HM Treasury, Open Consultation August 2022: Statutory Debt Repayment Plan: Consultation

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For the following reasons, this submission suggests that the introduction of Statutory Debt Repayment Plans (SDRPs) should be postponed, and that the Treasury should re-consult on a revised SDRP scheme after the cost of living crisis has eased:

1. The wrong time

This is nobody's fault really, but it turns out that the consultation on the SDRP is exceptionally ill-timed. One may say that at a time when the Insolvency Service is conducting a review of the wider insolvency landscape[1] the introduction of a new remedy outside the insolvency system is illogical and makes the reform processes even more unpredictable.[2] More seriously, with the Individual Voluntary Arrangement (IVA) and the Debt Management Plan (DMP) the system of England and Wales already has two debt remedies that are based on the completion of a long-term repayment plan. At a time when the cost of living crisis is deepening and households are using all forms of credit available to them to pay soaring food and utility bills,[3] the idea of introducing a third debt repayment solution seems irrelevant or even cynical. Resources should now be focused on supporting those with deficit budgets and providing increased opportunity for debtors to obtain quick and generous relief.[4] The SDRP proposal offers neither and its introduction should be postponed.

2. The wrong starting point

The SDRP consultation should not uncritically copy the debt management industry's established business practice but should seek to reform this system. In its current form, the SDRP proposal perpetuates harmful practice, and misses the opportunity to develop a meaningful alternative to DMPs and IVAs. After the cost of living crisis has eased, the Treasury should re-consult on a revised SDRP scheme.

[1] https://www.gov.uk/government/consultations/call-for-evidence-review-of-the-personal-insolvency-framework/call-for-evidence-review-of-the-personal-insolvency-framework.
[2] We Are Debt Advisers, The proposed Statutory Debt Repayment Plan - Policy Statement (2022).
[3] StepChange, Falling behind to keep up: the credit safety net and problem debt (2022).
[4] See We Are Debt Advisers, 'The proposed Statutory Debt Repayment Plan - Policy Statement' (2022).

Current policy documents uncritically reiterate basic assumptions of the debt management industry. They assume that non-statutory debt solutions, such as DMPs, will always be voluntary on behalf of both creditors and debtors.[5] Following on from this, two further assumptions are made, which are also widespread in the industry. First, it is assumed that none of the existing non-statutory debt solutions - such as DMPs - can ensure creditor compliance or provide legal protection to debtors. The implications of this assumption are far-reaching. Even if regular debt repayments are made over many years under a DMP, debtors are assumed to have nothing to rely on but the goodwill of their creditors. They are assumed to have no formal protection against possible enforcement action by their creditors or against the impact of ongoing interest, fees, and costs on their debts.

Second, it is assumed that due to their non-binding nature, DMPs can at best achieve a stretching out of the repayment period, but they cannot guarantee permanent debt relief. All DMPs are therefore geared towards full repayment of debt.

The above assumptions serve the interests of the debt management industry and creditors but lack a legal basis. English contract law is not debtor friendly and due to the requirement of consideration, for a contract to be enforceable it is a prerequisite that a benefit that must be bargained for between the parties. The requirement of consideration is problematic in all cases of contract variation and it is a long-established rule (Pinnel's Case[6]; Foakes v Beer[7]) that a creditor is not generally bound by a promise to a debtor to forego the balance of a debt. This rule is subject to exceptions, however, and despite the consideration requirement the binding force of composition agreements is well-established.[8] Based on their nature as a debt composition, DMPs should therefore be legally binding under contract law and as such, they could not just provide for a stretching out of the debt repayment period, but also for debt relief. A similar conclusion could also be reached by the application of the doctrine of promissory estoppel.[9] If therefore the SDRP introduces a legally binding debt repayment solution, the legislature provides no favour to debtors, but it only reinstates their position under contract law. If the SDRP regulations continue to deny a debt relief option outside of formal insolvency, they support the debt management industry in undermining the contractual rights of debtors.

