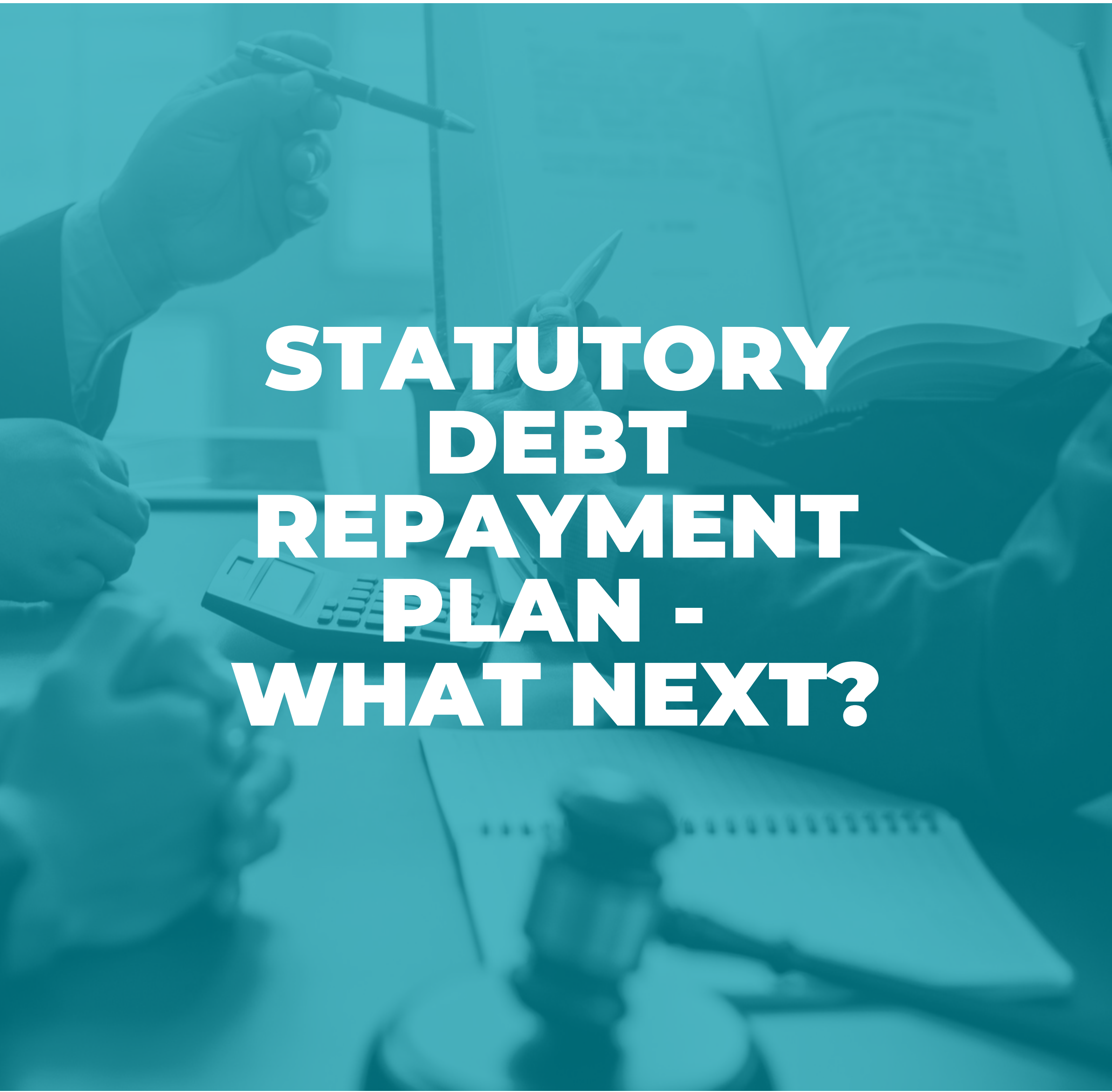
September 2022



STATUTORY DEBT REPAYMENT PLAN - WHAT NEXT?

CONTENTS

INTRODUCTION

The Statutory Debt Repayment Plan (SDRP) has been designed by the UK Government to fill a perceived gap in the range of debt support programmes and solutions currently available.

Whether there is a gap that needs filling, and whether SDRP can provide meaningful benefit to a segment of consumers in financial distress, has provoked extensive debate within the debt industry and beyond.

