

CREDIT COUNSELLING: A WAY FORWARD

Prepared for the
Financial Consumer Agency of Canada



Public Interest Advocacy Centre

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INTRODUCTION

Consumer credit counselling agencies (CCAs) provide debt reduction services and financial education to debtors. They assist consumers who are having problems dealing with the management of their personal finances and need help to pay down their debts and improve their credit rating.¹ The feature services are debt management plans or DMPs, widely known as “debt consolidation”, that consist of taking lump-sum payments from debtors facing financial struggles, or who are unable to keep up with their monthly bills, and re-distributing those monies to creditors on a pro-rated basis. Credit counselling agencies will notify the creditor that the consumer has signed in to a DMP, and forward a request to obtain relief, negotiate late fees and possibly obtain interest rate reductions at the discretion of each creditor.²

DMPs benefit creditors by lowering the risk of consumers filing for an assignment bankruptcy with the probable loss by the creditor of the full outstanding debt balance. In turn, the debtor obtains a benefit in the form of the relief described above, with the advantage of making payment in a consolidated form to the CCA, instead of obligations to multiple creditors.³

However, the main requirement for a customer to be eligible to have a debt consolidation plan approved, is a stable and regular source of income. Consumers who are unemployed, employed temporarily or without a reliable source of income are not eligible for debt consolidation, as creditors would not agree to consolidation in a context of income uncertainty regardless of the agency selected to set up the plan.

CCAs have become an important stakeholder in the credit system and provide valuable assistance to consumers and in general, to over indebted individuals.⁴ However, in the United States, some of the largest CCAs have been heavily criticized over the last years for a variety of reasons ranging from their close connection with the consumer credit industry and to their apparent failure to act in the best interest of their clients, financially vulnerable consumers.⁵

This report provides an overview and a description of the current structure of credit counseling services in Canada. The first part will provide a snapshot of the industry starting with its origins, the types of credit counselling agencies and services they provide; including funding models,

¹ Susan Lott, *Credit Reporting: How are Consumers Faring?* Public Interest Advocacy Centre, Ottawa, August 2005.

² Approval by creditors of a DMP proposal submitted by an agency and the subsequent payments, originates a “R7” or note in that consumer’s credit record, meaning “Making regular payments under a consolidation order or similar arrangement”. The note remains in the record for a period of six years after full completion of the plan. While some CCAs advertise that a note the debtor’s credit report about their credit counseling process can be read by creditors as meaning “slow payer” it also means that the debtor is red-flagged as high risk due procedural proximity to bankruptcy proceedings.

³ See Permanent Sub-Committee on Investigations of Committee on Homeland Security and Governmental Affairs, United States Senate, “*Profiteering in a Non-Profit Industry: Abusive Practices in Credit Counseling*” Report. U.S. Printing Office, Washington, 2005

⁴ The term “overindebtedness” is assumed to have a similar meaning to “insolvency” within the context of credit counseling, as an inability to meet payment deadlines on outstanding debt service obligations. See Saul Schwartz, *Counselling the Overindebted: A Comparative Perspective*, School of Public Policy and Administration, Carleton University, December 2005.

⁵ *Supra* note 2.

accreditation requirements for professional counselors and the challenges that the industry face in meeting the expectations of consumers. The second part will explore the legal framework, both at the federal and the provincial levels, to which the industry is expected to comply and the final part will include recommendations to improve credit counselling of services from the standpoint of Canadian consumers and their interests.

THE CREDIT COUNSELLING INDUSTRY

Origins of the Industry

While the history of the modern credit counselling industry stretches back to the 1960s, the origins of the industry go further back to the practice of debt-pooling or pro-rating in the United States in the late 1940s. During this time, pro-rating was a well-known practice by private individuals across the United States, and several states moved to regulate it by issuing licenses to those individuals engaged in the trade.⁶ In California particularly, as early as 1957 there were calls for the regulation of the nascent industry, and a statement issued by the office of the Attorney General of that state at the time referred to the issue as “credit-buying”:

“The vast expansion in credit buying in recent years and the resulting involvement by persons into heavy indebtedness beyond their means has brought forth this new business”.⁷

The expansion of consumer credit during the postwar, particularly the early 1950s attracted so many private debt-poolers and pro-raters into the market that some states moved to ban their operation, and introduced legislation that allowed pro-raters to operate only if they were incorporated as non-profit organizations.⁸

The first non-profit credit counseling organizations originated in the 50s and 60s as a consequence of a mixed set of circumstances: on the one hand, the new regulatory burden placed on private pro-raters and the exemption from regulation of non-profit organizations; and on the other hand, the interest of lenders and credit card companies that saw a “creative” opportunity to recover their overdue debt by funding and supporting their creation.⁹ The first non-profit consumer credit counseling agencies (CCCA) had the support of creditors and banks, who

⁶ One example of the laws governing debt-pooling was the *Check Sellers, Bill Payers and Proraters Law* (CSBPPL), enacted in the state of California in 1947. In 1957, the definition of “Prorater” is introduced in the CSBPPL, reading:

“A prorater is a person who, for compensation, engages in whole or in part in the business of receiving money or evidences thereof for the purpose of distributing the money or evidences thereof among creditors in payment or partial payment of the obligations of the debtor”.

See Department of Corporations, State of California, *Study of the Consumer Credit Counselling Industry in California and Recommendations to the Legislature Regarding the Establishment of Fees and Debt Settlement Plans for Debt Management Plans*, California’s Investment and Financing Authority, March 1, 2003, online: California’s Investment and Financing Authority < <http://www.corp.ca.gov/pub/ccrpt.pdf> >, See also, Financial Code § 12000 seq.

⁷ 30 Ops.Cal.Atty.Gen. 122 (1957).

⁸ Robert M. Hunt, *Whiter Consumer Credit Counselling? Business Review*, Federal Reserve Bank of Philadelphia, online: Federal Reserve Bank of Philadelphia <http://www.phil.frb.org/files/br/Q4_05_ConsumerCounsel.pdf>.

⁹ Deanne Loonin & Travis Plunkett, *Credit Counselling in Crisis: The Impact on Consumers of Funding Cuts, Higher Fees and Aggressive New Market Entrants, A Report by The National Consumer Law Center and Consumer Federation of America*, April 2003.

provided the lion's share of the funding necessary to run in the form of charitable donations referred to as "fair share" contributions.¹⁰

These non-profit CCCAs were nevertheless community-based, non-for-profit organizations where counselors and debtors arranged appointments to meet personally and discuss solutions to the financial problems of distressed debtors. They advised them on how to better manage their income and to rationalize their use of credit, in an effort to educate them on how to avoid falling into excessive debt. If after a number of meetings of budget analysis and counselling alone, the situation of a particular debtor did not improve, counsellors would recommend a course of action ranging from budget adjustment, a debt management plan (DMP) or legal assistance to consider a consumer proposal or bankruptcy.¹¹ Growing demand for these services gradually contributed to the transformation of the industry's original practices and over the last decade CCCAs have become an important stakeholder within the credit industry, attracting increased scrutiny, particularly in the United States.

Recent Developments of Credit Counselling Industry in the U.S.

The National Foundation for Credit Counseling (NFCC) is the largest non-profit credit counseling association in the United States, founded in 1951. Its 115 member agencies operate over 1,000 credit counselling offices across the country, serving a client base of two million.¹² The largest credit counselling and debt management trade association in the United States is the American Association of Debt Management Organizations (AADMO) with 150 affiliates that include for-profit and non-profit CCCAs alike.¹³

The Credit Counselling Industry in the United States has seen important legal developments over the last years, as the growing consumer debt translates into a bigger market for CCCAs.¹⁴ One of the most relevant has been the settlement of an anti-trust action brought by a number of non-NFCC (or private, for-profit CCCAs) against the National Foundation for Credit Counselling (NFCC), the largest association of American non-profit CCCAs, and some of its members.

¹⁰ *Ibid.*

¹¹ *Supra* note 3 at 4.

¹² Susan C. Keating, President and Chief Executive Officer, National Foundation for Credit Counseling NFCC, *State of the Credit Counseling Sector Address*, September 11, 2006, online: <<http://www.nfcc.org/Newsroom/shownews.cfm?newsid=370>>.

¹³ AADMO cites as its mission "to promote and ensure the continued operation and viability of credit counseling and debt management organizations" and to "respond to legislative and regulatory proposals adverse to the interests of our members and the industry". However, while AADMO advances the interests of the trade and not the interests of the financially distressed clients of its members, it does not hesitate to characterize those financially troubled consumers as its "grassroots network". See: American Association of Debt Management Organizations, online: <<http://www.aadmo.org/ci.php>>.

¹⁴ Consumer credit in the form of credit cards and retail stores lines of credit in the United States is widely advertised and available; consumer debt in that country has more than doubled in the past three years, with the country's total credit card debt today surpassing the \$735 billion. Contractual clauses in most credit card agreements stipulate penalties for missed payments that automatically trigger escalating interest rates consumers' incomes cannot possibly keep up with; as a consequence, since the mid-nineties, more than a million American consumers have filed for bankruptcy every year, with a record 1,66 million filings in 2003, according to the American Bankruptcy Institute. See *Supra* note 3.

The United States Senate and the Internal Revenue Service (IRS) also launched an inquiry into alleged illegal financial operations of burgeoning credit counselling companies like AmeriDebt Inc., American Financial Solutions (AFS) and Cambridge, which operated as non-profit agencies but used their charitable status as a tax-evasion strategy to siphon out their revenues to a network of for-profit associated CCCAs. Investigations launched against these agencies resulted in findings that these agencies provide poor service and little or no counselling to debtors, while counsellors were instructed on sales tactics to convince debt-ridden consumers to sign on their DMP programs.¹⁵

In response to the growing competition for “fair share” contributions among non-profit CCCAs; new, aggressive for-profit entrants who operated mainly online and as call centers, and the troubling findings of official inquiries into some CCCAs, creditors scaled back their contributions. Traditional non-profit NFCC affiliates have experienced negative financial impacts caused by creditors’ cut of funding and have been increasingly obliged to adopt the online and telephone interaction strategies of their for-profit peers to face their growing competition. As a result, “old school” one-on-one, non-profit comprehensive and personalized credit counselling is dwindling.¹⁶

Most recently, the Bush administration introduced the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* (BAPCPA),¹⁷ deemed the largest overhaul of the Bankruptcy Code since its enactment in 1978,¹⁸ making consumer bankruptcy more difficult and instead, requiring payment of the debt under a court-ordered payment plan over three to five years. The new legislation makes credit counselling, in the form of a personal financial management education package, mandatory for individuals as a condition precedent to filing for consumer bankruptcy.¹⁹ After October 2005, any American in a situation of insolvency and considering the alternative of bankruptcy to address it, must seek mandatory counselling from CCCAs; and agencies must have approval by the U.S. Trustee Program to act as providers of personal financial management.²⁰

¹⁵ *Supra* note 3.

¹⁶ It may very well be that in-person credit counselling to financially troubled consumers, even when delivered by non-profit organizations, may be losing ground and become an exception. A study commissioned and funded by the NFCC to measure the impact of the delivery channel (in-person, telephone and internet) on the effectiveness of the credit counselling experience when delivered through alternative electronic mediums other than in-person, did not find any substantial negative impact on the effectiveness of the counselling exercise. Data from 70,000 consumers was provided by ten NFCC, and while the study does not purport to be representative of industry-wide practices, it emphasizes that “it reflects what is obtainable from a group of agencies that emphasize client education and identification of the underlying cause of financial problems. Michael E. Staten & John M. Barron, *Evaluating the Effectiveness of Credit Counselling, Phase One: The Impact of Delivery Channels for Credit Counselling Services*, May 31, 2006.

¹⁷ *The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005* S. 256, Pub. L. 108-9.

¹⁸ *Bankruptcy Code* 11 U.S.C.

