncil.org/who-we-are

7 A small percentage of the debt settlement industry charged Fees based on a percentage of the Debt Reduction realized by the Client, often in combination with a monthly fee.

8 The FTC's jurisdiction extends only to certain persons who use an instrumentality of interstate commerce in the sale of service. However, the FTC Rule does not reach those whose sales process occurs in face-to-face interactions and persons operating under the provisions of Section 501(c)(3) and 501(q) of the Internal Revenue Code.

2.0 model effected a paradigm shift in terms of risk assignment. That is, the FTC Rule shifted the economic risk of program success from the consumer to the debt settlement service providers.[9] Providers incur considerable costs prior to obtaining a settlement. Now, per the FTC Rule, before the provider is entitled to recoup any of those costs, three contingencies must be satisfied: (1) the provider must negotiate the terms of settlement for a debt; (2) the Client must agree to the terms of the negotiated settlement; and (3) the Client must ratify that acceptance by making at least one payment to the creditor. If the Client fails to do any of these things, the provider will experience a financial loss because Fee revenue may only be realized when the Client actually agrees to a negotiated settlement.[10] Moreover, the Fee for the provision of debt settlement services may only be charged on a per-debt basis (*i.e.*, the provider may only collect the Fee attributable to the specific Debt being settled).[11] This model is referred to in this study as the Version 2.0 model.

e. Version 1.0 Accounts Are Nearly Extinct; Future Updates of This Report Will Focus Exclusively on Version 2.0 Outcomes

Many of the conclusions expressed in this Report provide comparisons between Version 1.0 and Version 2.0 Clients. At this time, the number of Version 2.0 Accounts exceeds the number of Version 1.0 Accounts in the data set. While most Version 2.0 Accounts are Active, the outcome of almost all Version 1.0 Accounts has already been determined (*i.e.*, either Settled or Terminated – only 6,000 Version 1.0 Accounts remain in Active status).

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[9] We understand that the FTC Rule's prohibition on the collection of fees in advance of delivery of settlements, resulted in approximately 80% of then-existing debt settlement service providers exiting the business. The exodus from the marketplace of many debt settlement service providers following the adoption of the FTC Rule was accompanied by the reactive – and temporary - rise of the so-called "legal model," which was touted as a way to avoid the reach of the FTC Rule. Under the legal model, a law firm serves as the interface for a debtor, enrolling the client in a face-to-face transaction while outsourcing the functions of marketing, customer service and negotiation to a third-party debt settlement services provider. Advocates of the legal model contend that, because a lawyer is actually enrolling the Client, the charging of advance fees is permissible. Both the FTC and certain state regulators and Attorneys General have sued different attorney model providers, with mixed results.

Legal model service providers that charge consumers fees in advance of the provision of debt settlement services are not eligible for membership in the AFCC. Thus, results from legal-model service providers are not included in the analyses presented in this report.

[10] Fees have generally increased to compensate the providers for assuming both the delay in revenue and the increased risk of Client rejection of a negotiated settlement. However, the negative impact on Savings resulting from higher fees has been offset by the improvement in timing of settlements (since funds accumulate more swiftly when Fees are not deducted), see Charts 5.2 and 5.4, and an improvement in the overall risk profile of Clients who no longer have to make an economic investment prior to obtaining Savings.

[11] The Fee that may be collected upon settlement of a debt must bear the same relationship to the total Fee for all Enrolled Debts as the settled debt bears to the total of all Enrolled Debts (*i.e.*, there is no "frontloading" of Fees allowed under the FTC Rule).

Consequently, and because Version 1.0 Accounts are no longer an option for consumers, subsequent updates of this analysis will only focus on the outcomes experienced by Version 2.0 Clients.

4. Scope of Engagement and Data Considered

a. Analytic Approach – Version 1.0 v. Version 2.0.

The objective of this report is to provide an independent and impartial analysis of the economic consequences of participation in a debt settlement program. It is premised on data obtained from the nation's largest debt settlement service providers, all of whom adhere to the AFCC's Code of Conduct. More specifically, the statistical data presented herein is representative of, and consistent with, entities that comply with the FTC Rule that Fees may only be charged at such time as the underlying Debt has actually been settled. The analysis includes approximately 297,000 Clients, with approximately 1,964,000 Accounts, residing in most of the 50 states as well as the District of Columbia and Puerto Rico. Ultimately, this analysis measures whether, and to what extent, a Client is economically advantaged by participation in a debt settlement program.[12]

As described below, in the Version 1.0 fee model Fees were assessed irrespective of outcomes at the Account level. For this reason, Savings is generally measured at the aggregate Client level. In the Version 2.0 fee model, however, Clients do not incur an obligation to pay Fees until they actually receive Debt Reduction via settlement(s) at the Account level. Thus, when measuring outcomes for Version 2.0 Clients, one should analyze Debt Reduction and Savings at the Account level. Indeed, a strong argument could be made that, for Version 2.0 Clients, economic outcomes should be measured ***only*** at the Account level, given that (1) Clients may accept or reject a settlement for any reason or no reason at all, (2) Clients may withdraw from a Version 2.0 program without penalty at any time and (3) Clients pay no Fees unless they accept an offered settlement.

b. Version 1.0 v. Version 2.0 Data

In the 2012 Report, the volume of available data for Version 1.0 Clients and Accounts was substantially greater than for Version 2.0 Clients. This relationship has now inverted.

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[12] This report has not excluded any Clients or Accounts based on their respective outcomes (*e.g.*, whether the Client terminated within one month of enrollment or exited without having achieved a settlement) despite the fact that valid reasons exist to consider such exclusions. Further, it was deemed to be beyond the scope of this report to address or attempt to monetize either the "soft" benefits (*i.e.*, the value to a Client of improved cash flow when the Client chooses to stop making minimum monthly credit card payments and substitutes a substantially reduced periodic deposit requirement) or the "soft" costs (the detriments of various debt relief alternatives, such as damage to one's credit report, the social costs of bankruptcy, etc.).

This is consistent with an increasing number of Clients enrolling in more recent periods (see Chart 4.2), as well as the FTC prohibition on Version 1.0 Fee models. Table 4.1 summarizes the distribution of Version 1.0 and Version 2.0 Clients included in the data sets analyzed in this report.

Table 4.1

Fee Model	**Version 1.0**	**Version 2.0**
Enrolled Clients	132,000	165,000
Enrolled Accounts	831,000	1,133,000
Total Enrolled Debt	$3.9 billion	$5.0 billion
Average Client Tenure	22.1 months	13.5 months
Average Account Tenure[13]	14.8 months	9.6 months

A significant reason that Version 2.0 Clients have a shorter Average Client Tenure and Average Account Tenure is that Version 2.0 Accounts settle more rapidly than comparable Accounts in Version 1.0 programs.[14]

Chart 4.2 below summarizes the Accounts included in the analysis herein based upon the date of enrollment as of March 31, 2015:

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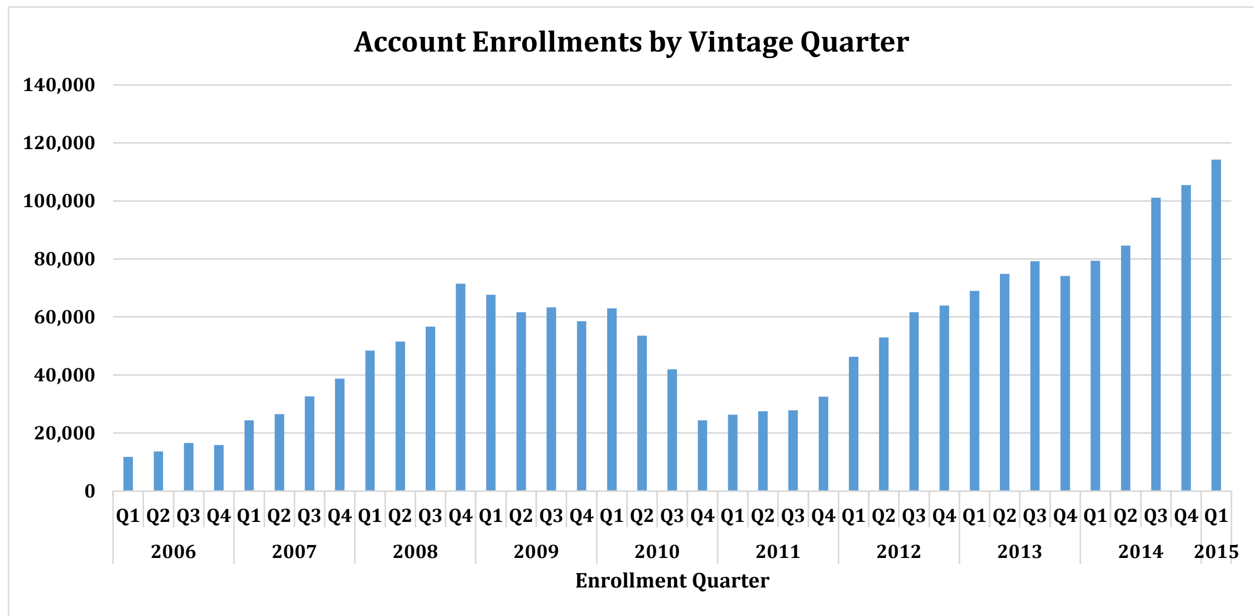
[13] Average Client tenure measures the total time that the Client (has) participated in the program based upon the longest-lived Account. Therefore, average Client tenure is greater than average Account tenure, which measures all Accounts irrespective of the related Client's total tenure in a debt settlement program.

[14] The Average Client and Account Tenure presented in Table 4.1 include all Clients and Accounts. As a result, the Version 2.0 values should be expected to increase over time as Clients and Accounts added in more recent periods progress through debt settlement programs.

Chart 4.2



The number of Account enrollments decreased precipitously in late 2010 as the industry contracted following the adoption of the FTC Rule (*i.e.*, the Version 2.0 fee model).[15] Subsequent to that time, the number of enrolled Accounts grew significantly, starting in late 2011.

c. <u>Critical Client and Account Attributes</u>

The data included in this report has been segmented into three principal categories:

- Completed: Clients that (i) in the case of Version 1.0 programs, have reached settlements of at least 75% of all of the Enrolled Debts, and (ii) in the case of Version 2.0 programs, have reached settlements of all Enrolled Debts that had not become Terminated Accounts;
- Terminated: Clients and Accounts that have withdrawn prior to completion and/or settlement; and
- Active: Clients and Accounts continuing to participate as of March 31, 2015.

Table 4.3 summarizes the status of the Accounts included in this analysis:

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15 Participants in this study have indicated that, following the adoption of the FTC Rule, they deliberately chose to limit enrollments due to negative cash flow considerations flowing from the adoption of the Version 2.0 model, considerations that required both increased capital investment and the slow build-up of expected Fee income associated with new enrollments.