As the UK's leading provider of independent advisory and professional services to collections and revenues teams across the private and public sectors, Arum has a unique lens through which it can view and contribute to this debate.

We have tried to use our own expertise, combined with the expertise of our partners and clients across the private, public and debt advice sectors to provide a balanced view from the entire industry.

Based on extensive conversations and our 25 years' experience, we have provided formal input to the Government SDRP consultation process (which closed on 5 August 2022).

This whitepaper is a distillation of Arum's perspective on the potential impact, benefits, and challenges of SDRP as it is currently proposed.

BACKGROUND

The SDRP was proposed as a bridge between existing non-statutory debt solutions (which are said not to have sufficient protections for some consumers), and statutory debt solutions (which have the protections in place, but can result in debt being written-off rather than repaid).

A question asked by a senior stakeholder in private sector global financial services institution was simply: "Why?"

From their perspective, they are not only bound by the Financial Conduct Authority's (FCA) rules, but Treating Customers Fairly is part of their culture and ethos, so SDRP protections feel largely unnecessary. Yet not all who hold debt are governed by the FCA, with energy/utility and government being the largest debt-owning sectors outside of the consumer credit market.

The inference we could draw from this is that the uneven legislative and operational playing field across different sectors in the industry is the root cause, and that SDRP addresses a symptom of the problem, but not the problem itself.

These symptoms become even more prevalent from the indebted person's perspective, often owing to multiple organisations. When an attempt is made to resolve their problem debt, they find that there are different rules, cultures and tolerance levels between financial services, energy/utilities, central government and local government. Furthermore, there is disparity within each sector, so for example, a sole trader who is VAT registered could also be in receipt of benefits, but a benefit overpayment will be treated very differently to a VAT debt.

The root cause is not something that will be fixed overnight, although there are some indications that the government may be thinking along these lines. One example is the Government Debt Standard[1], which mandates that: “Operational practices shall treat debtors in a manner appropriate to their circumstances.”

Wrapped up in that one, carefully worded phrase, lies Know Your Customer, Differentiated Treatments Paths, Signposting Debt Advice, Vulnerability Assessments and many other branches of best practice that the private sector has enjoyed through continuous improvement through the FCA.

Until such a panacea for debtor treatment is developed, there arguably remains a need for a solution such as SDRP and it is an acknowledgement of the challenges faced by those trying to resolve multiple debts.

The proposals are not without issue, but we should not underestimate that SDRP is a hard-fought for opportunity to improve the lives of people in problem debt, whilst respecting the right of debt owners to receive the money that is owed to them.

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[1] Government Functional Standard - GovS 014: Debt - GOV.UK (www.gov.uk)

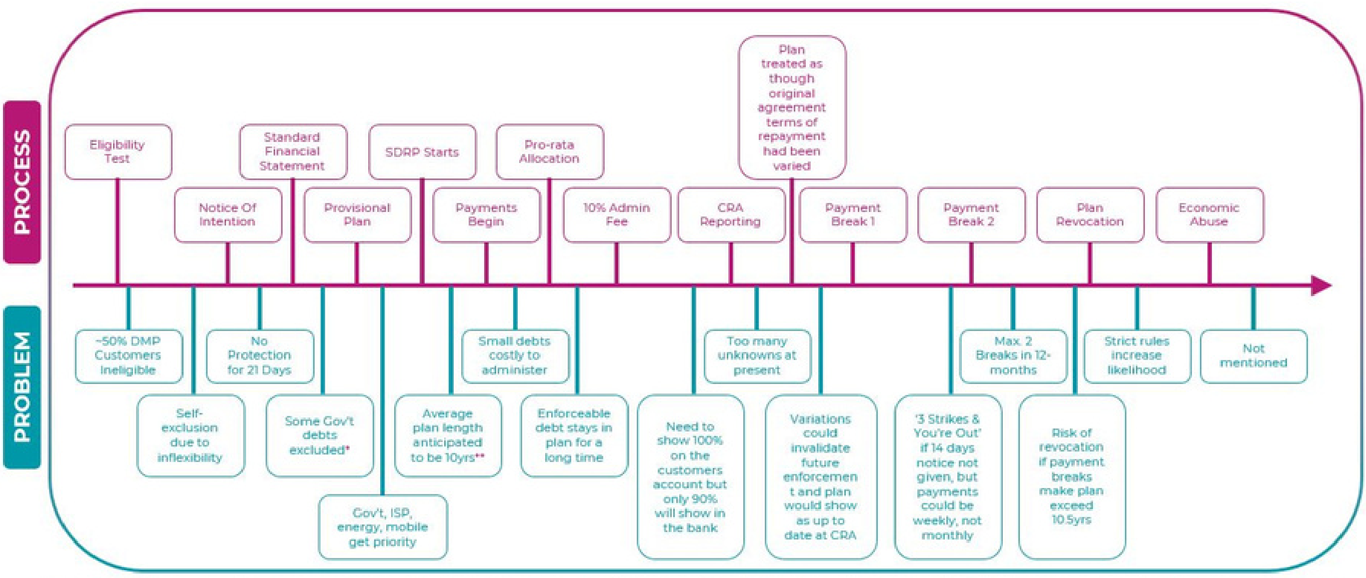
In this white paper, we will look at five themes that have arisen through our conversations with the industry:

