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Social Justice and Social Security Committee

15th Meeting, 2022 (Session 6), Thursday 12 May 2022

Inquiry into low income and debt problems – Issues paper

Purpose of this briefing

The purpose of this briefing is to highlight issues to discuss with witnesses as part of the Committee's consideration of debt and low income. The questions are for witnesses on the first panel.

Panel 1:

- **Poverty Alliance**
- **Citizens Advice Scotland**
- **Christians Against Poverty**
- **One Parent Families Scotland**

The Committee will also hear from a second panel of witnesses with expertise in mental health and debt issues. There is a separate issues paper for that panel.

Future evidence sessions will cover reforms to the statutory framework dealing with debt solutions and debt enforcement as well as improvements to processes and procedures for dealing with debts like rent and council tax.

The Committee is also working with a panel of people with lived experience of debt and low income to develop the outcomes of this inquiry.

Background

Debt and poverty discussion

In November 2021, the Committee had a meeting with people with lived experience of debt and low income. This inquiry follows on from that work. The key issues emerging from the discussion were:

- **digital exclusion, with a lack of skills, confidence and financial means to use online services being a major barrier**
- **the stigma people felt in admitting they had a debt problem, which delayed action to get support**
- **problems accessing free money advice – with online information directing people to paid-for services, difficulty identifying relevant services and issues with free services being over-stretched**
- **health – particularly mental health – problems associated with debt**
- **barriers to finding work created by childcare costs**
- **the impact of losing the £20 Universal Credit increase.**

Call for views

The Committee issued a call for views on the subject of debt and low income. The main issues emerging from that were:

- low income is a key vulnerability leading to digital exclusion – this creates barriers to accessing information and services, including money advice. Public services were particularly criticised for failing to cater for people who were digitally excluded

- there are a range of other barriers to people accessing money advice, including stigma and lack of awareness of services. There was discussion about better referrals from trusted local services, but pathways and availability of services are complex and not properly mapped

- free money advice services could not currently meet demand, and this was only likely to get worse in the future. Reduced funding from local authorities and project-based funding from national sources fed into this

- debt is both a cause and a symptom of mental health issues. There were challenges in providing money advice to people with mental health issues, but this was an important part of delivering the service

- bankruptcy is the main statutory debt solution available to people on low incomes. However, there were concerns that it could no longer work to provide anything but short-term relief if people did not have sufficient income to cover essential expenditure

- there were calls for reform to the statutory framework – including in relation to bank arrestments and providing for more flexible contribution levels in bankruptcy so that people could develop some financial resilience

- public sector arrears collection processes could be harsh, especially for council tax. More flexibility and engagement at an earlier stage were recommended.

- the social security system played a role in keeping people on low income in debt. A large proportion of new-style benefit entitlement can be taken in direct deductions, and the five week wait for Universal Credit can require households to borrow.

Scottish Government work

The Accountant in Bankruptcy (AiB) is the Scottish Government agency responsible for supervising statutory debt solutions (bankruptcy, Protected Trust Deeds and the Debt Arrangement Scheme). It is currently working with stakeholders to undertake a debt review.

Work at Stage 2 of the review has involved working groups looking at interim improvements for statutory debt solutions. Reports are either finalised or close to being finalised, but we are not aware of an exact date for publication.

Stage 3 of the review will involve a more fundamental consideration of the appropriateness of the legal framework for dealing with debt.

The AiB is also reviewing the framework for “diligence” (that is, court sanctions debt enforcement used by creditors – such as seizing money in bank accounts). It expects to consult on reform proposals soon.

Legal framework

There are three statutory debt solutions in Scotland:

- **Bankruptcy** – where an individual’s assets are managed (usually sold) by a trustee for the benefit of creditors. Once someone has completed the process, almost all remaining debts are written off. Minimal Asset Process bankruptcy is simpler and quicker and can be used by people with low income and few assets. Full Administration Bankruptcy covers all other circumstances.

- **Protected Trust Deed** – a more flexible form of bankruptcy where the trustee is an insolvency practitioner in private practice. To enter a Protected Trust Deed, someone must have sufficient assets or income to pay the trustee’s fees and offer some level of payment to creditors.

- **Debt Arrangement Scheme** – allows people to pay their debts in full over a longer period of time. There is very limited provision for debt write off in the Debt Arrangement Scheme, so people must have sufficient surplus income to pay their debts in the longer term.

Note though that most people in debt do not enter a statutory debt solution. Instead, they make reduced payments to debts through informal agreements with creditors.

Bankruptcy will be the main option for people on low incomes as they will lack any surplus income to pay fees or repay debts in full. However, there can be circumstances where a Protected Trust Deed or the Debt Arrangement Scheme could be used.

Issues for Panel 1

Delivery of money advice services

Impact of the pandemic and cost of living crisis

Before the pandemic, several pieces of research suggested that demand outstripped availability for money advice services. The Scottish Government's Debt Advice Routemap for Scotland (2019) acknowledged concern about demand and how this linked to low morale and high staff turnover among money advisers.

