MANAGING BORROWING AND DEALING WITH DEBT: CONSUMER CREDIT AND PERSONAL INSOLVENCY REVIEW

Call for Evidence Response Form.

Responses to the call for evidence should be received by Friday 10 December 2010.

Due to the tight timetable involved, **responses received after this date may not be considered as part of the review process.**

Completed copies of the response form should be returned:

Via email to: peter.lovitt@bis.gsi.gov.uk

Via post to:

Peter Lovitt
Department for Business, Innovation and Skills
Consumer and Competition Policy
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London SW1H 0ET

It may be possible to make other versions of this document available on request in Braille, other languages, large fonts and other formats – please contact Peter Lovitt at the above address.

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Please tick the box from the following list of options that best describes you:

- ☐ Business
- ☐ Representative Organisation
- ☐ Trade Union
- ☐ Interest Group
- ☐ Local Government
- ☐ Central Government
- ☒ Other (e.g. consultant or private individual)
  Credit Action is a national money education charity which aims to help people manage their money and stay in control of their finances.

Q1. Should the Government extend regulations on advertising for credit products beyond the cost of credit?

Comment

Evidence

Q2. Should consumer credit advertising rules be aligned with those which the FSA applies to secured credit?

Comment

Evidence

Q3. What would be the impact of a 7-day cooling off period for store cards on (a) consumer behaviour and (b) lenders?

Comment
a) consumer behaviour We believe that a 7-day cooling off period for store cards would have a beneficial impact on consumer behaviour by reducing impulse buying and similar tendencies which, if they become regular patterns of behaviour over the longer term, can have a destructive impact on an individual's personal finances by causing them to live well beyond their means (a significant problem in the UK, as outlined below). We would also suggest that there are other potential measures that could be taken to ensure that store cards are not used in an irresponsible manner, such as preventing retail staff (who may lack relevant expertise) from offering them at point-of-sale and requiring customers to proactively visit a customer services desk in order to take one out - this, in our opinion, would help promote more conscious and reflective decision-making on the part of consumers with regard to store cards. Equally, ensuring that store cards are labelled with a clear APR is of continued importance in this respect. We would also agree with the points made in Paragraph 22 of the consultation suggesting that one of the main reasons that consumers take out a store card is for the retail incentive that is offered on the day. However, given this, we question whether a 7-day cooling off period might have the unintended effect of encouraging stores to alter the incentive structure that they put in place around the use of store cards, or perhaps even stimulating store card providers to leave the market and return with a different credit product. Were new incentive structures or products to emerge, we would like to see Government ensure that new incidents of consumer detriment do not result, and that the impulsive behaviour that a cooling off period is intended to prevent is not simply promoted through different mechanisms.

Evidence
Living beyond one's means is a major source of financial distress in the UK. This was the cause of 26% of male bankruptcies and 34% of female bankruptcies in 2007/08 according to figures compiled by the Insolvency Service in its 2009 report "Profiles of bankrupts: 2005/06 to 2008/09" (p. 22). Meanwhile, a recent survey by Bright Grey has suggested that 14% of UK adults (equating to 7 million people across the whole population) are currently living beyond their means in order to fund their lifestyle.

While we recognise that, in isolation, placing conditions on the use of store cards will only have a limited impact on problems of this magnitude, any measures which promote more considered consumer behaviour are, in our view, welcome.

Indeed, we submitted evidence to the Competiton Commisson's inquiry into store cards, and argued that the key issue with respect to this was ensuring that customers had sufficient levels of financial capability to be able to use store cards effectively. They can in fact be useful means of payment (we suggested that if used skillfully store cards could give an interest free period of up to 60 days) but the essential factor is that consumers are sufficiently empowered to utilise cards in a measured rather than a reckless manner. For us, this is an issue which goes beyond pure sales restrictions, and we make further comment regarding store cards in our response to Question 9.

Comment
(b) lenders

Evidence

Q4. We would welcome your in views on the following OFT recommendations from the review of high cost credit:

a. *that the Government works with lenders to provide information on high-cost credit loans to consumers through price comparison websites.*

Comment
We would support these proposals, and believe that any measure that allows consumers to better drive competition within the high-cost credit market can only be beneficial. **However, we would suggest that in addition to high-cost lenders, any price comparison website should also display the rates charged by banks on unarranged overdrafts. The OFT themselves have suggested (as is outlined in the box below) that in certain circumstances an unarranged overdraft may be cheaper than certain types of high-cost loan, but that consumers still choose the more expensive option due primarily to issues of transparency and predictability.** **We believe that it is highly desirable for borrowers to be able to easily compare the costs of all the sources of credit open to them so that they are able to make fully informed decisions about which lenders to use, and that this should include unarranged overdrafts.** **We make further comment on this issue in our response to Question 8.**

