

MEMORANDUM

TO: File
FROM: Lawyers Alliance for New York
RE: Credit Counseling Services
DATE: October 24, 2007

This Memorandum addresses various issues of interest to nonprofit organizations proposing to offer consumer credit counseling services (“CC Services”), including certification or training requirements for organizations/counselors providing CC Services. As described in this Memorandum, while certification and adherence to prescribed training standards for individual credit counselors is certainly preferable and highly recommended (and the extent to which counselors are trained is a consideration for the Internal Revenue Service (“IRS”) in examining a nonprofit organization providing CC Services), there is no overarching clearly-defined requirement for certification or training.¹ As a result, organizations offering CC Services are largely left to define for themselves what standards to adhere to.

The CC Services industry has come under increased scrutiny from the IRS over the past few years, and Schedule A to the IRS Form 990 (the annual information return required to be filed by most nonprofit organizations) now requires the organization specifically to indicate whether or not it provides credit counseling, debt management or credit repair services.² Organizations that offer these services should be aware of the standards that are considered “best practice” for the industry as a whole, even if such services comprise only a small part of their overall activity and regardless of whether a fee is charged for such services. Organizations should then work to adhere to said standards, including in the arena of counselor training, in order to provide effective services in a manner that would satisfy both the IRS and other public constituencies in the event any questions are raised.

I. IRS Considerations

While the IRS generally imposes no specific legal requirements in examining or assessing the 501(c)(3) status of a nonprofit organization offering CC Services, e.g., licensing or certification of counselors, a significant factor required to be present to support such tax-exempt status is that counselors receive satisfactory education and training.³ The IRS recently conducted a Credit Counseling Compliance Project in which they focused on abuse by tax-

¹ As described below, there are certain circumstances in which an organization providing credit counseling services must be licensed or included on an approved list of providers, however, even in these instances, certification and training requirements of counselors are not clearly defined.

² 2006 Form 990, Schedule A, Part III, Question 3d.

³ 26 U.S.C. § 501(q) sets forth special rules with respect to the tax exempt status of organizations for which “the provision of credit counseling services is a substantial purpose.” August 17, 2006 and 2007 are the relevant dates.

exempt organizations offering CC Services and established an ongoing internal review/audit program to ensure improved compliance with the tax laws.⁴

As part of the Credit Counseling Compliance Project, the IRS published a Credit Counseling Core Analysis Tool designed to assist IRS agents in assessing the exempt nature of an organization's credit counseling program.⁵ In addition to looking at particular characteristics of the counseling sessions and the organization as a whole, the Core Analysis Tool considers whether the counselors:

- receive comprehensive training in counseling skills, personal finance, budgeting and credit and debt management in live or interactive training sessions and through detailed written manuals;
- receive training on how to develop options and recommendations that address the particular circumstances of each client; and
- are trained in identifying underlying personal problems (such as illness or loss of employment) that might contribute to financial problems and in making appropriate referrals.

The IRS further explains how the above factors are to be assessed in the "Instructions for Using the Core Analysis Tool."⁶ In general, for counselor education and training, it is stated that:

Information on this factor is likely to be found in qualifications used in job postings, training materials and manuals, curricula for training courses, credentials of instructors or authors of materials, tests or exams counselors must pass before working with clients, information about how counselors are supervised when they are new and as they gain experience, criteria for employee evaluations, individual employee evaluations, and criteria for pay, bonuses and raises. Information on the amount of time spent on training and on employee turnover might also be useful.⁷

⁴ Executive Summary, Credit Counseling Compliance Project, May 15, 2006, available at www.irs.gov/pub/irs-tege/cc_executive_summary.pdf. In general, the IRS's primary concern and reason for launching the Credit Counseling Compliance Project was that organizations offering CC Services were not operating in furtherance of educational purposes consistent with the initial recognition by the IRS of such organizations' tax-exempt status. The IRS noted that an increasing number of organizations offering CC Services were acting merely as sellers of debt management plans (organizations that "appear motivated primarily by profit, and offer little or no counseling or education") and in many cases "also appear[ed] to serve the private interests of related for-profit businesses, officers and directors." Id. Therefore, while an organization is not prohibited from directing clients to debt management plans when such a plan would be the most advantageous option for the client, such plans should be only one of a variety of options that are considered by a credit counselor and discussed with the client. However, see Section III of this memorandum for further considerations for an organization administering a debt management plan.

⁵ The Credit Counseling Core Analysis Tool can be found at: http://www.irs.gov/pub/irs-tege/cc_core_analysis_tool.pdf.

⁶ The Instructions for Using the Core Analysis Tool can be found at: http://www.irs.gov/pub/irs-tege/cc_core_analysis_tool_instructions.pdf.

⁷ Id., at 5.