¹⁹ The BAPCPA also introduced, among other major changes, a means test that lowers the availability of filing for bankruptcy to low-income, highly indebted individuals; increased time-periods (from 6 to 8 years) between bankruptcies filings; and no discharge of local and state taxes.

²⁰ United States Department of Justice, *Procedures and Criteria for Approval of Non-Profit Budget and Credit Counselling Agencies and Approval of Providers of a Personal Financial Management Instructional Course by the United States Trustees*, online:

<http://www.usdoj.gov/ust/ea/bapcpa/ccde/docs/Credit_Counseling_Interim_Rule.pdf>.

The Credit Counselling Industry in Canada

The origin of the Credit Counselling industry in Canada goes back to the 1960s. The largest and oldest consumer credit counseling agency in the country is the Credit Counselling Service of Toronto (CCST), a non-profit agency that operates the name Credit Canada. It was established in 1965 and modeled, like all other non-profit credit counselling agencies in Canada, on the American not-for profit CCCAs affiliated to the NFCC.²¹

While pre-bankruptcy mandatory credit counselling is a novel legal feature in the United States bankruptcy system, it has been in place for almost fifteen years in Canada. With the changes introduced in 1992 to the *Bankruptcy and Insolvency Act 1985* (BIA), Canada was, in fact, the first country to make credit counselling provided by qualified credit counsellors, a requisite prior to filing for an unconditional discharge from personal bankruptcy.²² However, it is important to note that this directive and compulsory credit counselling only applies to consumers within the context of a consumer proposal or a filing for a discharge in bankruptcy under the BIA. Likewise, only credit counselors qualified in credit management education under the BIA can provide counselling during consumer proposal or bankruptcy proceedings. Therefore, the type of counselling provided by CCCAs in Canada is not equivalent to the credit counselling prescribed under the BIA. This issue will be further discussed in the Credit Counselling Industry Accreditation chapter.

Compulsory bankruptcy credit counselling obtained support from a study published in 1990, indicating that 10 percent of the 35,000 bankrupts per year in the country during the late 1980's, were repeat bankrupts, and third or fourth-time bankrupts were increasingly common, in stark difference from the very rare repeat bankrupts during the decade of the 70s.²³ However, it should be noted that the study period was coincident with the commencement of a severe recession marked by job loss and high unemployment. The economic conditions does not appear to have been acknowledged as contributing factors to bankruptcy recidivism

Other studies at the same time largely assumed that Canadians in financial distress who filed for bankruptcy did it due to their "very little" knowledge about credit and financial mismanagement, features underlined as the cause of their financial demise.²⁴ Although the consumer education proposal was presented as "rehabilitating" and "dignifying" alternatives for consumers, the rationale for their introduction may be attributed to the interests of other parties, and particularly, creditors.

Notwithstanding the likely impact of the economic recession on bankruptcy levels, the adduced purpose behind the introduction of mandatory counselling sessions by the 1992 directive was consumer education. Education was then added as an additional element to the economic

²¹ The Credit Counselling Service of Toronto operates the name Credit Canada and the internet domain creditcanada.com, which serves as an information gateway that directs clients to use either their online interface or to call a toll-free number to obtain immediate response.

²² *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 157.1, as am. by *An Act to Amend the Bankruptcy Act and to Amend the Income Tax Act in consequence thereof*, S.C. 1992, c. 27, s. 58.

²³ W. Clare, *Repeat Bankruptcies of Consumer Debtors*, *Insolvency Bulletin* 201, 1990.

²⁴ J.W. Brighton & J.A. Connidis, *Consumer Bankrupts in Canada* (Ottawa: Consumer and Corporate Affairs Canada, 1982).

rehabilitation or “fresh start” process entailed by the bankruptcy proceeding. The educational goals of financial counselling thereafter were to assist consumers in examining their values, attitudes and beliefs. To “help them find solutions” to the financial and “personal problems” behind their insolvency.²⁵

The Exponential Growth of the Credit Counselling Industry

According to their 2005 annual report and information posted on their website, the CCST has grown to become the single largest CCSA in Canada, with twelve satellite branches of its own located across the Greater Toronto Area (GTA). It is also the largest DMP processing enterprise in Canada, through their cooperative sources program (CPR), an online business environment that includes education tools and marketing initiatives used by more than a dozen other agencies in the country. The CCST is also administrator of their programs.²⁶ Their client base has gone from 483 in 1965, their first year of operations²⁷, to 53,000 in 2005;²⁸ and it has opened files to over 500,000 financially distressed consumers over the last forty years; a double-digit client-base average growth rate per year.

Recent growth in demand for credit counselling can be illustrated by the fact that while by the end of 2000, the CCST alone was redistributing \$16 million back to creditors, by the end of 2003 that amount more than doubled, to \$33 million. The total debt load of all of CCST clients in the same year was \$168 million and the organization processed an average of 9,000 DMP of programs every month.²⁹

CCCA's in Canada have not been subject to the same level of critical scrutiny as their American counterparts over the last decade and appear to enjoy wide support among bankers, the financial industry, the consumer retail industry, merchant associations like the Better Business Bureau and the business community in general. Mainstream media conglomerates and government authorities at both provincial and federal levels also directly provide support for the non-profit model of credit counselling.

CREDIT COUNSELLING MODELS: NON-PROFIT AND FOR PROFIT

The Non-Profit Model

There are twenty-four non-profit counseling agencies in Ontario and three in Newfoundland that are part of an umbrella organization, the Ontario Association of Credit Counselling Services (OACCS). This organization represents over 70 percent of all the non-profit credit counseling

²⁵ See Ruth E. Berry & Sue L.T. McGregor, “Counselling Consumer Debtors under Canada’s Bankruptcy and Insolvency Act”, *Osgoode Hall Law Journal*, Vol 37, at 375.

²⁶ Credit Counselling Service of Toronto, *The Credit Canada Solution*, Annual Report 2005, online: Credit Canada < http://www.creditcanada.com/documents/Annual_no_graphs_05.pdf >.

²⁷ Credit Counselling Service of Toronto, *Helping More Than a Half Million Consumers Over Four Decades*, Annual Report 2004, online: Credit Canada < <http://www.creditcanada.com/documents/annualReport2004.pdf> >.

²⁸ *Supra* note 15.

²⁹ *Supra* note 12.

agencies in Canada, including the CCST.³⁰ In the fiscal year 1998, the OACCS opened 13,944 new counselling cases and 4,275 new debt management files that distributed \$22,5 million back to creditors, according to *OACCS Statistical Highlights 1998*.³¹ All the agencies associated with the OACCS, along with all the non-profit CCCAs in the rest of Canada, are part of the wider national organization Credit Counselling Canada (CCC). Both the CCC and the OACCS are also members of the NFCC.³²

Soon after the creation of the CCST in 1965, other CCCAs were created in Ontario.³³ Their incorporation was promoted and made possible thanks to the participation of the business and other community members and funding provided by creditors and the provincial government.³⁴

The Quebec Model: Associations Associations Cooperatifs d’Economie Familial ACEFs

Consumer credit counselling agencies are generally known in Quebec as family economy co-operatives, or Associations Cooperatifs d’Economie Familial (ACEFs) and have a long and prolific history that is intimately related to consumers associations in the province. An important characteristic that sets them apart from their counterparts in the rest of Canada is that they did not originate as charitable organizations but instead as an initiative of co-operative, grassroots movements consolidated during the sixties, at a time when the Quebecois society was transforming and modernizing under the period called ‘quiet revolution’.³⁵

ACEFs do help consumers to negotiate better repayment conditions with creditors and help consumers to assume control and manage their debt, but they do not process DMPs, take payments or deposits from consumers or become financial intermediaries. They contact creditors directly in the name of consumer debtors with the purpose of obtaining softer treatment from creditors.

There are currently twenty ACEFs in the province providing comprehensive preventive financial education, budget planning and debt relief services in exchange for fees that go from \$2 to \$12 per client, depending on the particular agency or co-operative. Their main services are budget

³⁰ To some legal commentators, non-profit debt repayment and credit counselling is a misnomer, adducing that since the beginning, the agencies have been equally active in running debt management programs for the benefit of debtors and their creditors. See Jacob S. Ziegel, Anthon J. Duggan & Thomas G.W. Telfer, *Canadian Bankruptcy and Insolvency Law, Cases, Text and Materials*, Emond Montgomery Publications Limited, Toronto, 2003.

³¹ *Ibid.*

³² Money 101, *A Financial Guide for Students*, Credit Counselling Service of Toronto, online: <<http://www.creditcounsellingcanada.ca/pdf/Money101.pdf>>.

³³ One of the oldest, and still “old-school” CCCAs in Ontario is the Consumer Credit Counselling of Simcoe County, operating in Barrie, ON, was incorporated under letters of patent on March 29th, 1973 to serve the region of Simcoe-Georgian Bay. The service was registered as a charitable organization on April 1st, 1973.

³⁴ See, Hansard of the Legislative Assembly of Ontario, *Standing Committee on Estimates and Ministry of Community and Social Services*, October 6, 1992, online: Legislative Assembly of Ontario <http://www.ontla.on.ca/committee-proceedings/transcripts/files_html/1992-10-06_e019.htm>.

³⁵ Henri Goulet, *Changements*, Vol 6, numéro 1, printemps 1996, p. 11-13, online: L’Union des Consommateurs, *L’Histoire du Mouvement des Consommateurs au Québec* <<http://www.consommateur.qc.ca/facef/24.htm>>.

counselling, debt management, micro-credit, efficient energy consumption, group consultation, and credit education sessions.³⁶

Subject to ACEFs counsellors' pre-assessment, some consumers facing debt difficulties may be eligible to small emergency personal credit or "tide-over" loans of up to \$1,000, made available on a non-profit basis by a third-party credit union.³⁷ While interest rates for these loans do not go beyond 12 percent, there are cases where consumers receive these loans interest-free for up to 24 months.³⁸ The only requirements for consumers to be entitled to these emergency loans, (when deemed necessary) are:

- be a member of a participating caisse or agree to become a member (membership costs are in the \$0 to \$12 range);
- agree to participate in budget consulting under the responsibility of the budget consulting organization associated with a Desjardins Mutual Aid Fund
- be able to repay the loan.

As co-operative, community organizations dedicated entirely to education instead of DMP-processing, ACEFs operating budgets are low. Funding for their operation comes largely from the Government of Quebec, through the The Minister of Employment, Social Solidarity and Family Welfare (Ministère de l'Emploi, de la Solidarité Social et la Famille MESSF),³⁹ responsible for administering Division III.1 of *An Act respecting the Ministère du Conseil Exécutif*,⁴⁰ concerning the *Fonds d'aide à l'action communautaire autonome FACA* (assistance fund for independent community action) and partially from membership fees and donations from charities like United Way.

Funding structure of the Non-Profit model

For decades, the largest revenue portion to the first CCCAs in Canada, excluding Quebec, has come directly from creditors. Once agencies received payments from customers to be remitted to creditors, 12 to 15 percent of each payment was donated by the creditor to the agency to cover operational costs such as salaries, equipment, bills, equipment and other expenses associated with the set-up of DMPs.⁴¹ The second most important revenue stream for CCCAs are the

³⁶ Option Consommateurs, *Des Conseillers Budgétaires Vous Aident*, online; Option Consommateur <<http://www.option-consommateurs.org/conseillers/>>.

³⁷ Loans are provided by Desjardins Mutual Aid Funds upon ACEFs referral, as confirmed to PIAC by an ACEF credit counsellor in Granby.

³⁸ Caisses Desjardins, Mutual Aid Funds, online: Caisses Desjardins, <http://www.desjardins.com/en/a_propos/profil/engagement/fonds_entraide.jsp>.

³⁹ The Ministry of Labour, Social Solidarity and Family in Quebec characterizes the ACEFs as community development corporations (CDCs) and channels substantial funding for their operation through the Secrétariat à l'Action Communautaire Autonome et aux Initiatives Sociales (SACAIS). According to the Ministry, the aim of the funding is "to offer support and financial backing to accredited community development corporations working to combat poverty."

