Financial Capability Strategy for the UK

People with financial difficulties

Summary

The Strategy's overall aim in this area is to improve financial capability, thereby reducing the number of people who become over-indebted and enabling more people to resolve their debt problems quickly, securely and sustainably.

Income shocks are the primary trigger for the majority of debt problems, so building the resilience of the many people who are only 'making ends meet', 'at risk of problem debt' or 'unable to keep up' is key. When debt problems do occur, they can escalate but there is scope to spot them earlier. Debt advice is effective but many people with debt problems do not access it early enough, if at all.

The key recommendations are:

- The Money Advice Service should lead work with the advice sector, DWP, housing associations and credit providers to **develop and extend effective methods to reach more of the people who are struggling to keep up so that they can absorb income shocks more effectively**.
- Work across the financial services industry, key creditors and debt advice sector to **identify where there is scope to spot problems earlier, before debt becomes unmanageable**.
- The debt advice sector, creditors and public services work together **to encourage more people with debt problems to seek debt advice earlier**.
- The Money Advice Service to initiate work with the debt sector to put in place **the right formal solutions to enable people to sustainably resolve their debt problem**.
- **Develop best practice for offering 'breathing space' and to encourage take-up of advice across** financial services, utilities and public sector creditors.
- On-going work led by the Money Advice Service with the debt advice sector to drive up quality, consistency and effectiveness of debt advice services, including **ensuring that more debt advice clients also receive money advice to increase their resilience in future**.

This is your opportunity to shape the UK Financial Capability Strategy's approach to helping people who are unable to keep up:

Consultation questions 13: How far do you support the Strategy's aims for people with financial difficulties?

Consultation question 14: What is your view of the recommendations for action relating to people with financial difficulties? How could they be improved?

See the complete list of consultation questions for the Financial Capability Strategy for the UK at **fincap.org.uk**

Context

Being unable to keep up with bills and financial commitments puts people at a significantly increased risk of debt problems. **The Strategy's overall aim in this area is improve financial capability, thereby reducing the number of people who become over-indebted and enabling more people to resolve their debt problems quickly, securely and sustainably**.

Problem debt has a devastating impact on individuals, families and communities. It also has wider costs for local authorities, housing associations, financial services firms and central government. However, debt advice is proven to be effective and has multiple benefits. When people access debt advice they see improvements to their health, their creditors get repaid more quickly and their ability to manage their money in the longer term improves.

The Money Advice Service has a statutory responsibility to work with partners to improve the availability, quality and consistency of debt advice. It will take a leading role in the delivery of this section of the Strategy.

Key facts

- One in two people between 25 - 64 say they find it a struggle to keep up with bills[1]
- Around 7% say they are falling behind or have real financial problems[2]
- Just under 9 million people in the UK are over-indebted[3]

Case study: Harry, 53

Harry lives in Kent where he shares a house with two of his friends. Harry used to be a full-time builder, but in 2010 work started to dwindle then eventually disappeared altogether. He has struggled to find anything but casual work since because of his age and the impact of the recession on the construction industry.

He spent freely while he was working and, just before his work situation worsened, he took out a £12,000 loan to pay for some home improvements. Six months after becoming unemployed Harry separated from his partner and was left with all the debt they had acquired. By continuing to borrow money during this time, Harry made his financial situation more difficult and, living solely off benefits plus the income from occasional casual work, he is unable to decrease his level of debt.

"I barely have enough to keep a roof over my head and buy food, there's nothing I can do."

