

# Breathing space: call for evidence – Responsible Finance Response

16 January 2018

## About Responsible Finance

Responsible Finance is the trade body for responsible finance providers (also known as community development finance institutions or CDFIs). Responsible finance providers offer loans and support to businesses and individuals that find it difficult to access finance from commercial banks. Responsible Finance's mission is to support the development of a thriving and sustainable sector that provides finance for underserved communities and, as a result, contributes to the increasing economic growth and prosperity of these communities.

Responsible Finance welcomes the Government's proposals on breathing space, as these are practices that responsible finance providers currently employ with their customers experiencing financial distress. For this reason we recommend that responsible finance providers as creditors are exempt from breathing space and statutory repayment schemes, in order to maintain the current good practice in place to ensure its customers are better off.

## Responsible Finance Response

**Question 1: In your opinion, how should the government decide who is eligible for a breathing space? In particular:**

- **How should the government define serious problem debt in the context of a breathing space?**
- **Should eligibility be determined by a set of defined characteristics, or should there be some discretion to determine eligibility?**
- **If there is some discretion, who should be tasked with exercising it – a regulated debt adviser, or some other person?**
- **Are there any other entry criteria and / or exemptions the government should consider?**
- **Who should be responsible for regulating and enforcing access to a breathing space and how can disputes be resolved?**

While assistance for people in genuine distress is welcomed, the breathing space scheme should only be targeted at consumers in debt. The evidence of how debt impacts on mental health is well documented. The impact that debt has on a consumer varies hugely, someone with £500 debt on a low-income and has missed 2 payments may spiral into depression and suffer with anxiety, whereas someone with £5,000 debt may not. In addition consumers may feel pressured to repay non-priority debt over priority debt when they cannot afford it because of the debt collection tactics used by those creditors. Therefore it is challenging to set statutory definitions as it depends on an individual's personal circumstances.

If a client is liaising directly to resolve a debt problem, or working with a debt adviser, the breathing space request should be approved upon request. Early intervention should be encouraged to resolve debt issues before they become longer term problems. Encouraging intervention at an early stage will assist creditors by minimising the potential of non-repayment.

Breathing space should only be available to consumers in financial difficulty, not to those who may be choosing not to pay a debt, so any eligibility criteria must take this into account.

To avoid fee charging 'experts' and profiteering from the breathing space scheme, all applications should be approved by a free intermediary.

Given its role in the market regulating lending activity, the FCA is well placed to regulate access to breathing space. Lenders can report on it as part of their regulatory obligations.

**Question 2: What should be the trigger point for a breathing space? In particular:**

- **Should a breathing space only be available for a person who seeks regulated debt advice?**
- **Should individuals have demonstrated they have already taken steps to try to manage their debt?**
- **If so, at what point should the six weeks start – for instance: once a breathing space has been requested, when the first advice session has occurred, or once adviser has confirmed a breathing space would be appropriate?**

Breathing space should be available to consumers who have demonstrated they have taken steps to manage their debt, such as seeking debt advice. This can then be confirmed by the

debt advice agency. It is important that the infrastructure for debt advice provision is sufficient to meet what is likely to be increased demand when the breathing space programme is launched.

Creditors should have an obligation to notify debtors that a breathing space option is available on request. It should be made clear to the consumer by their creditors that within 6 weeks they expect to be in a position to agree repayment and debt resolution. If working with a regulated debt adviser, they will work towards compiling a verified Standard Financial Statement (SFS) and discuss debt strategies within the 6 week period and liaise with the creditor.

Breathing space should start upon request; the purpose is to allow 6 weeks for the consumer to review their financial situation and be in a position to implement the appropriate debt strategy.

**Question 3: Should all debts be eligible for a breathing space?**

- **How should multiple debts be treated; is there a priority order of debts which should be included as part of a breathing space arrangement?**
- **Should some types of debt be exempt? In particular, where the debt is the late payment of a fine or penalty?**
- **In particular, should debt owed by self-employed / microbusinesses be included?**

For breathing space to have its intended impact of enabling a consumer to resolve problem debt, their financial position should be assessed as a whole, and all outstanding debt should be reviewed. Breathing space should apply to all debts at the point of request to enable full advice to be provided and debt strategies put in place.