The SDRP consultation does not only fail to scrutinise the legal foundations of repayment plans, but it also fails to subject them to a comprehensive policy assessment. As DMPs, SDRPs are designed to meet the objectives of their potential providers (e.g., StepChange and Payplan) and creditors, but they neglect the interest of debtors, as well as those of society at large. As regards the latter, it is alarming that the consultation paper fails to recognise the role of debt solutions in reducing the macro-economic externalities of household over-indebtedness. As the Bank of England has announced yesterday, this country is now entering

[5] HM Treasury, Statutory Debt Repayment Plan, Impact Assessment, 5.1.
[6] 1602) 5 Co Rep 117a.
[7] [1884] 9 AC 605.
[8] See Chitty on Contracts 34th Ed; Good v Cheesman (1831) 2 B. & Ad. 328.
[9] Central London Property Trust Ltd v High Trees House Ltd [1947] KB 130; Collier v P&MJ Wright (Holdings) Ltd [2007] EWCA Civ 1329.

a period of recession. Moreover, after the easing of the cost of living crisis households will be overburdened with debt,[10] and the depth and length of this recession will critically depend on our ability to overcome the debt overhang problem and to reinvigorate consumption. As the discussion of any other debt remedy, the discussion of the SDRP should be informed by the considerations of the relevant economic literature[11] and their quest for generous debt relief, which is deemed to be essential for generating aggregate demand and economic growth.

3. What is the statistical record of debt repayment plans???

The idea of a statutory debt repayment plan, which is based on the business practice of DMPs, is not new, but it forms the basis of the Scottish Debt Arrangement Scheme (DAS), which, in turn, has served as a model for the SDRP. If we are seeking to assess the potential impact of SDRPs, first and foremost we should therefore look at statistical data on the performance of the DAS, and unfortunately, these look bleak:

DAS Table 3: Number of Debt Payment Programmes (DPPs) under the Debt Arrangement Scheme (DAS) by outcome, duration, and length of survival, 27 July 2022[12]

Outcome Status (by approval year)	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
total	2,043	2,233	2,318	2,544	3,130	3,677	4,489
completed	691	626	500	329	229	94	16
% completed	34%	28%	22%	13%	7%	3%	0%
life	496	811	1,057	1,523	2,281	3,015	4,181
% life	24%	36%	46%	60%	73%	82%	93%
revoked	855	794	757	691	620	568	292
% revoked	42%	36%	33%	27%	20%	15%	7%

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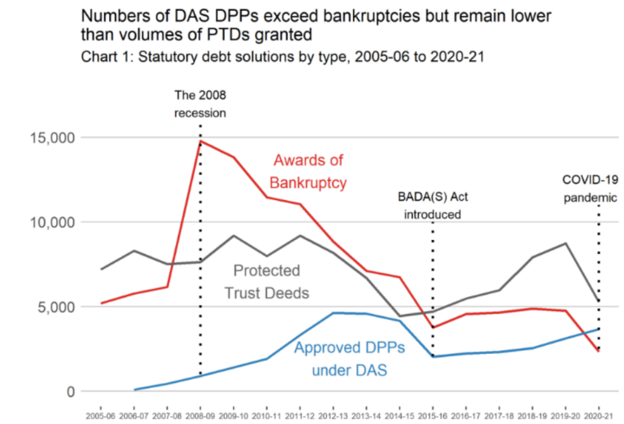
[10] See 1.

[11] See for example, Mian and Sufi, *House of Debt* (2014); Turner, *Between Debt and the Devil: Money, Credit, and Fixing Global Finance* (2015) 3; Mian, Straub and Sufi, 'Indebted Demand' (2021); Korinek and Simsek, 'Liquidity Trap and Excessive Leverage' (2016) 106 American Economic Review, 699; Cynamon and Fazzari, 'Inequality, the Great Recession and Slow Recovery' (2016) 40 Cambridge Journal of Economics, 373; Russo, Riccetti and Gallegati, 'Increasing Inequality, Consumer Credit and Financial Fragility in an Agent Based Macroeconomic Model' (2016) J Evol Econ, 26; Wisman, Wage Stagnation, Rising Inequality and the Financial Crisis of 2008 (2013) 37 Cambridge Journal of Economics, 921; Kumhof and Rancière, 'Inequality, leverage and crises' (2010) IMF Working Paper WP/10/268; Perugini, Hölscher and Collie, 'Inequality, credit and financial crises' 2016 (40) Cambridge Journal of Economics, 227.