⁴⁰ R.S.Q., c. M-30.

⁴¹ There is no current, updated information on whether or not "fair share" contributions to non-profit CCCAs by Canadian Creditors remain above the 12% levels, but in the U.S., given creditors' increasing difficulty to discern among so many "non-profit" CCCAs and competition by private agencies, their response was to decrease their contribution. Current "fair share" bank contributions from their major credit card services are: Citibank, 8%; Bank

“nominal fees” charged individually to each the debtor according to its economic circumstances and paying capacity to cover general marginal costs involved in the counselling, including the costs of paperwork, file set-up and DMP maintenance. In 2004, the CCST reported that 26 percent of the agency’s contribution sources were in the form of clients’ nominal fees.⁴²

Nominal fees charged to clients by Canadian non-profit CCCAs were minimal for many years and even today remain comparatively low, although the amounts to be charged to clients are at each agency’s discretion. The costs for a client who signs up for a DMP with a non-profit CCCA like the CCST include two services: a one-time \$25 set-up fee and, according to the agency’s assessment of client’s income after expenses presented to the counselor, a monthly fee that is deducted from each payment. The fee is variable with a maximum limit of up to 10 percent.⁴³ Therefore, the amount to be charged to each client is unpredictable and at the discretion of the agency after an assessment of the client’s financial situation. Beyond the above percentages, credit counsellors contacted by PIAC were not able to provide any specific estimates as to how much clients can expect to be charged for these services.

Traditional CCCAs in Canada are not-for profit charitable organizations, like all of the agencies affiliated with the OACCS. One of the most relevant implications in the operation of non-for-profit organizations is that their legal status allows them to be are tax-exempted. Additionally, since charitable status is conferred to them by tax and revenue authorities, they can issue receipts for the value of the donations, so that donor can use such receipts for income tax write-off purposes.⁴⁴

Creditors involvement and funding of Non-Profit CCCAs

Statistics on creditors funding of CCCAs, where available, are not very well detailed. While OACSS does not have annual reports available to the public, the CCST posts an annual report on its website, and according to its 2004 *Annual Report*, its sources of revenue that year were as follows:⁴⁵

Banks:	46%
Other:	25%
Clients:	26%
Retailers:	3%

Payments made by banks are, by far, the main source of revenue to the largest CCCA in Canada, which, simultaneously, carries the bulk of the file processing within the OACCS. The Canadian

One Corp-First USA, 0 to 8%; MBNA America, 0 to 10%; Chase Manhattan, 6 to 10%; Bank of America, 0 to 9%; Provident Financial Corp., 8%; Capital One Financial Corp., 9%; Fleet Boston Financial Corp., 6 to 9%; Household Credit, 3 to 10%; Wells Fargo Bank, 10%; Discover, 7%; Sears, 4 to 10%; American Express, 8%. *Supra* note 9 at 10.

⁴² *Supra* note 27.

⁴³ Fee schedule in place in December 2006, provided by a CCST representative during a phone interview .

⁴⁴ Terrance S. Carter, B.A., LL.B. and Karen J. Cooper. LL.B., LL.L., *The Legal Context of Nonprofit Management*, in *The Management of Non-profit and Charitable Organizations in Canada*, Edited by Vic Murray (Butterworths 2006) at 129.

⁴⁵ Actual revenue amounts are not posted. CCST Annual report, 2004

Bankers Association posts aggregate data of charitable donations made by Canada's largest banks on an annual basis in every province, but it does not detail the names of the charities and the amounts that are donated to each one of them.⁴⁶

However, those charities include the OACCS and its members, like the CCST, comprising well over 70 percent of all the CCCAs in Canada. In 2005, the total amount of outstanding DMP consumers' debt being handled by OACCS affiliates was over \$600 million.⁴⁷ If current fair share donations average 10 to 15 percent of outstanding debt, it would mean that OACCS and its member agencies receive the lion's share of all charity donations by Canadian banks

It is obviously in the best interest of creditors to support alternative avenues to bankruptcy to deal with high consumer debt loads. For them, the availability of bankruptcy and the implementation of the "fresh start" legal principle is a bad policy choice that allows debtors to have unsecured debt discharged and their financial obligations extinguished. The possibility of using DMPs as an alternative means to salvage payments from troubled debtors is compatible with the creditors' legitimate interest in profit-maximization. This, in turn, provides the strongest incentive for large creditors to play an active role in the operation of non-profit CCCAs, as well as their continued funding through "fair share" contributions.

Canadian creditors' presence in the credit counselling industry however, goes beyond being its largest source of funding through "fair share" donations. The Canadian Bankers Association endorses only the non-profit organizations to which its member banks advance "fair share" donations.⁴⁸ The CBA also endorses the OACCS and the CCC through links in the Association's website.⁴⁹ Historically also, Canadian CCCAs have had a significant share of representatives of the banking and credit industry in their boards of directors.

Board of directors' representation

The CCST has a board of directors comprised by twenty-one members, where every one of the following organizations from the banking, finance and credit industry are represented:

- MasterCard Canada, Inc.
- Royal Bank of Canada
- CIBC National Collection
- Chase Card Services, Sears Portfolio
- MJR Collection Services Limited
- Canada Mortgage & Housing Corporation
- Credit Union Central of Ontario
- Equifax Canada Inc.

⁴⁶ Canadian Bankers Association, Statistics, *Charitable Donations*, online: <<http://www.cba.ca/en/content/stats/DB%20283%20Eng%202005.pdf>>.

⁴⁷ Ontario Association of Credit Counselling Services, OACCS, Press release, online: <http://www.oaccs.com/news/OACCS_News_Release__August_2__2006.pdf>.

⁴⁸ Canadian Bankers Association, *Managing Money, A Guide to Budgeting, Credit Use and Avoiding Money Mishaps* (booklet), online: <<http://www.cba.ca/en/content/publications/ENManageMoneyFINAL.pdf>>.

⁴⁹ Canadian Bankers Association, *Managing Money*, Appendix, online: <<http://www.cba.ca/en/viewPub.asp?fl=6&sl=23&docid=27&pg=18>>.

- Trans Union of Canada Inc.
- Wells Fargo Financial Retail Services
- Sears Business Solutions
- The Investment Funds Institute of Canada
- Dynamic Funds

Sixty-five percent of the CCST's Board of Directors members are directly affiliated to the banking, finance, investment and credit sectors. One member is affiliated with a real state developer; one representative comes from the Ontario Trillium Foundation, an agency of the Ministry of Culture that also provides funding to the CCST;⁵⁰ and only one board member, or 5 percent of the Board's composition is a representative of a charitable organization, the Family Services Association of Toronto.⁵¹ The rest of the Board members are two chartered accountants and a lawyer.

The predominant representation of credit industry stakeholders in a credit counselling charitable organization raises questions from the standpoint of appropriate corporate governance as the risk for potential conflict of interest arises. Directors are vested with the decision-making powers to pass by-laws and to conduct all the particulars of the affairs of the corporation (a charitable, not-for-profit corporation, in the case of the largest credit counselling agency in Canada).⁵² In order to pass by-laws and make determinations, the quorum of the board is required,⁵³ and such quorum, under the Ontario Corporations Act,⁵⁴ is constituted by a majority of the board of directors. If a charitable organizations whose functions include to settle debtors' financial obligations owed to creditors, has a board of directors where the majority are creditors' executives and representatives, is hard to see how such credit counselling agency would not be governed in the creditor's best interest, instead of that of the troubled debtor. As opposed to trustees in bankruptcy, whose fiduciary duty is clearly specified as owed to creditors, such duty is not specified by legislation for credit agencies.

Ontario's government funding CCCAs

As mentioned, the province of Ontario, through its Ministry of Community and Social Services, financially supported CCCAs since their inception in the mid-sixties, as they took on the task of educating consumers about the pitfalls of accumulating debt and how to better manage their income and expenses while at the same time balancing quality of life and timely payment of credit obligations.

⁵⁰ Ontario Association of Credit Counselling Services, Press Release, *Ontario Trillium Foundation Funds New Projects to Teach Young Ontarians About Financial Responsibility*, August 2, 2006, online: <http://www.oaccs.com/news/OACCS_News_Release__August_2__2006.pdf>.

⁵¹ The Family Services Association of Toronto is a 90 year-old charity actively involved in promotion of social inclusion of disadvantaged groups, with social programs attending seniors, single parents, immigrants, HIV positive, gay & lesbian, and other groups. Online: <<http://www.fsatoronto.com/programs.html>>.

⁵² *Corporations Act*, R.S.O. 1990, c. C.38, s. 129.

⁵³ Donald J. Bourgeois, *The Law of the Charitable and Non-profit Organizations*, Butterworths Canada, Toronto, 1998. 55 to 63

⁵⁴ *Supra* note 48.

After the mid-eighties and throughout the early nineties, government spending was reduced in response to declining revenues from the recession and steadily climbing deficits.⁵⁵ As a result, funding of programs administered by CCCAs came to an end when the province implemented a number of cuts in provincial spending effective October, 1992.⁵⁶ It is important to note that back in the early nineties, while the Federal government was making consumer bankruptcy credit counselling compulsory arguing that the increased number of consumer bankruptcies were due to Canadians' spending habits and lack of financial planning instead of a consequence of the economic recession of the late eighties, Ontario's provincial government eliminated funding to consumer's credit counselling and education.⁵⁷

More recently, government funding to the CCCA members of the OACCS has been made possible through the Trillium Foundation, a charity agency of Ministry of Culture that allocates \$100 million in grants per year, generated by the Ontario Casino Initiative. For granting and award purposes, the Trillium Foundation favours the volunteer sector and programs related to arts, culture, community building, sports, social services and environment.⁵⁸

The For-Profit or Private Model

New entrants to the credit counselling market are incorporated, profit-driven business enterprises, and this is perhaps their main difference with the non-profit model. The main focus of their business is to deliver debt consolidation and settlement services to customers. These new enterprises have brought with them some degree of competition to a market where non-profit agencies have long been the incumbents.

For-profit CCCAs cannot rely on an incoming flow of revenue from creditors in the form of charitable donations as their non-profit counterparts. As a consequence, they need to have a much more streamlined operation, and be comparatively more efficient in signing clients to DMPs in order to raise the level of revenue that would allow them to be profitable.

Most private CCCAs in Canada are members of the Canadian Association of Independent Credit Counselling Agencies (AICCA). All of its member agencies are located and licensed in British Columbia but they operate on a national basis, as they conduct business with residents of all

⁵⁵ Tiff Macklem, Some Macroeconomic Implications of Rising Levels of Government Debt, *Bank of Canada Review*, Winter 1994-1995, 41 to 60.

⁵⁶ *Supra* note 34.

⁵⁷ *Ibid.*

⁵⁸ The granting principles of the Ontario Trillium Foundation are:

- The voluntary sector plays a critical role in building healthy and vibrant communities. OTF will work to achieve its mission by supporting the work and enhancing the long-term capacity of organizations in the sector.

- OTF grants will support organizations in the arts and culture, environment, human and social services and sports and recreation sectors.

- In small communities with a limited voluntary sector, OTF may support the work of municipalities or libraries in order to achieve its mission, specifically in the arts and culture and the sports and recreation sectors.

- Respect for diversity, inclusion and volunteerism are fundamental to the work of OTF.

- OTF offers three types of time-limited grants: operating, project and capital.

Online: Ontario Trillium Foundation <http://www.trilliumfoundation.org/cms/en/about_granting_princ.aspx>.

provinces. Given the size of the non-for-profit CCCAs associations, AICCA members' participation in the market at a national level is marginal.