The Core Analysis Tool Instructions document directs IRS agents to obtain relevant information (video recordings of the organization’s in-person training program, copies of written materials used or a detailed description of access to training given by another entity) or to conduct interviews with current or past counselors in order to assess the training given to counselors in substantive issues of personal finance, budgeting, and credit and debt management, as well as how counselors are trained to develop options and recommendations that address the particular circumstances of each client.

II. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the “Act”) prevents individual debtors from filing a petition under the Bankruptcy Code unless the debtor first receives credit counseling and a related budget analysis. The Act requires individual debtors to consult with approved agencies to receive a briefing on the opportunities for credit counseling and a budget analysis within 180 days before filing for bankruptcy relief.⁸ The Act also requires that, after initiating their filing with the bankruptcy court and before receiving a discharge of their debts, debtors participate in a personal financial management instructional course with approved providers to receive information on how to establish and maintain a budget, how to manage their money and how to use credit wisely.

Like other entities seeking to offer such services to individuals, nonprofit organizations need to file the appropriate form⁹ and fulfill the relevant requirements¹⁰ in order to be included on the list of approved nonprofit budget and credit counseling agencies under the Act. These standards include requirements that organizations 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

⁸ 11 U.S.C. § 109(h)(1).

⁹ The application form that credit counseling agencies should use to apply for approval in accordance with the Act is EOUST-CC1, “Application for Approval as a Nonprofit Budget and Credit Counseling Agency.” The application form that providers of a personal financial management instructional course should use to apply for approval in accordance with the Act is EOUST-DE1, “Application for Approval of Provider of a Personal Financial Management Instructional Course.” Each of these forms (as well as detailed instructions to complete the latter form) can be found at www.usdoj.gov/ust/eo/bapcpa/ccde/credit_counseling.htm.

¹⁰ 28 C.F.R. 58.15(f). Requirements include that the nonprofit organization: must have an independent board of directors with certain characteristics; may not have any connections with the United States Trustee Program or certain other federal positions; and should avoid any conduct or transactions that generate or create the appearance of generating a private benefit for anyone connected to the organization. At a minimum, an agency must have experience in providing credit counseling for the previous two years or have an office supervisor with experience of no less than two years in the five years preceding the application. Regulations also include limitations on the fees that can be charged to debtors for the service. For more specific information on the qualifications required for approval, see 28 C.F.R. 58.15. An application must be made annually for continued listing as an approved agency. 28 C.F.R. 59.16(f). Additional information regarding this program may be found in “Frequently Asked Questions regarding Credit Counseling,” which is published by the U.S. Trustee Program and is available at www.usdoj.gov/ust/eo/bapcpa/ccde/cc_faqs.htm.

financial difficulty.... A counselor shall be deemed to have adequate training and experience to provide credit counseling and budget analysis if the counselor is accredited or certified by a recognized independent organization, or has successfully completed a course of study acceptable to the United States Trustee and has worked a minimum of six months in a related area, including personal finance, budgeting, and debt management.¹¹

It is specifically stated that the United States Trustee Program does not endorse any specific course or certification program.¹²

III. Licensing Requirements by the Superintendent of Banking

Under Section 579 of Article 12-C of the New York Banking Law, a 501(c)(3) organization cannot engage in the “business of budget planning” unless it is licensed by the New York Superintendent of Banking.¹³ “Budget planning” is defined under Section 455 of Article 28-B of the New York General Business Law as:

making a contract between a person or entity engaged in budget planning with a particular debtor whereby the debtor agrees to pay a sum or sums of money periodically and the person or entity engaged in the budget planning distributes, or supervises, coordinates or controls the distribution of, the same among certain specified creditors in accordance with a plan agreed upon and the debtor further agrees to pay to such person or entity any valuable consideration for such services or for any other services rendered in connection therewith.¹⁴

¹¹ 28 C.F.R. 58.15(f)(1), (2).

¹² 28 C.F.R. 58.15(f)(2).

¹³ NY Banking Law, Article 12-C, § 579. Section 579 reads in its entirety:

Only a type B not-for-profit corporation as defined in section two hundred one of the not-for-profit corporation law of this state, or an entity incorporated in another state and having a similar not-for-profit status, shall engage in the business of budget planning as defined in subdivision one of section four hundred fifty-five of the general business law of this state except as authorized by this article and without first obtaining a license from the superintendent.

Id.