1. **Timing**
2. **Scope (comparative to the existing indebted population)**
3. **Flexibility (and restrictions within the proposals)**
4. **Length**
5. **Funding**

There are naturally other considerations, such as Credit Reference Agency (CRA) reporting, but these are nebulous at the present time and require far more discussion to resolve.

For reference, a more complete look at the end-to-end process and some of the other issues can be found below.

The SDRP legislative journey



*Broadly - 3rd Party Deductions From Benefits & UC Advances (until UC Rollout complete); IPA/IPO; Criminal Debt; Child Maintenance; Student Loans; Social Fund; future Council Tax / Non-Domestic Rating liabilities

**HM Treasury anticipated a maximum of 7 years and up to 10 years in exceptional circumstances. However, it also published average outstanding debt value: when divided by advice sector data on average disposable income, the average plan length is 10 years.

TIMING

"...the environment is now very different to when SDRP was first proposed..."

A brief recap on the timeline so far: the Debt Respite Scheme was proposed by Theresa May's government in the May 2017 Conservative Manifesto. It was less than a year since the nation had voted to leave the EU, and COVID would not become part of our everyday vocabulary until nearly three years later.

The economy was broadly stable – a slight jump in inflation and interest rates as a reaction to Brexit, but things settled down again pretty quickly. Demand for debt advice was high and the National Audit Office was preparing to publish its Tackling Problem Debt report and legislation was being drafted to create the Single Financial Guidance Body – which later became the Money & Pensions Service.

Fast forward to today, we are expecting COVID to lose its pandemic status at some point during the remainder of 2022 and the macro-economic situation is deteriorating quickly, exacerbated by an energy crisis triggered by war in Ukraine.

All of this matters because the environment is now very different to when the SDRP was first proposed.

This alone has prompted questions from several organisations – questions around whether the industry can afford to wait for SDRP or does the government need to act now, and if so, is now really the right time to be pushing on full steam ahead with SDRP or should the government be concentrating on developing a simpler, faster and more agile response to the current situation? This could be something as simple as a set of pre-action protocols for non-FCA regulated debt owners.

This links back to the fact that many see SDRP as a fix to a symptom rather than the root cause – and that the current economic climate is causing more symptoms to appear. As such, it may now be more efficacious to address the root causes.

It was also noted by the Debt Managers Standards Association (DEMSA) that there is a congested regulatory timetable at present, with the introduction of the FCA's Consumer Duty, reforms to the Consumer Credit Act, a continuing review on CONC 8 by the FCA and possible reforms to UK GDPR. Some DEMSA members therefore believe that the SDRP implementation period alone could extend beyond two years (against HM Treasury's assumption of 18 months).

These concerns should not be interpreted as inherent reluctance within the industry; in fact, we are also hearing that, while the timing is tricky and there is in fact a desire to do something sooner, organisations do not want to miss out on the opportunity that SDRP provides and will continue to work with the government to drive out a workable solution.

SCOPE

One of the most important voices belongs to the debt advice sector as it will be FCA-authorised debt advice providers that will need to assess their clients' eligibility for the scheme.

Christians Against Poverty and PayPlan both anticipate 5% or less of their customers would be recommended for SDRP versus a Debt Management Plan (DMP). Others, as canvassed by DEMSA, are higher than 5%, but many are only around the 12% mark.

StepChange also makes an interesting point insofar as the eligibility criteria may be determined by guidance that is yet to be written. This stems from a couple of parts of the draft legislation:

1. The SDRP Fair & Reasonable assessment could play a significant role in determining eligibility, and that the approach to F&R assessments can come from guidance published by the Secretary of State.
2. Debt advice providers may only propose plans of longer than seven years in exceptional circumstances, the details of which will be set out in future guidance.

