moneyadvicescotland
Scotland's Money Charity

HM Treasury

Breathing space: call for evidence

About Money Advice Scotland

1. Money Advice Scotland is Scotland's Money Charity. Our mission is to be the driving force towards financial wellbeing for the people of Scotland.

Summary

2. The new breathing space and statutory debt management plan will of course not apply to Scotland. However, as the only country in the UK which currently operates a statutory debt management plan in the form of a debt payment programme (DPP) under the Debt Arrangement Scheme (DAS), we hope it will be helpful to share our own views and experience.

3. While it is often said that Scotland leads the way, the number of people opting for a DPP under DAS has declined by 46% between 2014/15 and 2016/17. At the same time, other insolvency options (often less suitable to clients) are on the increase. Many people are also put off by the inflexibility once a DPP is in place.

4. Last year, the Accountant in Bankruptcy (AiB) consulted on proposals to improve and enhance DAS. This is set to be published within the coming weeks and may prove indicative to the development of HM Treasury's own proposals.

5. As we will set out within this response, in many ways DAS will be an example to emulate across the UK. Nonetheless, no system is perfect and flagging up some of the issues wherein DAS does not work well may prove useful to the development of a breathing space and statutory debt management plan for the rest of the UK.

Breathing space duration

6. Under DAS, a person in debt can access a six-week period of debt relief during which creditors cannot take any further action. This provides valuable breathing space, but

our members are of the view that six weeks is not long enough. We have previously made calls for an extension to this period. Six weeks is not a long time to attempt to resolve crises that are often years in the making.

7. Demand for advice is high and the application process can be inflexible. From an operational perspective, advisers also noted that moratoriums are not processed quickly enough. A number of advisers also noted that it should be possible to freeze interest, fees and charges from the point at which the breathing space is granted.

All debts within a statutory debt management plan

8. Our members have consistently reported concerns that the requirement to include all debts is a barrier for many clients who may otherwise enter a statutory debt management plan.

9. The Accountant in Bankruptcy recently consulted on whether to remove the all debts requirement, and indicated a willingness to allow rent or mortgage arrears to be excluded from a statutory debt management plan. Our members are of the view, however, that the flexibility to exclude rent and mortgage arrears does not go far enough and there is consensus that energy debts should also be excluded from a statutory debt management plan. An adviser noted that clients with energy debts are often making affordable repayments on meters and prefer to continue to do so. If priority debts are under control with working arrangements already in place, it is considered counter-productive to bring these debts to a head.

10. A number of advisers cited examples of clients who had opted for a DMP rather than a statutory debt management plan due to this inflexibility, or had delayed dealing with debts altogether. This option can lack some of the considerable benefits of DAS – most notably the freezing of interest and charges as well as the risk that creditors can unilaterally terminate a voluntary DMP at any time.

11. We are also aware of concerns around the implications for including guarantor loans within a statutory debt management plan given that a creditor can seek the balance from the guarantor at any time and this can deter the client from pursuing this option.

12. In our experience, the requirement to include all debts brings a level of inflexibility to a product that is designed to give people more flexibility and breathing space. To ensure that the proposals are flexible enough to ensure client take-up, we would advise against stipulating that all debts should be mandatorily included within the statutory debt management plan. The requirement to include all debts within a DPP (alongside other changes to regulations) has coincided with a 46% drop in applications to the Debt Arrangement Scheme.

Calculating a contribution to creditors

13. The methodology for calculating disposable income and the resulting contribution is at the very centre of the advice process. We were somewhat surprised, then, that this isn't mentioned within the Treasury consultation.

14. Before a person can enter into a DPP, they must first complete a financial statement – effectively an income and expenditure form. Currently, 100% of a household's surplus income is taken as a contribution to repay debts, with a contingency buffer permitted but limited to 10% of disposable income, capped at £20 per month.

15. The average duration of a DPP under DAS is 6-7 years. This is a long period to be paying out 100% of disposable income and leaves people going through the process susceptible to income shocks and the cost of unexpected expenditure.

16. During the recent review of DAS, we supported the option to introduce flexibility by removing the requirement to use the full surplus income as calculated by a financial statement to determine the level of contribution. If a person is repaying all debts with no element of write-off and for a longer period, then leeway should be allowed to improve the prospects of sustainability.

17. It cannot be restated often enough that a financial statement does more than set a contribution to creditors – it effectively sets out the standard of living for a debtor within the period of that agreement. This is a crucial consideration for every debt solution, but particularly for a statutory debt management plan that will run longer and debts are repaid in full.

Access to credit whilst in a statutory debt management plan

18. A client in a DPP can only access credit in limited circumstances and with the permission of the DAS Administrator. In most circumstances, those in a DPP have to apply to the DAS Administrator before obtaining any further credit, and this is usually only allowed for certain essential purposes.

19. The AiB has proposed to mirror the restrictions in bankruptcy so that a debtor will be required to notify any new potential creditor that they are in a DPP if they apply for credit of more than £2,000, or already have credit of £1,000 or more. We are of the view that the current limits on accessing credit are unduly stringent for what is effectively a voluntary payment programme. It must be emphasised that DAS is a debt management tool as opposed to an insolvency option and there ought to be clearer distinctions to assist people towards making informed choices.

20. As noted previously, DPPs typically run for longer periods than other debt solutions so dips and spikes in income and expenditure are more likely. Credit is often a useful tool to smooth out these fluctuations and shocks. The conditions around access to

credit are not included within consultation, but remains a pertinent point for HMT to consider.

Outcomes and benefits

21. A statutory debt management plan offers legal protection that is not available within informal debt management plans. The initial breathing space period also provides a spur to act, although as noted previously, this should be extended.

22. The freeze on interest and charges is a notable incentive, albeit our members are also of the view that this should take effect earlier in the process at the point when breathing space is granted. Under DAS, if a DPP fails, interest and charges are applied retrospectively. The failure of a DPP may not reflect fault on the individual, but instead may be explained by an unexpected change in circumstances. In this scenario, the application of backdated interest and charges is a disproportionate penalty and we would advise against this under the HM Treasury scheme.

23. We are unconvinced of whether a statutory debt management scheme necessarily drives people to seek advice at an earlier stage, however. By its very nature, people seek debt advice at the point of crisis.

24. A statutory debt management plan has brought noteworthy benefits for many people in debt in Scotland that HMT would do well to replicate. In our experience, there continues to be a stigma attached to bankruptcy and protected trust deed which is not associated with DAS, given that people are not known as bankrupts and they are not prohibited from actively engaging in certain aspects of society. People opting for a DPP are not faced with the same restrictions (for example, becoming an MP/MSP, or taking part in a School Board), nor does their estate vest with a Trustee.

25. Creditors also benefit from a statutory debt management plan. DAS is a less costly option for creditors who will in most cases get a substantial return – significantly more than through bankruptcy or Protected Trust Deed. In 2015-16, £37.8m was repaid through DAS, compared to £30.7m paid to creditors through protected trust deed.

26. If we were to impart one piece of advice as HMT sets out on its own development of a statutory debt management plan, it would be to ensure that the scheme is flexible enough to ensure that repayments are sustainable, leading to the right outcome for people in debt and creditors alike.

27. The success of the breathing space and statutory debt repayment plan can be measured by the sustainability of the agreements. We welcome the opportunity to respond to this consultation, but hope that HMT will also engage with people in debt who have been in debt management plans, whether informal or statutory. The experience of the person in debt is often absent from the policymaking process, but few if any people are better placed to inform and influence.

16 January 2017