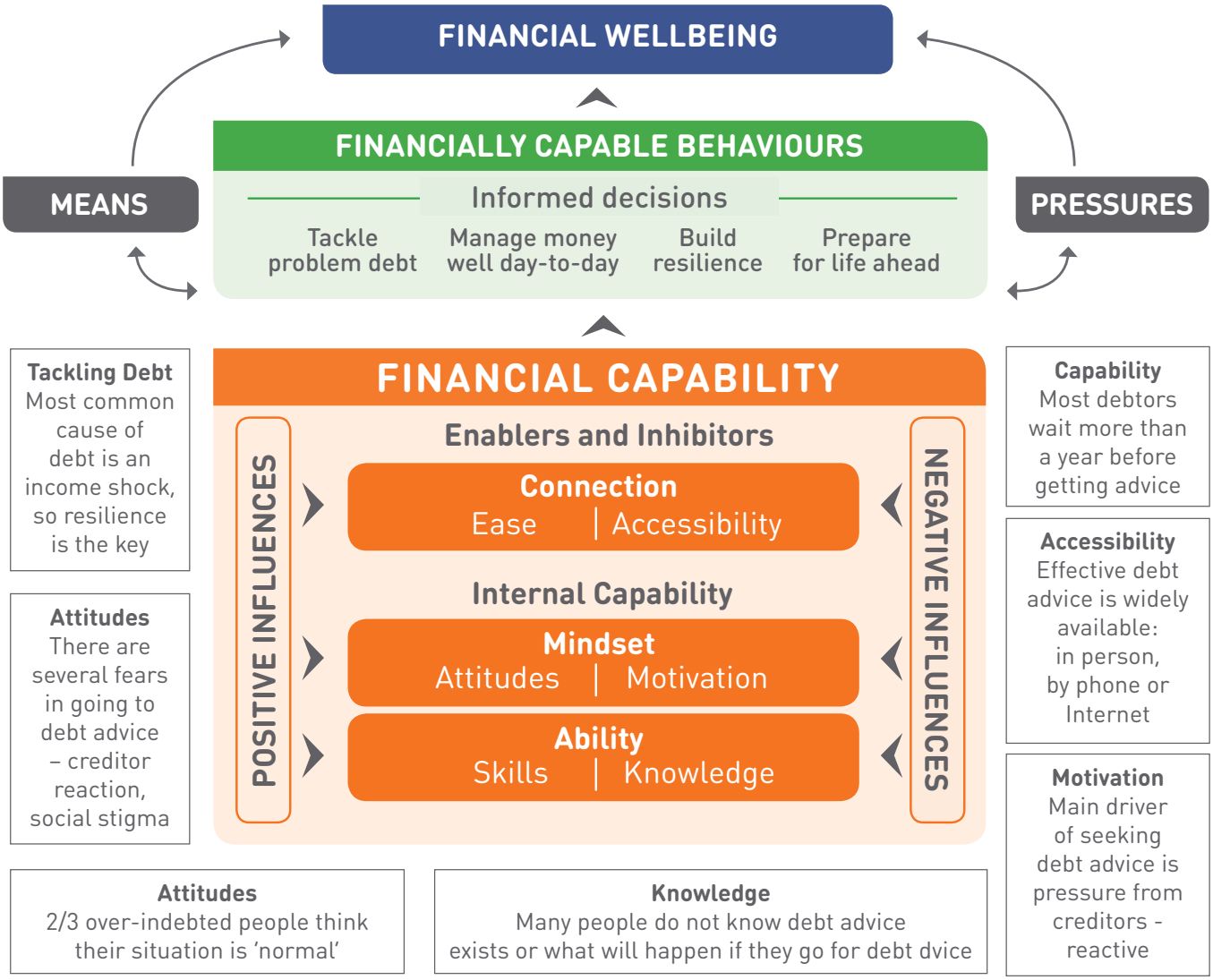
Harry does not like to think about his financial situation so just ignores the repayment demands that he receives. He doesn't believe that this situation will change until he finds stable work again but is unsure how to do this. He knows that one option would be to declare bankruptcy but he is worried about doing this and, in addition, is reluctant to ask for help from anyone as he does not want other people to know about his finance issues or see him as a failure. This feeling of being judged has deterred him from speaking to any advice-giving agency, even the Citizens Advice Bureau which is just across the street from his house.

"I know someone who works in there, I can't let her see me in there, I can't stand in line and admit that I haven't been able to manage my money."

Source: Money Advice Service (2014)

Financial capability: insights and analysis

The Financial Capability Framework diagram below describes some of the most relevant insights about problem debt and suggests how they could be mapped to the financial capability framework set out in the core consultation document.



Key insight 1: Income shocks are the primary cause of the majority of debt problems

The most common cause of over-indebtedness is an inability to cope with the financial consequences of a drop in disposable income either through a fall in overall income[5] or an increase in essential expenditure.[6]

Rising costs of essential spending combined with fixed incomes may explain why older people who do have problem debt are experiencing more significant debt problems than in the past.

There is strong evidence of the financial behaviours and attitudes that can help people recover from the impacts of income shocks, such as better budgeting, controlling spending and using credit responsibly. This suggests that there is scope to take a preventative approach and target financial capability interventions at people with pressured finances in order to boost their financial resilience.

A key challenge will be engaging people before they experience financial problems and recognise that they need help. The Strategy will need to identify points of engagement when the many people who may be vulnerable to income shocks are both reachable and teachable. The introduction of Universal Credit may provide a significant opportunity to talk to around 12 million claimants on mid-low incomes about their money habits.