Table 4.3

Type	Version 1.0	Version 2.0
Settled	348,000	376,000
Active	6,000	427,000
Terminated	477,000	330,000
Total	831,000	1,133,000

At any point in time an Active Client is likely to have multiple Accounts, each with a different status. In fact, there are many Clients that have settled one or more Accounts but have other Accounts that continue to be Active. At the Client level, this Client would be considered Active.

Clients enroll a median of six (6) Accounts into programs ranging from 24-48 months in duration. Debt Reduction may be generated from the settlement (*i.e.*, completion) of any one or more of these Accounts. It is notable that many Terminated Clients have experienced Savings (see §5 below).

d. <u>Vintage Analysis</u>

The data in this report has been analyzed and presented on a vintage basis. A vintage analysis examines the performance of a group of Clients that have been segmented by dates of enrollment. In this way, Clients that enrolled Debt in a given period may be compared more readily to Clients enrolling at different times. For example, the outcomes of Clients enrolling in December 2008 can be compared to the outcomes of Clients that enrolled in January 2011 after the same number of months has passed (*e.g.*, how much Debt Reduction was generated within 24 months of enrollment?).

Vintage analyses are the best way to achieve accurate analyses of performance when time is relevant to Client outcomes. By way of illustration, colleges report graduation rates as a percentage of students eligible for graduation. The graduation percentage is typically calculated by dividing the number of graduating seniors by the number of freshmen that entered the same class four years earlier. Stated differently, the graduation rate is not computed by dividing the number of graduating seniors by the total number students at the college because most college students have not completed enough coursework to be eligible for graduation at that time.

A concept similar to a graduation rate applies in the debt settlement industry (*i.e.*, a completion rate). That is, a Client that enrolled in January 2012 is less likely to have completed the program by December 2012 than a Client that enrolled in January 2010 or earlier. This is why vintage analysis is both relevant and necessary to an accurate

presentation of outcomes. Chart 4.4 illustrates how Accounts move from Active status to either Settled or Terminated over time:

Chart 4.4

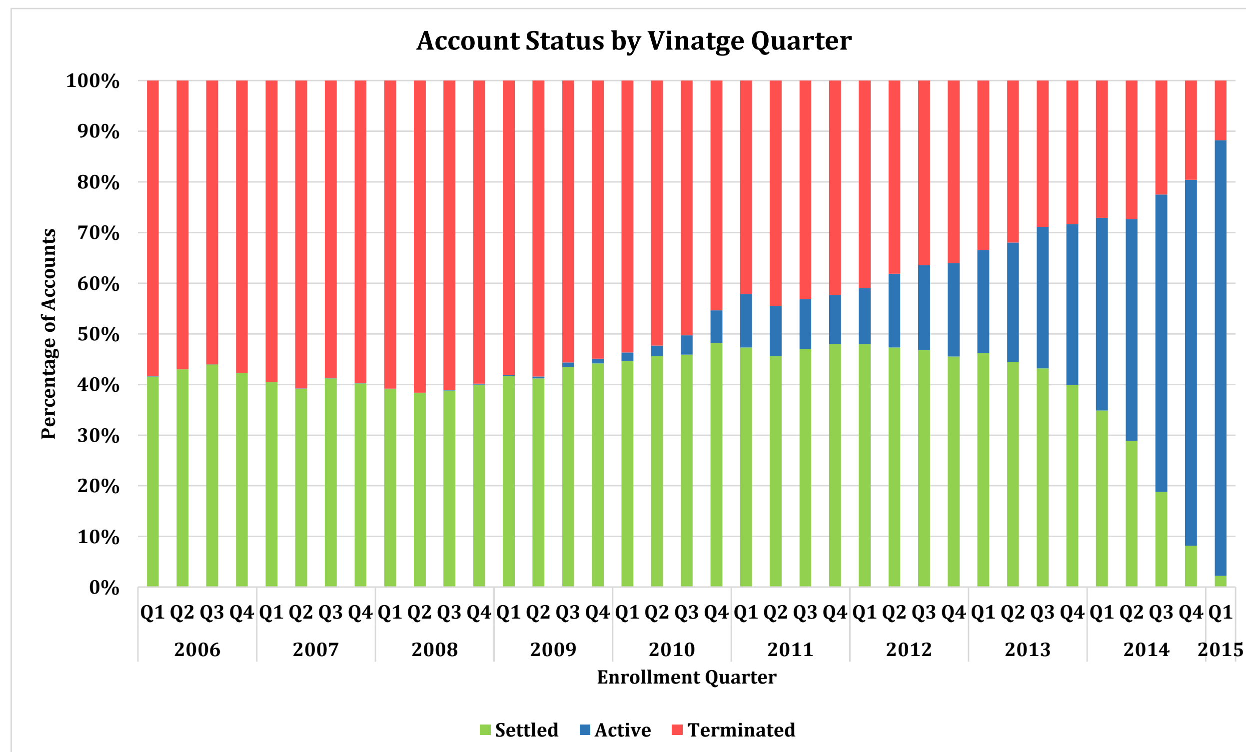
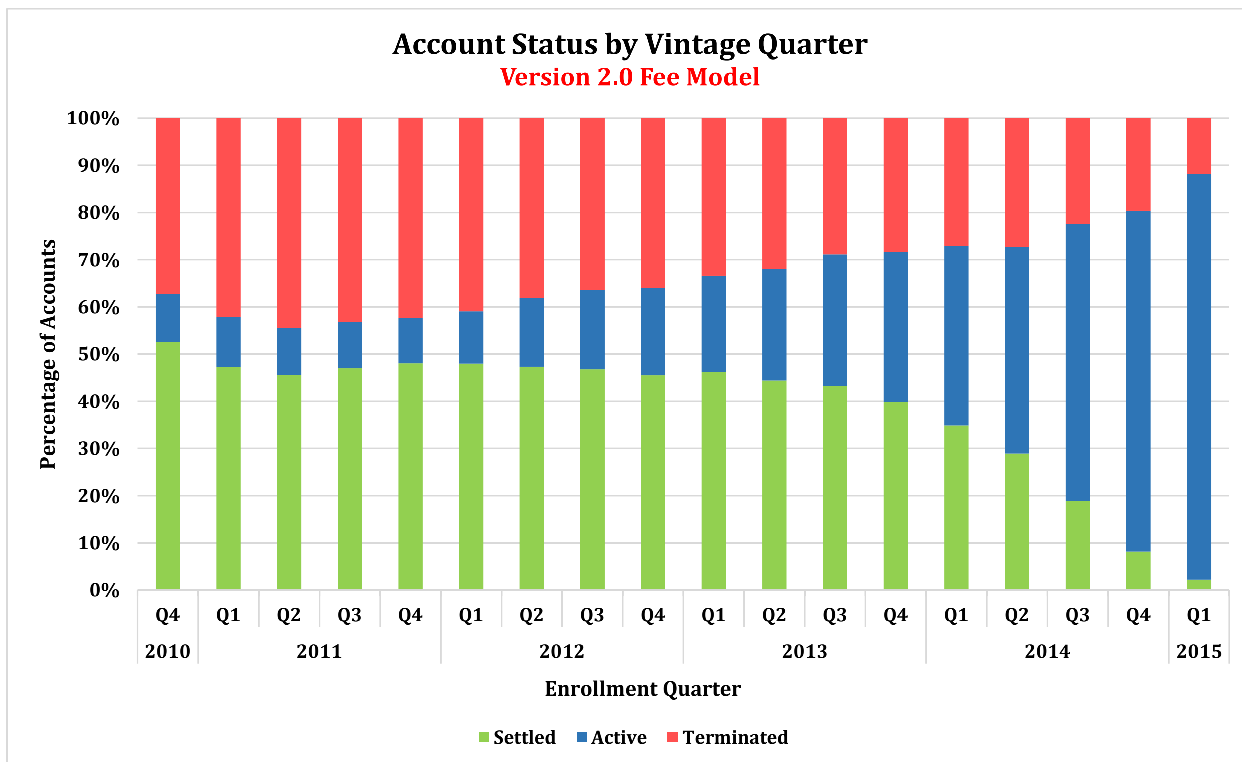


Chart 4.4 demonstrates that Terminated Accounts frequently materialize quite quickly after enrollment in the program. While Chart 4.4 includes all Terminated Clients, it is noteworthy that Version 2.0 Clients did not pay any Fees for Accounts that were not settled. Therefore, a reasonable argument can be made that classifying Version 2.0 Clients who have withdrawn prior to settlement of all Enrolled Debt as "Terminated" inappropriately inflates the termination statistics. Nevertheless, to be conservative, this analysis includes all "Terminated" Accounts (including Accounts withdrawn from a program by a Client who remains in Active status).

Chart 4.4 also illustrates that activity in vintages from 2006 through 2010 (i.e., most Version 1.0 programs) is substantially over (*i.e.*, there are relatively few Active Accounts remaining). From 2008 to 2010, the completion rate for Version 1.0 programs (which is measured at the Account level) ranges from approximately 38% to 45%.

To date, the completion rates for Version 2.0 Accounts have been demonstrably higher than for comparable vintages of Version 1.0 Accounts. For the earliest vintages (those from the fourth quarter of 2010 through the first quarter of 2012, the completion rate is approaching 50%.

Chart 4.5



In most Version 2.0 vintages, there are a substantial number of accounts that continue to be Active. Given the experience of these clients, it is reasonable to expect them to realize additional settlements.[16] For example, the typical Version 2.0 Client (*i.e.*, that is still active) that enrolled in the first quarter of 2011 has four (4) Settled accounts and two (2) accounts remaining Active. Thus, it is likely that completion rates (*i.e.*, settlement rates), on the Client rather than the Account level, for Version 2.0 Clients will also stabilize above 50%.

5. The Benefits of Participation in Debt Settlement Programs

a. <u>The Aggregate Economic Benefits of Debt Settlement Programs</u>

Chart 5.1 summarizes the total Debt Reduction and Fees experienced across all Client outcomes:

[16] *See* "Can Small Victories Help Win the War? Evidence from Consumer Debt Management," Journal of Marketing Research, Vol. XLIX (August 2012), pp. 487–501. This research found that achieving settlements earlier in a debt settlement program increased the probability of achieving subsequent settlements.