[12] Accountant in Bankruptcy (2022) Ad-hoc Statistics Release: The Debt Arrangement Scheme (DAS) cases. Available at: Scottish Statutory Debt Solutions Statistics: Financial year 2021-22 - excel tables; just email aib_statistics@gov.scot, if you should have problems to find/ understand any of the material.

As you can see from the table above, on 27 July 2022, of the 2,043 debt repayment programmes that had been approved in the year 2015-16, 42% had failed and 24% were still ongoing. This means that only 34% of the programmes that had been approved 7 years earlier had been successfully completed. In contrast, for two-thirds of DAS users, the process did not result in them becoming debt-free, although their participation in the programme generated revenue for the programme providers and returns for their creditors. These results are not atypical. Rather, older DAS data sets show that failure rates of over 40% and success rates of only 30-40% are the norm.[13]

The above data needs to be seen in the wider Scottish context. The DAS has not been used excessively but it is only one of several insolvency solutions:



Source: Scottish Statutory Debt Solutions Statistics: April to June 2021 (2021-22 Quarter 1)

In addition, the Impact Assessment indicates that informal DMPs still remain more popular than formal repayment plans under the DAS.[14]
The only conclusion that can be drawn from the Scottish experience, therefore, is that SDRPs are a potentially very dangerous product that only provides a debt solution in rare cases. This type of remedy may be suitable for a very small minority of people in debt, but although it has been used restrictively in the Scottish context, it has harmed the majority of its users.
Extremely long repayment periods, failure rates and ultimately the denial of debt relief not only harm the well-being of debtors, but also the economy, as debtors are not enabled to return to positions in which they can resume spending.
It is remarkable that the consultation process has not yet analysed the above data. Quite obviously, the outcomes of the DAS look so terrible that they should call the whole project of the SDRP into question. We should not proceed with the SDRP project until we have a clear prospect that, unlike the DAS, it can provide a sustainable debt solution. At the moment this

[13] Accountant in Bankruptcy (2021), (2020), (2019) Ad-hoc Statistics Release: The Debt Arrangement Scheme (DAS) cases.
[14] Over the last five years, 52.6% of all Scottish debt advice clients, who were recommended either a DMP or a

is not the case; on the contrary, as we will see below, the SDRP is stricter in many areas than the current Scottish solution.

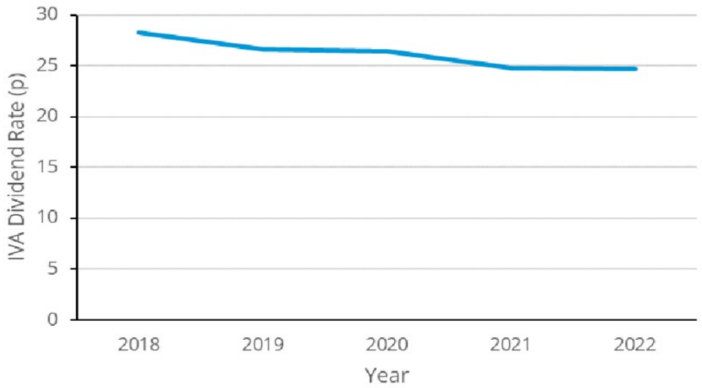
The consultation process is quite right to take account of the experience gained in the DMP market in addition to the experience with the Scottish DAS. Indirectly, the consultation could thus contribute to a growing transparency and potential reassessment of the DMP market. So far, however, this analysis has remained far too superficial. For example, the Impact Assessment claims that about 34% of DMPs fail, but this claim is not supported by any statistical analysis. The Impact Assessment also assumes that 29% of SDRPs will not be successfully completed, meaning that the completion rate of SDRPs is likely to be 5 % higher than that of DMPs. Even if one accepts this assumption, this is a very high failure rate, which would not be unproblematic. However, it is very doubtful that the assumed SDRP failure rate is realistic. SDRPs will have a much lower level of flexibility than the Scottish DAS and, as we have just seen, the DAS failure rate is over 40%.
More serious collection and analysis of empirical data is needed to move forward in this consultation process. We need data on the annual number of DMPs, their providers, their user groups, their annual default rates, their duration, the frequency and duration of payment breaks and, crucially, the success rate of DMPs. All this data is key to understanding whether and how the SDRP could be transformed into a realistic and sustainable debt solution.