The Committee heard from frontline advisers in its last evidence session that services were now stretched to breaking point. This meant long waiting times for appointments, some services having to prioritise clients in crisis over longer-term interventions and burnt out advisers.

Several respondents to the Committee's call for views on low income and debt problems also highlighted that the worst was likely still to come. People's financial circumstances are likely to have become worse over the course of the pandemic. In addition, protections created by emergency coronavirus legislation and creditor forbearance have shielded people from the effects of debt. However, these protections are now being rolled back.

A YouGov poll conducted for Citizens Advice Scotland suggested that, during the pandemic, more than 60,000 people in Scotland had either got into debt for the first time or seen existing debts get worse.

The cost of living crisis is also expected to exacerbate debt problems. The Committee has heard that people with low incomes and debt problems may already struggle to meet essential expenditure. As costs increase, the problem is only likely to get worse.

In order to meet demand for money advice, there have been calls for "channel-shifting" from face-to-face advice provision to telephone and online. Witnesses at the last evidence session highlighted successful delivery of remote money advice. However, the general view of respondents to the call for views was that the emphasis should be on "channel choice".

Funding for money advice services

Money advice services are mainly funded by local authorities, and funding has been cut significantly over the past ten years. There are other sources of funding – e.g. from the Scottish Government, charities and creditors themselves.

The UK Government places a levy on providers of credit, which is used to support money advice. Spending the money raised by that levy was devolved to the Scottish Government in 2019. In its Debt Advice Routemap for Scotland (2019), the Scottish Government estimated that this would provide around £4million per year to the money advice sector in Scotland.

At its last evidence session, the Committee heard that funding was often short-term (usually one year) and project-based. This made it difficult to build sustainable services, as well as creating job insecurity for money advisers. Some witnesses called for the provision of debt advice to be a statutory duty on local authorities.

Barriers to accessing money advice

Respondents to the call for views highlighted a range of barriers to people accessing money advice. The key issues were:

- digital exclusion
- not knowing where to go for advice
- stigma.

The Committee has heard how digital exclusion comes in several forms. It can be about lack of “kit, connectivity or confidence”. However, people who are in debt and who were previously able to use online services may also have to cut back because of the pressures on their budget.

Digital exclusion makes accessing services more difficult, but it also creates barriers to managing finances and getting basic information about dealing with debt. Witnesses at the last evidence session described how losing online access makes everything else worse.

Not knowing where to go for advice may mean people’s debt problems get worse. The Poverty Alliance highlighted that, in research it had carried out into accessing welfare and debt advice in Edinburgh, “almost all” participants did not know where to go.

A theme from the call for views was the importance of trusted relationships in the advice process. It was argued that people were more likely to approach services they were already in contact with for advice – such as community groups, health professionals or other support services. People were also more likely to feel comfortable opening up about their problems in these situations.

As these services were unlikely to be able to provide in-depth money advice, they would need to refer on to specialist services. However, it is not clear how aware various support groups or professionals are of the need for money advice, or where to make appropriate referrals. It is also not clear whether specialist services can meet demand.

Issues for people experiencing low income and debt

Changing profile of debt clients

Respondents to the call for views, and witnesses at the last evidence session, described the issues facing low income debt clients. They may have “deficit budgets", meaning they can't afford to meet essential expenditure, even after support with income maximisation and budgeting.

There are no easy solutions for people in this situation, so the advice process is complex and time-consuming for both clients and advisers. Because clients may have no option but to run up debt to access essential services, even bankruptcy may only provide temporary relief.

The Committee has also heard that the types of debt people have has moved away from credit cards and loans (although those debts may still feature) to debts for essential services, such as rent, fuel and council tax. Debts like these – where there are significant consequences from non-payment for the client – are often called "priority debts" by money advisers.

Non-payment of priority debts can result in harsh enforcement – such as eviction or being cut off from fuel supplies. A related issue is that the enforcement of public sector debts tends to be less flexible and more severe than standard consumer credit debts.

Council tax is an example of this, where unpaid bills move quickly to enforcement via "summary warrant" (an expedited enforcement process for public sector creditors). This incurs a 10% surcharge, with the likelihood of formal enforcement ("diligence") via options such as bank arrestment or earnings arrestment increasing.

Experiencing debts related to rent arrears, council tax and fuel makes it more likely that the client will end up in a crisis situation. This, in turn, makes it more difficult to maintain a budget where there is no flexibility to deal with income shocks. It also creates more work for money advisers.

Access to debt solutions

Statistics from the Accountant in Bankruptcy show that, broadly, the number of bankruptcies have remained fairly steady over the course of the pandemic. In contrast, the number of Protected Trust Deeds have decreased and the number of Debt Payment Programmes under the Debt Arrangement Scheme have increased.