Chart 5.1

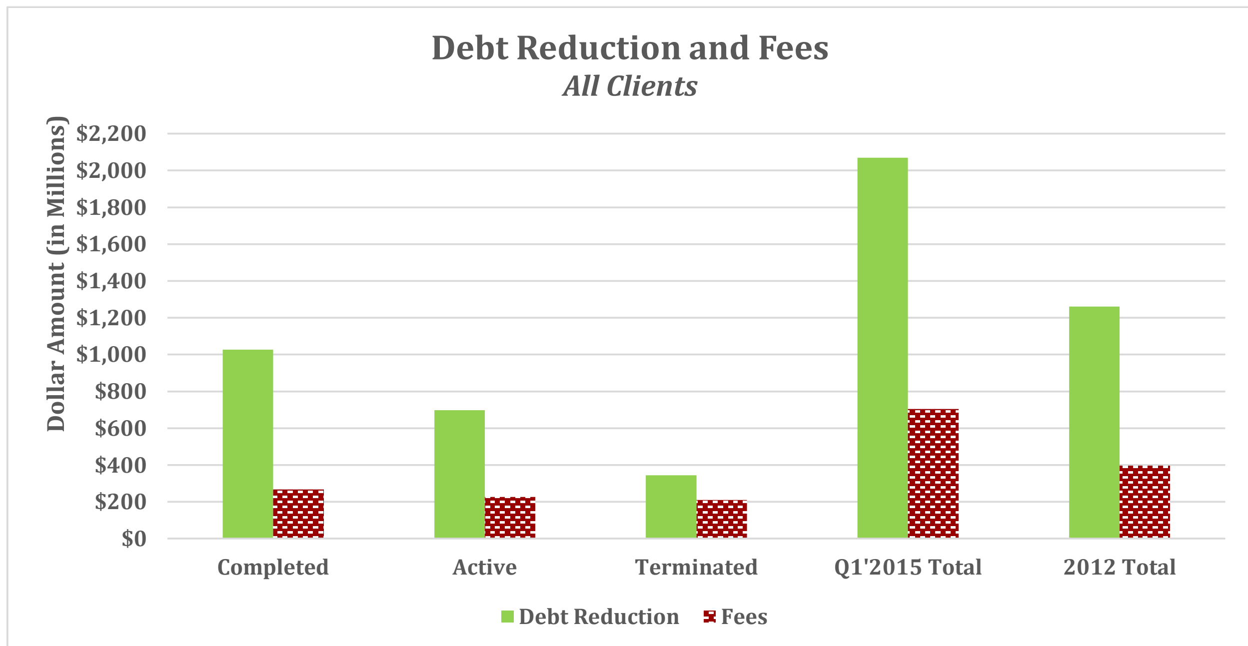
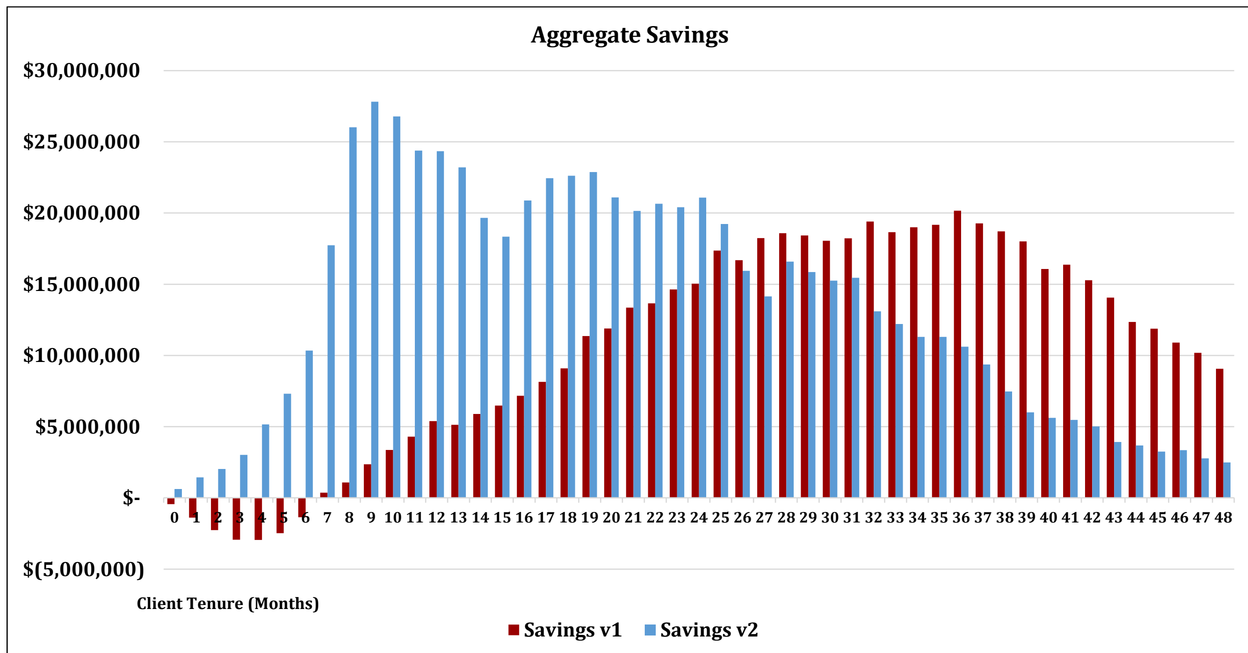


Chart 5.1 illustrates that all of the Clients studied for purposes of this report (including Terminated Clients) have realized $2.1 billion in Debt Reduction (*i.e.*, the difference between the Debt at the time of settlement and the amount actually paid to settle that Debt) while incurring Fees of $0.7 billion (*i.e.*, Savings of $1.4 billion, or approximately $4,600 per Client, regardless of status). In the aggregate, each segment of Clients (including Terminated) has experienced Savings.

In numerous ways, our analysis found a persuasive relationship between program tenure and Debt Reduction. Chart 5.2 illustrates the correlation between Savings (*i.e.*, Debt Reduction minus Fees) and program tenure even more directly. Chart 5.2 illustrates that Version 1.0 Clients typically achieved breakeven (that point where Debt Reduction equals Fees) after approximately six months. As a result, the only Client categories that did not experience Savings are those 1.0 Clients that did not remain in the program for more than six months.

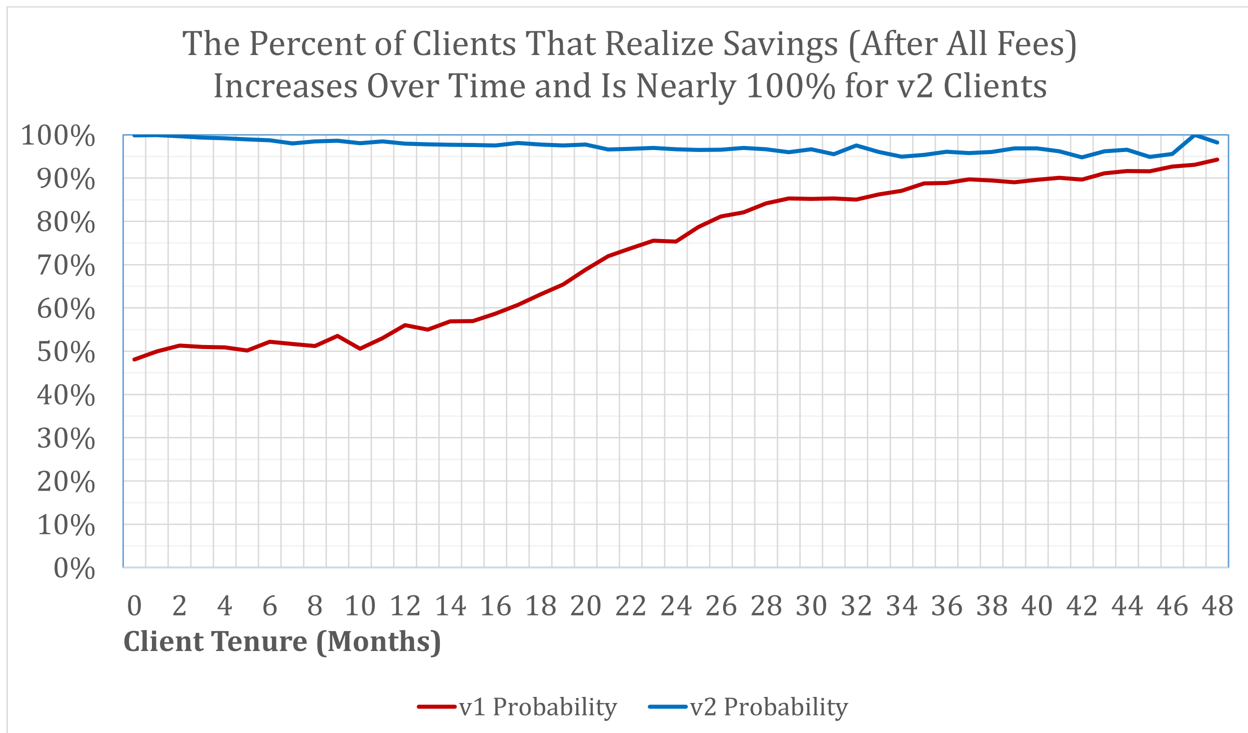
Chart 5.2



The economic outcomes of Version 2.0 Clients are more clearly positive. Since Fees are not paid by Version 2.0 Clients until such time as they realize a settlement, ***Version 2.0 Clients experience Savings in all periods after reaching the first settlement***. Since almost all settlements result in Debt Reduction that is greater than the Fees associated with the respective settlement, Version 2.0 Clients generally experience Savings with each settlement. This phenomenon is summarized in Chart 5.3, which shows that irrespective of Client tenure, more than 95% of Version 2.0 Clients realize Savings. In this way, the likelihood of success for Version 2.0 Clients is dramatically higher than for Version 1.0 Clients. These observations are consistent with other data-specific research regarding consumer experience in Version 2.0 models as compared to Version 1.0 models.[17]

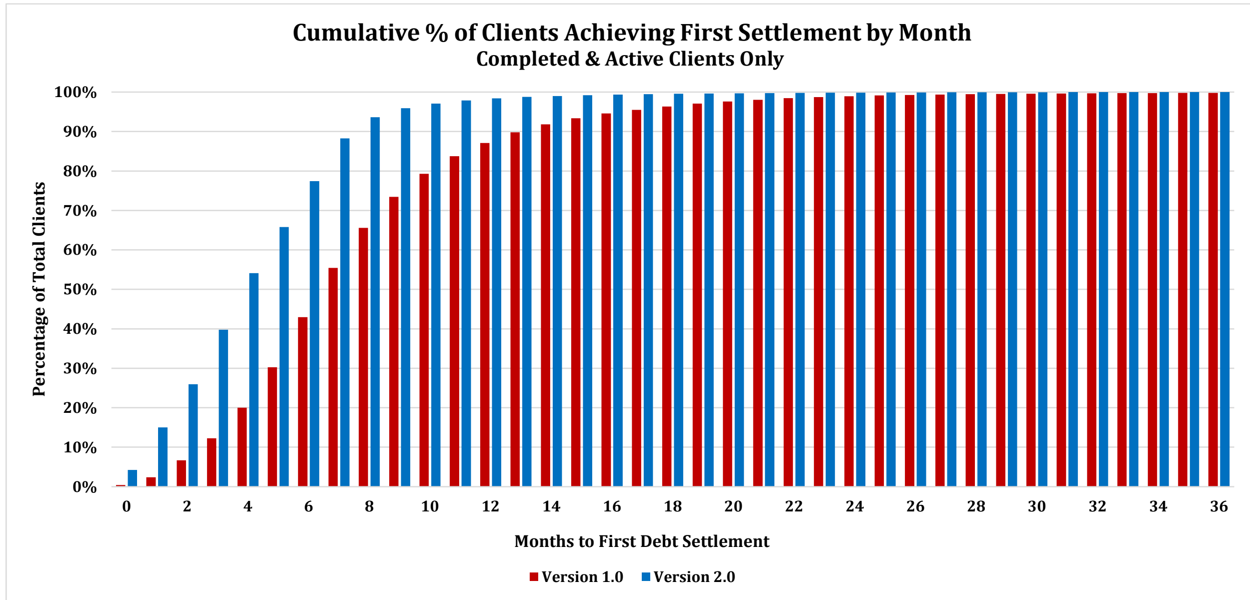
[17] The preliminary results of this report were presented at the AFCC's annual conference in March 2015. At that time, I participated on a panel with Professor Will Dobbie of Princeton University. Professor Dobbie presented the results of his ongoing study entitled "Pay-for-Performance in Consumer Finance: Evidence from the Debt Settlement Industry." Those results included that Version 2.0 Clients had a significantly higher likelihood of Debt Reduction in excess of Fees than Version 1.0 Clients.