Evidence
We believe it is highly significant that, according to the OFT's own analysis, consumers may in some circumstances be turning down unarranged overdrafts in favour of some forms of high-cost credit even in instances where the former are cheaper, and that this is primarily because of issues of transparency. **In its June 2010 "Review of high cost credit: Final Report" the OFT drew a number of strong links between high-cost lenders and overdraft charges. The competition analysis undertaken in Annex E of the paper is especially informative in this regard, and we would draw particular attention to Paragraphs 3.11 to 3.19.** **In this section it is noted that while a payday loan may be cheaper than an unarranged overdraft for those who need to make multiple withdrawals on different days of the month, "For others who do not**

need to make multiple withdrawals, the unarranged overdraft may be cheaper ... However, what is certain is that the costs of the payday loan are much more transparent than the costs incurred by the unarranged overdraft and for many customers this certainity about charges is valuable and may be sufficient to persuade them to borrow from the payday lender." (Annex E, p. 19)

Therefore we strongly favour measures to ensure that the pricing structures of unarranged overdrafts are explained in a transparent way that allows customers to make informed decisions when they borrow.

b. *that the Government explores whether there is scope under the European Consumer Credit Directive for a requirement that high-cost credit suppliers must include 'wealth warning' statements on advertisements for high-cost credit*

Comment

Evidence

c. *that the Government works with credit reference agencies to explore ways in which payday lenders and rent-to-buy suppliers could provide suitable information to credit reference agencies about the payment performance of their customers, in turn allowing those with good payment records to use mainstream lenders more easily in the future*

Comment

Evidence

d. *that the OFT collects essential information on the high-cost Credit sector, such as the volume, value and pricing of credit, levels of repeat business and defaults among customers as needed. This will help OFT understand the effect of its recommendations and provide better evidence for future policy making*

Comment

Evidence

e. *that the relevant trade associations for home credit suppliers, payday lenders and pawnbrokers establish a code or codes of practice covering best practice policy including on: complaints and advice to customers, policies on rolling over of loans, limits for amounts to lend to consumers, avoiding misleading consumers through advertisements and ensuring that* *consumers are aware of the ultimate owners of brand names*

Comment
We believe that the establishment of a clear and rigorous code of practice for the home credit, payday lender and pawnbroker industries would be a positive development. While there may be a place in the market for these high-cost providers, ensuring that consumers are adequately protected from improper and abusive business practices is in our opinion utterly essential. The creation of an industry code would undoubtedly help facilitate this, and provide a clear standard enabling consumers to identify instances of detrimental practise. In order to be effective such a code would need to be vigorously policed, and firm sanctions taken against those organisations that continually break it. **In particular, we would like to see provisions which mandate high-cost lenders to provide borrowers with greater support in managing their finances responsibly. In its August 2010 report "Keeping the plates spinning: Perceptions of payday loans in Great Britain", Consumer Focus recommended that when individuals take out or roll-over a specified number of loans in the space of a year, this should be seen as a sign that they are in financial difficulty and they should subsequently be directed towards independent sources of financial advice and support (p. 7). We whole-heartedly endorse this proposal, and would like to see this sort of requirement included in any code of conduct governing the behaviour of high-cost lenders. We believe that it would help address some of the weaknesses in the market which were recently identified by the OFT, as we outline in the box below.** **Furthermore, we feel that some form of third-party quality check on the standards of correspondence that high-cost lenders send to their clients may be beneficial, and that such a system could potentially be built into any industry code. We already operate a kite-marking initiative with a number of major creditors, whereby we examine the content of their correspondence and approve it with an official mark if we feel it meets appropriate standards (eg. that the letter does not use intimidating language that is likely to frighten the debtor). We believe this sort of model could be easily applied to the high-cost lending industry as well.**

Evidence

With regard to the potential value of directing users of high-cost credit towards sources of independent support, we would point to comments made by the OFT themselves in their "Review of High Cost Credit: Final Report", in which a number of "deep seated issues" in the high-cost credit markets which inhibit effective competition are identified. Significant amongst these is the "relatively low ability and effectiveness of consumers in driving competition between suppliers, given their low levels of financial capability" (p. 6). The OFT go on to suggest that more fundamental changes in approach are necessary to deal fully with this problem, including a step change in building financial capability within this group, potentially through a large scale adult education initiative (p. 8).

We would whole-heartedly endorse such sentiments, but also believe that high-cost lenders themselves could reasonably be expected to contribute to resolving these problems. Requiring such lenders to monitor the levels of borrowing by a particular individual and directing them towards appropriate guidance and advice, as suggested, would in our opinion be an intelligent way of intervening to help build the financial capability of those who engage with the high-cost market on a regular basis.