¹⁴ Note that there is no requirement for licensing under the Banking Law unless the not-for-profit is, essentially, administering a debt management plan for clients and charging a fee for it. The organization is not required to be licensed unless it is holding a debtor’s money in trust to make payments to creditors and accepts valuable compensation from the debtor for doing so. Therefore, there is no licensing required if an organization is providing only educational services and charging a fee for such educational services, or if the organization is accepting payments to pay out to creditors as part of a debt management plan but is accepting no fee for such service. See, e.g., State of New York Banking Department Staff Interpretation re: NYSBL 579 and General Business Law 455, dated August 1, 2006, which can be found at www.banking.state.ny.us/legal/lo060801.htm (stating that an organization that collects fees for credit counseling and financial management education does not meet the definition of budget planning “because it does not enter into budget planning contracts with [debtors] and in connection therewith distribute, supervise, coordinate or control payments made by the debtors to specified creditors.”), and State of New York Banking Department Staff Interpretation re: Licensing Requirements for Out-Of-State Budget

There is no certification or training requirements for counselors as a condition for an organization to be licensed by the Superintendent of Banking. Rather, a license can be granted upon a finding that the “financial responsibility, experience, character and general fitness of the applicant, and of officers and directors thereof are such as to command the confidence of the community and to warrant belief that the business will be operated honestly, fairly and efficiently.”¹⁵

IV. Trade Organizations and General Recommendations

Certain membership organizations of credit counseling agencies have set standards applicable to their members. Two of the larger organizations are the National Foundation for Credit Counseling (the “NFCC”)¹⁶ and the Association of Independent Consumer Credit Counseling Agencies (the “AICCCA”),¹⁷ each of which is a national association of consumer credit counseling services. An agency must be “accredited” within the guidelines of the particular organization in order to become a member, and membership requires such agency to adhere to specified industry standards and be subject to the organization’s oversight.¹⁸ In return, the member agency may use the “seal of approval” from the organization and can benefit from the implicit assumption of trustworthiness that is derived from having obtained membership.

These membership organizations require that counselors at member agencies be trained by certification services as specified by the particular organization. For instance, all NFCC and AICCCA member agency counselors must complete an approved training program.¹⁹ However, there is no legal requirement that a credit counseling agency belong to a membership organization. As a result, these certification requirements and industry standards are not legally required or enforceable.

Planners, dated January 27, 2000, which can be found at www.banking.state.ny.us/legal/lo000127.htm (noting, in response to an inquiry about whether services provided without charge by an out-of-state organization to New York State debtors would require licensing, that “the definition of ‘budget planning’ says ‘with consideration.’”).

¹⁵ NY Banking Law, Article 12-C, § 581.

¹⁶ Additional information regarding NFCC may be found at www.nfcc.org.

¹⁷ Additional information regarding AICCCA may be found at www.aiccca.org. The Association for Financial Counseling and Planning Education (the “AFCPE”) is a similar membership organization; however, AFCPE membership consists primarily of individuals rather than agencies, and the AFCPE promotes itself as an organization providing networking opportunities while “supporting, promoting and advancing the field of financial counseling and planning education,” rather than one for policing industry standards. Additional information regarding AFCPE may be found at www.afcpe.org.

¹⁸ Find the NFCC Member Quality Standards at http://www.nfcc.org/mo/membership/Member_Quality_Standards_as_of_August_19_2005.pdf. The AICCCA has both a Code of Practice, located at <http://www.aiccca.org/images/AICCCA%20Code%20of%20Practice.pdf>, and a report on Standards and Best Practices located at <http://www.aiccca.org/images/Standards%20of%20Compliance.pdf>.

¹⁹ NFCC Member Quality Standard No. 04.01; AICCCA Standards of Best Practice, III(2). NFCC provides a Consumer Credit Counselor Certification Program that requires counselors to pass a series of examinations based on twelve modules in the “Counselor Certification Manual” and is administered through an online program at www.testutor.com. The AICCCA refers members to the certification program provided by the AFCPE (which is a separate arm from the membership arm of the AFCPE referred to above). The AFCPE offers certification for both an Accredited Financial Counselor and a Certified Housing Counselor. See http://afcpe.org/pages/page.cfm?page_id=20&top_id=20 for more information.

There is a variety of literature available from government and consumer organizations regarding how best to find a trustworthy credit counselor. It is often recommended that one review the professional memberships of the agency and ask questions regarding certifications and training requirements of the agency's credit counselors.²⁰ However, this may be a larger consideration for an agency offering credit counseling as its primary purpose, rather than for an organization offering it as a service for clients participating in other programs.

²⁰ See, e.g., "Shopping Tips for Selecting a Debt Counselor" published by The Foundation for Credit Education, at http://www.foundationforcrediteducation.org/chooscslr/shop_tips.asp. The Foundation for Credit Education is an organization "dedicated to improving the financial well-being of consumers through education and counseling in the areas of money management and credit." To this end, The Foundation for Credit Education offers educational services to accredited credit counseling agencies, social service agencies, community organizations, employers, individuals and others. The Foundation for Credit Education also offers The Consumer Information Bank, which is a free resource designed to promote general financial literacy education for the general public through the use of helpful articles, a newsletter, credit education and money management guidelines, interactive calculators, worksheets and a variety of money-management and money-saving tips. See <http://www.foundationforcrediteducation.org>.