Chart 5.3



Another important conclusion that may be drawn from Chart 5.2 is that Version 2.0 Clients are experiencing Savings much earlier than Version 1.0 Clients did. This issue is addressed further in Chart 5.4 below. Specifically, Chart 5.4 illustrates the timing of the first settlement achieved by Completed and Active Clients, and demonstrates that over 50% of these Version 2.0 Clients experienced at least one settlement within four (4) months of enrollment. By month eight (8), over 90% of these Version 2.0 Clients had experienced at least one settlement. In comparison, only 12% of Completed or Active Version 1.0 Clients had obtained a settlement by month four (4) and just 65% had obtained a settlement by month eight (8).

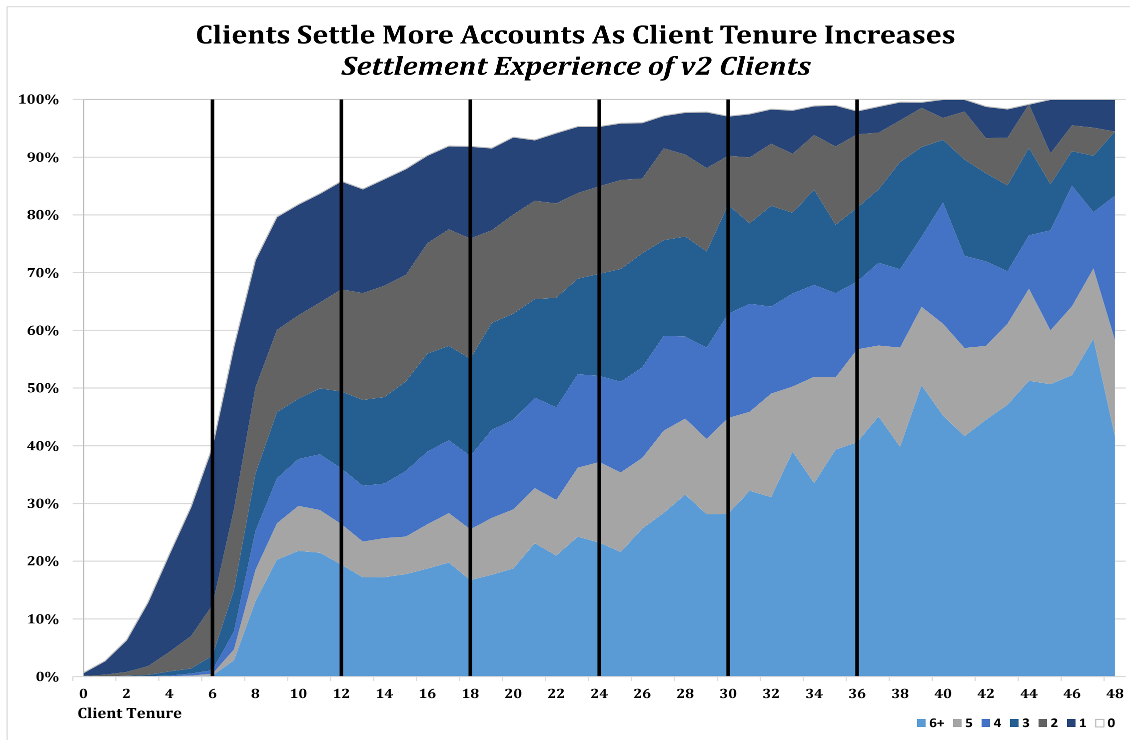
Chart 5.4



This effect is not isolated to the first settlement: having achieved a first settlement earlier, Version 2.0 Clients are therefore able to pursue subsequent settlements earlier.

Chart 5.5 expands on Chart 5.4 to include the settlement outcomes of Version 2.0 Clients of all types (*i.e.*, including Terminated Clients) based on Client Tenure. Chart 5.5 demonstrates how Version 2.0 Clients accumulate additional settlements as program tenure increases. For example, of all Clients with 30 months of tenure, 28% settle six or more accounts, 45% settle 5 or more accounts, 63% settle four or more accounts, 82% settle three of more accounts, etc.

Chart 5.5



b. Benefits as Measured at the Client and Account Levels

A useful measure of Client success in a debt settlement program is Debt Reduction per dollar ($) of Fees (*i.e.*, Debt Reduction ÷ Fees). Stated another way, if Debt Reduction is greater than $1.00, the client has realized Savings but if Debt Reduction is less than $1.00, the client has not realized Savings. Table 5.6 summarizes Debt Reduction per dollar of Fees across all Version 1.0 Client types:

Table 5.6

Client Type	**Version 1.0**
Completed	$4.56
Active	$4.33
Terminated	$1.42
Aggregate	$3.04

For Version 2.0 Clients, Debt Reduction is consistently in the range of $2.75 to $3.13 per dollar of Fees for all Client types (Completed, Active, *and* Terminated) (*i.e.*, Savings of $1.75 to $2.13 per dollar of fees for all Client types). Once again, this is because Fees are only paid at the Account level once the Client approves a settlement, which eliminates the sensitivity of Savings to Client type. Note that the reduction in the ratio of Debt Reduction ÷ Fees for Completed Clients from Version 2.0 to Version 1.0 reflects the economic effect of the FTC Rule to consumers.[18]

The following series of charts examine this metric across the Client tenure spectrum. Chart 5.7 summarizes the outcomes of Completed Clients.

Chart 5.7

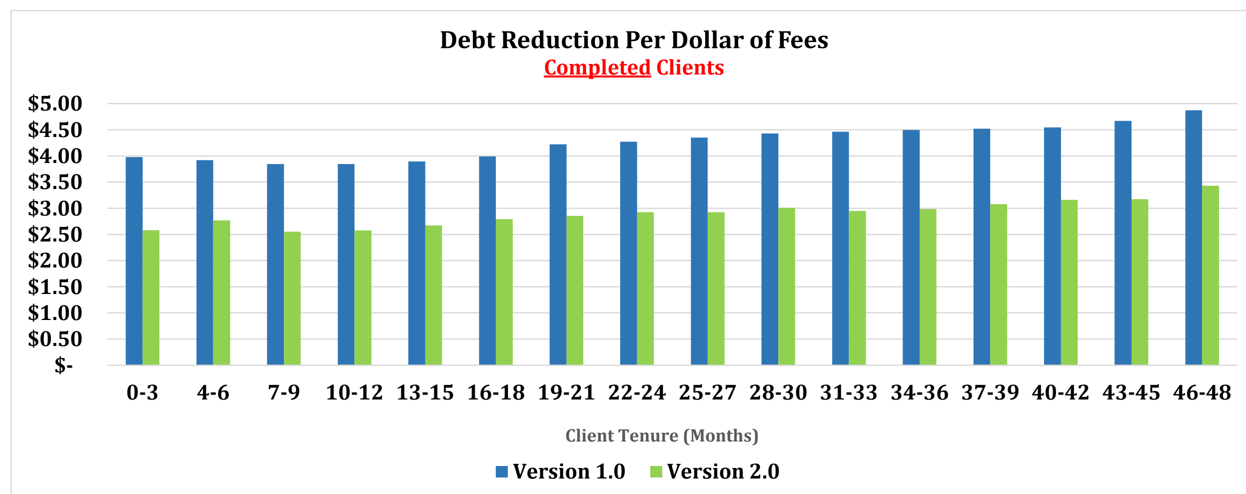


Chart 5.8 presents the same analysis for Active Clients. All segments of Active Clients have also received at least $2.85 in Debt Reduction for every $1.00 in Fees.[19]

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[18] See §3.d for additional discussion of this consideration. While there is increased certainty that Clients will obtain Savings in the Version 2.0 model, the lengthening of the term of the providers' revenue stream (with the attendant effects on cash flow), coupled with an increased risk of possibly not receiving Fees at all, has forced debt settlement service providers to adjust upward Fees associated with Version 2.0 programs to levels that are above those found in Version 1.0 programs.

[19] As of the time the data was obtained, there were no Active Version 1.0 Clients with a tenure less than 48 months.