However, we would also stress that such measures will only provide part of the solution to the problem, and believe that there is an undoubted need for complementary action on a much wider level, as the OFT suggests. Making financial education a compulsory part of the school curriculum could be one way of achieving this.

Q5. Is there a need for greater sharing of data between the consumer credit industry and other bodies, including utility companies, local authorities and HMRC?

Comment
We believe that there is a need for greater sharing of data between the consumer credit industry and other bodies, and that improving such arrangements may have significant benefits in terms of financial inclusion objectives. **In particular, we believe that the current credit scoring system is stacked against people who choose not to borrow but who can still be very responsible in terms of their everyday financial management, and**

that greater information sharing between the consumer credit industry and likes of utility companies and local authorities could help address this. We offer an illustrative example of the sorts of problems that might be posed by the current system, and how data sharing might help address this, in the box below.

Evidence

As an illusrative example of flaws in the nature of the current credit scoring process, we would consider the position of social housing tenants who pay rent to a social landlord, bills to utility companies and council tax to their local authority, but who do not hold a mortgage or utilise personal loans. In these circumstances it is possible that such individuals could have exemplary repayment records but, without ever having held any form of commercial credit, minimal credit history. While we recognise that certain pieces of information will be held in a credit score, such as an individual's presence on the electoral role and whether or not they have a bank account, we maintain that this does not necessarily provide a full picture.

Such individuals may, objectively, represent a better credit risk to a mainstream lender than someone with a mediocre credit history, but as their full repayment history would not be captured by the current system, they are more likely to be refused if ever applying to a bank for credit (in the event of an emergency for example). Enabling greater sharing of data between the consumer credit industry and bodies such as local authorities and utility companies would resolve many of these issues.

Q6. It has also been suggested that there needs to be greater transparency around credit scoring and the impact of credit scores on charges. Do you agree?

Comment

We would agree that greater transparency around credit scoring and it's impact would be beneficial. In our experience (an example of which we outline in the box below), this is one area in which there is particular confusion on the part of consumers.

We recognise that credit reference agencies, and indeed educational organisations such as ourselves, have an undoubted role to play in ensuring that consumers are aware of the fact that they actually have a credit rating. However, we feel that consumers often have only a limited understanding of how the system actually works - the fact that a particular customer can be refused credit by one bank but accepted by another due to differences in internal scoring mechanisms can seem very strange for example.

We accept that there may be certain issues of commercial sensitivity when it comes to asking banks to reveal details of their internal processes, and they may have legitmate concerns about being obliged to divulge too much. However, one area in which we feel banks could be more proactive is in giving consumers who have had their applications for credit rejected more information about why this decision was taken, and what action they could take in order to increase the possibility of success in the future.

Evidence

In January 2008 we undertook some media work with BBC Newsbeat in order to raise awareness of ways of managing money effectively in difficult economic conditions. Part of this involved a "Debt Diaries" project, whereby BBC Newsbeat would introduce us to listeners who were encountering financial difficulties so that we could advise them on how to deal with their problems.

One of these cases was paricularly informative from the perspective of credit scoring. The individual in question was a chef whose job required him to regularly move around the country (he had therefore had 16 addresses in 8 years) but who was unable to access mortgage finance in order to buy a house. He did not understand why his repeated attempts to apply for a mortgage had been declined. After contacting the relevant agencies, we were informed that the reason credit had been repeatedly declined was the fact that regular changes of address had shown up on the individual's credit record - this was, however, not something he had ever been made aware of.

It is in situations such as these that we believe greater feedback on the part of banks about the reasoning behind a particular decision would be beneficial, and would enable the customer concerned to take proactive action to improve their credit rating.

Q7. Which of the stakeholder proposals at Annex A do you consider would bring benefits to industry or consumers and what would these be? Please provide evidence in support of your view.

Comment

Evidence

Q8. Do you believe that the current voluntary, market-driven initiatives to address concerns about unarranged overdraft charges are delivering, or will deliver, sufficient improvements for consumers? If not, what would the wider implications of limiting bank charges be? Please provide evidence in support of your views.

Comment

We recognise that there is an inherent difficulty in intervening to limit or abolish unarranged overdraft charges, in that the funds raised from imposing them allow current accounts to be offered for free as outlined in Paragraph 39 of the consultation.