The number of moratoriums on diligence (creating a legal pause on creditor enforcement action while someone seeks money advice on the most appropriate debt solution) has increased markedly. There were 190 moratoriums in the first quarter of 2020/21 (the start of the pandemic) and 727 in the last quarter of 2021/22. The moratorium period was increased from six weeks to six months by emergency legislation to provide protection for people in debt (and to reflect the increased difficulty in accessing money advice as services stopped face to face contact).

The main statutory debt option open to people on low income is bankruptcy, as they may not have sufficient surplus income to access Protected Trust Deeds or the Debt Arrangement Scheme. Informal solutions are also used – such as negotiating lower repayments with individual creditors.

Direct deductions from social security benefits can be used to repay certain debts, including rent, council tax and water and sewerage charges. Concerns were raised in the call for views that a larger proportion of Universal Credit can be taken towards debt repayments than with previous benefits. This can make it difficult for people to managed essential expenditure.

Witnesses also highlighted that people can struggle to maintain payments towards current liability because of direct deductions in relation to arrears. This was a particular problem for council tax.

Key issues for people with low income and debt problems

Witnesses at the last evidence session highlighted the following issues:

- The impact of the pandemic followed by the cost of living crisis has meant that people have no financial resilience.

- Lack of income was a key issue – so solutions needed to look at increasing income, not just improvements to debt processes.

- Advisers spend significant amounts of time sorting out crisis situations for clients, which cuts into the time they can spend doing proactive or preventative work.

- There are limited options for clients with deficit budgets – support can include accessing help from charities and renegotiating arrears payments to focus on current liabilities.

- Harsh enforcement of public sector debts causes distress to clients and takes up adviser time – and there were questions about whether this was cost-effective.

Suggestions for reform (from witnesses at the last evidence session and the call for views) include:

- increasing the Minimum Protected Balance (the amount left in someone's bank account) in a bank arrestment to £1,000

- reducing the barriers to accessing bankruptcy created by fees (e.g. by removing the fee for Minimal Asset Process bankruptcy or for those who are assessed as having no surplus income)

- creating a financial buffer in bankruptcy and Protected Trust Deeds by allowing people assessed as having surplus income to keep some of it

- removing the debt threshold in bankruptcy so that people aren't prevented from applying because they do not owe enough

- creating more flexibility (for creditors to reduce the payment required) and better co-ordination in relation to various types of earnings arrestment

- making other statutory debt solutions more accessible to people on low incomes (e.g. increasing opportunities for debt write-off in the Debt Arrangement Scheme)

- improvements to council tax billing, collection and enforcement processes – with a move away from inflexible, punitive approach to one which looks at individual circumstances

- more work to highlight benefit entitlement and encourage take-up

- consideration of writing off some public sector debt.

Witnesses and respondents also highlighted problems with creditors (and, in some cases, court officers) failing to recognise that clients were protected by a statutory debt solution. Some creditors had poor understanding of the effects of the Debt Arrangement Scheme. And there were examples of clients being subject to debt enforcement when they were protected by being in a statutory debt solution.

A particular problem discussed by witnesses at the last evidence session was creditors selling on debt which was included in a Debt Arrangement Scheme, without notifying advisers, clients or the Accountant in Bankruptcy. Advisers had to spend significant amounts of time liaising with creditors to resolve this.

It is common practice for creditors to sell on debt when they judge it too difficult to collect. The debt is sold at a discount, to represent the risk of non-payment. This allows the original creditor to get some return on their money. There are dedicated businesses which specialise in buying discounted debts (and make money by collecting on some of them), including those where the person in debt is in an insolvency procedure.

Questions

Panel 1

Suggested issues to raise:

<u>Theme 1: delivery of money advice services</u>

- **How has the delivery of your service changed between the start of the pandemic and now? Were you able to provide any face to face contact during the pandemic?**

- **What are the advantages and disadvantages of remote delivery – and is a shift to remote necessary to meet demand?**

- **What can be done to improve the funding environment for money advice services?**

- **The role of trusted partners in the advice process has been emphasised to us. Do you think a model where trusted support services or professionals**

make onwards referrals to specialist money advice services is the best way to address some of the barriers to accessing advice?

- **Does your organisation have any other suggestions for addressing barriers like digital exclusion, a lack of knowledge of services and stigma?**

Theme 2: key issues for people with low income and debt problems

- **How has the profile of people using your services – particularly money advice – changed since the pandemic? Have there been changes to the way you deliver your service as a result?**

- **What are the key issues for people with low incomes and debt problems? Do these issues vary for different client groups, for example women and people with specific protected characteristics?**

- **What options are there for people with low incomes to resolve their debt problems?**

- **Have you got any suggestions for reform of the legal framework for dealing with debt?**

- **Are there improvements which could be made to the processes and procedures used by creditors which would help people with low incomes and debt problems?**

- **The Committee has been told about issues with creditors understanding the protections created by statutory debt solutions, or undertaking enforcement action when someone is in a statutory debt solution. Is this something your organisation has seen?**

- **Do panellists have any comments on evidence heard last week regarding bank arrestment, reduced fees and increased income disregard in bankruptcy?**

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9 May 2022