Chart 5.8

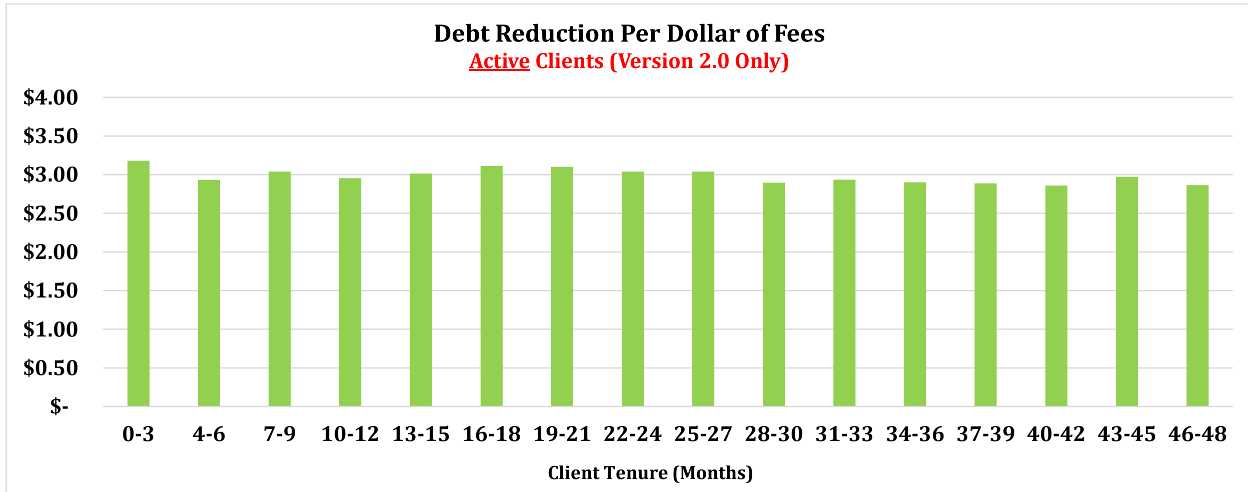
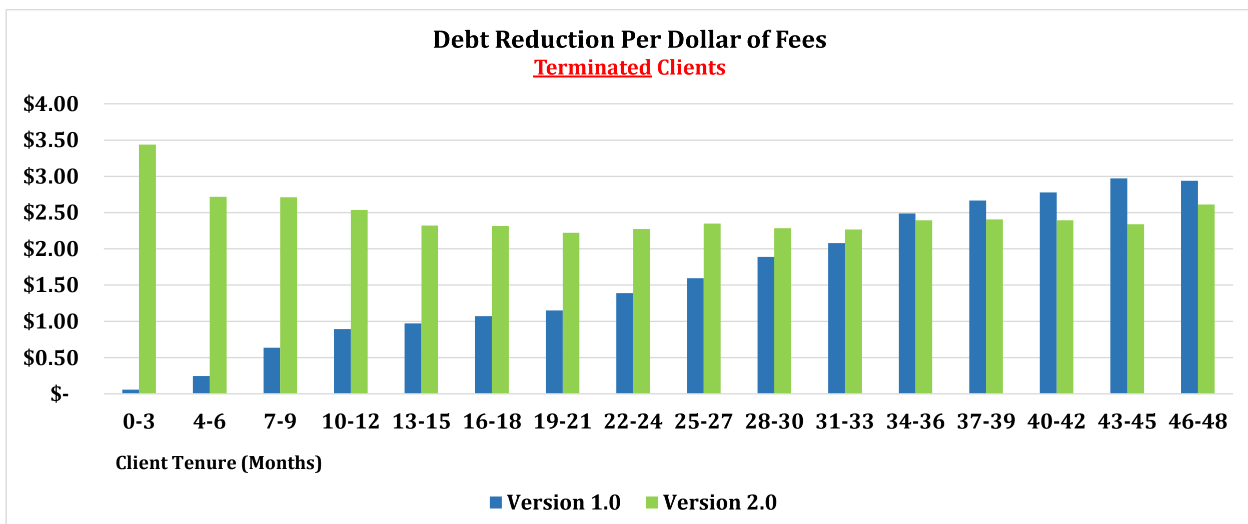


Chart 5.9 illustrates that Terminated Clients exhibit the same relationship between tenure and Debt Reduction. Chart 5.9 is consistent with Chart 5.2 in that the only segment of Clients that have not experienced Savings are, on the average, those Version 1.0 Clients that could not commit to a debt settlement program for more than six months. In fact, Chart 5.9 illustrates that ***all*** vintages of Terminated Clients with a tenure greater than 30 months experienced ***at least*** $2.00 of Debt Reduction for every $1.00 in Fees (*i.e.*, $1.00 of Savings), and ***all*** vintages of Version 2.0 Terminated Clients experienced at least $2.25 of Debt Reduction for every $1.00 in Fees, ***regardless of tenure***. This analysis explains why an examination of Client Savings is more meaningful than Client-level completion rates, and provides support for the thesis that, for Version 2.0 programs, analysis at the Account, rather than at the Client, level is the most meaningful way to assess economic outcomes.

Chart 5.9



c. <u>The Debt Reduction Experienced By the Typical Version 2.0 Completed Client</u>

Chart 5.10 summarizes the weighted-average outcomes for Completed Clients of all tenures included in this analysis. Once again, Chart 5.10 illustrates the correlation between the amount of Debt, Debt Reduction, and Client tenure.

Chart 5.10

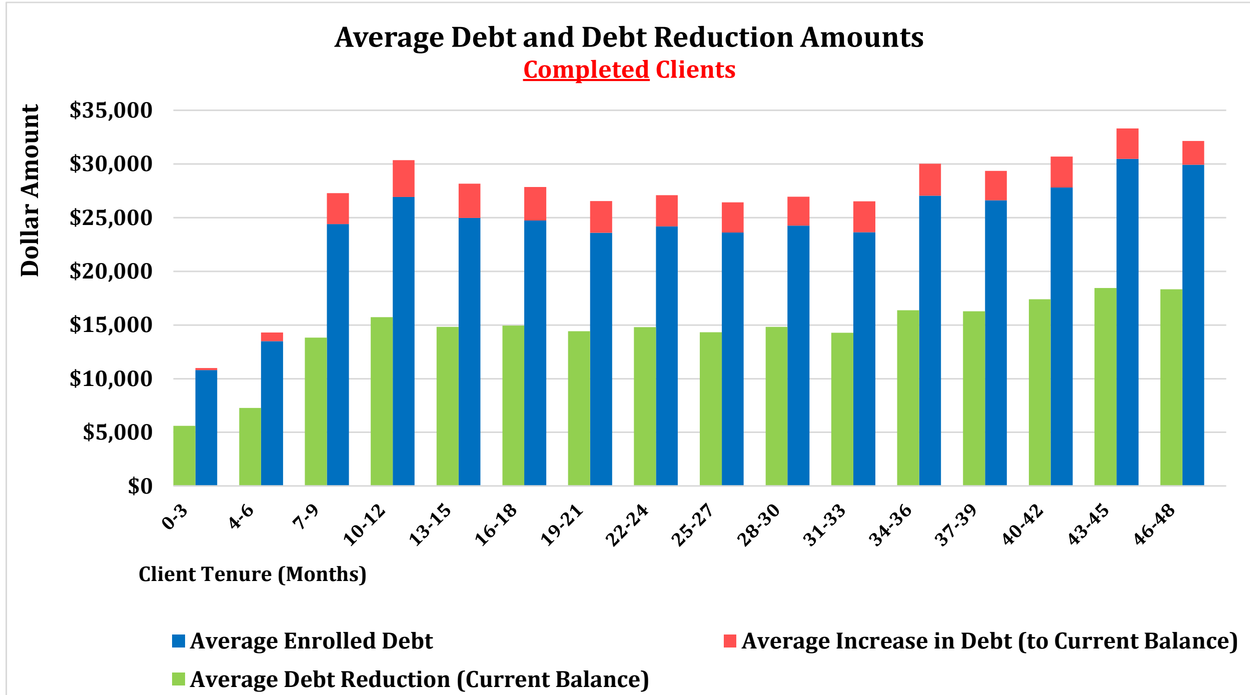


Chart 5.11 compares the typical Completed Client performance at the Account level for each Fee model:

Chart 5.11

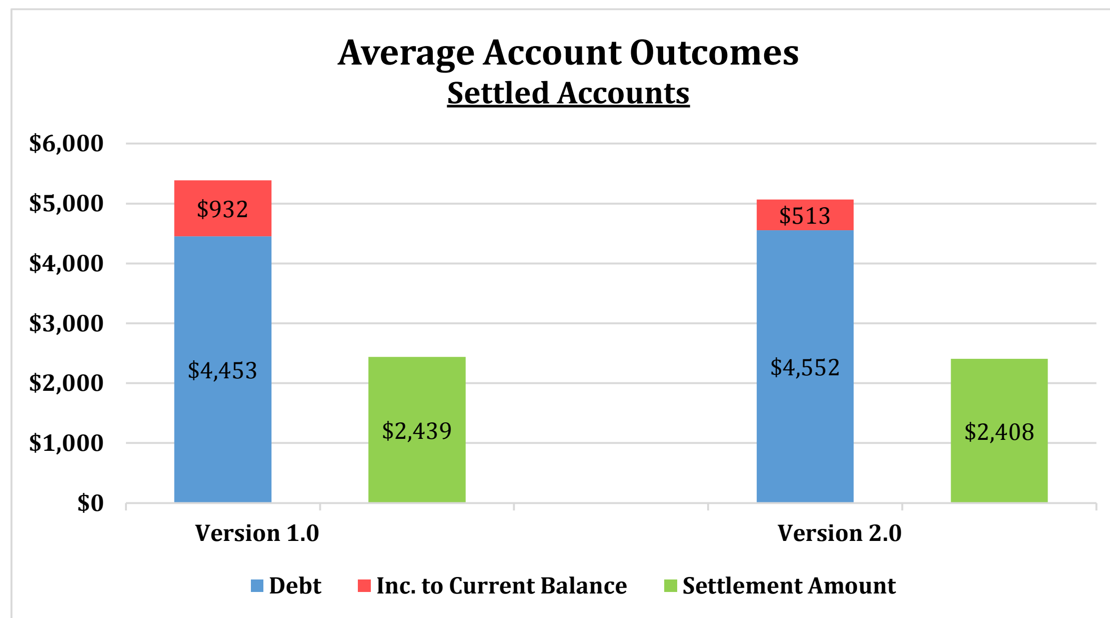


Chart 5.11 illustrates that the typical Settlement Amount for Version 2.0 Accounts is approximately 48% of the balance owed at time of settlement (exclusive of Fees) whether the analysis is conducted at the Client-level or Account-level. Stated another way, these Charts demonstrate that Completed Clients experience Debt Reduction equal to more than 50% of the amount owed at the time of settlement.

One important observation is that Version 2.0 Accounts experience significantly reduced accretion (*i.e.*, the change from Debt to Current Balance) relative to Version 1.0 Accounts. There are at least two factors influencing this result. First, settlements occur earlier, which reduces the time during which accretion occurs. Second, typical prevailing interest rates are relatively lower following the onset of the Version 2.0 model.[20] The issue of accretion is addressed in the next section of this report.

6. Accretion of Accounts in Debt Settlement Programs Is Demonstrably Lower Than for Other Alternatives

Consumers who obtain credit do so with the expectation that the borrowed amount will be repaid in full, either when due or repaid over-time, in both cases with interest. The

[20] For instance, the Prime Rate is frequently used as the foundation for credit card interest rates (*see e.g.*, https://www.bankofamerica.com/credit-cards/education/what-is-credit-card-apr.go, "A variable APR is calculated by adding a set number determined by the credit card issuer (called the margin) to a reference rate (called the index) such as the U.S. Prime Rate. When the Prime Rate goes up or down, your variable APR may change, depending on whether your issuer updates your rates monthly or quarterly."). Since 2009, the Prime Rate has consistently been approximately 3.25%. Prior to that time, however, the Prime Rate was significantly higher, such as in 2007 when the Prime Rate was 8.25%.

change in the amount that a consumer owes to resolve the debt is referred to as accretion. While the amount of accretion is generally a function of the amount of time needed to repay the borrowed amount, it is also a function of the borrower's status (*i.e.*, current v. delinquent). Stated differently, if a consumer borrows $10,000, the total of all payments needed to resolve the debt will typically be less if the amount is repaid in one-year as compared with two-years. Similarly, if a borrower does not make timely payments on the borrowed amount, accretion is likely to occur at a greater rate. This is because the lender typically applies a higher interest rate to the debt as the risk of default increases.