Having chosen to address the issue through a voluntary, market-driven approach, we welcome the focus that has been given to the "clarity and predicatbility" of unarranged overdraft charges by the OFT, as noted in its "Personal Current Accounts in the UK: Progress Report" update in September 2010 (p. 21). We believe that the OFT's overall objective in this respect, to "make charging structures more simple to understand and predict, and to make comparisons of the costs of using unarranged overdrafts between PCA providers and with other forms of short-term credit more effective", is of considerable value in helping consumers make informed decisions about financial products and meet their payment obligations.

However, we would stress that in order to achieve this objective, an effective measure needs to be developed that allows consumers to easily compare the cost of unarranged overdrafts. In order to make a voluntary, market-driven approach work, ultimate power needs to rest with the consumer. We are concerned that there is a significant issue around the visibility of unarranged overdraft charges (some evidence of this is offered by Citizens Advice Scotland and is outlined in the box below), and that consequently consumers may be unaware of what they are actually paying, which inhibits their ability to drive competition within the market.

We understand that the OFT has developed a set of illustrative charging scenarios to support customers in this regard, but also note that there remain issues around how clearly signposted this information is on bank's websites, as outlined in the OFT's September 2010 update (p. 19). Our view is that prominent and standardised labelling of overdrafts, which is clearly visible to consumers up front so that they are fully aware of the costs they are liable for when taking out a current account, is preferable to any other illustrative mechanism and is something which relevant agencies should be actively working towards.

While we recognise that the diversity of charging models used by banks with respect to unarranged overdrafts presents certain difficulties in this regard, we maintain that there is an urgent need for some form of transparent and standardised measure. We would reiterate our view that unless consumers are able to compare products easily and effectively, their ability to drive competition will be impaired. In our opinion this will fundamentally undermine any attempt to address the issue of unarranged overdraft charges through a voluntary, market-driven approach.

Evidence

Evidence from Citizens Advice Scotland suggests that a lack of transparency around overdraft charges can result in significant incidents of consumer detriment. In its report "Fully Charged: Evidence on overdraft charges from Scottish Citizens Advice Bureaux", which was published earlier this year, Citizens Advice Scotland examined the impact of overdraft charges on their clients. It stated that:

"Many of the clients that incur charges do so with little knowledge of the level of charges and the circumstances in which they would be charged. Indeed, many clients were not aware that these charges existed before incurring them. This is partly due to lack of financial capability on the client's behalf, but it is also due to the lack of transparency that banks show over charges leading to customer confusion". (p. 8)

Q9. Should interest rates on credit and store cards be subject to a cap? If so, should this apply to all interest rates or only those which apply to existing borrowing?

Comment

We are sceptical about the application of interest rate caps in all contexts, whether it is specific to credit and store cards or applied more generally to all forms of credit. We fear that caps, even if only applied to one specific section of the credit market, could create flight on the part of certain lenders which would prevent borrowers from meeting their needs and prospectively drive loan shark activity. We remain to be convinced about the effectiveness of capping, although do engage actively in the debate, and would be keen to see any new evidence regarding the extent to which actions such as capping would benefit consumers.

Of far more significance for us with regard to credit and store cards specifically is the need for sufficient levels of financial capability amongst consumers, which we referred to in our response to Question 3. Ensuring that customers are able to utilise credit and store cards to their advantage, rather than spending recklessly on them, is in our opinion the primary concern. This is something that will only be achieved by supporting consumers' ability to access adequate sources of financial education and advice, which is something we consider in greater detail in the box below. For us, capping may well constitute something of a blunt instrument which could inadvertently exclude those who would otherwise use credit and store cards intelligently to meet their needs.

Evidence

In our submission to the Competition Commission's inquiry on store cards we argued that the most effective thing store card providers could do to support consumers was to set certain "trigger points" for the build up of store card debt and interest, meaning that if the balance owed exceeded a certain "trigger" level the provider would be required to contact the debtor and direct them towards free sources of debt advice (it was our understanding at the time that GE was already doing this). Facilitating access to advice in this way is in our opinion a far better way of addressing the issue of reckless spending on store cards, without potentially excluding those who use such cards appropriately. We believe that these principles are equally applicable to credit cards, and that requiring credit card providers to implement such "trigger points" would also be a very positive step forward.

Indeed, in the case of store cards, this approach may have a broader impact on debt problems than a pure cap. In our Competition Commission submission we suggested that the store card market was mature, and the fact that they were used on comparatively few and relatively small purchases meant that they were unlikely to be a major factor in many debt cases. This was in fact echoed in the 2004 OFT report "Store cards: Report of the OFT's inquiry" which instigated the Competition Commission's investigation, which commented that "Debt is a problem that is best looked at in aggregate and store cards make only a small contribution to total consumer debt" (p. 14). As a consequence of this, taking action such as capping which is specific only to the store card market may not have much impact on the broader problem of debt in society. However, utilising the store card market to faciliate access to more general debt advice, which is what our

preferred method aims to do, would give store card debtors the opportunity to tackle any wider debt problems they had as well, effectively dealing with the problem of debt "in aggregate". Extending the necessary mechanisms, such as "trigger points", to credit cards as well would clearly support such efforts even further.

