Election 2017: Turning round lives held back by debt

A challenge to UK political parties to tackle problem debt in the next parliament

The problem debt challenge

This briefing sets out a challenge to our political parties and policy makers: to make a clear commitment to tackle problem debt in the next parliament. Household debt doesn't get the same focus at Election time as health, the economy, housing, education or welfare. But debt and its root causes are a common theme across many of the big economic and social issues that the next Government will have to confront. Dealing with problem debt head on will improve opportunities for children and young people, help working people get on at work, reduce the incidence of mental health problems, and reduce strain on hospitals and GPs. This briefing explains how.

2.9 million people are struggling with severe debt problems right now. Over 9 million more are showing signs of financial distress[1].

At StepChange Debt Charity, we are contacted by someone struggling with debt every 53 seconds[2]. So every day we see the devastating harm that problem debt is creating across the UK.

The strain of dealing with problem debt shatters self-confidence and makes people ill: When we asked our clients 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. 53% said that they didn't feel they were worth much as a person[3].

Problem debt harms children and families: Nine in ten parents in indebted households told us they had cut back on essentials for their children in order to keep up with debt repayments. More than half of children aged 10-17 in families with problem debt said they had been embarrassed because they lacked things their peers had. Children in families with problem debt were twice as likely as other children to say they had been bullied at school.

57% of indebted parents said debt put their current or most recent relationship under strain. 7% said their relationship broke up because of debt[4].

Problem debt damages jobs and productivity: 43% of StepChange Debt Charity clients polled said that being in debt led to them being unable to concentrate at work.15% say that their debt worries led to changes in attendance such as arriving late or taking more time off

2% said that it led to them losing their job. If scaled up to the 2.9 million people with severe debt problems this means nearly 60,000 people are out of work as a result of problem debt[5].

It makes it harder for people to find work or move to better paid work: 61% feel 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[6]

The harm that debt causes in ill health, lost productivity, family breakdown and thwarted aspirations creates a cost that falls on UK society as a whole. We estimate that the external social cost arising from 2.9 million people in serious financial difficulty to be £8.3 billion[7].

Improving the resilience and financial health of households

Hopes for a strong economy and a just society rest on the financial health and resilience of UK households. But confidence can't spread to households who are forced to borrow to pay bills, who worry about spiralling bank charges, or who fear the bailiff's knock on the door.

We know that financial difficulties are most often triggered by a negative life event. Seven in ten StepChange Debt Charity clients say the main cause of the debt problem was job loss, reduced work income, illness, relationship breakdown or business failure.

With 14 million people experiencing a negative change of circumstances over the last year, a constant stream of new households are falling into difficulty.

Some households are more vulnerable than others. Our research found that people with insecure jobs are twice as likely to experience an income shock. Households with lower incomes and households with children are significantly more likely to experience serious debt problems[8]. One in four people with a mental health problem is living with debt or arrears[9].

Too many households have too little to fall back on. A £1,000 pot of rainy day savings provides a powerful protection against debt, yet over 7 million households lack this[10]. In contrast some 6 million households use credit as a safety net to cope with income shocks, a strategy that makes them 20 times more likely to fall into serious problem debt.

Lower income working households are also using credit to try to make ends meet. Some 8.8 million people turned to credit to pay for everyday household expenses in the last year. Over half of these were in employment, 41% in full time work[11].

A direction of travel on tackling problem debt

With inflation heading upwards, the Bank of England predicting a squeeze on real household income growth this year[12] and consumer lending approaching pre-crash heights, the pressures on households, and lower income working households in particular, are not likely to reduce anytime soon.

So, despite record levels of employment and a return to economic growth, the financial health and resilience of households most vulnerable to debt is not going to improve just by itself. People living with insecure work, low pay and rising living costs cannot build the resilience to weather shocks and plan for the future.

These households need help from the next Government through policy action to tackle the causes of household debt head on and deliver better help for those households struggling now. So we are calling for a commitment from UK political parties to address four key drivers of problem debt

Households need secure and sufficient incomes to make ends meet

We estimate that some 3 million people fell behind with household bills in the last year, and 2.5 million used credit to keep up with household bills[13]. 40% of people seeking help from StepChange Debt Charity have arrears on essentials like rent, fuel and council tax. The number of people we see struggling with household bills has doubled over the last five years. Some 29% of StepChange Debt Charity clients simply do not have enough money to make ends meet or get back on track with household bills even after budget counselling. 40% of these households have someone in full or part time work.

