

**DEPARTMENT OF JUSTICE
EXECUTIVE OFFICE FOR UNITED STATES TRUSTEES**

FINAL AGENCY ACTION

**APPLICATION FOR APPROVAL AS NONPROFIT BUDGET
AND CREDIT COUNSELING AGENCY, 1005-CC-00220**

REVIEW OF DECISION TO DENY APPROVED STATUS

Consumer Legal Referrals, Inc. (the "Applicant") seeks review of the decision denying its application for approval as a nonprofit budget and credit counseling agency dated February 2, 2006.

I. Course of this Proceeding

The Applicant first applied for approval as a nonprofit budget and credit counseling agency on September 8, 2005. After review of its application, an initial determination was made that the Applicant did not satisfy the applicable standards for approval set forth in 11 U.S.C. § 111(c). By letter dated October 12, 2005, [redacted] the president of the Applicant, was notified of the decision to deny the application and was provided with an explanation for the denial. On October 17, 2005, the Applicant reapplied for approval. This application (the "application") was assigned number 1005-CC-00220. The application was reviewed and it was again concluded that the Applicant failed to satisfy the standards set forth in 11 U.S.C. § 111(c). [redacted] was notified of this decision by letter (the "denial letter") dated February 2, 2006.

On March 2, 2006, [redacted] wrote a letter requesting reconsideration of the denial of the application. On March 29, 2006, he was advised that he could seek further review of the denial decision on behalf of the Applicant by following certain procedures.

On April 12, 2006, [redacted] wrote a letter to the Director of the Executive Office for United States Trustees in which he alleged that the Applicant had been discriminated against because it was not affiliated with the consumer credit counseling industry or with "a small nucleus of organizations that the Department of Justice appears to have given special treatment and applied different standards [to] than those applied to [the Applicant]." The Director treated [redacted] letter as a request for administrative review.

II. The Denial Decision

In the denial letter, it was noted that the Applicant failed to satisfy the standards for approval under 11 U.S.C. § 111(c) for three distinct reasons.

1. The Applicant failed to establish that it was operating as a nonprofit entity with an independent board of directors.
 - a. While the Applicant stated that it had applied for 501(c)(3) status on June 30, 2005, it had not yet received the designation from the Internal Revenue Service.

- b. The Applicant was organized on June 5, 2005. Since the date of organization, the constituency on the board had changed three times, all in response to concerns raised by the United States Trustee. At the time of denial, the board consisted of three members: [redacted] [redacted] and [redacted] [redacted] also served as the president of the Applicant and no other officers were identified. The board of directors was determined to lack independence due to its small size, and because it seemed to make changes to membership at will and did not have members who were representative of the community and the public interest.
- c. The Applicant entered into an arrangement with a for-profit entity, On-Track Motivation Training ("On-Track"), to perform most of its services, including providing all materials, providing and training personnel, hosting software, maintaining records, and advising and assisting in all aspects of the Internet program. For these services, the Applicant agreed to pay On-Track a variety of fees that could add up to 75 percent of the net revenues that the Applicant earned from credit counseling services. The Applicant also sublet office space from Emico, Inc., the parent company of On-Track, and shared employees.
2. The Applicant requested approval in the 88 judicial districts where the United States Trustees have jurisdiction, although the Applicant employed only four counselors, and a substantial portion of its services would be provided through an Internet program. The Applicant failed to demonstrate that this self-help approach to credit counseling was of sufficient quality; that it provided adequate counseling to the consumer; and that adequate safeguards were incorporated into the program to verify the identity of the individual or married couple receiving the instruction, to verify the information entered into the program, or to ensure that the individual or married couple completed the program as designed.
3. The Applicant stated that it was reviewing state law compliance, but did not believe that it was subject to licensing requirements because it did not offer debt management plans. The Applicant's assumption was incorrect. For example, in Oregon, agencies who provide any advice, assistance, instruction, or instructional materials to a consumer with regard to improving, saving, or preserving a consumer's credit record, history, or rating must be registered with the Oregon Department of Consumer and Business Services. Ore. Rev. Stat. §§ 646.382(2)(a)(C) and 646.386(1). The Applicant did not appear to be in compliance with this provision in the State of Oregon or other states where similar requirements may apply.

III. Standard of Review

In conducting this review, the Director must consider two factors:

1. Does the denial decision constitute an appropriate exercise of discretion?
2. Is the denial decision supported by the record?

IV. Analysis

A. Duties of the United States Trustee

Under 11 U.S.C. § 111, United States Trustees are required to approve nonprofit budget and credit counseling agencies for inclusion on a list maintained and made publicly available by the clerks of the United States Bankruptcy Courts. Agencies on approved lists are authorized to issue credit counseling certificates that individual debtors are required under 11 U.S.C. § 521(b) to file with their petitions.

Section 111(b) of the Bankruptcy Code provides in relevant part:

(b) The United States trustee . . . shall only approve a nonprofit budget and credit counseling agency . . . as follows:

(1) The United States trustee . . . shall have thoroughly reviewed the qualifications of the nonprofit budget and credit counseling agency . . . under the standards set forth in this section, and the services . . . that will be offered by such agency . . ., and may require such agency . . . that has sought approval to provide information with respect to such review.

(2) The United States trustee . . . shall have determined that such agency . . . fully satisfies the applicable standards set forth in this section.