Q10. Are there any alternative measures which would reduce the scope for consumers to be exposed to higher interest rates on credit and store cards?

Comment

Evidence

Q11. How effective have the Competition Commission's remedies been at improving prices for home credit customers? Is further action needed to ensure that consumers of home credit get a fair deal?

Comment

Evidence

Q12. What role should the court play in the debt recovery process? Should it be restricted to genuine points of law and disputes between the parties?

Comment

Evidence

Q13. Are court-based enforcement mechanisms fit for purpose? If not how would you like to see them improved or added to?

Comment

Evidence

Q14. What impact would a £25,000 threshold have on your ability to enforce unpaid debts by means of 1) charging orders and 2) orders for sale? What alternative action might you take?

Comment
1) Charging orders Although we are not directly involved in the enforcement of unpaid debts, Credit Action as an organisation has certain concerns about the use of charging orders which we would like to register. We strongly believe that a clear division needs to be maintained between secured and unsecured credit, and that charging orders undermine this by effectively converting unsecured debt into secured debt. In our opinion, ensuring such a distinction exists is only fair to the consumer. Those who take out unsecured debt make up for their lack of collateral by paying higher interest rates - this is something that is agreed to in the initial terms of the loan. By collateralising an unsecured loan without the debtor's consent through the use of a charging order, the initial terms are undermined. While we recognise that creditors do need some form of last resort in instances where debts are not repaid, we are uncomfortable with the use of charging orders as a mechanism for achieving this. There are concerning signs that charging orders are being seen as an easy solution to ensure that debtors repay (as outlined in the box below). In circumstances where debtors have encountered genuine financial difficulties, or only owe relatively small

amounts, this is something that we feel is highly inappropriate. To suddenly collateralise a loan by way of a charging order is also unfair to those debtors who would have been able to keep up with interest payments on a secured debt.

As outlined in our answer to the next question, we are supportive of the introduction of a threshold on orders of sale. However, with respect to charging orders specifically, we would stress that the issue is not just about setting a particular fixed amount below which orders of sale will not be considered (and applications for charging orders therefore rendered redundant). It also concerns the need to address the unreasonable use of charging orders more generally, regardless of the actual amount of debt that is involved.

Evidence

Citizens Advice examined the issue of charging orders in a June 2009 evidence briefing entitled "Out of order: CAB evidence on the use of charging orders and orders for sale in debt collection". Using figures from 2007 from the Ministry of Justice, Citizens Advice calculated that there had been a 722% increase in the number of charging order applications by unsecured creditors since 2000. They went on to suggest that:

"CAB evidence shows that some creditors are using the threat of court action followed by a charging order to intimidate people in financial difficulties to pay more than they can reasonably afford. The growing ease with which creditors are obtaining charging orders is undermining good debt collection practises. It rewards lenders who will not accept reasonable repayments from people in financial difficulties who are doing everything they can to deal with their debt problems." (p.1)

This sort of analysis concerns us that a particular culture around the use of charging orders may have developed over the past few years which is detrimental to the interests of the debtor. The recent news that the OFT has uncovered problems in the way a number of large banks utilise charging orders suggests that some problems may still be occuring.

While we whole-heartedly welcome the OFT's action as a clear sign that the relevant bodies are monitoring the situation and are prepared to implement enforcement measures where necessary, we also hope that Government and the relevant regulatory bodies vigorously maintain this

focus and commitment in the future, so that the possibilty of persistent abuse of charging orders is mitigated.

Comment
2) Orders for sale We are supportive of the introduction of a threshold on orders of sale, and believe that debtors should be protected from the risk that a creditor may force a sale of property for a relatively small amount of debt. Incidents of creditors applying charging orders for small amounts of debt have been well-publicised for a number of years (as referred to in the box below). While we recognise that the proportion of charging orders which are actually converted into orders for sale is quite low, we believe that there is still value in the introduction of a threshold. Removing entirely the risk that these debtors could lose their homes would in our opinion have a significant effect on their state of mind. In our experience, debtors who approach their problems in a positive mindset usually end up being the most efficient repayers. This is supported by informal conversations our staff have had with debt collectors, who have told us that creditors who deal with debtors in a sympathetic manner tend to ultimately recover more than if they act aggressively. Introducing a threshold for charging orders, and lifting the threat of property loss for those with relatively small amounts of debt, may therefore end up being beneficial for both creditors and debtors.