So we call on the next Government to develop a strategy to ensure that working households are able to afford basic household bills like rent, fuel and council tax without having to use credit. ***The challenge is to halve the number of households struggling with bills or using credit to pay bills by the end of the next parliament.***

Households need effective safety nets against shocks

Our research shows that income shocks are common and can be devastating for lower income households in particular. Welfare reform has been focused on helping people into work, but households need help to manage through periods of income shock. Benefits and tax credits provide an important safety net for financially vulnerable households; without them over two thirds or our clients would have negative budgets, including 55% of clients in working households.

But the system is not helping enough households through periods of reduced or low income. Only around two in three of our clients in receipt of Employment and Support Allowance and a half of those who receive Jobseeker's Allowance are able to meet their essential costs. Around 17% of our clients in receipt of child tax credits with three or more children showed a negative budget; we estimate that the two child limit could increase this to 90%.

The administration of welfare benefits can also be a driver of debt problems - 11% of people who applied for benefits said the waiting time for benefits to be paid was a key factor that meant they didn't have enough money to make ends meet[14].

The welfare system is no longer working effectively for households who are most vulnerable to common income shocks. So we call on the next Government to develop a social insurance strategy that does a better job at helping households through periods of reduced income. ***The challenge is to significantly reduce the 6 million people using credit to cope with income shocks.***

Build up households' financial resilience

The financial resilience of UK households is too low. A survey of lower income households seeking help from StepChange Debt Charity found over three quarters facing an unexpected cost at least once a year. Without a pot of savings to draw on, a significant number cut back spending on essentials (37%) or borrowed money (21%), coping strategies that can increase vulnerability to debt[15]. The Help to Save scheme due to commence in 2018 aims to help to estimated 500,000 lower income households to save for a rainy day in the first two years. This is a good start but there is still a long way to go to meet UK households' minimum precautionary savings need, let alone build financial resilience more generally. ***The challenge for the next Government is to develop a strategy to improve household resilience that will reduce the 8.8 million households using credit for essentials.***

Break the vicious circle of debt

We know that many households struggle to cope with financial difficulties for long periods before finally being overwhelmed by problem debt. Around a half of people seeking help from StepChange had been worrying about debts for a year or more before seeking advice. This is the period where debt problems can spiral out of control if people don't get the help they need.

A key part of the help that people need is forbearance from their creditors. 60% of StepChange Debt Charity clients said that their financial situation stabilised once all of their creditors agreed to freeze further interest, charges and enforcement action. But no one said their finances had stabilised in cases where creditors had not agreed to give this help. Around a third of our clients said their creditors had not offered this help and none of them said their finances stabilised.

The consequences are clear: Around six in ten of those that did not get help they needed from their creditors went on to take out more credit to try and cope with their debt problems. 29% said that a creditor's demands prompted them to pay that bill and fall behind on other bills and 28% said the associated stress made it harder for them to apply for new or better paid work[16].

People struggling with financial difficulties need a better guarantee of help if we are to break the vicious cycle of spiralling debt. ***The challenge for the next Government is to deliver the better protection that people in financial difficulty need to regain control of their finances. This must include a commitment from the Government itself to improve its own practice as a creditor.***

Ideas for action now

By building our understanding of the problems that our clients have experienced, StepChange Debt Charity has developed a number of specific policy proposals that the next Government can implement to quickly get much needed help to households trapped in problems debt.

1. A breathing space scheme for hard pressed households

We know that getting the right help at the right time is crucial for people to recover from financial difficulties. Recovery is dependent on getting effective protection from three key drivers of worsening debt problems: further interest and charges that inflate debts; pressure to meet unaffordable repayments; and collection and enforcement action by creditors. Currently in Scotland, the Debt Arrangement Scheme offers such protection, but the same level of protection isn't available in any other part of the United Kingdom. So we urge Westminster to look at adapting aspects of the Scottish model to help those with debts. We are calling for a new statutory breathing space scheme that will provide:

- A period of protection against further interest, charges, collection and enforcement action for up to one year while people benefit from debt advice so they can stabilise their financial situation and start to resolve their debts; and
- Continuing protection from further interest, charges, collection and enforcement action where people are keeping up agreed affordable debt repayments.