Responsible finance providers provide finance and financial capability support to consumers and microbusinesses that are often low-income or can experience vulnerability. They treat customers fairly and aim to generate positive outcomes for their customers throughout the lifetime of the loan. Responsible lending also means not approving a loan that will make a consumer worse off, and directing that individual to appropriate support. Responsible finance providers exercise forbearance when consumers encounter difficulty repaying their loan, and work with the individual to establish a new repayment plan. Responsible finance providers signpost loan applicants who exhibit high levels of debt, as well as some existing customers whose circumstances change and their debt becomes unsustainable, to debt advice, where requesting a breathing space may be a suitable option. We recommend that where the creditor is a not for profit lender such as a responsible finance provider, this debt is not eligible for a blanket breathing space given that other forbearance arrangements are likely to already be in place.

There should be an order of priority once the breathing space has ceased, but first it is important for the consumer or the money advisor to look at the whole situation in order to implement effective debt strategies that will be maintained.

Self-employed individuals and microbusinesses should have the same opportunity to apply for breathing space.

**Question 4: Should all interest, fees and charges be frozen throughout the breathing space period?**

For eligible debt, the interest, fees and charges should be frozen during breathing space. Creditors should not be permitted to add fees and charges or accelerate interest to debt during breathing space. If a breathing space agreement is granted then there is no additional collection work or costs on the creditor's part and therefore it is justifiable to suspend interest and fee repayments.

As part of the breathing space agreement, the creditor should provide a statement of the balance due and the original agreement for the debt in order for the individual/money adviser to compile an accurate financial statement and seek an appropriate debt solution.

As mentioned in the response to Question 3, we recommend that responsible finance providers are exempt from the breathing space proposals, given that existing arrangements with customers in financial distress will have been arranged. This will also include arrangements for how interest is treated during the forbearance period.

**Question 5: What activities must the breathing space participant continue with to remain eligible? For instance:**

- **Should they be required to attend advice sessions?**
- **Should they be required to make any repayments during a six-week breathing space, if their financial situation allows it?**

Although it is preferable that the breathing space participant undertakes specific activities to remain eligible, the time taken to monitor a wide range of appropriate actions may be onerous and therefore not practical.

Breathing space is to allow consumers to try to take steps to manage their debts. By requesting the breathing space a person is thinking about their financial difficulties and looking to put strategies in place to deal with them. This should be seen as a positive request for a creditor.

If working with an adviser the consumer should continue to engage with the advice process. If they disengage the adviser should be responsible for notifying the creditor that they are no longer working with the agency and that would terminate the breathing space – unless the consumer has contacted directly to inform the creditor that they have decided to use an alternative service, or are taking steps to resolve their own financial situation within that time frame.

Suspending debt repayments on eligible debt during this period should be automatic at first, until a full financial statement has been prepared and priority and non priority debts identified and verified. People with multiple debts would then not be required to continue payments or encounter further financial difficulties unless their financial situation changes and they are able and wish to make repayments.

**Question 6: Are there circumstances in which a breathing space period could end before six weeks, such as if an appropriate solution is found? Who could be responsible for enforcing this?**

It should be possible to end the breathing space period if:

- 1) the consumer disengages from an advice service and the creditor has been notified;  
or
- 2) the consumer agrees a repayment plan and makes a formal proposal to the creditor

The consumer or money adviser would be responsible for notifying the creditor of the decision to end the breathing space, either due to lack of engagement or because an appropriate debt strategy has been implemented.

**Question 7: Should breathing space protections only cover debts existing at the outset, or also include new debts arising during the six-week period?**

The consumer should agree at the outset of the arrangement not to take on new debts during the breathing space period.

**Question 8: Should a breathing space be noted on a person's credit file?**

No, as the missed payments will be recorded on the credit file, requesting a breathing space should not negatively impact a consumer's credit file. This is the main area of concern to consumers – that seeking debt advice negatively impacts their credit score so if a breathing space does this then it ceases to be a viable option and could influence the decision to continue engaging for debt advice.