Evidence
The application of charging orders for small amounts of debt has taken place for a number of years. **Comments made by members of the OFT with regard to the action they took on charging orders in November, describing cases where these were implemented to secure debts of less than £600, demonstrates that this is recent occurance. Further evidence of this has been provided in**

Citizens Advice's June 2009 "Out of order: CAB evidence on the use of charging orders and orders for sale in debt collection" briefing, which contains several examples of instances where charging orders have been implemented for amounts totaling less than £1000. This includes a couple from Wiltshire who received a charging order for £690 of credit card debt, and a CAB client from North West Wales who was given a charging order for £852 of store card debt (p. 5)

We feel this practice is inappropriate, and that it is detrimental not only to the debtor but also potentially to the creditor as outlined in the box above. As suggested, we would therefore be supportive of introducing a threshold on orders for sale.

Q15. How can debtors be encouraged to seek early support to help manage their debt problems?

Comment

We agree very strongly with the sentiment outlined in Paragraph 59, that it is "important that individuals facing financial difficulty should seek advice early rather than wait until a problem is compounded". In addressing this issue, we believe there is a place for the development of some form of "early warning" mechanism which would identify those who had fallen into arrears relatively recently or were at risk of doing so, and signpost them towards some form of money education or advice before their financial difficulties became too severe. We could forsee such a system potentially drawing on the records of credit reference agencies or banks to flag up such individuals. They might include: people who had missed payments in several consecutive months; people who had missed a certain number of payments in the space of a year; people who had only been making minimum repayments for a certain period (for example 6 months) and whose debts were continuing to grow larger as a result. Those in question might then be contacted and directed towards organisations that could provide them with appropriate advice and support. Alternatively, along similar lines, lenders could be required to write to all debtors who were at least one month in arrears with details of where they could access free money advice.

As a further point, we believe that there is a relevant and valuable

rehabilitative role for money education in supporting those who have already encountered serious debt problems, and who may be in formal insolvency procedures. In this context, we believe that there is a genuine opportunity to help debtors achieve behavioural changes that will enable them to avoid falling into difficulty again in the future. In a sense, this represents a particular form of early support, in that it would help provide debtors with the skills necessary to deal more effectively with debt in the future as they embark on a "fresh start". We would envisage integrating some form of money education course into the procedures for the various types of insolvency, so that this forms part of the process that debtors follow on the path to paying down or discharging their debts. Given that robust money management skills are likely to be essential to such debtors in the short to medium term (due to the obvious difficulties they will encounter in attempting to access mainstream credit, as well as the fact that certain types of procedure such as Individual Voluntary Arrangements demand strict adherence to a repayment plan) we would argue that there is a great deal of value in offering this sort of support. Indeed, pre-discharge debtor education is already a compulsory part of the bankruptcy process in the United States (with a certain amount of evidence suggesting that it does have a positive impact on debtor behaviour, which is outlined below) and we believe that there is a strong case for adopting the practice in this country. Equally, we think that there may be scope for integrating financial education courses into less formal arrangements such as Debt Management Plans as well.

Evidence

Pre-discharge debtor education has been a mandatory part of the bankruptcy process in the United States since the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act in 2005. Since then several studies have examined the effectiveness of such programmes and produced largely positive findings.

An evaluation study was commissioned by the US Department of Justice, and was published in May 2008. Of the debtors surveyed, it found that 97% believed that their ability to manage money had improved as a result of the course. 44% said that they intended to adopt at least one financial practice which they had not planned to before, or that they planned to adopt a practice sooner than expected. Three months later, 22% of debtors reported actually following through on this.

In the same month, credit counselling and education provider Money Management International published a separate evaluation study that it had undertaken with the University of Illinois. 98.3% of respondents felt their ability to manage their finances had improved as a result of the course they undertook. Furthermore, a behavioural analysis demonstrated that debtors were in what was called a "teachable moment" during which they were open to new information and to changing existing behaviour.

While it is admittedly difficult to generalise on the basis of any one of these studies, it is notable that there is a certain level of consistency in the findings, both in terms of the numbers of respondents who reported that the courses were helpful and in the apparent openness of participants to behavioural change. In our opinion, these findings attest to the potential value of such debtor education courses.

Q16. Do the current debt relief options strike the right balance between the needs of the debtor and the rights of creditors?

Comment

Evidence

Q17. What problems are encountered with the current range of debt solutions and how could they be improved to ensure all debtors have an option and that the choices are clear?

Comment

Evidence

Q18. Is there sufficient flexibility within the current range of debt solutions to allow for debtors changing circumstances?