2. Access to safer and more sustainable credit

8.8 million households are using credit for everyday living expenses, including 1.1 million having to turn to high cost credit. Households using credit to get by are significantly more likely to get into financial difficulties.

Problem debt is primarily driven by persistently low incomes and income shocks, like job loss or relationship breakdown, that can undermine a household's finances.[17] Those using credit to cope after an income shock are twenty times more likely to fall into problem debt than those who were able to adjust their finances without credit.[18]

Those having to turn to credit to meet the cost of essentials need access to safer and more sustainable credit options. This should include further action to tackle harmful existing credit products and better alternatives to high cost credit:

Action to tackle harmful credit

Policy action to tackle the harm caused by payday loans was welcome and effective. But there are other high cost products still causing harm to struggling households. Charges for unauthorised overdrafts can be more expensive than a payday loan.[19] Rent to own agreements can see hard pressed households pay more than double for household goods compared to those who can shop in mainstream outlets.[20] Logbook loan borrowers can end up repaying substantial amounts and still see their car taken away. The next Government needs to address the harm caused by all forms of high cost credit used by financially vulnerable households through:

- An independent and fair cap on unarranged overdraft charges.
- Extending the 'total cost cap' principle from payday loans to other high cost credit products to protect borrowers from excessive costs.
- Legislating to bring logbook lending up to modern standards of consumer protection.

A better alternative to high cost credit

Despite stronger regulation of payday lending and support for the growth of credit unions, there are still 1.1 million people having to use high cost credit to get by. The scale of alternative lending is still limited and the availability of no-interest loans and grants for the most financially excluded has reduced through cuts to the Social Fund. Previous research highlights the importance of the discretionary Social Fund that was used by 21% of people in the lowest income quintile[21]. The local welfare system that replaced it faces funding constraints and is not widely enough used. Our 2016 research found only 1% of people who needed 'safety net' credit using local welfare provision, compared to 8% using payday loans and 63% using credit cards[22].

Provision of affordable alternatives to high cost credit can be increased by:

- Government bringing together the investment and innovation potential of community lenders, other third sector affordable credit providers and accessible FinTech solutions.
- Government introducing or underwriting the development of a new scheme for low and no interest loans and grants to help the most financially excluded who struggle to safely access any form of commercial credit. This could be achieved in partnership with commercial lenders and the voluntary sector, following the Australian example of Good Shepherd Microfinance that has helped over 100,000 people avoid high cost lenders.

3. Help households build rainy day savings to protect against shocks

The odds of a family facing problem debt is cut by 44% if they have cash savings of £1,000. For families with a lower income the chance of debt is reduced even more. Helping every household to save £1,000 could reduce the number in problem debt by 500,000[23].

- The next Government should set a target of all families having at least £1,000 in rainy day savings. This would focus policy attention on lower-income savings, and give families a clear and achievable target to help overcome the inertia and procrastination that prevents many from saving.

Improve Help to Save

Help-to-Save recognises the value of helping low income families build a strong financial buffer.

Yet only one in seven people eligible for Help-to-Save is expected to take advantage of the scheme. Some 3.5 million people in receipt of working tax credit or universal credit are eligible, yet the Government's impact assessment says it will probably only reach 500,000 people by 2020/21.

- The next Government must tackle the anticipated low take-up of Help-to-Save and ensure the maximum benefit among eligible households.

Commit to auto-enrolment to help families build short-term savings

Almost 15 million people cannot save. To help all these families more innovative approaches are needed.

The most effective approach would be to harness the existing pension auto-enrolment system, adapting it so pensions can include an accessible precautionary savings pot.

There are clear advantages in using the system as a basis for increasing accessible savings:

1. It is already working effectively with a suitable system of earnings thresholds and eligibility requirements.
2. It contains a proven nudge –using inertia to deliver good outcomes.
3. It contains a match – employer and tax contributions boost individual saving.