Key insight 2: When debt problems do occur, they can escalate and spiral very quickly

When debt problems do occur, they can spiral very quickly. Detrimental financial behaviours, attitudes and wider factors can all contribute to escalating debt problems. For example:

- Credit is easily accessible and tempting but can come at a high cost and risk. Evidence suggests that many consumers value the speed and convenience of payday loans despite it being a very expensive and risky way to borrow.
- Many people have a limited understanding of the true costs of credit. Few consumers fully consider the cost of additional fees, rollover costs and default charges when choosing credit products.
- At the point of taking out credit, many people are overly optimistic about their chances of meeting repayments.
- Social norms have legitimised credit use and debt. Using credit and being in debt have become accepted as a 'normal' way to support lifestyles and meet wider social pressures to spend.[7]

To address this, the Strategy should aim to identify where there is scope to act early, before debt becomes unmanageable.

Key insight 3: Debt advice is effective but many people with debt problems do not access it early enough, if at all

Debt advice works[8] and is available through a wide range of free services delivered across the UK through a comprehensive range of channels.[9] However only 17% of over-indebted people seek advice; of those who do, most wait more than a year before coming forward for help.[10] There are a number of reasons:

- Many people do not think they have a problem. More than 50% of over-indebted people believe that in the current economic circumstances their situation is normal.[11]
- Awareness of available support is low. A significant number of people remain unaware of the multi-channel free and effective advice services that are available across the UK.
- There are powerful attitudinal barriers to seeking help. Many people feel ashamed of their debt problems and remain uncertain about the consequences of both problem debt and advice seeking.[12] This fear can stop people seeking advice and have an impact on their willingness to access the most appropriate advice solution for them.
- There is a good understanding of the triggers of debt problems, such as income shocks and life events. However, services and support are not always designed to respond to these events. Consequently opportunities to refer people to advice early, and at a point that they are receptive, may be lost.
- People are not routinely referred to debt advice from other agencies. Whenever someone identifies that a person they are working with has debt problems they should be able to quickly and easily direct them to sources of free, high-quality advice. Some health professionals, social services and housing providers have established channels for referral.[13] However, they are not as widely embedded as they could be.

Encouraging people to seek debt advice is a significant challenge but there are lessons from existing approaches.

- Marketing campaigns by StepChange and the Money Advice Service have shown that direct-to-consumer marketing can prompt people to get in touch with advice services. However concerted efforts will be required to normalise advice seeking and disseminate as widely as possible the benefits of accessing advice.
- People remain uncertain about the consequences of both problem debt and advice seeking. This fear can stop people seeking advice and have an impact on their willingness to access the most appropriate advice solution for them. The Insolvency Service has worked to make insolvency more of an administrative process rather than a judicial one, firstly with Debt Relief Orders and now with Bankruptcy. This is an important step but changing wider attitudes to what can still be a stigmatising issue will require concerted action by all those committed to the delivery of this Strategy.

- When someone working with a person identifies they have debt problems they should be able to quickly and easily direct them to sources of free, high-quality advice. Recent work by the Church of England and the Money Advice Trust in this area provides a model of good practice that could be built on in other areas.[14] Developing and disseminating straightforward, effective referral protocols could help boost engagement through the intervention of a trusted third party. These could take the form of simple sets of questions to enable debt problems to be identified and people referred on to local sources of support.

- Encouraging referrals from a wider range of agencies will require a stronger business case setting out the wider benefits of debt resolution. The benefits of debt advice at an individual level are well understood and accepted by most financial services creditors. There is evidence that the benefits of debt advice extend more widely[15] but there remain gaps in the literature demonstrating those benefits clearly to the health sector, housing providers, the criminal justice sector and utility firms. These benefits could also be quantified in terms of the public finances and the completion of this investment case should be a key part of the development of this Strategy.

Key insight 4: There is evidence that the existing suite of formal and informal debt solutions does not meet the needs of increasing numbers of people with problem debt

The existing suite of formal solutions does not meet the needs of increasing numbers of people with problem debt and informal solutions have a number of inherent weaknesses.[16] For example, whilst progress has been made on creating a formal basis for debt repayment arrangements in Scotland, this has not been mirrored across the rest of the UK. There is an opportunity to learn from the experience of the Debt Arrangement Scheme in Scotland and identify appropriate legislative responses for the rest of the UK that build on existing legislation.[17]

Key insight 5: Creditors are uniquely positioned to support indebted customers

Creditors have a key role to play in helping people resolve problem debt both by early identification of risk and by giving customers with debt problems who get in touch appropriate support and assistance. This does not apply only to financial services creditors. While most money owed is owed to banks and other lenders, some of the most serious problems can occur when people fall into arrears with council tax, rent or utilities.