Funding structure of the For-Profit or Private model

Private CCCAs are privately owned enterprises that depend entirely on clients' fees as the source of agencies revenues. However, overall fees paid by clients are not necessarily higher with these for-profit agencies than with non-profit agencies.⁵⁹ Their service consists of negotiating with creditors to obtain debt reduction for debtors. Banks and creditors generally agree to reduce their interests through these agencies to somewhere between 0 and 5 percent, and the fees are set in a similar way to the non-profit CCCAs, according to client's paying capacity. When contacted over the phone or through the Internet, for-profit credit counselors generally do not appear to spend much time with a client without prior disclosure of the clients regular source of income. If the client does not have employment, private CCCAs will generally not take the client.⁶⁰

Once a regular source of income is established, preferably generated by full-time employment, then the next step is the assessment of the consumers' budget along with her payment capacity and an explanation of the fee schedule. Set-up fees for a DMP are calculated based on the amount of the debtors' outstanding debt, the number of creditors involved (as a different proposal has to be submitted to each one of them for approval), and the time-length of the plan. DMPs must run from a minimum of 36 to a maximum of 60 months.

The initial fee to be paid by the debtor, according to the above criteria, ranges from 5 to 15 percent of the debt to be consolidated. Once arrangements have been reached with creditors, the consumer must forward or authorize her payments every month, and, again, depending on the payment amounts and the consumer's budget, the monthly agency's set fee varies from a minimum of \$35 to a maximum of \$200. Similarly to non-profit agencies, credit counsellors in the for-profit sector contacted by PIAC could provide with any set guidelines to calculate how much a prospective client would be subject to pay for their services.

Another service available at private agencies is the debt settlement plan (DSP), which consists of a submitting a proposal to creditors to negotiate the total amount of the debt in exchange for a single payment of a lower amount. Since this kind of arrangement allows for the elimination of the debt at once, consumers do not have to be employed on a full-time basis or have a stable amount of income. A debtor who's earned sudden amount cash or benefited with a windfall could be the right candidate for this service, and the fee to be charged is higher: it is a one-time fee of around \$1000 charged to the client. However, settlement plans or proposals are not well regarded among creditors, and a settlement note on the credit report has more negative effect on the debtors' reading of a credit report than a DMP. It is perhaps for this reason, along with the

⁵⁹ During an interview, a credit counselor from a private agency stated that fees collected from clients were how they private agencies "made their money" as they did not receive any "kickbacks" from creditors.

⁶⁰ PIAC found the case of a private CCCA that would not set appointments with counselors over the phone without first having consumers submit all their personal and financial information through an online form posted in their website.

higher cost of debt settlement, that these plans have a very low demand, according to the for-profit agencies consulted.

Credit Counselling Industry Accreditation System

The *Superintendent of Bankruptcy's Directive Respecting the Counselling of Bankrupts, Debtors and Consumer Debtors*,⁶¹ instructs that individuals providing counseling should assist the consumer debtor, bankrupt or relative of a bankrupt to “acquire money management and budgeting skills, in addition to explaining the bankrupt or consumer debtor on how to analyze monthly income and expenses”.⁶²

However, the *Directive* only applies to counsellors giving advice to consumers filing proposals or seeking a discharge in bankruptcy under the BIA, and not to counsellors giving advice to the financially troubled consumers of CCCAs. There are currently no statutory qualification requirements or specific rules regulating the work of these credit counsellors.

The Canadian Association of Insolvency and Restructuring Professionals (CAIRP) does administer the Insolvency Counsellor's Qualification Course (ICQC), as part of the National Insolvency Qualification Program (NIQP), required for individuals seeking certification as trustees in bankruptcy. Credit counsellors who work for CCCAs may want to enroll in the ICQC at their own discretion, but they are not obliged to do so under any statute at the provincial or the federal level.

The legal and accounting community, and particularly Bankruptcy and Insolvency practitioners, through the Insolvency Institute of Canada (IIC), have raised the concern that given the surge in DMP-focused credit counselling services, some CCCAs and their counselors may not be making their best efforts, in many cases, to advance the interests of clients and consumers but only the particular economic interest of the agency itself and that of creditors, from whom non-profit agencies receive “fair share” donations (or interest relief in the case of private CCCAs) for every client that signs in to a DMP program.⁶³

REVIEW OF LEGISLATION

The federal government does not regulate the credit counselling industry. Rather, the jurisdiction to regulate this industry is considered to fall under provincial powers because CCCAs typically

⁶¹ Consumer Bulletin, *Directive 1R Respecting the Counselling of Bankrupts, Debtors and Consumer Debtors*, Superintendent of Bankruptcy, June 1st, 1993.

⁶² *Ibid.*

⁶³ The Personal Insolvency Committee (PIC) of the Insolvency Institute of Canada (IIC) reports that it has been the experience of many trustees that counselling is simply not necessary for many individuals, and further, many individuals will not benefit from counselling in any event. The IIC is not aware of any studies or data gathered to assess whether or not mandatory counselling has been successful and no benchmarks indicating what elements would qualify as success have been developed. See *Report of the Personal Insolvency Committee of the Insolvency Institute of Canada, Recommendations for Reform and Further Amendments to the Bankruptcy and Insolvency Act, Personal Insolvency*, January, 2001, online: Insolvency Institute of Canada <<http://www.insolvency.ca/papers/PICReport.pdf>>.

do not operate on a national basis and generally restrict their business activities to operations within a province. Moreover, the principal responsibility for consumer protection resides with the provinces. Nevertheless, some federal legislation may pertain to certain activities of credit counsellors, to the extent that such activities touch upon federal jurisdiction. For instance, credit counselors must abide by the federal *Income Tax Act*⁶⁴ when incorporating as a non-profit enterprise; and marketing activities in general are governed by the Competition Bureau and office of Consumer Affairs.

A canvass of provincial consumer protection legislation reveals that there is little uniformity in the treatment and regulation of CCCAs across Canada. Since there are no nation-wide regulations in place to govern the activities of these businesses, a hodge-podge of provincial legislation has developed; often leaving considerable gaps in the regulation and enforcement of this industry. For instance, not all provinces regulate CCCAs, and those that do, generally only do so to a minimal extent (by imposing licence or registration requirements).

It is beyond the scope of this paper to provide a detailed overview of the legislative requirements governing CCCAs in each province. Rather, a general overview of provincial legislation is provided below, along with highlights of some noteworthy provisions found in the consumer protection laws of Alberta and Ontario.

GENERAL OVERVIEW OF PROVINCIAL LEGISLATION

Every province has enacted its own set of consumer protection laws, which are designed to protect consumers from unscrupulous merchants. Each province has also set up a ‘Consumer Affairs Bureau,’ which, among other things, addresses consumer complaints and oversees the enforcement of the province’s consumer protection laws. However, despite having the infrastructure to deal with a wide range of consumer affairs, not all provincial consumer affairs bureaus have the legislative mandate to address the operation of the credit counselling industry, precisely because not all consumer protection laws extend to credit counselling operations.

In contrast, all provinces regulate the debt collection industry, either through general consumer protection laws, or through specific laws and regulations targeted at debt collectors. For provincial regulatory purposes, the credit counselling industry is treated as a subset of the debt collection industry and is generally regulated as such. The problem with such treatment is that credit counselors provide a different service than debt collectors and may not, therefore, fall within the often narrow scope of debt collection laws. For instance, each province requires debt collectors to obtain either a licence or register with the Provincial Registrar, depending upon the particular province. This licensing requirement may or may not carry-over to credit counselors, depending on whether they are captured under the existing provincial ‘debt collector’ laws. Unfortunately, this determination is not always straight-forward.

Based on the wording of applicable consumer protection laws, CCCAs in Newfoundland, Prince Edward Island, Nova Scotia, Ontario, Manitoba, Saskatchewan, and Alberta – would likely all be captured under the existing debt collection laws and therefore be subject to a licensing or

⁶⁴ R.S.C. 1985, c. 1 (5th Supp.).

registration requirement. However, adding more uncertainty is the fact that in some provinces the licensing requirement may not always be applicable, depending upon the type of services offered by the CCCA. For instance, British Columbia only regulates CCCAs whose activities can be classified as a “Debt Pooling System”. Under section 125 of B.C.’s *Business Practices and Consumer Protection Act*,⁶⁵ a “debt pooling system” means “an arrangement or procedure under which a debtor pays to a debt pooler money to be distributed or paid, according to a system, by that debt pooler to 3 or more creditors of the debtor.” Thus, a CCCA that merely provides counselling or negotiations with creditors on behalf of its clients would not be captured under this narrow definition. Moreover, under this definition, a CCCA that collects money from a client and distributes it to less than three debtors would also not be captured by this definition.

In contrast, Alberta’s *Collection and Debt Repayment Practices Regulations*,⁶⁶ under the *Fair Trading Act*,⁶⁷ provides a much broader definition. “Debt Repayment Agency” means “a collection agency that carries on the activities of offering or undertaking to act for a debtor in Alberta in arrangements or negotiations with the debtor’s creditors in consideration of a fee, commission or other remuneration that is payable by the debtor.”⁶⁸ With the inclusion of the terms “arrangements or negotiations”, all traditional CCCAs are captured under this definition, whether or not they merely negotiate with the debtor’s creditors or actually collect and distribute money on behalf of the debtor.

While a number of provinces have imposed licensing or registration requirements, there seems to be little to no regulation of the industry beyond this administrative requirement. Additionally, it is not known how many licence applications get rejected every year, how much scrutiny they undergo, or how rigorously the standards are enforced. Very little policing of the industry seems to be taking place at the provincial level. A notable exception is the Ontario Ministry of Consumer and Business Services who, in 2002, laid 19 charges under the *Collection Agencies Act*⁶⁹ against a CCCA for acting as an unregistered collection agency.⁷⁰

Alberta

Alberta’s legislation is arguably the most comprehensive with regard to the regulation of CCCAs. It generally contains the same legislative requirements as most other provinces that regulate the credit counselling industry, but also includes a number of unique provisions that provide a more thorough legislative landscape through which to address the regulatory concerns of consumers vis-à-vis the credit counselling industry.

Alberta requires all collection agencies, collectors, debt repayment agencies and debt repayment agents to be licensed under the *Fair Trading Act* and the *Collection and Debt Repayment*

⁶⁵ S.B.C. 2004, c. 2, s. 125.

⁶⁶ Alta. Reg. 194/1999.

⁶⁷ R.S.A. 2000, c. F-2.

⁶⁸ *Collection and Debt Repayment Practices Regulations*, Alta. Reg. 194/1999, s. 1(g).

⁶⁹ R.S.O. 1990, c. C.14.

⁷⁰ “Unregistered company offering credit repair, credit counseling and debt management services charged” online: Ontario Ministry of Government Services <<http://www.cbs.gov.on.ca/mcbs/english/5BFQH5.htm>>.

*Practices Regulation.*⁷¹ As indicated above, CCCAs are captured under the definition of “debt repayment agency”, and are thus fully subject to the legislation. Additionally, Alberta’s legislation provides that all locations at which collection or debt repayment activity occurs must be registered on the licence, and holds the agencies responsible for the behaviour of their employees.

Listed below are some of the key provisions contained in Alberta’s consumer protection legislation pertaining to the regulation of CCCAs.

With regard to the payment of fees, the law provides for three important protections:

1. **Administration Fees:** A debt repayment agency is allowed to charge the client a one-time administration fee. However, if the repayment agreement includes a schedule of payments to the creditors, the administration fee cannot be more than the average monthly payment that is set out in the agreement. The agency can also charge 15 percent of the gross amount of the payments received from the debtor for distribution to the debtor’s creditors.
2. **Lump-Sum Payments:** If the debt repayment agency successfully negotiates a settlement of a one-time payment with the creditors that is acceptable to the debtor, the agency is allowed to charge a single fee of no more than 10 percent of the debt owed in addition to the payment made to the creditors.
3. **Contract Requirements:** Finally, the debt repayment agency must provide the client with a signed copy of the contract before providing any services. If the agency fails to do this, it cannot charge any fees, commissions or disbursement costs for its services.⁷²

Alberta’s consumer protection legislation also sets out comprehensive records keeping requirements, including records of all contacts with creditors and debtors; receipt and disbursements; and the establishment of trust accounts. In addition, there are a number of contract requirements that are applicable to credit counselling firms. For instance, according to Alberta’s Government Services website, a debt repayment contract must:

- Be in writing, dated and signed by the debtor and the debt repayment agency;
- Include the debtor’s name, address and telephone number and that of the debt repayment agency;
- Fully describe all the services that will be provided;
- List and itemize all the fees that the debtor is required to pay;
- List all creditors that will be paid under the agreement; and

⁷¹ Alta. Reg. 194/1999. Of note, the legislation does not apply to businesses or people collecting debts for which they are the original creditor or owner of the debt, a lawyer who is collecting a debt for a client, a civil enforcement bailiff or agency while seizing security or people working while licensed under the Insurance Act.