Comment

Evidence

Q19. Do the current options allow and encourage those who are in a position to repay their debts to do so? If not, why not, and how might any incentives be improved?

Comment

Evidence

Q20. Do the current options allow a person to deal effectively with a temporary income 'shock' and if not, what is needed?

Comment

Evidence

Q21. Is some form of moratorium on creditor action required to a) allow a short time period for a debtor to seek and act on advice from a qualified adviser and b) allow a more extended period for a debtor suffering from a temporary difficulty to recover and start making repayments once more. If so, how might such an arrangement work, and what safeguards are required to ensure that creditor rights are protected?

Comment
We believe that a moratorium on creditor action would in many circumstances be desirable, but that there are certain practical considerations necessary to make such systems work: **a) A short term moratorium to enable a debtor to seek and act on qualified advice would, in our opinion, be beneficial in terms of allowing debtors some period of respite during which they could talk through their debt problems with an advisor in a rational manner. In our experience, many creditors will in fact voluntary ease the pressure on debtors if they receive a clear signal that the debtor is actively seeking advice to deal with their problems. However, if such a moratorium were to be formalised, we recognise that some creditors might have understandable concerns over whether a debtor who says they are seeking advice actually goes on to follow through on their commitment. We know that in practice, the Consumer Credit Counselling Service provides all its clients with a reference number which creditors ask for as proof that the debtor in question is seeking help. If a short term moratorium were to be formalised, all advice agencies might need to operate a similar reference number system to provide evidence to creditors that a debtor was known to a particular agency.** **b) In our experience, creditors are likely to be relatively accomodating to debtors who suffer temporary difficulties, providing that their repayment history to date is good and that they can prove that such difficulties will only be of a limited duration. All the same, we believe that the proposal for some form of moratorium on creditor action may well be beneficial - ultimately, full bankruptcy is a situation in which almost everyone involved loses and if it can be avoided, within reason, then this is an outcome which is positive for all. However, we would caution that if there is little prospect of the situation improving in the longer-term, a moratorium may end up being counter-productive by prolonging a situation which it is in the best interests of both debtors and creditors to be dealt with immediately.** **We believe this also raises a connected issue concerning circumstances in which debtors with very high levels of debt and low incomes can be placed onto formal Debt Management Plans with unrealistic repayment schedules (the Citizens Advice Bureau have previously calculated the length of time it would take their clients to meet their non-prioirty debts - the type of debt normally covered by Debt Management Plans - which is refered to in the box below). The**

reality of such situations is that insolvency procedures may ultimately be preferable to repayment plans stretching over, say, several decades, in that they offer debtors and creditors the opportunity to deal with the problem in a comparatively short time frame and move on.

We would therefore propose introducing a recommended (although, we would stress, not compulsory) 10 year limit on the duration of Debt Management Plans, unless a debtor's financial circumstances are likely to improve in the short to medium term. If repayments cannot be completed within the recommended period, serious consideration should be given to directing the debtor towards an appropriate insolvency procedure. In instances where it is judged that a debtor's financial circumstances might realistically improve, they could initially be placed on a Debt Management Plan for a period of 2 years. At the end of this period a compulsory review might then take place and a final decision made as to whether to continue with the Plan or administer insolvency.

We would also like to make one additional point in response to this question regarding a particular instance in which we feel people may be uniquely vulnerable to falling into debt, and in which creditor forebearance may be especially desirable - bereavement. We believe there are substantial flaws in the current procedures for reporting a death that not only makes the experience more distressing for the bereaved than it needs to be, but also enhances the risk that they could encounter serious financial difficulty as a result of a loved one's death.

Following a bereavement to one of our staff, we have become aware of the extreme complexity of the reporting process - different banks have entirely different reporting requirements and forms, meaning the process of notifying all the financial institutions that held funds for the deceased can be a long and arduous one. Once banks are informed of the death accounts are frozen, but further information is then required in order to release funds once a will is executed. We are accutely aware that if an individual relied on their deceased spouse for financial support, these funds could potentially be denied to them for an extended period of time which may ultimately push them into serious debt. While we recognise that creditors can already be sensitive to these issues when such instances occur, we would like to take this opportunity to urge Government, on a wider level, to review the procedures for reporting a death, and in particular to examine the possibility of developing a single, universal format which could be used to notify all financial institutions (while this latter point is not of direct relevance to Question 21, we feel strongly that it is a significant issue which deserves attention).

Evidence

With regard to the issue of unrealistic Debt Management Plan repayment schedules, we would point to a briefing paper produced by the Citizens Advice Bureau in February 2009 entitled "A Life in Debt", which profiled the financial circumstances of new debt clients advised during 2008.