Data from the Money Advice Trust and the Money Advice Service indicates that debts to non-financial services creditors have increased significantly over the past year and are taking up a substantial amount of adviser time, despite often being relatively small sums.[18] The Strategy aims to identify effective pre-arrears practices and supporting their dissemination and implementation across the creditor sector.

Key insight 6: Debt advice services are effective but there are opportunities to further improve the quality, consistency and effectiveness of debt advice

The debt advice sector in the UK contains a wide variety of providers working to different standards and with different aims. Progress has been made to provide standardised tools for measuring quality and impact.[19] However more work must be done to build a more coherent sector focused squarely on delivering the best possible outcomes for over-indebted people. Given its statutory role in this area the Money Advice Service will take the lead on this work in close partnership with funders, creditors and the wider advice sector. There is a particular role for funders to implement good practice in their own commissioning and improve co-commissioning arrangements to promote excellence, reward innovation and avoid duplication.

There is also a strong case for more closely integrating financial capability support into existing debt advice. Debt advice can improve financial capability but explicit financial capability interventions are not currently part of the mainstream debt advice process.[20] Training is available for debt advisers to enable them to support clients improve their financial capability and some funders, including the Money Advice Service, require those receiving funding to embed financial capability interventions into the debt advice process. Evidence also suggests there is demand for financial capability support amongst people in acute financial distress who have entered formal insolvency solutions.[21] The Scottish Government has recently mandated in law the provision of financial education for people going through bankruptcy.[22]

Recommendations for priorities and actions

Priorities and recommendations for action have been developed based on the insights from the Financial Capability Framework and engagement with debt advice stakeholders.

- **Priorities**: what the Strategy will focus on
- **Actions:** how these priorities can be delivered

The consultation period will be used to gather views and build consensus on the way forward. The next step will then be to work with partner organisations to develop detailed action plans ready for publication in the final Strategy.

Priorities

There are six key priority areas that form the core objectives of the proposed Strategy for people with financial difficulties.

Key insights	Priorities
1. Income shocks are the primary cause of the majority of debt problems.	1. Develop and extend effective methods to reach more of the people who are struggling to keep up so that they can absorb income shocks more effectively.
2. When debt problems do occur, they can spiral very quickly.	2. Identify where there is scope to spot problems earlier, before debt becomes unmanageable.
3. Debt advice is effective but many people with debt problems do not access it early enough if at all.	3. Encourage more people with debt problems to seek debt advice earlier.
4. The existing suite of formal and informal debt solutions does not meet the needs of increasing numbers of people with problem debt.	4. Ensure the right formal solutions are in place to enable people to sustainably resolve their debt problems.
5. Creditors are uniquely positioned to support indebted customers.	5. Develop best practice for offering 'breathing space' and to encourage take up across the financial services, utilities and the public sector.
6. Debt advice services are effective but there are opportunities for further improvement.	6. Continue to drive up quality, consistency and effectiveness of debt advice services.

Recommendations for action

Delivering against these priorities will require action from a wide range of organisations working in partnership with the Money Advice Service. In some areas the necessary steps are clear, but in others we need to work together to identify and agree the way forward. Drawing upon a wide range of expertise, the Money Advice Service has taken the lead and developed a set of proposed actions to deliver the Strategy.

Priority 1. Develop and extend effective methods to reach more of the people who are struggling to keep up so that they can absorb income shocks more effectively

Income shocks are a key driver of debt problems. There is strong evidence on how to build resilience to cope and adapt but there are challenges in engaging those who are most at risk. The recommended actions are that the Money Advice Service should lead work with the advice sector, DWP, housing associations and credit providers to:

- **Develop and promote implementation of effective early intervention strategies:** Encourage budgeting, spending control and resilience building through multiple, trusted, channels.
- Work with the industry to explore options to encourage low earners to **build resilience through saving**.
- Work with DWP to help people with moving onto **Universal Credit to manage the changes**, e.g. moving to monthly payments in arrears and the end of direct payments to landlords.
- Work with employers and others to help the rising number of part-time, zero-hours and self-employed to manage **variable incomes**.

Priority 2. Identify where there is scope to spot problems earlier, before debt becomes unmanageable

Debt spirals can occur very quickly. There is scope to spot problems and act earlier to stop debts snowballing into an unmanageable problem. The recommended action is that the Money Advice Service should lead work with the financial services industry, key creditors and debt advice sector to:

- Identify signs of risk from income shocks, life events, missed bills and escalating credit card debt to develop a better and more effective **early warning system**.