There is no "but/for" correlation between accretion and participation in a debt settlement program: accretion occurs in all debt with, as pointed out above, the rate dependent upon account status. To understand the impact of accretion on the overall efficacy of debt settlement, it is relevant to compare the overall accretion a Client experiences while enrolled in a debt settlement program with the accretion a Client would have experienced if the Client had not enrolled in a debt settlement program.

An important factor to consider is that debt settlement programs are only available to financially challenged consumers who are, or are about to become, delinquent on all or a substantial percentage of their debts. Consequently, the accretion rate experienced by a Client may be significant due to, for example, increased interest rates, fees, or penalties imposed upon the Client because of a failure to make regular payments on Enrolled Debts.

a. <u>Total Accretion</u>

Chart 6.1 below assembles the data from the more than 375,000 settlements of Version 2.0 Accounts that have occurred as of March 31, 2015. The green line, "Total Accretion at Settlement," represents the total amount, in percentage terms that Enrolled Debt had increased as of the time of the settlement. For example, after six months, the average Debt enrolled in a debt settlement program had increased by approximately 11.5%. The other line provides context for this accretion rate. It represents accretion at currently available credit card rates of interest (16%).[21] Note that this rate is highly likely to understate the accretion rate for a delinquent borrower.

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[21] This rate reflects current credit card interest rates for non-delinquent accounts and is used here to calculate the effective accretion on reducing monthly balances taking into account regular payments of principal. (see http://www.bankrate.com/finance/credit-cards/current-interest-rates.aspx).

Chart 6.1

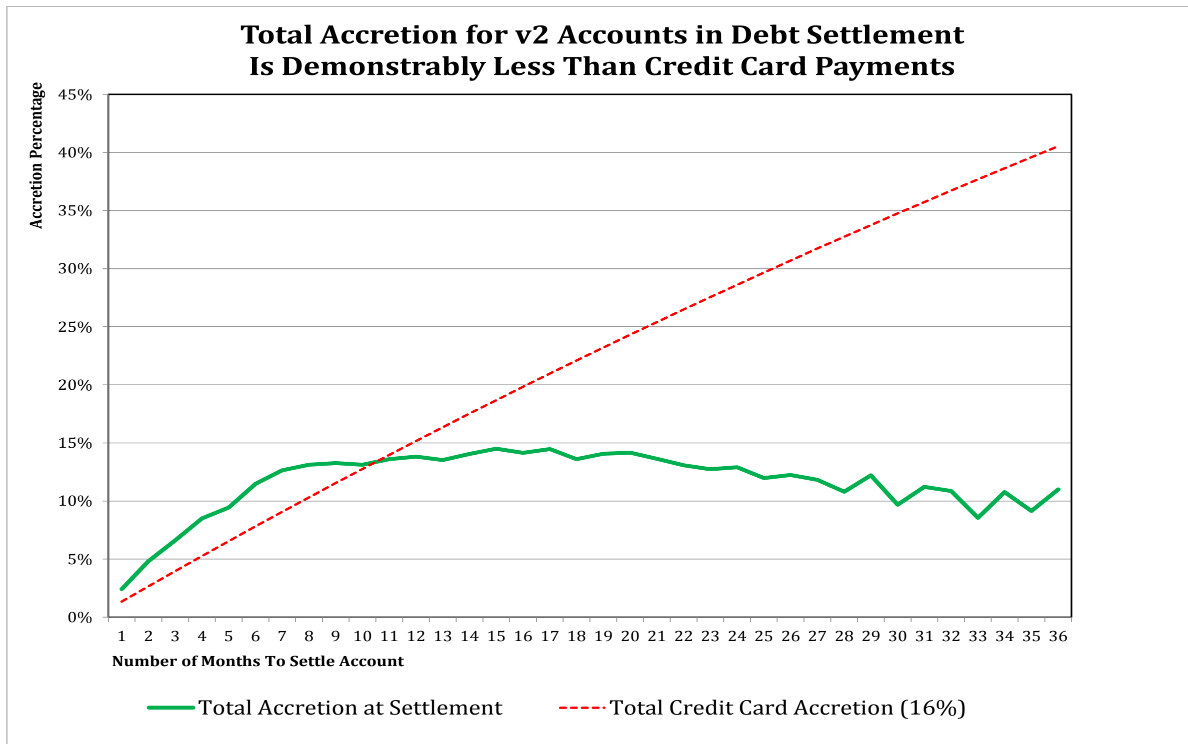
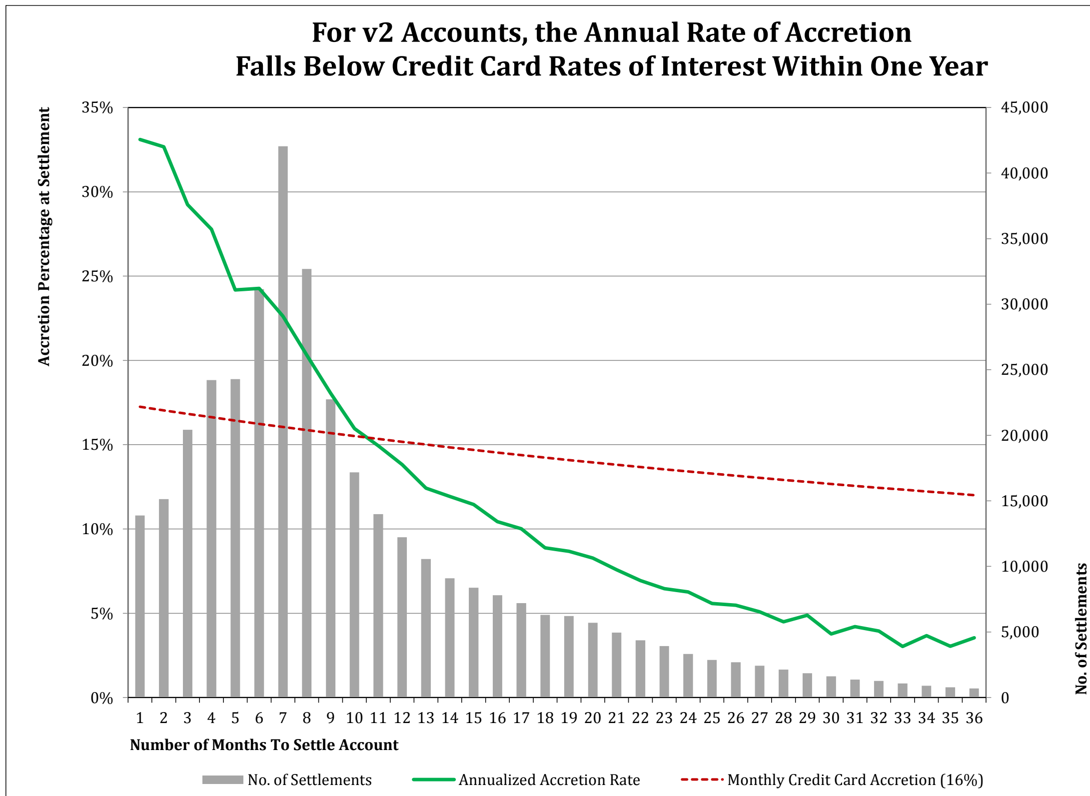


Chart 6.1 is instructive. The effect of accretion in debt settlement programs cannot be analyzed independently of the alternatives. In other words, how different is the accretion experienced by the consumer in debt settlement as compared to the accretion the consumer would have experienced continuing to make minimum monthly credit card payments? In the initial year of a consumer's participation in a debt settlement program, the accretion effect is not significantly different than if the consumer had continued to incur credit-card-related interest (with the early imbalance attributable to the effect of penalty rates of interest typically associated with defaulted credit card debt). Over time, however, while the accretion experienced by consumers outside of debt settlement continues to increase, the data indicates that accretion of debts *within* debt settlement programs stabilizes at total rates from approximately 15% to 20%.

b. Annualized Accretion

Another way to present accretion is to illustrate its effect if the accretion rate is annualized. This is the same tool commonly used to express the effective annual interest rate on a credit card (*i.e.*, annual percentage rate or APR). Chart 6.2 highlights that the effect of accretion is most significant within the first nine months of a debt settlement program. However, after twelve months in a debt settlement program, on average the annual accretion rate falls to 12%, and by the eighteenth month the annual accretion rate has fallen below 10%.

Chart 6.2



Charts 6.1 and 6.2 together demonstrate that, whenever a consumer requires more than nine months to repay a particular debt, that consumer would experience greater accretion (and potentially substantially greater accretion) by continuing to make his minimum monthly credit card payments than by enrolling his credit card debt in a debt settlement program. At all times thereafter, total accretion taking place within a debt settlement program is less than the alternative, thereby actually benefiting the consumer rather than disadvantaging the consumer.

c. Comparing Accretion in a Debt Settlement Program With Accretion Incurred with Credit Card Payments

The effect of accretion on debt settlement Clients may be illustrated as follows. For Version 2.0 Clients, the median Enrolled Debt involves six accounts totaling $25,200 (average account size is $4,203). As described in §5.a, Completed or Active Version 2.0 Clients settle at least one Account by Month Four. Thus, conservatively assuming a first settlement in Month Six and accreting that Account by 12%, which is the average accretion amount for all Accounts enrolled in a debt settlement program at that account tenure (see Chart 6.1), that Account would have accreted (increased) by approximately $509. By comparison, the average credit card account balance would have incurred accretion of approximately $330 by maintaining minimum monthly payments (again, the difference attributable to the higher rates of interest associated with defaulted balances).[22] In other words, the Client would have experienced $179 of incremental accretion on that Account ($509 minus $330) as compared with making minimum credit card payments at a non-default rate of interest.

Extrapolating the above analysis over an entire portfolio of Enrolled Debt, the Client's total accretion over the first six months would be $3,057 in a debt settlement program versus $1,970 by making minimum monthly payments ($3,057 minus $1,970 equates to $1,087 incremental accretion). However, at the end of Month Six the Client would have completely eliminated $4,203 of his Enrolled Debt (17%), whereas by making the minimum monthly payments the Client would have reduced principal by only $1,512 (approximately 6%).

Critically though, after payment of the Settlement Amount and Fees associated with a typical settlement, the Client would have earned Savings of $1,568.[23] Thus, even after considering accretion on all accounts, the Client would have improved his financial position by approximately $481 ($1,568 Savings minus $1,087 incremental accretion) after the first settlement.

Thereafter, the Client's Savings, even after accretion, continues to increase in all months in which the Client participates in the debt settlement program (even including the differential between default and non-default rates of interest). In fact, as time progresses, the effect of accretion actually benefits the Client in debt settlement. This is, in part, because accretion ceases on any settled accounts (*i.e.*, that portion of the balance falls to $0), whereas

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[22] This is a conservative approach to compare these programs (*i.e.*, it uses the rate of interest associated with maintained current minimum monthly payments). Persons eligible for debt settlement programs are generally unable to maintain their minimum monthly payments, and as a result, are subject to a higher default rate of interest.