11 U.S.C. § 111(b).

Section 111(c) of the Bankruptcy Code sets forth the standards for approval of nonprofit budget and credit counseling agencies:

(c)(1) The United States trustee . . . shall only approve a nonprofit budget and credit counseling agency that demonstrates that it will provide qualified counselors, maintain adequate provision for safekeeping and payment of client funds, provide adequate counseling with respect to client credit problems, and deal responsibly and effectively with other matters relating to the quality, effectiveness, and financial security of the services it provides.

(2) To be approved by the United States trustee . . ., a nonprofit budget and credit counseling agency shall, at a minimum--

- (A) have a board of directors the majority of which--
 - (i) are not employed by such agency; and
 - (ii) will not directly or indirectly benefit financially from the outcome of the counseling services provided by such agency;
- (B) if a fee is charged for counseling services, charge a reasonable fee, and provide services without regard to ability to pay the fee;
- (C) provide for safekeeping and payment of client funds, including an annual audit of the trust accounts and appropriate employee bonding;
- (D) provide full disclosures to a client, including funding sources, counselor qualifications, possible impact on credit reports, and any costs of such program that will be paid by such client and how such costs will be paid;
- (E) provide adequate counseling with respect to a client's credit problems that includes an analysis of such client's current financial condition, factors that caused such financial condition, and how such client can develop a plan to respond to the problems without incurring negative amortization of debt;
- (F) provide trained counselors who receive no commissions or bonuses based on the outcome of the counseling services provided by such agency, and who have adequate experience, and have been adequately trained to provide counseling services to individuals in financial difficulty, including the matters described in subparagraph (E);
- (G) demonstrate adequate experience and background in providing credit counseling; and
- (H) have adequate financial resources to provide continuing support services for budgeting plans over the life of any repayment plan.

11 U.S.C. § 111(c).

B. Basis for Denial

1. Nonprofit Status of the Applicant

The Applicant operates in office space sublet from Emico, Inc., a for-profit corporation. Emico, Inc., is the parent corporation of On-Track, which is itself a for-profit entity. The denial letter accurately described the intertwined relationship of the Applicant and On-Track. The Applicant agreed to pay to On-Track a variety of fees that could add up to 75 percent of the net revenues that the Applicant received from credit counseling services as consideration for On-Track's agreement to provide the Applicant with a broad variety of services. These services included providing all materials, providing and training personnel, hosting software, maintaining records, and advising and assisting in all aspects of the Internet-based program the Applicant proposed to implement. Furthermore, the Applicant proposed to share an employee, [redacted] who is a key employee of On-Track.

Based upon the foregoing and the administrative record, it was properly concluded that the Applicant proposed to contract away basic services to a for-profit entity, On-Track. From the record, I must conclude that the Applicant would serve as little more than a conduit to permit On-Track to provide pre-bankruptcy counseling services that On-Track, as a for-profit entity, may not provide under the Bankruptcy Code.¹ It is clear under applicable provisions of section 111 that counseling services are to be provided by a nonprofit entity, not by a for-profit entity under contract with a nonprofit entity that serves as a front end for the for-profit entity.

2. Ability of Applicant to Provide Adequate Counseling Services

The decision not to approve the Applicant was also based upon concerns about the adequacy of the Applicant's staffing, the efficacy of the counseling program, and the weakness of the Applicant's mechanisms to verify the identity of those undergoing counseling.

While the Applicant is organized largely to deliver Internet-based counseling, the program proposed by the Applicant clearly contemplated telephone contact between the Applicant and clients. The Applicant sought approval to provide counseling in 88 judicial districts, yet it employed only four counselors, at least one of whom it shared with On-Track. When asked how four counselors could handle the volume of telephone calls that would be generated from approval of the Applicant for nationwide service, the Applicant replied that On-Track, its parent Emico, and another Emico entity, Acu-Shield Financial, would provide access to their existing staff to handle an increase in calling volume. While this explanation provided some evidence that call volume could be handled, it also served to highlight the extent

¹ The denial decision was also based on the fact that the Applicant had not received a 501(c)(3) designation from the Internal Revenue Service and that the Applicant's board of directors was not sufficiently independent. Because the Applicant's relationship with On-Track is sufficient standing alone to warrant the conclusion that the Applicant is not truly a nonprofit entity of the type envisioned by the Bankruptcy Code, I need not reach these issues.

to which the Applicant would be dependent upon for-profit entities to handle its day-to-day activities. As discussed above, such an arrangement is not acceptable.

3. State Law Compliance

The final ground cited for the denial of approval was the Applicant's failure to comply with applicable state laws governing credit counseling agencies. The Applicant's position was that because it did not propose to offer or to administer debt management plans, it was not subject to those state regulations. The denial letter correctly states that certain jurisdictions, such as Oregon, require licensing or registration for any agency offering credit assistance, without regard to whether debt management plans are offered. The Applicant offered no substantive argument in response. State law compliance is the responsibility of the Applicant, and the Applicant failed to demonstrate sufficient sensitivity to that responsibility. However, if the application had not suffered from other substantial deficiencies, it may have been subject to approval in those jurisdictions where the Applicant could demonstrate compliance with state law.

V. Conclusion

Based upon my review of the record, I affirm the decision to deny the application of Consumer Legal Referrals, Inc., for approval as a nonprofit budget and crediting counseling agency.

The foregoing conclusions and decisions constitute final agency action in this matter.

Dated: August 10, 2006



Clifford J. White III
Acting Director
Executive Office for United States Trustees