StepChange Debt Charity Scotland Briefing

Beating problem debt: How the next government can reduce the harm problem debt is causing now and boost households' financial resilience

We estimate that over 700,000 Scots are at risk of or already living in problem debt.

Many will see their financial difficulties worsen without better help and support.

Last year, StepChange was contacted by over 34,000 people across Scotland for help with their debt problems. We are supporting Scots in every constituency. But there are many more out there who need access to free debt advice.

A strong economy and a just society rely on the confidence and financial resilience of households. Yet confidence can't spread when people are worrying about how much they will earn month to month, when they need to borrow just to pay bills and are caught in a spiral of stress and debt.

We believe that Scotland can do better.

We are calling on the next UK government to commit to reducing the harm problem debt is causing, as well as working to prevent future debt problems by increasing the financial resilience of households most vulnerable to problem debt. We want Scottish MPs to work to support this and cooperate with Local Authorities and the Scottish Government to take action on problem debt.

This should include:

- Creating **binding good practice standards for public sector debt collection** and enforcement - this includes Local Authorities pursuing Rent and Council Tax Arrears.
- Committing to **pilot a no-interest loan scheme** in the UK to support those who might otherwise have to turn to high-cost credit or go without essentials
- **Strengthening the hand of the Financial Conduct Authority** with a clear mandate and responsibility to deliver a safe and fair credit market for consumers
- Setting out a **strategy to reduce the number of people using credit for essential household bills**, emergency expenses and essential household goods
- Strengthening the safety net, by **improving the benefits system** and making it more responsive to crisis needs – **including ending the five-week wait for Universal Credit**
- We want the Scottish Government **to introduce a coordinated action plan to address problem debt.** The social cost of problem debt is around **three-quarters of a billion pounds**; impacting all public services, individuals, families and communities.

Reducing the harm problem debt is causing now

The pressure of living under problem debt shatters people's health: When we asked our clients across the UK about how debt affected them, over half said they had been treated by their GP or a hospital for debt related physical or mental health problems.[i]

Problem debt harms children and families: 57% of indebted parents said debt put their current or most recent relationship under strain. 7% said their relationship broke up because of debt. Children from families in problem debt were twice as likely to say they had been bullied at school compared to children whose families were not in problem debt.[ii]

Problem debt damages jobs and productivity: 43% of StepChange Debt Charity clients polled said that debt anxiety left them unable to concentrate at work. 15% said that their debt worries led to changes in attendance such as arriving late or taking more time off and 2% said that it led to them losing their job.[iii]

Debt makes it harder for people to find work or move to better paid work: 61% felt less confident about getting a promotion at work. 48% of those who had fallen out of work were worried about unaffordable debt repayments if they took a new job[iv]

The problems debt creates puts a cost on us all: We have estimated that the harm experienced by over 3 million people across the UK in severe problem debt creates external social costs of over £8 billion.

1. Scotland needs a coordinated plan for addressing problem debt

Problem debt lies alongside multiple key areas of policy for the Scottish Government. It's therefore vital that the impact of problem debt is assessed across these policy areas and steps are taken to develop successful pathways out of problem debt that allow people relief from, and to avoid falling into, problem debt in the first place. The public health impact of problem debt is significant and growing. Over 40% of Scottish clients say they are suffering from mental ill-health.

Incorporating the impact on indebtedness and financial wellbeing as measures of policy outcomes, especially for Scottish welfare, is vital so that government policy does not exacerbate or open the door to greater financial vulnerability. In addition, we want the UK and Scottish Governments to work together to ensure that all policy areas are contributing towards a strategy that addresses **prevention, de-stigmatises, supports early intervention and financial education** and that addresses **how to reduce vulnerability** to problem debt. It is also crucial that the plan addresses how to unlock **increased funding for all channels of free debt advice**, as well as ensuring **Scottish debt solutions** administered by the Accountant in Bankruptcy **are fit for purpose and accessible to those who need them.**

We want to see the Scottish Government develop a plan that addresses the impact of problem debt in Scotland which will alleviate the poverty which is all too often a consequence of falling into problem debt.

2. Create binding good practice standards for public sector debt collection and enforcement.

Debt Advice agencies continue to highlight problems with the way in which debt is collected by government departments and local government.

Many advisors find that advocating on behalf of clients with both HMRC and DWP debt can be very challenging. Staff at these departments appear to receive inconsistent training and there is mixed awareness of Scottish Statutory solutions with little consistency in how these are processed.

Collection processes also may have highly detrimental effects, where a client attempting to organise their affairs is thrown back into crisis when court enforcement action is taken against them, despite the department being made aware that the client is seeking assistance.

We strongly believe that the public sector should be leading by example in their treatment of the most financially vulnerable; but the current approach risks driving them into further difficulty.