4. **There should not be a requirement of full debt repayment.**

As shown in the previous section, full debt repayment is not a realistic option for most debtors. The drafters of the SDRP regulations should therefore consider breaking with the current practice in the DMP market and offering the option of debt relief. This approach would take into account the economic need for household debt relief and the position of contract law, which also allows for an agreement on permanent debt relief. Most importantly, it would allow for a fair balance between the interests of debtors and creditors. The debt relief option under the SDRP would be designed to improve creditors' returns compared to their returns under formal insolvency solutions, especially IVAs. On the other hand, SDRPs would offer debtors some debt relief that is not available under DMPs.

Unlike the SDRP, the Scottish DAS allows for a composition of debt if the debtor has already paid back more than 70% of her debts or if she has been paying for 12 years. The SDRP should expand both aspects of this provision to support more realistic composition agreements and to create a remedy that is more successful than the DAS.

According to TDX data published in the Insolvency Service's *Call for evidence: Review of the personal insolvency framework* (2022), IVA returns to creditors in 2021 were on average 24%.



If an SDRP achieves a significantly better creditor return than would be possible under any other insolvency solution, it should be accepted as fair and reasonable. Thus, if the debtor offers a repayment rate of 30-50%, this should be sufficient for the Insolvency Service to approve the arrangement, depending on the circumstances.

Furthermore, as in Scotland, the possibility of debt relief should be made dependent on the length of the repayment period. If the debtor agrees to a five-year debt repayment period, this should be rewarded by the promise of debt relief at the end of that period. A five-year repayment period is usually the same as the IVA repayment period and it is much longer than the duration of repayment periods under other insolvency solutions. Since, in the case of an IVA, creditor repayments are significantly reduced by provider's fees (currently averaging around £4,000), creditors would benefit significantly from the introduction of the SDRP process, despite the promise of debt relief.

5. **There should be a limit on the length of debt repayment plans, which is significantly shorter than 10 years.**

Long-term debt repayment plans may be producing modest income for individual creditors, but one must really question whether it is acceptable to have individuals shackled to a repayment plan for many years.[15] Long-term living at subsistence level affects the life quality of debtors and their families and has effects on their health and well-being. Most seriously, as seen above, there is always a very severe risk that long-term repayment plans will fail and that they will ultimately leave their users in a state of over-indebtedness. Countering these arguments, one may suggest that people enter these plans on the basis of a free decision and should usually know what is best for themselves. Experiences with DMPs and IVAs suggest, however, that individuals may commit to long-term repayment plans because they have time-inconsistent preferences or are over-optimistic. Consumer debtors usually prefer the least

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[15] See Iain Ramsay, 'Is the Scottish Debt Arrangement Scheme (DAS) a Success?' https://creditdebtandinsolvency.wordpress.com/2018/01/25/is-the-scottish-debt-arrangement-scheme-das-a-success/.

formal or least invasive debt remedy, and the availability of an SDRP might tempt them to choose this solution even if an insolvency solution would be more appropriate.
As the above data concerning the DAS show, this danger is very real. Over 60% of the users of this scheme have failed to resolve their debt problem after seven years and due to exorbitant revocation rates, many of them will never succeed under this scheme. It is very likely that for the majority of DAS users an alternative debt solution would have been more suitable and that their decision in favour of the DAS was a mistake.