**Question 9: How frequently should a debtor be able to access a breathing space, and what criteria should control the frequency of access?**

The aim for the breathing space scheme should be that a consumer gets their financial position under control, and access to a breathing space agreement should be limited to no more than once each year, with three in total.

Responsible finance providers report that consumers can disengage at an early stage from debt or money advice for a variety of reasons including health, mental health, fear, confusion and anxiety. Therefore, if a second request is made in due course this should be granted to enable the individual to seek debt resolution.

This should also be considered for a change of circumstances. For example an individual may be made redundant and need to review their current debt strategy, and the waiting times for new benefits (Universal Credit) means that an individual has to wait up to 6 weeks for first payments. It may also be necessary to request a further breathing space if there have been difficulties obtaining information and compiling a financial statement. For example, if an adviser or the consumer identifies that they may not be able to engage with the advice service without the appointment of a support worker. This is a common scenario often delaying the process as the individual may require a mental health assessment before engaging in the money advice process. Specialist advice may need to be sought which could influence the debt options available to the client including a Debt & Mental Health Evidence form for example therefore an extension to the initial breathing space may be required.

Any further request made should be fair, in the best interests of the consumer and the creditor. The breathing space, used correctly, will assist the individual and creditor towards a resolution.

This should also be regulated by the FCA, if a second request is unfairly declined, then a challenge should be made directly to the creditor. If unresolved, the account should be put on hold while the FCA investigates the complaint.

**Question 10: What challenges would creditors face in implementing the scheme?**

Potential challenges for creditors include administration of the scheme and liaising with advisors. Assessing whether a consumer is unable to pay and in financial difficulty could also be a challenge for some creditors.

**Question 11: Who would be responsible for notifying creditors that a customer has entered a breathing space? What updates are required during the breathing space period?**

Whoever has arranged the breathing space, either the money advisor or the individual, should be responsible for notifying the creditor that a breathing space has been requested and the date at which it commences.

The creditor should be contacted before the end of the breathing space period to notify them of the consumer's status on developing a financial statement and debt strategy.

**Question 12: Would a breathing space scheme impact on business revenue or have any other significant detriment?**

Implementing a breathing space impacts on creditors' revenue through lost interest and fees and the time spent by staff on arranging and monitoring the scheme. However, if the breathing space period enables the consumer to stabilise their financial position and get back on a repayment plan, then breathing space could have a long-term positive impact on revenue.

**Question 13: Should any creditor be exempt due to the size of their business?**

As mentioned in the response to Question 3, not for profit creditors, such as responsible finance providers, should be exempt from the scheme. This is due to their social objective, as they are already taking measures to ensure their customers only take out credit they can repay, and if there are difficulties repaying, that they receive the support they need to gain resilience.

The Government may also wish to consider appropriate timeframes for requests for information from creditors, given Data Protection regulations.

**Question 14: What benefits could creditors see as a result of a statutory breathing space scheme?**

As mentioned in the response to Question 12, creditors could see a longer-term benefit of higher repayment rates from clients in financial distress, debt that would otherwise have been written off. Other benefits to creditors could include:

- Better communication with their customers

- Appropriate and maintained debt solutions for repayment of debt
- Reduction in collection fees/resources/credit control
- Gain a better understanding of financial difficulties leading to better lending decisions
- Support the economy
- Reducing bad debt write-offs.

**Question 15: How could the government ensure that a breathing space works with and adds value to existing support structures?**

This can be done through regulation by the FCA. The option for a breathing space can be written into credit agreements so that consumers are aware that it is an option should they encounter financial distress.

**Question 16: What safeguards are needed to prevent the scheme being abused?**

Potential safeguards include designing a way in which consumers can be fairly assessed as to whether they are genuinely unable to pay or able to pay. If working with a Money Advice agency, the adviser would be able to assess and establish if an individual is able but choosing not to pay. For individuals not engaged with advice, the creditor can advise the client that their agreement to breathing space is made on the condition that they contact an agency for debt advice if they have a legitimate concern about the individual's motive for requesting it.