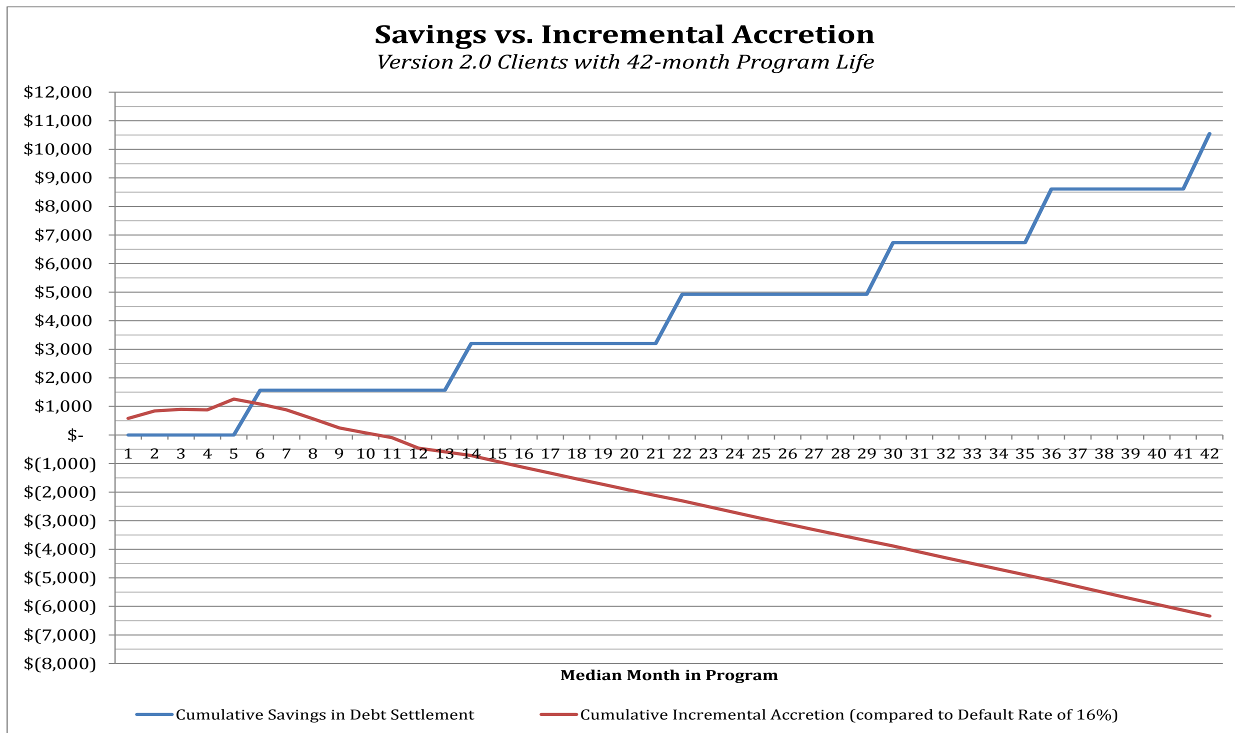
[23] This amount can be computed as Enrolled Debt ($4,203) plus Accretion ($509) or $4,712 minus the typical Settlement Amount (48% of $4,703 = $2,262) minus Fees (21% of $4,203).

if the Client had not enrolled in debt settlement and instead made minimum monthly credit card payments, that portion of the total debt would have continued to incur interest. Again, this can be seen through an illustration. As described in §5.a, for those Version 2.0 Clients that participated in a debt settlement program for at least 30 months, 63% settled four or more Enrolled Debts. Based on the data set, over these 30 months, the example Client would have incurred approximately $2,930 of accretion in his debt settlement program across those four settled accounts. By comparison, if the Client had not enrolled in a debt settlement program and instead made minimum monthly credit card payments during this same period, the Client would have experienced approximately $5,830 of accretion (interest) on those same four accounts. Stated differently, on a cumulative basis, the example Client experienced approximately $2,900 less accretion in his debt settlement program (*i.e.*, $2,930 minus $5,830). More importantly, though, the Client would have earned total Savings of approximately $6,700 after a fourth settlement (not including any benefit from reduced accretion).[24]

Chart 6.3 illustrates these concepts graphically. The blue line (Cumulative Savings in Debt Settlement) depicts the accumulation of Savings after each settlement (*i.e.*, the step-up in the blue lines in months 6, 14, 22, 30, 36, and 42). The red line (Cumulative Incremental Accretion) separately illustrates the difference in the cumulative accretion experienced by the Client in debt settlement as compared to the Client making minimum monthly credit card payments. As noted above, over time, in debt settlement, accretion increasingly benefits Clients as compared to continued credit card payments.

[24] For comparison purposes, the Client would have incurred total accretion of approximately $4,900 in a debt settlement program across all six accounts. If the Client had continued to make minimum credit payments, the Client would have incurred approximately $8,800 of total accretion on the six accounts. Thus, the same conclusion is reached if all accounts are analyzed (*i.e.*, more accretion would have been incurred outside of the debt settlement program).

Chart 6.3[25]



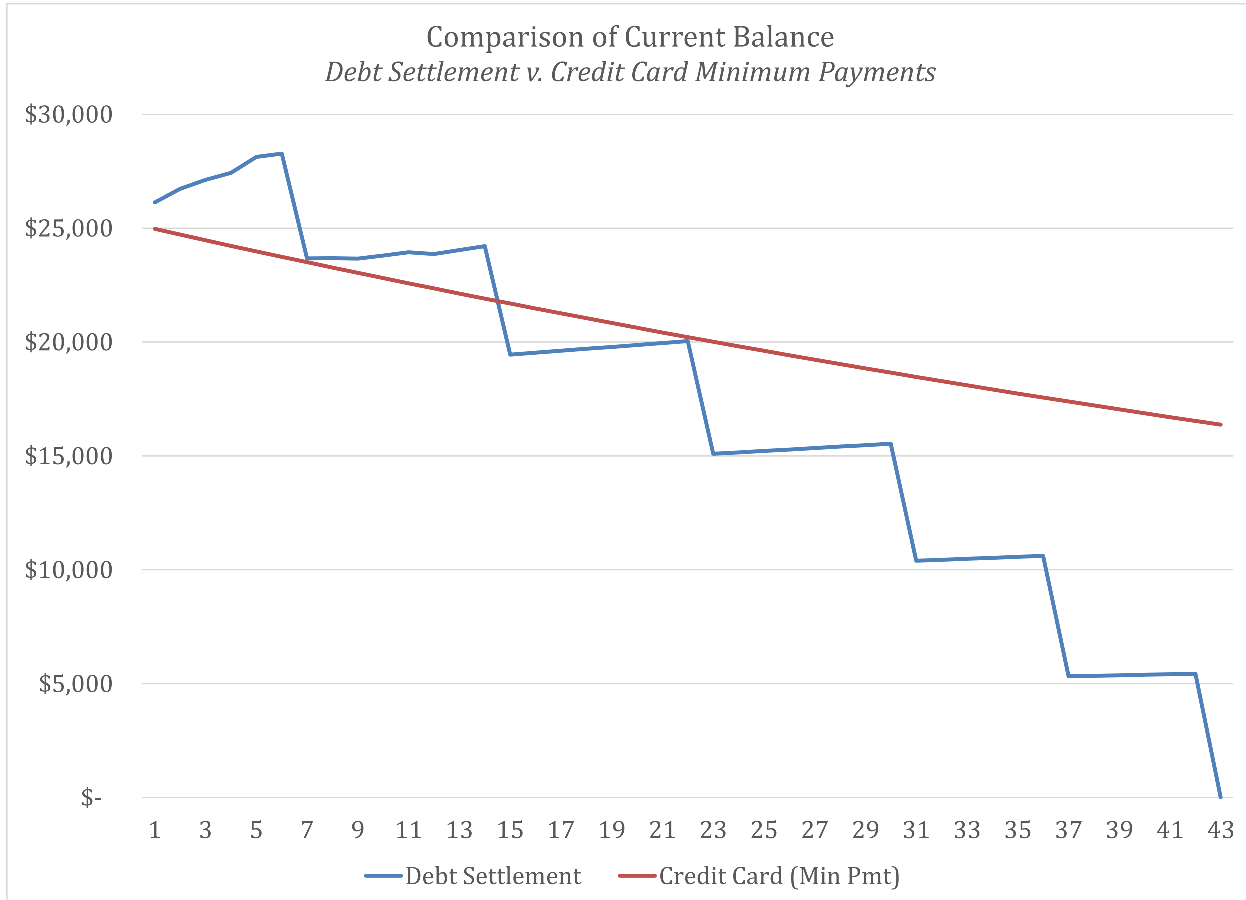
Settlement No.		**1**	**2**	**3**	**4**	**5**	**6**
Settlement Month		**6**	**14**	**22**	**30**	**36**	**42**
Enrolled Debt (Settled Accounts)	[a]	$ 4,203	$ 8,407	$ 12,610	$ 16,813	$ 21,017	$ 25,220
Cumulative Accretion (Settled Accounts)	[b]	509	1,148	1,954	2,929	4,029	5,256
Current Balance (Settled Accounts)	[c]=[a]+[b]	4,713	9,554	14,564	19,742	25,046	30,476
Total Settlement Amount	[d]	(2,262)	(4,586)	(6,991)	(9,476)	(12,022)	(14,629)
Total Fees	[e]	(883)	(1,765)	(2,648)	(3,531)	(4,414)	(5,296)
Cumulative Savings (Blue Line)	[f]=[c]-[d]-[e]	$ 1,568	$ 3,203	$ 4,925	$ 6,735	$ 8,610	$ 10,551
Total Accretion - All Accounts (Debt Settlement)	[g]	$ 3,057	$ 3,701	$ 4,373	$ 4,878	$ 5,130	$ 5,256
Total Accretion - All Accounts (Credit Card)	[h]	$ 1,970	$ 4,419	$ 6,679	$ 8,764	$ 10,222	$ 11,594
Cumulative Incremental Accretion (Red Line)	[i]=[[g]-[h]	$ 1,086	$ (718)	$ (2,306)	$ (3,887)	$ (5,092)	$ (6,338)

Also important for a financially challenged consumer, Savings in a debt settlement program, as illustrated in Chart 6.3, does not come at the expense of increased cash outflow. Chart 6.4 compares the then-Current Balance of the Client's Enrolled Debt at each month, assuming typical settlement progress, compared with the amortization of the Client's Enrolled Debt, assuming minimum monthly payments. In debt settlement, Clients have

[25] The calculation of "Total Accretion – All Accounts (Debt Settlement)" in the table conservatively assumes an accretion rate that exceeds the rates presented in Charts 6.1 and 6.2. Specifically, for purposes of these calculations only, these calculations assume that, after Month 14, accretion continues at a rate of 0.5% per month (*e.g.*, the analysis assumes that total accretion is approximately 23% as of Month 30).

demonstrated an ability to settle all Enrolled Debt after 42 months. If the Client had instead continued to make minimum monthly credit card payments, the Client would have had a remaining debt in excess of $16,000:

Chart 6.4



One commentator has analyzed the efficacy of debt settlement programs with reference only to Enrolled Debt (referring to the Client's hypothetical "net change in financial position"). This analysis incorrectly implies that accretion is incurred as a result of the Client's entry into a debt settlement program. As described above, accretion is a financial certainty whether or not a Client enters debt settlement. Further, because the Client has the ability to exit a debt settlement program at any time, an analysis of a Client's "net change in financial position" must evaluate the Client's position at one or more specific points in time, such as after each settlement.[26] Indeed, as demonstrated above, the typical Version 2.0 Client experiences Savings after the first settlement ***even after consideration of accretion***.