It found that more than half of CAB debt clients would take more than 10 years to repay their non-priority debts in full, the average being 93 years. Furthermore, 16% of clients would take more than 100 years to repay their non-priority debts in full (p. 18). Citizens Advice concluded that "It is therefore important that advisers and clients should consider other options for dealing with debt such as bankruptcy and other forms of insolvency".

Allowing Debt Management Plans to endure over excessive timespans effectively traps an individual in a lifetime of debt repayment. Introducing recommended limits on the duration of Debt Managment Plans as outlined above would in our opinion help prevent this. However, we would also stress that there may be individual cases where Debt Management Plans lasting more than 10 years are appropriate, so would caution against introducing compulsory limits.

Q22. How does a person find out where to go for debt advice and assistance? What are the advantages and disadvantages of each method?

Comment

There are a number of ways in which people are directed towards debt advice, including creditor referral, personal recommendation, television and internet advertising, or by proactively searching themselves.

However, evidence suggests that one of the key factors influencing the choice of a particular provider of debt advice is their visibility (we outline this in the box below). In this context, one of the major problems facing debtors who are seeking debt advice remains the fact that fee-charging debt management companies have considerably greater exposure compared to free debt advice agencies.

We welcome recent enforcement action taken by the OFT with regard to misleading advertising on the part of 129 such fee charging companies. However, we also believe that more needs to be done to actively promote the visibility of free advice agencies, who simply do not possess the resources to compete with fee-charging providers in terms of advertising and marketing.

We believe that measures such as requiring lenders to write to all customers who are in arrears in order to inform them about sources of free advice through web-based, telephone and face-to-face services would be beneficial in this regard (we also raised this suggestion in our response to Question 15 with respect to encouraging debtors to seek early advice for their problems, and believe it is the sort of measure that could meet multiple objectives).

Furthermore, an absolutely ideal solution might involve creating an internet or mobile phone based system which allowed users to easily access information about free, reliable and independent sources of debt advice. This could include details of where to find advice services and providers which operate online, by telephone, and face-to-face (with the latter prospectively using some form of postcode search facility). We have in fact created a web-based facility called the "Money Advice Map" which enables people to locate local debt advice centres using a post code search, and believe this is the sort of concept which has the potential to be developed much further.

Evidence

We would cite the Personal Finance Research Centre's July 2009 research entitled "An independent review of the fee-charging debt management industry", which was commissioned by the Money Advice Trust and also referred to by the OFT in their "Debt management guidance compliance review", as indicative of the problems that we have outlined above.

In the Executive Summary document to this research, it is striking that the Personal Finance Research Centre stated that:

"The interviews with customers indicate that CCCS and Payplan [two of the largest free advice agencies] have a low visibility among debtors in the general public, relative to fee-charging companies that offer debt management and other debt remedies ...

People were attracted to the fee-charging company for two main reasons ... First these companies were highly visible to the general public through television, newspaper and internet advertising. Secondly, they delivered direct and simple marketing messages, namely that they could help people manage their debt problems, take away the anxiety of dealing with their unsecured creditors, and reduce their debt payments to an affordable amount.

Once they had made initial contact with a fee-charging debt management company, the customers we interviewed were unlikely to speak to any other companies". (p. 6)

In our opinion, this situation calls not only for careful regulation of existing advertising by fee-charging companies, but also more proactive steps to raise awareness of free advice providers of the sort described above.

Q23. How does a person know that he/she has been given the ‘right’ advice?

Comment

Evidence

Q24. What evidence do you have to suggest that debtors end up in the 'wrong' solution and what is the scale and impact –for the debtor, the creditors, and the economy?

Comment

Evidence

Q25. Is it clear in all circumstances what the 'right' solution should be?

Comment

Evidence

Q26. How often do debtors move from one remedy to another and could the costs be reduced in any way?

Comment

Evidence

Q27. Should there be more consistency on how a debtor's income, assets and expenditure are calculated and treated in different procedures?

Comment

Evidence

Q28. Should any changes be made to investigation and enforcement action in relation to debtors entering insolvency procedures?

Comment

Evidence

Q29. What outcomes should such investigations be looking to achieve – for example, should they just relate to restrictions on future conduct or should they also impact on a debtor's discharge from his/her liabilities?

Comment

Evidence

Q30. Are the practical effects of entering the different debt remedies satisfactory e.g. future access to financial services? Should this be influenced by the outcome of any investigation/enforcement?

Comment

Evidence

Q31. Is there a role for a "gatekeeper" to provide a common entry point to all formal insolvency procedures? If so, what would be the benefits and costs, who would perform such a function and how would the system operate?

Comment

Evidence