In addition limiting the number of times a consumer can resort to the scheme, can prevent the scheme from being misused.

**Question 17: Should a breathing space be extended to Wales and Northern Ireland as well as England?**

Yes, regardless of a consumer's post-code if they are in financial difficulty and the purpose of the breathing space is to allow them to review and regain control.

**Question 18: How could a statutory debt repayment plan be administered?**

The current arrangement for informal debt management plans (DMP) is generally negotiated through the money adviser and creditor. This is reliant on creditors supporting proposals and agreeing the repayment proposal. These are rarely for the lifetime of a debt as many creditors request regular reviews of informal DMPs. We support the continuation of informal debt management plans as a debt option.

A statutory payment plan could be administered by trained and regulated non fee charging debt/money advice agencies in the same way that a debt relief order (DRO) is prepared by a qualified money/debt adviser before submission to the Insolvency Service.

The Insolvency Service could be responsible for formally agreeing the statutory debt repayment plan as they are with the current DRO system.

**Question 19: What challenges would be faced in administering a statutory repayment plan?**

Potential challenges in administering a statutory repayment plan include adequate time and resources to do so, and securing the continuing cooperation of debtor once scheme was in place.

It should not present more challenges than the current statutory debt options, however the volume of cases will likely be higher.

**Question 20: What protections should apply during the statutory repayment plan?**

- **For instance, should it protect debtors from interest and fees and charges or just a selection of the three? If a selection, which of these three should be prioritised?**

Charges and fees should be frozen during the statutory repayment period. Interest could be charged at a reasonable rate (e.g. the repayment covers capital borrowed, not just services the interest so the debt is being repaid).

There could be a maximum interest rate chargeable set by the FCA during breathing space periods. Creditors would still be earning some interest on money lent but individuals would then be repaying the amount borrowed and reducing their debt liability over the agreed timeframe.

**Question 21: For whom and for what debt solutions will a statutory repayment plan be most appropriate?**

Where an individual has verified disposable income to service and repay their debts over an appropriate timeframe.

**Question 22: How will a debt adviser determine if a statutory repayment plan is appropriate?**

As with all money/debt advice, a verified financial statement is prepared and all options are explored to enable the client to ascertain the appropriate debt solution: that they are eligible for and that enables them to resolve their debt issues. A statutory repayment plan would be particularly beneficial to individuals whose circumstances are unlikely to change or where there is a possibility that it may improve over a time period, this would enable them to maintain payments at an agreed rate and repay their debt over an appropriate time frame for their financial circumstances.

**Question 23: If a statutory debt repayment plan cannot be agreed, how could the behaviour of creditors be managed immediately after the Breathing Space?**

The creditor should have the account on hold while the Insolvency Service assesses the application for a Statutory Debt Repayment Plan. If the plan is declined by the Insolvency Service, the consumer will need to review their debt options in order to move forwards positively with an appropriate debt strategy. The creditor should be prepared to accept a further “breathing space” while options are explored and an alternative strategy sought.

**Question 24: Should the repayment plan apply to all debt?**

Further to the responses to Questions 3 and 13 responsible finance providers should be exempt creditors due to existing breathing space and repayment plan arrangements they put in place with their customers.

**Question 25: For the included debts, should some debts be prioritised for repayment?**

Priority debts (such as rent, utilities, council tax) should receive a higher proportion of a consumer's disposable income.

**Question 26: What should happen if one or more creditors disagree with the plan?**

If the plan has been approved by the insolvency service the Statutory Debt Repayment Plan should be enforced so that creditors accept the agreed payments based on the clients financial situation and affordability, verified by the insolvency service's approval of the statutory repayment plan.

**Question 27: What activities must the statutory debt repayment plan participant continue with to remain eligible? Must they simply meet agreed repayments to remain eligible?**

The following activities could qualify eligibility;

- Payments are maintained
- No significant material changes in circumstances
- No further borrowing

There could be challenges monitoring adherence to this, therefore meeting of the agreed repayments would be the most cost effective way of measuring continued eligibility.