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[26] The commentator's analysis compounds its error by assuming that Clients are locked into the debt settlement program for 36 months with various possible settlement outcomes, including zero settlements. This

d. The Effects of Taxation

This report does not attempt to examine (or incorporate) the effect of most externalities, including those viewed as either positive (improved cash flow attributable to ceasing to pay the full amount currently due) or negative (reduced access to credit). However, because the potential taxability of debt settlement benefits would directly affect the economic outcomes described in this report it is worth spending a moment on the concept of "relief of indebtedness" income.

It is possible that a consumer will be deemed to have received a tax benefit as a result of the forgiveness of debt associated with a negotiated settlement of unsecured indebtedness. However, consumers are typically able to file IRS Form 982, "Reduction of Tax Attributes Due to Discharge of Indebtedness." This filing enables consumers to avoid adverse tax consequences associated with the discharge of indebtedness. Consequently, any analysis of after-tax Savings that ignores this option would clearly misstate Savings.

7. The Economic Benefits of Debt Settlement Compared With Other Alternatives

At the time of enrollment, Clients may have had other alternatives available to them for debt relief, including filing for bankruptcy, entrance into a debt management plan (DMP) offered by a credit counselor, securing a home equity loan for debt consolidation purposes or continued attempts at self-management of accounts. Each of these alternatives has different risks and costs as well as different potential benefits. This section compares the likely outcomes of participation in Version 2.0 debt settlement programs with the anticipated outcomes associated with these other possible alternatives.

a. Minimum Credit Card Payments

The average Client (all statuses) enrolled Debt totaling approximately $28,950, substantially all of which was credit card-related. Most of these Clients were either only able to make the minimum monthly payment or were unable even to pay that amount. If a Client were able to pay the minimum monthly payments, the total cost to settle this Debt (*i.e.*, principal plus interest) would be $66,813 over 443 months (approximately 37 years).[27]

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is wrong: a Client can freely exit a debt settlement program at any time. Further, the data demonstrates that it is highly unlikely that a Client participating in a debt settlement program for 36 months would experience less than four settlements (80% of Clients with this tenure had achieved four or more settlements). See Chart 5.5.

[27] This amount has been computed using an amortization table with an interest rate of 16% and a minimum payment of current interest plus 1% of the principal amount each month. These amounts are consistent with current industry standard requirements. *See, e.g.*, "The minimum payment on credit card debt is calculated as a percentage of your total current balance, or as all interest plus 1 percent of the principal. Card issuers also set a floor to their minimum payments -- a fixed dollar amount that the minimum payment won't fall below." (http://www.creditcards.com/calculators/minimum-payment.php) This calculation is consistent

Stated differently, by making only the required minimum monthly payments, the Client would have incurred a cost of more than $38,000 *over and above the principal amount owed.* As described more fully below in the presented hypothetical, debt settlement programs compare favorably to this alternative.

b. <u>Credit Counseling Programs</u>

Another available alternative might have been a consumer Credit Counseling Agency (CCA) offering a DMP. A DMP is available to consumers who are able to make a monthly payment substantially in excess of that required for a debt settlement program but involves only concessions on the interest rate charged on outstanding balances, not a reduction in principal. However, because DMPs have costs that make the monthly minimum payment requirement comparable to the minimum monthly payments that would otherwise be required by the creditors, DMPs are generally not available to those in situations of serious financial hardship (there is relatively little overlap between the client constituencies of CCA and debt settlement).

We understand that less than 30% of individuals that contact a CCA qualify for a DMP. Further, it has been reported that persons who qualify for a DMP actually complete the program at somewhere between 20-35% (the credit counseling industry has declined to publish completion statistics).[28]

Table 7.1 compares the results of a hypothetical debt settlement client with the anticipated outcomes of enrollment in a DMP, obtaining a home equity loan for debt consolidation purposes and simply continuing to amortize the existing debt on a monthly basis by making only the minimum monthly payments required by the creditors. The comparison analysis assumes the availability of all described options (although, practically speaking, few if any of these options would be available to a consumer in the ongoing state of financial distress common to consumers eligible for a debt settlement program) to a consumer with $30,000 of credit card debt under prevailing market conditions).

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with the calculations of interest set forth in § 6 above. These calculations may be replicated at http://www.bankrate.com/calculators/managing-debt/minimum-payment-calculator.aspx.

Further purposes of clarity, this amount also assumes (1) a static interest rate of 16% on a declining principal balance, (2) no additional card usage and (3) no additional charges or fees, such as over-limit fees, late fees, etc.

[28] "Behind the Credit Counseling Curtain," by Fred O. Williams, February 4, 2013 (www.creditcards.com/credit-card-news/business-credit_counseling-1282.php)

Table 7.1

$30,000 of Debt At Enrollment	Debt Settlement	Credit Counseling	Minimum Monthly Payments[1]	Home Equity Consolidation Loan[2]
Months to Pay Off or Settle All Debt	48[3] (4 years)	60 (5 years)	443 (36 years, 11 months)	60 (5 years)
Monthly Payment/ Program Deposit	$491.25	$658.29[4]	$676.00[5]	$557.93[6]
Interest Rate On Outstanding Balance	n/a	8%[7]	16%	4.375%[8]
Total Program Interest	n/a	$6,497	$38,062	$3,475
Program Fees	$6,080 [9]	$3,000 [10]	n/a	$375[11]
Amount to be Paid to Pay off Enrolled Debt	$16,675[12]	$28,950	$28,950	$28,950
Total Program Cost Paid By Consumer	**$22,755**	**$35,447**	**$67,012**	**$32,425**
Fair Share Payments by Creditor to nonprofit CCCS	n/a	$1,975[13]	n/a	n/a

[1] Assumes (1) minimum payment of the greater of (A) interest and fees plus 1.0% of outstanding principal balance or (B) $15, (2) static interest rate of 16% on declining principal balance, (3) no additional card usage and (4) no additional charges or fees, such as over-limit fees, late fees, etc. See http://www.creditcards.com/glossary/term-minimum-payment.php : "The industry standard is now to calculate the minimum in one of two ways: either 3 percent to 5 percent of the total balance due, or, all fees and interest due that month, plus 1 percent of the principal amount owed."

[2] Assumes good credit, sufficient home equity (80% LTV) and no change in interest rate over the term. See http://www.bankrate.com/calculators/mortgages/mortgage-calculator.aspx?MSA=4472. A five-year HELOC term was chosen for a more "apples to apples" comparison with debt settlement and CCCS program terms.

[3] Program term depends upon such factors as creditor composition, rate of funds accumulation, account accretion, etc. Debt settlement programs generally require between 24-48 months to complete, so use of the longer 48-month term is conservative.

[4] Calculated by dividing (A) the sum of (i) total program interest, (ii) total program fees and (iii) amount to be paid to pay off enrolled debt by (B) the months to pay off or settle all debt.

[5] Initial payment. Payment amount will decline as principal is reduced (or increase if interest rates rise).

[6] Assumes 4.375% interest for five-year term: www.bankrate.com/calculators/credit-cards/use-home-equity-consolidation-calculator.aspx

[7] Estimate, based on inquiries with three separate credit counseling organizations.

[8] HELOC rate quoted by Wells Fargo Bank, NA, as of July 13, 2015.

[9] Assumes a Fee of 21% of Enrolled Debt.

[10] Assumes a fee of the lesser of (1) $50 per month or (B) 15% of client payment. Fees for debt management plans vary greatly by provider, are subject to statutory limits in certain states and are not widely or uniformly reported. The assumptions set forth here reflect the most common statutory limitations.

[11] Assumes five-year term loan with no fees other than a $75 annual fee.

[12] Assumes (1) average account accretion of 20% from time of enrollment to time of settlement and (2) average settlement percentage of 48% of amount owed at time of settlement.

[13] Assumes 5% of client payments, see page 16 of Wilson, "Meeting the Demand for Debt Relief," Federal Reserve Bank of Philadelphia (August 2011). See also https://www.nfcc.org/wp-content/uploads/2014/03/NFCC-Member-Quality-Standards.pdf indicating that fair share payments may run as high as 15% of the payment made by the debtor.

Thus, financially, a Client's outcome from participation in a debt settlement program appears to be significantly superior to all other available forms of debt relief.

c. Chapter 13 Bankruptcy Statistics

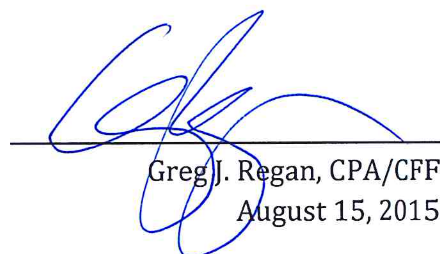
Some Clients may have had the alternative of declaring bankruptcy. The chapter of the United States Bankruptcy Code that provides for adjustment of debts of an individual with

regular income is Chapter 13.[29] This type of bankruptcy is similar to debt settlement programs in that it enables individuals to establish a plan to repay part or all of their debts, and similar to credit counseling, in that it requires participants to pay a monthly amount to the bankruptcy court for distribution, after fees, to approved creditors. Table 7.2 displays statistics on the completion rates of Chapter 13 bankruptcy matters in the three most recent twelve-month periods for which data is available (years ending December 31st):

Table 7.2[30]

Year	Cases Closed	Plans Completed	Completed/Cases (%)
2012	289,125	106,543	36.8%
2013	336,858	152,333	45.2%
2014	351,960	178,369	50.6%

Over this timeframe, the bankruptcy completion rate has increased principally due to the tracking methodology. Chapter 13 plans require approximately three-to-five years to complete, under ongoing court supervision, and relevant data has been monitored only since October 17, 2006. The completion rates appear to match the equivalent completion rates for debt settlement clients, however individuals typically incur substantial upfront costs to enroll in a Chapter 13 bankruptcy plan, including filing fees and attorney costs.[31] Those fees are not refundable if the individual does not ultimately complete the plan. As such, the client risk in bankruptcy exceeds the comparable situation in the Version 2.0 of the debt settlement programs.



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August 15, 2015

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29 http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter13.aspx

30 2014 Report of Statistics Required by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 at www.uscourts.gov/data-table-numbers/bapcpa-6

31 These costs average approximately $3,000. See, *e.g.*, http://www.natlbankruptcy.com/how-much-does-it-cost-to-file-bankruptcy/