Priority 3. Encourage more people with debt problems to seek debt advice earlier

The primary challenge when seeking to support people out of problem debt is to increase engagement with high-quality, free, multi-channel advice. The recommended actions are:

- The debt advice sector and creditors work together to **improve awareness of the availability and effectiveness of debt advice**.
- The debt advice sector and creditors **address the fears of creditor reaction and social stigma with targeted actions**.
- Money Advice Service lead work with public services, housing associations, key creditors and the debt sector **to explore developing new referral pathways into debt advice**.

Priority 4. Ensure the right formal debt solutions are in place

The existing suite of formal debt solutions does not meet the needs of increasing numbers of people with problem debt and informal solutions have a number of inherent weaknesses. The recommended action is:

- **Money Advice Service initiate work to ensure that the right formal solutions are in place to enable people to sustainably resolve their debt problem**.

Priority 5. Encourage creditors to support customers with debts

Creditors have a key role to play in helping people resolve problem debt both in early identification of risk and in ensuring that when customers with debt problems get in touch, they are given appropriate support and assistance. The recommended actions are:

- The debt advice sector and key creditors from financial services, utilities and the public sector **develop best practice for offering 'breathing space' and to encourage take up**.
- Make the business case to create creditor processes that help people lift themselves out of debt.

Priority 6. Continue to drive up quality, consistency and effectiveness across the debt advice sector

Debt advice services are effective but there are opportunities to further improve quality, consistency and effectiveness across the debt sector.

- Money Advice Service will continue work with the debt sector to drive up quality, consistency and effectiveness and co-ordinate supply to meet need.

Consultation questions 13: How far do you support the Strategy's aims for people with financial difficulties?

Consultation question 14: What is your view of the recommendations for action relating to people with financial difficulties? How could they be improved?

See the complete list of consultation questions for the Financial Capability Strategy for the UK at **fincap.org.uk**

1. Financial Capability Tracker data 2013-14, (Money Advice Service, Forthcoming).

2. Ibid.

3. Indebted lives: the complexities of life in debt, (Money Advice Service, 2013).

4. See for example The Debt Trap: Exposing the impact of problem debt on children ,(Children's Society, 2014), Restoring the Balance: Tackling problem debt,(Centre for Social Justice, 2014) The Money Advice Service Debt Advice Review 2013/14, (Money Advice Service/Optimisa, 2014) Strength Against Shocks: Low-income families and debt, (IPPR, 2010).

5. The Money Advice Service Debt Advice Review 2013/14, (Money Advice Service/Optimisa, 2014).

6. Changing Household Budgets, (Money Advice Trust, 2014), The Money Advice Service Debt Advice Review 2013/14, (Money Advice Service/Optimisa, 2014) Debt and The Family: Debt and Household Incomes, (Financial Inclusion Centre, 2011).

7. See for example, FCA Consumer Credit Research: Payday Loans, Logbook Loans and Debt Management Services, (ESRO, 2014) and Consumer Credit: Deep dives into Credit cards and Unauthorised overdrafts, (Jigsaw Research, 2014)

8. The effectiveness of debt advice in the UK, (Money Advice Service/YouGov, 2012).

9. Debt advice channel strategy research, (Money Advice Trust, 2012).

10. Indebted lives: full data files, (Money Advice Service, 2013), StepChange Statistics Yearbook 2013, (StepChange, 2014).

11. Indebted lives: full data files, (Money Advice Service, 2013).

12. Indebted lives: full data files, (Money Advice Service, 2013).

13. E.g. Final Demand, (Royal College of Psychiatrists, 2009).

14. See the work of the Church Credit Champions Network coordinated by the Centre for Contextual Theology

15. Funding debt advice in the UK - A proposed model, (Money Advice Service/London Economics, 2012).

16. A barrier to accessing bankruptcy in England, Wales and Northern Ireland is the high cost, while an inherent weakness of debt management plans is the lack of protection from creditor action during repayment.

17. Tribunal Courts and Enforcement Act 2007, Part 5, Chapter 4.

18. Changing Household Budgets,(Money Advice Trust, 2014), The Money Advice Service Debt Advice Review 2013/14, (Money Advice Service/Optimisa, 2014).

19. Debt advice organisational and individual quality frameworks, (Money Advice Service, 2013) Debt advice evaluation toolkit, (Money Advice Service, 2013.

20. Citizens Advice is currently running a number of pilots testing out such integration using funding from Money Saving Expert. Research from Toynbee Hall in 2009 showed the positive impact of debt advice on levels of financial capability.

21. Unpublished bankruptcy and DRO research, (Financial Services Authority, 2009).

22. Bankruptcy and Debt Advice (Scotland) Act 2014, Section 2.

Financial Capability Strategy for the UK

September 2014

fincap.org.uk