⁷² *Consumer Tipsheet: Bill Collection and Debt Repayment*, online: Alberta Government Services <http://governmentsservices.gov.ab.ca/tipsheets/bill_collection.cfm>.

- Provide a detailed accounting of the debtor's payment plan, including: the total amount owed by the debtor, the amount of each payment, the schedule of payments and the total number of payments for each creditor⁷³

In addition, Alberta's Government Services website provides consumers with a useful list of activities debt repayment agencies are prohibited from performing. For instance, a debt repayment agency cannot:

- Charge any fee for an NSF cheque unless the agency has disclosed in writing prior to the submission of the cheque that a fee will be charged
- Make any arrangement with the debtor to accept a sum of money that is less than the amount of the balance that is due and owing to a creditor as a final settlement without the prior express consent of the creditor
- Give any false or misleading information including references to the police or law firm, credit history, court proceedings, lien or garnishment
- Lend the debtor money to pay the outstanding debts
- Offer to pay or give the debtor any other form of compensation for entering into a debt repayment agreement
- Collect any fee for referring or assisting the debtor to obtain an extension of credit from a lender, creditor or service provider
- Fail to provide a receipt for all cash transactions or payments made in person or at the debtor's request
- Discuss the debtor's debt or the existence of the debt with any person except the debtor, a guarantor of the debt, the debtor's representative or the creditor of the debtor
- Make a claim for breach of contract if the debtor cancels the repayment agreement⁷⁴

Finally, Alberta's consumer protection legislation also attempts to provide more regulatory control over the credit counselling industry through the establishment of the Orderly Payment of Debts (OPD) program, which it is statutorily confined to a single provider. Under Alberta's legislation, the Credit Counselling Services of Alberta (CCSA) is the only organization in Alberta legislated to provide the OPD program.⁷⁵

Under the OPD program, CCSA makes an application to the court on behalf of the debtor for a consolidation order. This order allows the debtor to make payments, which the CCSA will distribute pro rata to the debtor's unsecured creditors. The OPD program has a number of consumer benefits. For example, by obtaining a consolidation order, the interest rate is automatically reduced to five percent; the debtor is shielded from some legal actions; and the payment schedules are based on the debtor's ability to pay. However, the OPD program does have its limitations. Most secured credit (such as property mortgages or car loans) cannot be placed within the OPD; and if the debtor enters into such a program, he or she can maintain secured credit payments outside of the OPD program, but is prohibited from getting any new credit. Moreover, if the debtor defaults while on OPD, the court will make an order permitting all

⁷³ *Ibid.*

⁷⁴ *Ibid.*

⁷⁵ *Ibid.*

registered creditors to proceed independently to enforce their claims. They do not have to sue the debtor to proceed with legal action to collect the debt.⁷⁶

By restricting the OPD program to one credit counselling provider, Alberta has gained an increased measure of control over the operation of the credit counselling industry within the province. However, there are some potential drawbacks to such a scheme. Only those consumers who seek the assistance of CCSA will be afforded the option of such a program, leaving many consumers out in the cold. Also, such a scheme may artificially restrict the ability of the alternate CCCAs to offer their clients the debt repayment program that is most appropriate for their circumstances.

Ontario

In Ontario, recent changes to the *Consumer Reporting Act*⁷⁷ now offer consumers increased protection from so-called “credit repair” companies. Credit repair companies advertise that they will repair an individual’s credit rating for a fee (usually a very large fee). However, the reality is that an individual’s credit rating or credit history cannot be changed, except in very limited circumstances. Ontario’s new regulations are aimed at those credit repair companies that are making false claims about their ability to ‘repair’ or ‘fix’ consumer credit. Specifically, the legislation prohibits a credit repairer from stating (orally, in writing or through advertising) that it will improve a consumer’s credit file unless:

- The credit repairer has reviewed the consumer’s credit file;
- The information on the file has been found to be inaccurate or incomplete; and
- The credit record would be materially improved by correcting the deficiencies.⁷⁸

This is a much needed addition to general consumer protection laws and will serve as a useful tool in combating unscrupulous businesses that prey on vulnerable consumers who are looking for a quick fix to their credit troubles.

EFFECTIVENESS OF LEGISLATION

Governance Through Industry Associations

Due to the limited provincial regulatory oversight of CCCAs, the policing of this rapidly expanding industry is largely left up to national or provincial credit counselling associations who govern their members through the use of voluntary standards and Code of Ethics. However, CCCAs, whether independent or non-profit, are under no obligation to join an industry association. Moreover, little is known about the extent to which voluntary associations police their members, or the effectiveness of the self-regulated industry.

The Canadian Association of Independent Credit Counselling Agencies (CAICCA) is one of Canada's largest independent credit counselling organization. According to its website, the

⁷⁶ *Ibid.*

⁷⁷ R.S.O. 1990, c. C.33.

⁷⁸ “Unregistered company offering credit repair, credit counseling and debt management services charged” online: Ontario Ministry of Government Services <<http://www.cbs.gov.on.ca/mcbs/english/5BFQH5.htm>>.

CAICCA “acts as industry source for its members when representing Association interests in private sector and public sector forums, and has been proactive in ensuring that the Canadian Credit Counselling Industry evolves in accordance with society’s changing needs.”⁷⁹ The CAICCA has developed a Code of Ethics for members, and purportedly “monitors member compliance through consumer and government reporting channels.”⁸⁰ However, a review of the CAICCA’s ‘Code of Ethics’ reveals a short, simplistic, and ambiguous Code that is woefully lacking in substance.⁸¹

The Ontario Association of Credit Counselling Services (OACCS) provides a similar organizational structure for non-profit credit counseling agencies. OACCS member agencies represent approximately 70 percent of the non-profit credit counselling agencies in Canada, however membership is currently limited to Ontario and Newfoundland. Under the OACCS, accreditation is a mandatory requirement of membership, which is designed to ensure that members adhere to its Standards of Practice and the Code of Ethics. Interestingly, although the OACCS makes reference to its Code of Ethics numerous times throughout its website, the Code is not posted, providing no opportunity for consumers to evaluate the OACCS’s claims of high ethical standards made throughout the website. The website does state that the Association and each member agency is managed by a professional staff and is governed by a Board of Directors. Moreover, according to the OACCS website, in order to qualify for accreditation and membership, credit counselling agencies must:

- Prepare extensive documentation demonstrating that its Board, staff and program structures meet the rigorous standards set by the OACCS;
- Closely consult with OACCS regarding the operations of the Agency; and
- Undergo scrutiny by OACCS Reviewers who have visited the agency and have examined financial, management and program records to ensure that standards have been met.⁸²

Interestingly, the website states: “community members such as agencies, clients and creditors provide critical input regarding how the agency is serving the community.”⁸³

Of note is the fact that “creditors” are listed as community members whose “critical input” is sought by the association. The degree of influence the creditors have over the association and its members, is unclear. At the very least, such a relationship leads to potential conflict of interests. Further investigation into the nature of the relationship between creditors and the credit counselling industry is warranted, to ensure that consumers are not unwittingly falling victim to industry collusion and the inappropriate pursuit of self-interests.

A Nation in Debt

⁷⁹ Canadian Association of Independent Credit Counselling Agencies (CAICCA), online: <<http://www.caicca.ca/index.php>>.

⁸⁰ *Ibid.*

⁸¹ CAICCA Code of Ethics, online: <http://www.caicca.ca/code_of_ethics.php>.

⁸² Ontario Association of Credit Counselling Services (OACCS), online: <<http://www.oaccs.com/main.html>>.

⁸³ *Ibid.*

In order to properly evaluate the effectiveness of Canada's legislation governing the credit counselling industry, it is important to understand the environment in which this industry operates. The stark reality is that Canada is a nation in debt. According to Statistics Canada, in 1984, Canadians owed about \$187 billion in personal debt. Today, Canadians owe more than \$801 billion. Even more alarming is that since 2003, nearly the average Canadian household has owed more than its annual take-home pay.⁸⁴ Personal bankruptcies are at a record high, savings are at a record low, and consumer debt levels are rising faster than incomes, and have been doing so for years. A major contributor to this debt crisis is Canadians' addiction to credit. Canadians carry 74 million credit cards, which amounts to roughly three credit cards for every Canadian over the age of 18.⁸⁵

Given Canadians' addiction to credit, it's not surprising that the credit counselling industry is one of the fastest growing industries in the country, with credit counselling agencies across Canada reporting record business.⁸⁶ The problem is that there are few, if any, regulations that govern this rapidly expanding industry.

ABUSES IN THE CREDIT COUNSELLING INDUSTRY

United States

Over the last several years, the credit counselling industry in the United States has come under intense fire for what can only be described as widespread, systemic abuses within the credit counselling industry. These abuses have prompted American lawmakers to clamp-down on the previously unregulated industry and impose tougher laws to compel more transparency and accountability into an otherwise secretive industry.

The American credit counselling industry has come under siege from all sides: the Federal Trade Commission (FTC) has launched investigations and court challenges against some of the largest CCCAs, most notably AmeriDebt Inc.; a number of state Attorney Generals have followed suit and filed lawsuits against unscrupulous companies operating in their states; both the U.S. Senate and House of Representatives have put the industry and its practices under a microscope, finding widespread abuses throughout the industry; and the Internal Revenue Service (IRS) conducted an unprecedented, industry-wide audit of the entire credit counselling industry. Below is a mere sampling of the efforts undertaken by American law enforcement officials to curtail the rampant abuses that tainted an entire industry.

⁸⁴ According to a study conducted by Stats Canada, over the past two decades, Canadian households have been spending more and saving less. The study indicates that 47% of all households were spending more than their pre-tax income in 2001, up from 39% in 1982. Between 1982 and 2001, per capita debt doubled, stemming from dramatic increases in both mortgage and consumer debt. See, "Study: Household spending and debt", Statistics Canada, The Daily (March 22, 2005). Available online at: <<http://www.statcan.ca/Daily/English/050322/d050322c.htm>>.

⁸⁵ CBC Marketplace, "Debt Nation: Are we in over our heads?" Broadcast: January 15 and 22, 2006. Online: CBC News <<http://www.cbc.ca/consumers/market/files/money/debt/index.html>>.

⁸⁶ See Margaret Johnson, "Credit Counselling: A great alternative to Bankruptcy!", Online: Canada Home Guide <http://www.canadahomeguide.ca/_vsite/10094388.100.24.10482784.aspx>.