Adapting the system would not be overly complicated for employers or pension funds as it would be based on the existing auto-enrolment framework. Analysis shows that the impact of the change on retirement earnings would be limited

- The next Government should commit to adapting the employer-led auto-enrolment framework to help people build a short term pot for a rainy day.

4. Significantly improve the conduct of public sector creditors

In a 2016 survey, StepChange Debt Charity clients said that public sector creditors were most likely to treat them unfairly[24]. Half of respondents said they had been treated unfairly by bailiffs (around a half of debts enforced by private bailiffs are council tax arrears[25]). More than 40% said they were treated badly by a local authority creditor, and HMRC debt collection practices were rated no better than payday lenders.

We know that unfair creditor practices can drive people further into debt. Six in ten of those people that did not get the help they needed from their creditors went on to take out more credit to try to cope with their debt problems, while 29% said that a creditor's actions prompted them to fall behind on other bills.

We call on the next Government to significantly improve public sector creditor practices:

- Introducing an independent statutory regulator to raise standards among individual bailiffs and bailiff firms. This should be accompanied by a free, clear, transparent and accessible complaints procedure for members of the public.
- Introducing a statutory code for public sector debt collection to ensure that:
    - Standards and oversight are raised to at least match those applying to consumer credit lenders – payday lenders operate to higher standards than public creditors.
    - Public sector creditors do not pass anyone for enforcement who has been assessed as being in vulnerable circumstances.
    - Good practice guidance for the collection of Council Tax arrears is legally binding upon local authorities; including a requirement to prove efforts to arrange an affordable repayment plan before pursuing people through formal enforcement action. The proportion of people we see with Council Tax arrears has grown significantly in recent years. People facing an unaffordable payment demand for Council Tax are almost three times as likely to borrow more money and almost 50% more likely to fall behind on other bills to try to meet that demand.

[1] StepChange Debt Charity analysis of YouGov online survey. Total sample size was 5,389 adults Fieldwork was undertaken between 21st and 25th April 2017.   The figures have been weighted and are representative of all GB adults (aged 18+).
[2] StepChange Debt Charity (2017): 2016 Statistics Yearbook
[3] StepChange Debt Charity (2015) Statistics yearbook personal debt 2014
[4] The Children's Society and StepChange Debt Charity (2014) The Debt Trap: Exposing the impact of problem debt on children
[5] 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
[6] StepChange Debt Charity (2015): Held back by debt: How Britain's lack of financial resilience is tipping people into a debt trap
[7] StepChange Debt Charity (2014) Cutting the cost of problem debt: The £8.3 billion challenge. See also: Clifford, J., Ward, K., Ross, C., and R. Coram, 2014. Transforming Lives: A review of the social impact of debt advice for UK individuals and families, evaluated using SROI. Available from: www.stepchange.org
[8] StepChange Debt Charity (2015): Navigating the new normal: Income shocks and financial difficulty
[9] Mind (2011), Still in the red: Update on debt and mental health
[10] StepChange Debt Charity (2015) Becoming a nation of savers: Keeping families out of debt by helping then prepare for a rainy day
[11] StepChange Debt Charity analysis of YouGov PLC online survey. Total sample size was 3,204 adults. Fieldwork was undertaken between 15th-19th December 2016. The figures have been weighted and are representative of all GB adults (aged 18+). Figures have been grossed up, using the ONS 2015 Mid-Year estimates of adults in Great Britain: 49,921,573.
[12] Bank of England (2017): Inflation report 2017
[13] StepChange Debt Charity analysis of YouGov polling conducted April 2017
[14] Navigating the new normal
[15] StepChange Debt Charity (2016) Response to the HM Treasury consultation: Help to Save: consultation on implementation
[16] Safe Harbours
[17] DWP (2017) Improving Lives: Helping Workless Families, Analysis and Research Pack, page 100
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[19] Accessible: press.which.co.uk/whichpressreleases/overdraft-charges-more-expensive-than-payday-loans/
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[22] StepChange Debt Charity (2016) The credit safety net: How unsustainable credit can lead to problem debt and what can be done about it
[23] Becoming a nation of savers
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[25] Ministry of Justice (2013) Transforming bailiff action impact assessment

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For help and advice with problem debts use our online debt advice tool, Debt Remedy: www.stepchange.org