Given StepChange noted that 25% of its DMP customer base has a plan length of 7-10 years at inception, the guidance will indeed play a critical role if this significant proportion is to be classed as exceptional under SDRP.

It believes that this group would simply end up in a DMP and therefore miss out on the protections that SDRP offers.

There is also an element of consumer choice to factor in. Some in the advice sector have seen that:

- Many customers who are eligible for an IVA end up opting for a DMP with double the term because it feels like a less formal option.
- Even when bankruptcy would be a cheaper option for eligible consumers, many still choose a DMP because it is less formal and has more flexibility.

So, both eligibility and customer choice could lead to lower numbers of SDRP users. In turn, this may also reduce the economies of scale argument that supports the proposed fee structure.

"...this group would simply end up in a Debt Management Plan and therefore miss out on the protections that SDRP offers..."

FLEXIBILITY

The flexibility, or perceived lack thereof, is one area that has attracted much commentary from the industry. Many also cite the current economic climate as a reason for greater flexibilities, with DEMSA suggesting SDRP needs to be able to adapt to "events outside the control of consumers, as experienced with the pandemic and tailored forbearance schemes."

"In a DMP, StepChange accepts written consent from the debtor to discuss their case with their representative, whereas the proposals for SDRP require a legally appointed person"

There are several concerns highlighted across the industry that the number of the restrictions could lead to unnecessary breakages:

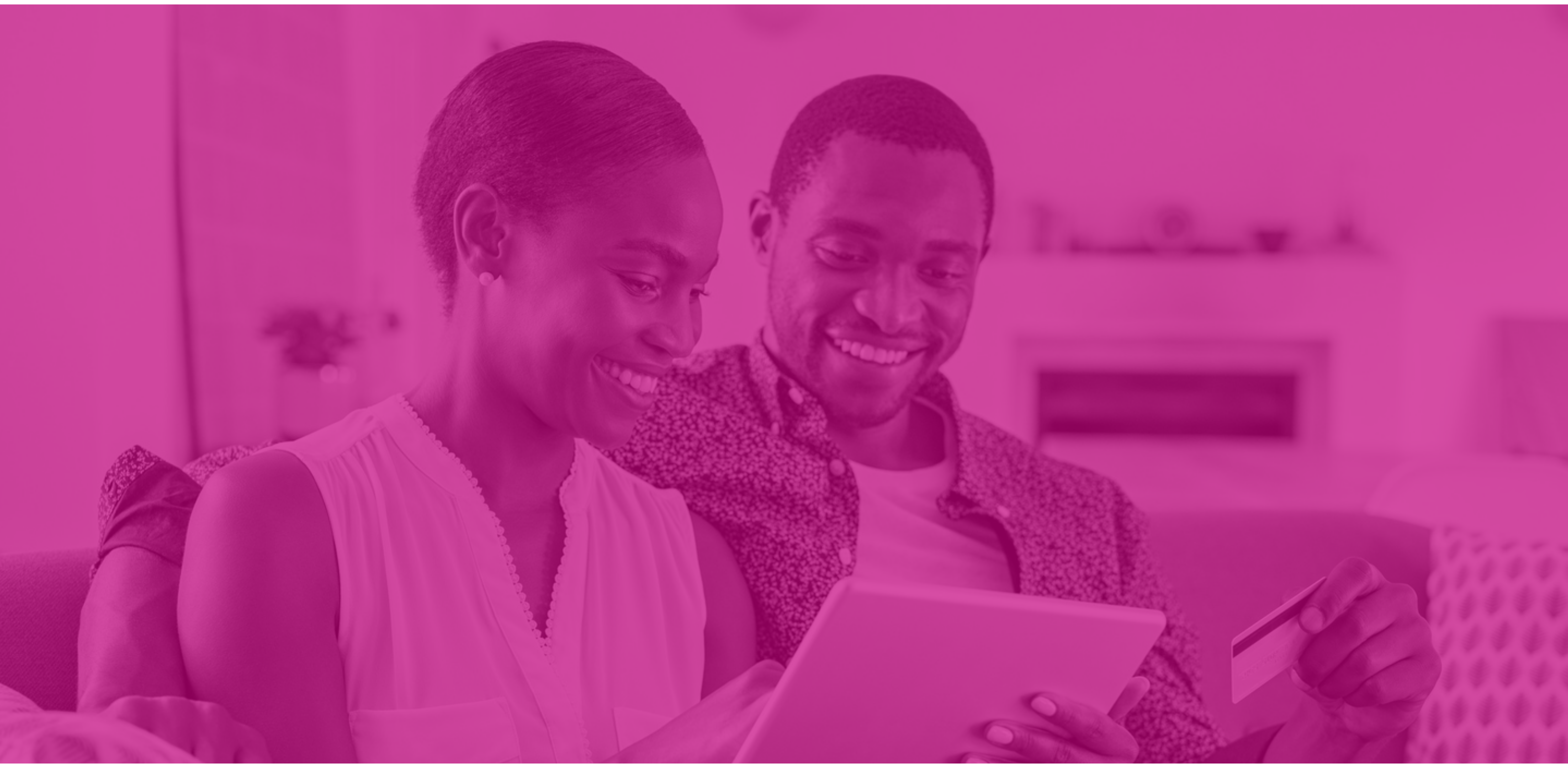
- StepChange noted that no-fault additional debt could lead to failures in SDRPs.
- The charity also called out that the rules around who can represent the indebted person are complex. In a DMP, StepChange accepts written consent from the debtor to discuss their case with their representative, whereas the proposals for SDRP require a legally appointed person, namely:
  - legally appointed guardian
  - court appointed deputy
  - person with an enduring power of attorney.