AmeriDebt Inc. case

On March 21, 2005 the Federal Trade Commission (FTC) announced that one of the largest non-profit credit counselling firms in the United States, AmeriDebt Inc., agreed to shut down its debt management operation as part of a settlement resulting from FTC charges that it deceived consumers into paying over \$170 million in hidden fees. The FTC charged that the company misrepresented itself as a non-profit credit counselling organization that would teach consumers how to manage their finances for no up-front fee. The FTC charged that, rather than operating for charitable purposes as advertised, AmeriDebt was funneling profits to affiliated for-profit entities. According to the FTC, AmeriDebt deceived new clients into making a “voluntary contribution” to enroll in the counselling program. The FTC alleged that AmeriDebt kept the so-called “contributions” as fees without consumers’ knowledge, rather than disbursing the money to consumers’ creditors as suggested. [9] The FTC’s complaint also charged that, despite promises to teach consumers how to manage their money and avoid future debt, AmeriDebt employees simply enrolled all customers in debt management plans (DMPs). In the DMP, consumers made a single monthly payment to AmeriDebt for all their unsecured debts, with the payment then disbursed to the consumers’ creditors.⁸⁷

The settlement further prohibits AmeriDebt from misrepresenting that it is a nonprofit organization; that it does not charge up-front fees for its services; and that it will counsel consumers about their finances. In addition, the order contains a judgment of \$170 million against AmeriDebt that the FTC will seek to collect during AmeriDebt’s bankruptcy proceedings.⁸⁸

U.S. congressional reports

In March 2004, the U.S. Senate Permanent Subcommittee on Investigations tabled a report entitled “Profiteering in a non-profit industry: Abusive practices in credit counselling”. The report uncovered numerous tales of abuses committed at the hands of financial counselling and support providers. In its final report, the Committee concluded that the proliferation of so-called “non-profit” credit counselling and debt management companies is threatening to change the industry into a debt collection mill instead of an industry whose focus should be on consumer counselling and education.⁸⁹

The previous year, the U.S. House of Representatives Subcommittee on Oversight of the Committee on Ways and Means, conducted its own hearing regarding the practices of credit counselling firms. Steven Rhode, president and co-founder of Myvesta,⁹⁰ testified at the hearings

⁸⁷ “FTC Settles with AmeriDebt: Company to Shut Down”, Federal Trade Commission (March 21, 2005). Available online at: <<http://www.ftc.gov/opa/2005/03/ameridebt.htm>>.

⁸⁸ *Ibid.*

⁸⁹ U.S. Senate Permanent Subcommittee on Investigations, “Profiteering in a Non-Profit Industry: Abusive Practices in Credit Counseling”, March 24, 2004. Available on-line at: <http://govt-aff.senate.gov/_files/032404psistaffreport_creditcounsel.pdf>.

⁹⁰ The Myvesta Foundation is an outgrowth of the non-profit Myvesta organization that closed on March 31, 2006. Today, the Foundation provides consumers with free access to self-help consumer education resources via its web site. The Myvesta Foundation does not provide any hands-on assistance, specific advice, referrals or assistance to individuals in the United States regarding debt management programs but serves as a public repository of free self-help information and resources for consumers. For further information, see the Myvesta Foundation website at: <<http://myvesta.org>>.

and gave a scathing review of the industry. Among other things, Rhodes charged credit counsellors as being mere puppets of the credit card companies:

“Because credit card companies are the primary funding source for counseling programs, they exert inappropriate control over the industry. Credit card companies dictate the way all credit counselling organizations function. They have silently forced the counselling agencies to perform like paid collection agents. Some even offer collection bounties for certain types of payments. Counselling agencies, in an effort to maintain funding and provide assistance, have been left with no choice other than to comply with the wishes of credit card companies collection departments.”⁹¹

IRS investigation

On May 15, 2006, the IRS released a report, “Credit Counseling Compliance Project” on its examination of abusive practices by non-profit credit counselling organizations. The report was the culmination of over two years of work in which the IRS conducted 743 compliance checks, evaluated 110 applications, and conducted 63 audits of non-profit credit counselling agencies. Following its industry-wide investigation, the IRS revoked the tax exemptions of 41 non-profit organizations (comprising \$410 million of the \$1 billion revenues generated annually by the credit-counselling industry).⁹² The revocations result from these organizations failing to provide the level of public benefit required to qualify for tax exemption. Many of these agencies offered little or no counselling or education and appeared to be primarily motivated by profit. In many instances, these agencies also served the private interests of related for-profit businesses, officers and directors.⁹³

According to IRS Commissioner Mark W. Everson, “[o]ver a period of years, tax-exempt credit counselling became a big business dominated by bad actors... Our examinations substantiated that these organizations have not been operating for the public good and don’t deserve tax-exempt status. They have poisoned an entire sector of the charitable community.”⁹⁴

Commissioner Everson went on to state that: “We are taking the unprecedented step of contacting every known organization in the tax-exempt credit counselling world to determine if there are further problems. And we are issuing guidance to assist those smaller organizations who do play it straight and want to continue to stay on the right side of the law.”⁹⁵ In addition, the IRS has tightened up its review of new applications by credit counselling firms for tax-

⁹¹ Statement by Steven Rhode on the Credit Counselling Hearing Held by The Subcommittee on Oversight of the Committee on Ways and Means. November 20, 2003. Available online at: <<http://www.bankruptcyaction.com/BankruptcyNews.htm>>.

⁹² Internal Revenue Service, “Credit Counseling Compliance Project: Summary of Results” (May 15 2006). Available online at: <http://www.irs.gov/pub/irs-tege/cc_summary_of_results.pdf>.

⁹³ “IRS Takes New Steps on Credit Counselling Groups Following Widespread Abuse”, Internal Revenue Service (May 15, 2006). Available online at: <<http://www.irs.gov/newsroom/article/0,,id=15699,00.html>>.

⁹⁴ *Ibid.*

⁹⁵ “Credit Counsellors under Scrutiny by Canada’s Office of Consumer Affairs”, Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/blog/credit-counsellors-under-scrutiny>>.

exempt status. Since 2003, about 100 applications have been reviewed, but only three have been approved.⁹⁶

Canada

The widespread abuses in the United States have prompted many Canadians to question the integrity of the credit counselling industry north of the border. Canada's Office of Consumer Affairs is currently undertaking a study of credit counsellors, in order to "ensure that consumers are well served and to reduce the risk of fraud or conflict of interest".⁹⁷ Indeed, Canada has not been immune from charges of fraud and deceptive practices in the industry and cracks are starting to appear that suggest the need for immediate action.

Renew Credit Services Canada Inc. case

In 2002, the Ontario Ministry of Consumer and Business Services laid 19 charges under the *Collection Agencies Act* against Renew Credit Services Canada Inc. for acting as an unregistered collection agency. The company left consumers in financial turmoil after offering to help financially distressed consumers negotiate with their creditors, while charging significant up-front fees in excess of \$1,300. The ministry stepped in after receiving complaints from consumers across southern Ontario about the company. Despite having paid up-front fees and enrolling in Renew's financial management plans, complainants continued to receive repeated calls from their creditors and were unable to contact anyone at Renew.⁹⁸

According to Tim Hudak, former Ontario Minister of Consumer and Business Services: "The ministry receives numerous complaints from consumers about unethical debt management and credit repair companies that scam vulnerable consumers."⁹⁹

RECOMMENDATIONS

Canada needs to have a healthy discussion about creating a better, more accountable, system for consumers who find themselves in financial difficulty. Consumers deserve a credit counselling industry that gives them unbiased, comprehensive assistance.

The following is a brief list of recommendations, that if adopted, would serve to better ensure that consumers seeking credit counselling services are provided with high quality, unbiased advice from an industry that is transparent, accountable and designed to serve the best interest of the consumer.

1. Provincial Licensing Requirements

As noted above, not all provinces have enacted licensing requirements for CCCAs. The lack of legislative attention devoted to this industry is cause for concern. At the very minimum, CCCAs

⁹⁶ *Ibid.*

⁹⁷ Canada's Office of Consumer Affairs, Project Summary # 9 - Credit Counselling Consultation Practices and Ethics. Available online at: <http://strategis.ic.gc.ca/epic/internet/inoca-bc.nsf/en/ca02078e.html>.

⁹⁸ "Unregistered company offering credit repair, credit counseling and debt management services charged" online: Ontario Ministry of Government Services <<http://www.cbs.gov.on.ca/mcbs/english/5BFQH5.htm>>.

⁹⁹ *Ibid.*

doing business in Canada should have to obtain a licence or registration from the provincial registrar of the province in which it is conducting business. In the U.S., nearly half of the states have gone a step further and enacted legislation requiring some type of registration or licensing requirement for credit counsellors.¹⁰⁰

2. Increased Regulatory Oversight

Mandatory licence requirements represent only a minimal level of regulatory oversight. Such a system risks becoming meaningless unless proactive steps are taken by the Provinces to police the requirements of their consumer protection legislation that licensees must obey. In order to be effective, the law must be strictly enforced against those that fail to comply. For instance, if a CCCA fails to abide by provincial regulations, then it must be subject to a range of financial sanctions, which would include having its licence revoked. Provincial legislation should also be amended to include substantive provisions providing further safeguards, such as setting fee limits, and requirements that consumers be given written contracts and bond requirements. Increased regulatory oversight of the credit counselling industry would help to ensure that consumers, in a position of some vulnerability are not being taken advantage of. It would also serve to put credit counselling firms on notice that the provincial government has the ability and willingness to enforce provincial laws.

3. Mandatory Membership in Provincial/National Industry Association

Membership and accreditation in a provincial or national industry association would help to ensure that every CCCA adheres to rigorous Standards of Practice and Code of Ethics set by a provincial or national association. Adhering to such industry standards and codes of conduct would help foster integrity and trust within the industry and serve to establish high standards in governance, accountability, services and ethics.

An accreditation program would also ensure strong and consistent operating practices. Accreditation requirements are generally based on professional service delivery standards, legal criteria and the association's standards of excellence. Achieving accredited status ought to be a mandatory requirement for membership of any provincial or national association. Other requirements could include that the association and each member company is managed by professional staff and is governed by a Board of Directors.

4. Industry Quality Standards

Creditors in Canada ought to learn from the experience of their American counterparts, where levels of consumer dissatisfaction with major CCCAs reached historical heights. Lack of scrutiny by the credit granting industry over the practices of CCCAs in the U.S. led to many inconsistencies and inappropriate debt relief plans being adopted by unwitting consumers. Debtors who should not have been advised to adopt debt consolidation were being placed on DMPs; while consumers with the financial capability to pay for their debts were being advised into debt consolidation, providing them with unfair breaks. As a result, some of the largest U.S. creditors introduced stricter requirements on CCCAs, such as ISO 9000 certification, as a mandatory requirement for eligibility into the "fair share" contributions program.

¹⁰⁰ "Credit Counseling in Crisis Update: Poor Compliance and Weak Enforcement Undermine Laws Governing Credit Counseling Agencies", Report by the National Consumer Law Center (November 2004) at p. 4.

The experience in the U.S. suggests that large creditors can be an effective means to enforce best practices, ethical standards, corporate social responsibility and increased transparency within the credit counselling industry.

5. Increased Audits by CRA

Given the widespread abuses by credit counselling firms uncovered by the FTC and the IRS south of the border, it would seem appropriate for the Canadian Revenue Agency (CRA) to conduct similar investigations into the practices of Canadian-based CCCAs operating under the auspices of a non-profit designation. As previously indicated, the results of the IRS's industry-wide audit were startling. Credit counseling firms were found to be hiding behind their non-profit status, while siphoning huge profits to their for-profit affiliates. Moreover, many of the credit counselling agencies did not provide meaningful education or counselling. For example, some organizations put their clients on fixed payment plans to pay down their debt. But an organization that offers only this service, without significant education and counselling, would not qualify for tax-exempt status. Abuse of the non-profit tax designation by CCCAs is likely not a phenomenon restricted to the United States. The CRA should take proactive steps to stem the tide of abuses before they reach the levels previously found to exist in the United States.

6. Stricter Evaluation of Applications for Non-Profit Status by CRA

The CRA should also implement measures to introduce stricter requirements in the evaluation of new applications for non-profit status by CCCAs. Among other things, consumer education and counselling should be the predominant focus of a CCCA applying for non-profit status.

Abuse of the "non-profit" designation presents particular dangers for vulnerable consumers who are more likely to trust a company that has been granted non-profit status by the government. The fear is that when dealing with "non-profit" organizations, consumer confidence may overshadow or replace the normal degree of scrutiny the typical consumer would apply to financial dealings.

