

Consumer Alert Issued: IRS and FTC Investigates Credit- Counseling Organizations

The Internal Revenue Service and Federal Trade Commission announced a joint advisory, warning consumers of some of the pitfalls of Credit Counseling. They plan to team up to investigate both deceptive practices of the industry and the often-misleading nonprofit status of some of these credit-counseling agencies.

"Consumers who are struggling financially need to be careful not to lose even more money to someone offering a quick and easy way to fix credit problems," said Timothy J. Muris, Chairman of the FTC. "We want all consumers seeking help to take some common sense precautions."

The IRS, FTC, and state agencies urged consumers to be wary when choosing a credit counseling organization. A large number of complaints from consumer advocate groups have alerted these groups of some of the deceptive practices and hidden costs associated with some credit counseling agencies. Consumer complaints have centered on high fees, hidden charges, and the lack of actual help these organizations have been able to offer.

The IRS is concerned that some credit counseling agencies are abusing their status as "tax exempt organizations" in order to avoid state and federal consumer protection laws. Many credit-counseling agencies have been able to operate using deceptive practices and hide under their "nonprofit" status. As nonprofits, the agencies are now exempt from dozens of state and federal regulations.

The IRS also warns consumers that a "nonprofit" status does not ensure the quality of an organization; it is merely a tax code classification. Consumer groups have also criticized the large salaries of many of the credit counseling agencies' executives. "Consumers need to know not to read too much into not-for profit status - that's no guarantee that someone is legit," said a director of the FTC's Midwest Operations.

The IRS has begun auditing some credit counseling services to see if they meet the criteria for their nonprofit status. To obtain tax exempt status, a credit counseling agency must limit its services to poor customers or must primarily provide education and counseling to the

public. Many credit counseling agencies have been criticized for focusing on higher profitability and just acting as a middle man funneling money to the creditor and just taking a cut of the payments. The IRS said that simply enrolling people into payment plans is not enough. They also plan to more aggressively screen new applicants from credit counseling organizations.

There is heightened concern as more and more consumers enter into credit counseling programs. The number of consumers involved in some sort of credit counseling sky rocketed to an estimated 9 million in 2002. This number is expected to grow as more and more consumers will be required to undergo some sort of credit counseling prior to filing bankruptcy under the proposed new bankruptcy laws.