In Scotland Local Authorities in particular, operate multiple collection policies, which often have detrimental impacts on clients. Over 46% of Scottish clients are in arrears with Council Tax, owing an average of £2,017.

Ultimately these policies are self-defeating. They may result in clients ignoring what they see as an unsolvable problem, leaving them sinking deeper into debt. For many clients taking out high cost credit to cover the bill drags them deeper into an unaffordable cycle of debt or leads to unsustainable reductions to key expenditure. Increasing reliance on foodbanks, crisis payments, emergency psychiatric support or risk of homelessness demonstrates the detrimental impact of these collection policies.

StepChange is working with other stakeholders to develop a best-practice toolkit for Local Authorities to improve collection policies so that Local Government can better understand and avoid these pitfalls. We want the Scottish Government and COSLA to support the introduction of the toolkit across Scotland so that public services in Scotland do not make debt crisis worse. We will continue to lobby the UK Government to adopt similar policies.

Therefore, we urge the next government, to bring forward UK legislation and bind public authority debt collection and enforcement practices to fairness standards on affordability, harm reduction and supporting financially vulnerable households to recover from financial difficulties, and work closely with the Scottish Government to ensure comparable protections

Preventing the 10 million people experiencing financial distress now from falling into serious problem debt in the future

Across the UK millions of people are living precariously, at risk of falling into problem debt. Life events, such as being given reduced hours at work, being made redundant, falling ill or splitting up with a partner can quickly tip people into serious financial difficulty.

We estimate that almost 23 million people in the United Kingdom experienced a life event like this in their household in the last two years.

Over half of these, 12 million people, were worse off financially and 5.7 million experienced signs of financial distress such as falling behind on essential bills, getting late payment charges and using credit to keep up with bills or make it through to payday.

Despite the fact that these life events are common, most people don't have the financial resilience to cope with them. With holes in the safety net, many people are having to use coping strategies that simply aren't effective at keeping them out of problem debt. People who had to apply for benefits, borrow money or cut back on expenditure were all more likely to fall further into serious debt problems. People who used credit cards or an overdraft to cope were ten times more likely to be in problem debt than those who got by without them.

This highlights the limited options that many people have to cope with a period of financial distress, and it helps explain why 1.4 million people are using high cost credit for essential household bills.[v]

We are calling on the next UK government to take action to improve the options for people trying to cope with financial distress by:

- **Reducing the harm caused by distressed credit use**
- **Making the benefits safety net more responsive to crisis needs**
- **Increasing help with essential expenditure for the most financially vulnerable**

1. Reducing the harm caused by distressed credit use

While most people will benefit from using consumer credit at some point in their lives, credit products can be a cause of serious harm when they compound financial difficulty and trap people in a spiral of rising debt and hardship. We know that the Financial Conduct Authority has made some good progress in addressing some longstanding problems in consumer credit markets; but a good deal of detriment remains through irresponsible lending, excessive charges and exploitative product design.

We are calling on the next government to strengthen the hand of the Financial Conduct Authority with a clear mandate and responsibility to deliver a safe and fair credit market for

consumers. This mandate should include:

- **Introducing a legal duty of care for financial services firms** to ensure they do not profit from consumer vulnerabilities, behavioural biases and constrained choices.
- A stronger and clearer requirement on firms to deliver **early identification and support for people showing signs of financial distress** to prevent this developing into more harmful problem debt.
- **Extending the principle that no one should pay interest and charges that are over 100% of the amount borrowed to all forms of consumer credit.** Westminster acted decisively in 2014 to cap the cost of payday loans and the Financial Conduct Authority recently introduced a 100% cost cap for rent-to own-agreements on the grounds that the prices firms charge for servicing a vulnerable consumer base can cause harm simply because they are too high'. We agree – this principle should now be extended to all forms of consumer credit.

Addressing harmful practice in credit markets is only half the story. Households managing on a tight budget will continue to need help with large, or unexpected costs – such as replacing a fridge, repairing a car or buying new school uniforms. We still see too many people having to use high-cost credit to cover these essential costs, putting more pressure on household budgets and increasing vulnerability to problem debt.

People need affordable alternatives to harmful, high-cost credit. A no-interest loan scheme, based on the successful Good Shepherd model from Australia, would support people who are currently excluded from being able to access reasonably priced credit, for example from mainstream lenders, credit unions or community development finance institutions (CDFIs). In 2019, the government commissioned London Economics to deliver a feasibility study on a UK wide no-interest loan scheme, setting out how this could work. We now need the scheme to proceed urgently to a pilot, with a commitment to roll-out nationwide if proved successful.

We are calling on the next government to set out a strategy to reduce the number of people using credit for essential household bills, emergency expenses and essential household goods.

This should include a commitment to pilot a no-interest loan scheme in the UK to support those who might otherwise have to turn to high-cost credit or go without essentials.