Even if debtors and creditors rationally agree on the conclusion of a long-term repayment plan, this agreement may have negative externalities. As indicated above, overly long repayment periods increase the debt overhang problem, as they prevent debtors from returning to positions in which they can resume spending; the use of long-term repayment plans will deepen and prolong the forthcoming recession.
In light of these arguments, it seems that the limit on the duration of debt repayment plans should be significantly stricter than the 10-year limit proposed in the SDRP regulations. The Australian legislature has taken this approach by limiting the duration of repayment plans to 3 years in general and 5 years for homeowners. This submission acknowledges that there are several arguments that can be put forward against the introduction of such strict time-limits. First, strict time-limits are always arbitrary and curtail the discretion of individual debt advisors. As currently proposed, the appropriateness of SDRPs should therefore be clarified through the instrument of guidance, but this guidance should stipulate that under normal circumstances repayment plans are only acceptable if they can be completed within a period of 3 -5 years. In some cases, if the debtor is a homeowner and has a very stable income, longer repayment periods may be acceptable.
Secondly, it may be suggested that time-limits may have an exclusionary effect, as they will deprive low-income groups of the SDRP remedy and push them into formal insolvency. If, as suggested in the previous section, the requirement of full debt repayment was relaxed, this would also mitigate the exclusionary effect of time-limits. Furthermore, usually it is just not desirable for low-income clients to enter into prolonged and ultimately unsustainable repayment agreements. This type of client should receive swift debt relief under personal insolvency and lobbying should focus on providing a better framework for such debt relief.

6. There must be a greater level of flexibility.

The SDRP proposes lengthy repayment terms but does not provide sufficient flexibility to accommodate changes in the circumstances of debtors over these. In this context, we could learn from the Scottish DAS regulation that offers greater flexibility than the current SDRP regulations in several important respects.

First, this concerns the possibility of long-term payment breaks, enabling debtors to defer payments for a period of 6 months, if they suffer from a 50% decrease of disposable income resulting from:

(a) a period of unemployment or change in employment;

(b) a period of leave from employment for maternity, paternity, adoption or to care for a dependant;

(c) a period of illness.[16]

Any of the above circumstances can be unpredictable, and over a period of several years these things happen in people's lives. Revoking the SDRP in these circumstances would be highly unfair to the debtor, it would not be in the interest of the general public, and it may not even be in the interest of their creditors. Consideration should also be given to making the above catalogue more flexible to allow for the inclusion of other emergency situations.

Also, the SDRP regulations should follow the Scottish example by dropping the limit of £500 on additional credit. This limit is likely to be exceeded in many daily life situations and may inadvertently lead to the revocation SDRPs. The lack of a clear definition of the term "credit" in the context of the regulations increases the level of uncertainty. Furthermore, the need for debtors to seek the adviser's permission if they want to exceed the £500 limit is an anathema to advisers and misunderstands their role and responsibilities. Advisers receive instructions from clients and act, as a solicitor might, on their behalf. They do not tell their clients what to do but rather offer advice, guidance and information. Maintaining the permission requirement would therefore fundamentally change, for the worse, the relationship between advisers, and the people they are engaged to help.[17]

The absolute credit limit of £2,000 may create problems too. For example, this limit falls short of the amount needed to purchase a second-hand vehicle. Homeowners may face similar issues, for example, if they need to replace a boiler or have to conduct other essential maintenance. Also, self-employed clients will be disproportionately affected by this rule. As a way to resolve these issues, the legislature should consider the following measures:

- The upper limit on additional credit should be raised significantly, for example to £5,000.

-The definition of credit should be clarified and explicitly exclude insurance contracts paid by monthly instalments, and utility supplies.

[16] Debt Arrangement Scheme (Scotland) Regulations 2011, r. 37.

[17] We Are Debt Advisers, 'The proposed Statutory Debt Repayment Plan -Policy Statement' (2022).