**Question 28: How should changes in income be dealt with? Should it be possible to suspend a plan, or have reduced payments for a period of time?**

If there is a significant material change in circumstance the individual should be responsible for notifying the insolvency service. Any request for changes to the amount repaid should be made by the insolvency agency to the creditor.

**Question 29: What happens if a plan fails? Should creditors be able to apply any interest, fees or charges that they were prevented from charging during the plan?**

If an individual stops making payments because of a detrimental change to their circumstances that they evidence then no. However if an individual stops making payments and provides no evidence to the creditor then it is fair that interest and charges be applied.

**Question 30: Should there be a regime for sanctioning debtors where there is misconduct in relation to a breathing space or statutory debt repayment plan, as there is for bankruptcy and DROs?**

Yes, the same rules should apply.

**Question 31: Should a statutory debt management plan be extended to Wales and Northern Ireland as well as England?**

Yes.

**Question 32: For each of (1) a six-week breathing space, and (2) a statutory debt management plan, please describe in detail, and with supporting evidence, the positive impact expected through:**

- **Improved access: How will it encourage more people to seek debt advice earlier?**
- **Better support: How will it improve outcomes for customers who are already in problem debt?**
- **Increased repayments: How will it increase the amount of debt repaid to creditors?**

More can be done to encourage consumers to seek advice earlier before the point of crisis, supporting the breathing space. In particular priority creditors making referrals to advice agencies. Responsible finance providers already do this, working closely with local debt and money advice agencies.

In responsible finance providers' experience, people want to resolve their debt issues but do not have the time to think or seek advice which means that hasty decisions are made, repayment plans are accepted that are unaffordable and not sustainable or they ignore creditors. This can result in more anxiety and stress for the debtor and creditors having to take further action to resolve arrears – adding cost to the recovery process.

**Question 33: Once implemented, how could the government determine whether the breathing space and statutory repayment plan have been successful? What metrics would be appropriate to use?**

The FCA regulates lending activity and therefore it would make sense to incorporate breathing space as part of a creditor's obligation to report to the FCA which would capture the number of clients accessing the breathing space and the repayments made following the breathing space.

If the Insolvency Service takes responsibility for approving Statutory Debt Repayment Plans they could report on the number approved/declined and the status of account supporting the creditors reporting to the FCA.

Metrics to report on could include;

- Communication with consumers in breathing space periods
- Appropriate and maintained debt solutions for repayment of debt
- Reduction in collection fees/resources/credit control

- Reduction in bad debt write-offs.

### **Case study: Wessex Resolutions**

Wessex Resolutions provides a money advice service - Wiser£money. Wiser£money has provided debt advice to 1,216 clients and financial inclusion services to 5,227 people. From 1<sup>st</sup> April 2016 to 20<sup>th</sup> November 2017 Wiser£money received 748 referrals, of which 430 clients (57%) engaged and became active cases. Of those:

- 119 (28%) had previously sought advice from another agency specifically for debt advice
- 28 (6.5%) were returning clients to Wiser£money

A very small proportion of customers returned for further advice as every client who proceeds through the advice process has a verified financial statement compiled to discuss the debt strategies available to them; enabling them to choose a debt strategy that is appropriate to their situation and sustainable, resulting in better outcomes for the customer and the creditor.

In Wessex Resolutions' experience as a creditor, working with consumers and offering a breathing space results in:

- Better communication with individuals
- Appropriate and maintained debt solutions for repayment of debt
- Reduction in collection fees/resources/credit control
- A better understanding of financial difficulties leading to better lending decisions (and appropriate and maintained debt solutions for repayment of debt)
- Reducing bad debt write-offs – Wessex have lent over £5.7m with bad debts totalling £26k – 0.47% - over their entire lending history.

From their experience it is extremely rare for a borrower to suddenly decide they do not wish to pay their debt. When a customer misses payments there is usually a valid reason for doing so – redundancy, benefit sanction, relationship breakdown, health issue or change in circumstances to name a few.