7. Increased Institutional Transparency

It is crucial that CCCAs act in the best interests of the debtor, as opposed to simply advancing the financial interests of the creditor or agency. Authorities in Canada, both at the federal and provincial levels, ought to closely examine the business relationship that exists between non-profit CCCAs and credit lenders. There is a real risk that the lines have become blurred when it comes to whose interests are the CCCAs truly representing and whether or not credit counsellors owe a fiduciary duties to either the debtor or the creditor. As the U.S. Senate report warned, when a profit motive is injected into a non-profit industry, it should come as no surprise that harm to consumers will follow.¹⁰¹

Another practical lesson to take away from the experience of our neighbours to the south is the dangers that can arise from the traditionally heavy volume of creditors on CCCA Board of

¹⁰¹ Permanent Sub-Committee on Investigations of Committee on Homeland Security and Governmental Affairs, United States Senate, "*Profiteering in a Non-Profit Industry: Abusive Practices in Credit Counseling*" Report. U.S. Printing Office, Washington, 2005, at 1.

Directors. A lawsuit by independent CCCA's against the NFCC in 1994 ended with a settlement that included the removal of creditors' from the NFCC board of directors.¹⁰²

8. Increased Consumers Representation on Boards of Directors

The consumer credit counselling industry in Canada prides itself on its achievements in representing and assisting all vulnerable Canadians, yet it is precisely this demographic that is being ignored within the CCCAs' corporate governance structure.

The current governance structure of CCCAs is characterized by over representation of banking, finance, retail and other closely related sectors within the Board of Directors of non-profit CCCAs. In sharp contrast lies the marked under representation of consumer groups and credit users on these same Boards. Non-profit credit counselling agencies are designed to serve the interests of the consumer, therefore, adequate levels of representation by credit users and consumer groups and community groups in the decision making practices of these bodies are the best guarantee of increased decision-making transparency and serve as a deterrent to abuses.

Additionally, consumers' and credit users' representation in boards is a much needed way of bringing legitimacy and consumer confidence to the credit counselling industry and to strengthen the credit system in Canada.

9. Increased Emphasis on Consumer Education

Above all, more needs to be done in terms of educating vulnerable consumers as to their options when faced with significant debt obligations. Depending on their particular financial circumstances, different people will require different types of financial management assistance. In order to turn the tide in the rising debt-to-income ratio in Canada, consumers need to become empowered with knowledge about debt management and budgeting. Consumers need to be provided with honest, unbiased information on what types of services are available and what their rights are under the law.

Until consumers themselves look for counseling, it is desirable that the government promote the objectives of consumer education.¹⁰³ The fact that a consumer opts for filing for a bankruptcy discharge does not necessarily imply that the consumer would not have made the same choice absent credit counseling. There may be cases where consumers who opted for credit counseling and DMP programs would have been better off had they filed for bankruptcy and exercised their right to a "fresh start". Therefore, consumer financial education should be focused on enabling and habilitating consumers to make the good financial decisions according to their individual circumstances, needs, and quality of life factors.

If the government, through its own, or in cooperation with other stakeholders is not engaged in promoting citizen education with respect to credit use, the resulting harmful consequences will likely be disproportionately costly. These will likely include not only consumer financial misfortunes caused by the lack of financial management skills, but also unproductive and inefficient societal costs associated with family breakdowns triggered by financial crises and

¹⁰² *Ibid.* at 35.

¹⁰³ Berry & McGregor, *Counselling Consumer Debtors Under Canada's Bankruptcy and Insolvency Act*, Osgoode Law Journal at 376

corresponding increased risk for lenders arising on default. In addition as we have discussed, such ignorance may also be the seed for the growth of an industry that flourishes with elevated rates of consumer debt.

CONCLUSION

Consumer credit counselling agencies have become an important and influential stakeholder in the Canadian credit industry. They provide valuable assistance to over-indebted individuals through a number of services, including working with creditors: to consolidate debt payments, reduce existing debt, and improve credit ratings. Most importantly, the majority of credit counselling agencies provide important educational tools to enable over-indebted individuals to successfully manage their debt and personal finances.

However, the credibility of this industry has increasingly come under attack, particularly in the United States, where the industry has been marred by scandals and has been the subject of numerous high-profile government investigations. Here in Canada, cracks are beginning to form. Increases in consumer complaints and media coverage has exposed unethical debt management practices perpetrated against vulnerable consumers at the hands of CCCAs.

Canada's economy is faced with unprecedented levels of consumer debt. The availability and ease with which consumers can access credit has meant that many Canadians are plagued with an over-reliance, and dependency, on credit. As such, it is imperative that Canadian consumers have a reliable and effective credit counselling industry in which to turn, especially when it comes to preventative education and debt management assistance. This industry has the potential to help thousands of vulnerable consumers out of financial straights and onto a renewed path to healthy financial planning. However, the risk remains that without swift and decisive action on the part of legislators, industry stakeholders, and consumer groups, the Canadian credit counselling industry may head down the same path that befell its American counterpart.

As such, we feel the time has come to have a frank discussion about creating a better, more transparent and accountable system for consumers who find themselves in financial difficulty. Channels need to be created through which an open dialogue can take place among *all* stakeholders throughout the industry. Furthermore, legislators need to take proactive measures by addressing some obvious gaps in the legislative roadmap. Consumers deserve a credit counselling industry that gives them unbiased, comprehensive assistance and provides them with the educational tools they need to successfully manage their debt and personal finances.

As outlined above, there is no uniform law governing credit counselling services in Canada. Instead, there is a patchwork of provincial legislation throughout the country that features some very large, gapping holes. Some provinces simply have no laws governing credit counselling services, while others provide minimal legislative oversight, usually in form of licence or registration requirements.

This general lack of regulatory oversight is compounded by the lack of consistency within the industry. In the rush to capitalize on Canadians' lack of credit management skills, businesses are

setting up shop under a myriad of different names - Credit Counsellors, Debt Counsellors, Money Management Consultants, Financial Consultants, Planners, etc. – all hoping to attract desperate consumers seeking financial help. Moreover, credit counselling services can provide vastly different services, charge different fees, and provide different information to consumers regarding their general rights and obligations. As a result, the quality of service provided to consumers varies greatly depending upon the particular credit counselling agency.

PIAC considers it of deep concern that none of the provincial legislation currently in place addresses the relationship between non-profit CCCAs and major creditors. Credit counsellors that operate as "non-profit" are funded by various credit grantors - such as banks, credit card companies and department stores; who also control their Boards of Directors. This relationship represents a clear conflict of interest. The creditor's effective decision-making control over non-profit CCCAs (who rely on them for funding), makes it unclear as to who's interest the credit counsellor is truly representing. Consumers need to approach these non-profit CCCAs with a healthy dose of skepticism and an eye to ensuring that they are getting the best advice for their particular financial circumstances.

At present, it is very much a "consumer beware", "use-at-your-own-risk" industry. Given the lack of regulatory oversight, the lack of accountability, and the size of the capital at stake, the credit counselling industry in Canada is ripe for abuse. The example from south of the border provides ample evidence of what can happen when an industry is left unchecked. Given the troubling history of credit counselling in the United States, Canadian regulators should be taking proactive steps to address the potential abuses before they become a cancer that spreads throughout the industry. We have an opportunity to learn from the mistakes that happened in the United States and we have the benefit of using that knowledge to prevent a similar situation from developing here at home.

The lack of regulatory oversight and adequate policing of the credit counselling industry means that consumers need to be aware of the risks and avoid the pitfalls of the credit counselling industry.

The larger problem, in PIAC's view is that there is little, if any, opportunity for consumers make truly informed decisions as to their credit counselling options. The industry itself operates unchecked behind a large cloak that makes it virtually impossible for organizations such as PIAC to accurately compare one credit counselling model to another, or attempt to make any overall conclusions as to the effectiveness, reliability, or trustworthiness of the industry as a whole. The lack of transparency and openness within the credit counselling industry has directly hindered PIAC's ability to draw any conclusions, or offer any advice, as to which model (for-profit or non-profit) would be a better option for consumers. From the little insight into the inner workings of the industry that PIAC was able to obtain from its research, there appears to be little in the way of uniformity or predictability in the way in which credit counselors apply fees, counsel clients, or arrange re-payments terms with creditors. At this time, it is simply not possible to reach any solid conclusions as to which model, if either, is to be preferred. What is evident, however, is that more research needs to be done in order to provide consumers with an accurate picture of the industry as a whole.

In this regard, PIAC strongly recommends that a comprehensive side-by-side comparison of the two credit counselling models be undertaken by regulators, so that consumers can decide for themselves which model best meets their needs. Moreover, a comprehensive comparison of the two models would allow consumers and regulators to see precisely where consumer's money is going, what they are receiving for it, and ultimately, who's interests are truly being served. It is only once such an analysis is undertaken that regulators will be in a position to take proactive steps to identify shut down unscrupulous operators. At present, enforcement is largely reactive, with law enforcement stepping in only after numerous consumers have fallen victim to credit counselling scams.

Once again, it should be emphasized that the evidence suggests that most CCCAs carry out financially sound and ethical credit counselling practices. Nevertheless, consumers must be cognizant of the "bad actors" within the industry and take steps to avoid those unscrupulous companies that are only out to make a profit (even if they claim to be "non-profit"). Thus, what is needed is a combination of legislative action on the part of regulators, more oversight within the industry itself, and more awareness by the public about the potential for abuse within the industry.

As previously outlined, PIAC has compiled a list of recommendations that we feel would better ensure that consumers seeking credit counselling services are provided with high quality, unbiased advice and assistance. The goal is to have a successful industry that is transparent, accountable and designed to serve the best interest of the consumer. PIAC's recommendations include: strengthening provincial licensing requirements; increasing oversight of the industry (whether it be through government regulatory bodies or increased industry oversight); imposing mandatory membership in a provincial or national association; imposing quality standards throughout the industry; increasing the number of audits conducted by the CRA and imposing stricter evaluation of applications for non-profit status by the CRA; increasing institutional transparency; adopting stricter requirements for membership in Boards of Directors for non-profit CCCAs; and finally (and most importantly), increased emphasis on consumer education.

In order to better assist consumers, PIAC has also compiled a list of "Consumer Best Practices" when dealing with the credit counselling industry. These are designed to arm consumers with the knowledge necessary to successfully navigate the credit counselling roadmap while avoiding the pitfalls set by the few unscrupulous bad actors.

CONSUMER BEST PRACTICES

So, what does all this mean for Canadian debtors looking for financial counselling? The lack of regulatory oversight and adequate policing of the credit counselling industry means that consumers need to be aware of the risks and avoid the pitfalls of the credit counselling industry. Most CCCAs carry out financially sound and ethical credit counselling practices. Nevertheless, consumers must be armed with the knowledge necessary to make an informed decision as to: 1) whether or not credit counselling is the best solution to their financial problems, 2) whether a for-profit or non-profit credit counselling agency will best meet their needs, and 3) whether the

particular credit counselling agency they choose will provide them with reliable and comprehensive service, with their best interests in mind.

Understand the Difference Between Consumer Finance Services

First and foremost, it is vital that consumers understand the difference between the different types of financial services offered to consumers seeking debt assistance. Being able to identify a particular type of company may be more difficult than one would think. As discussed earlier, the industry does not employ standard terminology and therefore it may be difficult to identify the true nature of a business. Thus, do not be fooled by a name or title. It is important to be able to identify the nature of the business by its services and characteristics.