2. Making the benefits safety net more responsive to crisis needs

The next government should strengthen the social safety net to help people manage life events without experiencing poverty and destitution

The social security system is failing to provide an adequate safety net and support people to manage life events and transitions without experiencing poverty and destitution. These issues stem from inadequate levels of support, particularly as housing and childcare costs have increased in recent years. Key design features of Universal Credit are also contributing to financial problems and debt.

To strengthen the social safety net, the government should:

- **End the 'benefits freeze'** and **bring support in line with living costs** and **re-align Local Housing Allowance rates** with at least the bottom 30% of market rents.
- **End the five-week wait for Universal Credit** for all new claims and for those moving to Universal Credit from legacy payments.
- **Ensure that deductions from social security payments to repay debt are affordable** by applying industry standard affordability assessments.
- **Extend access to, and the flexibility of, Universal Credit budgeting advances** by widening eligibility criteria, allowing more than one loan at a time and extending the repayment period up to 24 months.
- **Re-invest in comprehensive crisis support** to prevent hardship and destitution, providing ring-fenced funding allocations to local authorities supported by statutory guidance to help councils implement best-practice and ensure a consistent level of support.

3. Increasing help with essential expenditure for the most financially vulnerable

StepChange is seeing more people without the means to meet everyday expenses. 30% of our clients have a negative budget (meaning they do not have enough money coming in to cover essential expenditure) even after receiving budgeting advice from us.[vi] Two in five clients are behind on one or more households bills like Council Tax, energy or rent.[vii] These problems are far more pronounced among our clients with poor mental health and physical health conditions.

Despite the introduction of the energy price cap, we have seen an increase in the proportion of StepChange clients who are behind on their energy bills. In the first half of 2019, 18% of new StepChange clients with responsibility for paying an electricity bill were in arrears when they came to us for help (compared to 13% in 2016). Meanwhile, 13% of new clients with responsibility for paying a gas bill had fallen behind (compared to 12% in 2016).[viii]

Research by Ofgem has also found that hundreds of thousands of people have temporarily disconnected from their energy supply or have rationed their energy use, often due to affordability concerns.[ix] Furthermore, the Department for Business, Energy and Industrial Strategy found that many fuel-poor households were significantly under-using energy compared to what a household of their size should. This can leave people living in cold homes and have an ongoing effect on their physical and mental health.

We are calling on the next government to address the basic living costs crisis that pushes the most financially vulnerable households into problem debt and a commitment to introduce energy social tariffs, to help people who cannot afford their gas and electricity bills.

4. A long-term UK strategy to improve the financial resilience of households and reduce vulnerability to debt

Since July 2017, just after the last general election, to June 2019 around 1.25 million people have contacted StepChange for debt advice - 2.5% of the UK adult population.

Debt doesn't affect all of society equally – some groups are heavily over-represented among those seeking help from us. Our *Life Happens* report found that working age people, parents, lower and middle income households and renters were all at higher risk of problem debt following a life event. StepChange clients are disproportionately single parents, adults under 40, renters (and increasingly in the private rented sector) and people with disabilities or mental health problems.

The scale of ongoing demand for debt advice and the circumstances of people contacting us signals that problem debt is being driven by a set of underlying vulnerabilities to household financial resilience. We will not be successful at preventing millions more households from experiencing harm and hardship from problem debt unless policy makers get firmly focused on the underlying causes.

We are calling on the next government to work with the Scottish Government to develop a strategy over the life of the next parliament to develop effective policy responses to address the underlying causes of problem debt.

This won't be easy, but there is a way in by focusing on the groups of people most heavily over-represented among our clients.

We therefore urge the next government to set out an action plan to improve the financial resilience of single parents, adults under 40, renters (particularly those in the private rented sector) and people with physical and mental health problems.

For more information on any of the issues set out in this briefing, please contact lawrie.morganklein@stepchange.org. For further information on UK policy, such as Bailiff regulation or Breathing Space, contact grace.brownfield@stepchange.org

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[i] StepChange Debt Charity (2015) Statistics yearbook personal debt 2014
[ii] The Children's Society and StepChange Debt Charity (2014) The Debt Trap: Exposing the impact of problem debt on children
[iii] StepChange Debt Charity (2015): Safe Harbours: Why we need a new extended breathing space guarantee to help people in temporary financial difficulties recover from debt
[iv] StepChange Debt Charity (2015): Held back by debt: How Britain's lack of financial resilience is tipping people into a debt trap
[v] StepChange Debt Charity (2018) *Behind on the Basics: A closer look at households in arrears on their essential bills*
[vi] StepChange Debt Charity (2019) *Personal Debt in the UK: 2019 Statistics Mid-Year Update*
[vii] Ibid
[viii] Ibid

[ix] For more information, see:
https://www.ofgem.gov.uk/system/files/docs/2019/08/proposals_to_improve_consumer_outcomes_self-disconnection_and_self-rationing_1.pdf