Credit Counselling Agencies (CCCA's)

A debt repayment agency, or CCCA, is a business that charges a fee to act for the debtor in negotiating or making arrangements with creditors to pay back the monies owed. This is a voluntary agreement between the debt repayment agency (acting for the debtor) and the creditors.¹⁰⁴

There are two types of credit counsellor: independent credit counsellors and those who advertise as “non-profit”. The two types of credit counsellors have similar services. The main difference is that the “non-profit” credit counselling firms get funded from various credit grantors such as banks, credit card companies, and department stores. Credit counsellors can assist individuals in debt in acquiring the discipline they need to get control of their debt.¹⁰⁵

It is important to note that industry licensed credit counsellors do not lend money; neither do they arrange loans for clients. They will not charge a fee to refer a consumer to a Bankruptcy Trustee or to fill out forms.¹⁰⁶

Debt Consolidation Companies

These companies offer loans to settle consumers’ debt by paying off current debt obligations. The process involves combining several loans or liabilities into one loan, a “consolidation loan”. Essentially, debt consolidation is the process of taking out a new loan to pay off a number of other debts. Most people who consolidate their debt are usually doing it to attain a lower interest rate, or the simplicity of a single loan. Nevertheless, these loan agreements can feature high interest rates and extensive penalty fees, which are not well disclosed. Reliance on these types of consolidation loans often result in more debt. One of the dangers is that many consumers sign up for consolidation loans to pay off their credit cards, and keep using their credit cards. The outcome: they are stuck with the loan and the new credit card bills and the deep debt cycle

¹⁰⁴ *Consumer Tipsheet: Bill Collection and Debt Repayment*, online: Alberta Government Services <http://governmentsservices.gov.ab.ca/tipsheets/bill_collection.cfm>.

¹⁰⁵ “What Credit Counsellors are and how they operate”, Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/Credit-Counsellors.htm>>.

¹⁰⁶ *Consumer Tipsheet: Bill Collection and Debt Repayment*, online: Alberta Government Services <http://governmentsservices.gov.ab.ca/tipsheets/bill_collection.cfm>.

continues. However, if a consumer uses a debt consolidation to pay-off multiple credit card accounts and is careful to repay the loan and discontinue use of those credit card accounts (to ensure they are not piling on more debt), a consolidation loan can be a useful financial tool.¹⁰⁷

Credit Repair Companies

Beware of companies that claim they can “fix” or “repair” consumers credit. This is not the case. If a file includes accurate, yet negative information about your credit history, this information cannot be changed before the legal time period has expired. For instance, Ontario’s *Consumer Reporting Act*¹⁰⁸ allows creditors to submit factual information on a consumer’s payment history to the credit bureaus that reflects the consumer’s payment history and amounts owed. This information can remain on your report for 7 years under this Act.¹⁰⁹ Therefore, do not believe anyone who claims they can get negative information removed from your credit report faster than is legally required. There are no “loopholes” or laws that credit repair companies can use to get correct information off your credit report.¹¹⁰

The reality is that most consumers can do for themselves what these companies will charge for. This fee is often as high as \$1500. In most cases, when a credit repair company “repairs” a consumer’s credit, they are simply helping to remove erroneous information and/or items over seven years old on the consumer’s credit report. Any consumer can do this by obtaining a copy of their credit report and filing a request with the credit bureau to remove erroneous or expired account information. When a consumer files a dispute or requests an investigation of account information, credit bureaus are required to verify with a consumer’s creditors that all information is accurate. If the credit bureau is not able to verify the data, the bureau must remove the information from a consumer’s credit report.¹¹¹

Again, no credit repair company has the power to change or erase accurate information in a consumer's credit file. The only way to improve a poor credit rating is to adopt sound credit practices and work with your creditors and show that your payment habits have improved.

Understand Your Rights as a Consumer

The best way to protect yourself is to be fully informed of your rights before entering into contracts with credit repair and debt management companies.

Effect of Credit Rating/Credit History

¹⁰⁷See “Debt Consolidation”, online: Canada’s Office of Consumer Affairs
<<http://strategis.ic.gc.ca/epic/internet/inoca-bc.nsf/en/ca02156e.html>>.

¹⁰⁸ R.S.O. 1999, CHAPTER C-33.

¹⁰⁹ *Ibid.*, s. 9(3).

¹¹⁰ “See “Consumer Protection: Credit Repair”, Online: Ontario Ministry of Government Services
<http://www.gov.on.ca/MGS/en/ConsProt/STEL02_045974.html>.

¹¹¹ *Ibid.*

A debt management program does not change your credit history. For instance, under most provincial legislation, accurate information about your accounts can stay on your credit report for up to seven years (ten years in some provinces depending on the information).¹¹²

All credit counselling programs will have an effect on your credit rating. The credit bureau will record that a debt repayment plan is in place.¹¹³ In most cases, credit counselling programs will provide you with an R7 credit rating and will remain on your credit bureau file for two to three years after the completion of the program.¹¹⁴

Are your Payments too High?

Setting your monthly payments too high is common. As a general rule, your payments should be high enough so that a significant amount of your debt is paid down every month; however, your payments should not be so high that you have no life. Financial experts caution that when individuals do not have money left over at the end of the month to pay for the small pleasures in life, they are far more likely to end up defaulting on their payments to the credit counsellor. Thus, payments should be set at a manageable level so that individuals are not forfeiting their life in order to pay down their debt.¹¹⁵

What Should Your Monthly Payments Be?

Many experts suggest that the Superintendent of Bankruptcy Standards¹¹⁶ on required payments in a bankruptcy or a proposal are a good indicator for establishing the maximum payments that should be made in a monthly payment schedule set up by a credit counsellor. The standards for 2006-07 are:

- One Person = 50% of monthly take home pay in excess of \$1,755/mo;
- Two People = 50% of monthly take home pay in excess of \$2,194/mo;
- Family of Three = 50% of monthly take home pay in excess of \$2,729/mo;
- Family of Four = 50% of monthly take home pay in excess of \$3,303/mo.
- Family of five = 50% of monthly take home pay in excess of \$3,693/mo;

¹¹² See Margaret Johnson, "Credit Counselling: A great alternative to Bankruptcy!", Online: Canada Home Guide <http://www.canadahomeguide.ca/_vsite/10094388.100.24.10482784.aspx>.

¹¹³ "What Credit Counsellors are and how they operate", Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/Credit-Counsellors.htm>>.

¹¹⁴ An "R7" credit rating indicates that you are "making regular payments through a special arrangement to settle your debts". Every piece of credit history information in your credit file is assigned a rating by the credit grantor. The most common ratings are "R" ratings. These are known as North American Standard Account Ratings and are the most frequently used. The "R" indicates that the item being described involves revolving credit. If you always pay on time, it will be coded an R1. If an amount was written off because you never paid it back, it is coded R9. The "R" ratings are a coding system that translates "on time", "one month late", "two months late", etc., into two-digit codes. See "Credit Rating", Online: Canada's Office of Consumer Affairs <<http://strategis.ic.gc.ca/epic/internet/inoca-bc.nsf/en/ca02179e.html>>.

¹¹⁵ "What Credit Counsellors are and how they operate", Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/Credit-Counsellors.htm>>.

¹¹⁶ The Superintendent of Bankruptcy Standards are found in Directive No. 11R, Surplus Income, of the *Bankruptcy and Insolvency Act*. The Standards are available online at: <<http://strategis.gc.ca/epic/internet/inbsf-osb.nsf/print-en/br01055e.html>>.

- Family of six = 50% of monthly take home pay in excess of \$4082/mo; and
- Family of seven+ = 50% of monthly take home pay in excess of \$4471/mo.¹¹⁷

How Long Should You Pay?

Most financial experts agree that the term should be a maximum of three to four years. It is a stipulation in the *Bankruptcy and Insolvency Act* (BIA) that the term for a "Consumer Proposal" be no more than five years. It has been found that terms exceeding this timeframe have a very high failure rate, because people cannot see a "light at the end of the tunnel".¹¹⁸

Important Consumer Tips

Below is a compilation of important tips for consumers when seeking the help of a CCCA. The list was produced after a canvassing of articles and writings by industry experts, which included numerous recommendations for consumers seeking to avoid the pitfalls of the unregulated world of credit counselling.

Counsellor Qualifications – Credit counsellors are under no obligation to receive specialized training or accreditation. Credit counsellors will therefore have varying levels of knowledge about the industry. Some companies employ highly trained Registered Insolvency Counsellors (RQIC) under the *Bankruptcy and Insolvency Act*¹¹⁹ (BIA); other companies are less rigorous about the training requirements of their counsellors. Always ask about the counsellor's qualifications, including: education, specialized training, and years of experience. Those in the industry warn that having worked in insurance sales, as a financial planner or in a bank, may not be enough credit knowledge to provide you with the best advice. Do your homework before you make your decision to hire a particular credit counsellor.¹²⁰

Do Some Research – It is important to do your homework before deciding upon a particular credit counselling agency. The best approach is to interview several companies before making a selection. Ask if the company is a member of the Better Business Bureau, and if so, check with the Bureau to find out if any consumers have filed complaints about the company you are considering. Also, consider contacting the Consumer Affairs Office in your province to find out more about companies that are licensed.

¹¹⁷ *Ibid.* The Superintendent's Standards are derived from the Low Income Cutoffs (LICO) released by Statistics Canada. The Superintendent uses the before-tax LICO for urban areas 500,000 people and over. The 2006 standards are updated adding to the 2001 LICO the 2002, 2003, 2004 and 2005 Consumer Price Index (CPI), 2.2%, 2.7%, 1.9% and 2.2% plus a 1.9% adjustment reflecting the 2006 CPI expectation.

¹¹⁸ "What Credit Counsellors are and how they operate", Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/Credit-Counsellors.htm>>.

¹¹⁹ R.S., 1985, c. B-3.

¹²⁰ See Margaret Johnson, "Credit Counselling: A great alternative to Bankruptcy!", Online: Canada Home Guide <http://www.canadahomeguide.ca/_vsite/10094388.100.24.10482784.aspx>.

Get a Second Opinion – It is always a good idea to get a second opinion from a Trustee-in-Bankruptcy or an Insolvency Lawyer. Trustees will give free consultation with no obligation to use their services. Insolvency lawyers will charge between 1-1.5 hours of their time.¹²¹

Find Out the Basics - Before you make a decision, find out some of the basics, including: Is the company set up as a non-profit or independent business? What are the company's sources of funding? You want to find out whose interests are most represented and protected by the agency – remember that the non-profit CCCAs are funded by the creditors, so before you sign on, you'll want to be assured that they are clearly representing your interests and not those of their sponsors.

Ask for Contract Specifics – Ask for time to review the contract before signing and make sure that all fees, payment obligations and other responsibilities are clearly laid out in the contract. You'll also want to find out what happens if you miss a payment or your financial circumstances change and the repayment plan becomes more than you can afford. Make sure any penalty fees are clearly laid out in the contract.¹²²

Personal Information Handling Practices – Find out how the company is going to handle your personal information - what is their privacy policy? Never allow the agency to sell or trade any of your information with any third party without your explicit written permission.¹²³

Once You've Made a Selection – After you've done your homework and are satisfied in your selection of credit counselling agency, you must still remain vigilant about keeping track of how your finances are being handled. You should ask to receive status reports at regular intervals (60 or 90 days) and ensure that you can get a written report at any time. Always get a receipt for any cash money paid and always make payments “in trust” to the agency (this should be set out in the contract).¹²⁴

Records Management – Keeping accurate and up-to-date records of your finances and dealings with the credit counsellor is essential. For instance, you should keep thorough records of: how much you have paid on your debts, who you paid, when you made payments, the form of payment you used (cash, cheque, debit card, money order, etc.), who you talked to about your debt and any payment arrangements you agreed to. Make sure you are able to verify (by receipts, cancelled cheques, etc.) any payment you made to an agency or creditor.¹²⁵

¹²¹ “Credit Counsellors under Scrutiny by Canada’s Office of Consumer Affairs”, Online: BankruptcyCanada.com <<http://www.bankruptcycanada.com/blog/credit-counsellors-under-scrutiny>>.

¹²² See Margaret Johnson, “Credit Counselling: A great alternative to Bankruptcy!”, Online: Canada Home Guide <http://www.canadahomeguide.ca/_vsite/10094388.100.24.10482784.aspx>.

¹²³ *Ibid.*

¹²⁴ *Ibid.*

¹²⁵ *Consumer Tipsheet: Bill Collection and Debt Repayment*, online: Alberta Government Services <http://governmentservices.gov.ab.ca/tipsheets/bill_collection.cfm>.

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