  This means that somebody who is unable to manage their own financial affairs (hence the requirement for a representative) needs to have access to somebody who has gone through (or is willing to go through) a legal process in order to offer support.

  This could be exacerbated by the fact that the representative could already be acting on behalf of the indebted person until the point in the process where SDRP is identified as the best option. The choice then will be to either (a) pause the SDRP process and begin the legal process or (b) choose a DMP instead.

- UK Finance shares our concerns that the mandatory 14-day notice period required to take a payment break, especially for people on variable incomes, will lead to unnecessary plan breakages – breakages which, again, are less likely to happen under a DMP. It also pointed out that plans could fail if allowable payment breaks push the plan over 10.5 years in length.
- StepChange data showed that of 15,000 DMP clients (who have successfully completed their plans or are still in a paying plan i.e.- plans that have not failed), 57% would have required a payment break extension and/or a variation, which it believes would have placed those plans at a greater risk of failure had they been SDRP.
- DEMSA has also called for greater flexibility around missed payments, variations and the length of plans, having noted in its response to HM Treasury that the flexibilities under SDRP are limited in comparison to IVAs and DMPs.

SDRP needs to be flexible enough to support its users, otherwise it will not encourage the volumes required to make it financially viable for the advice sector to administer, and creditors will miss out as a result.



LENGTH

As a repayment solution, the government has proposed that plans should not exceed seven years, although in exceptional circumstances plans may be extended to 10 years. The term can be extended beyond 10 years as payment breaks have the effect of increasing the overall length of the plan. However, these extensions have a hard cap at 10 years and six months, beyond which no further payment breaks are allowed to extend the term.

In terms of data regarding the length of plans:

- DEMSA, using DMPs as a comparator, has shown that 45% of cases are more than seven years in duration with an average of 9.2 years.
- StepChange suggest 25% of DMPs have a projected repayment term between 7-10 years at inception.
- UK Finance makes an interesting point insofar as there may be non-eligible debts that will come to an end after an SDRP has started: this could mean that a plan would exceed 10 years at inception but would reduce sufficiently in length once additional surplus income from these non-eligible debts becomes available.

"Debt advisers have a balance to achieve between ensuring that repayments are sustainable, and not keeping people in debt for longer than necessary."

- The Money Advice Trust also picked up on this point and gave the example of a return to work following maternity leave as an example of a known future increase in income.
- Citizens Advice took a different view of this – no less valid – as it believes that extending a repayment plan for longer than seven years is unlikely to be a suitable option for the customer. Instead, it objects to the extension to 10 years in exceptional circumstances, as the test for this limits the amount of choice available to the debt advice provider and the indebted person. It also has concerns that a hard deadline could create a cliff edge and instead argues for an element of discretion.

One of the benefits of having FCA-authorised debt advice providers at the heart of SDRP is that the length of the plan will not be allowed to override the principle of affordability. Debt advisers have a balance to achieve between ensuring that repayments are sustainable, while not keeping people in debt for longer than necessary. As such, any cap on length will simply rule out the scheme if repayments under (or close to) the maximum term are unaffordable.

FUNDING

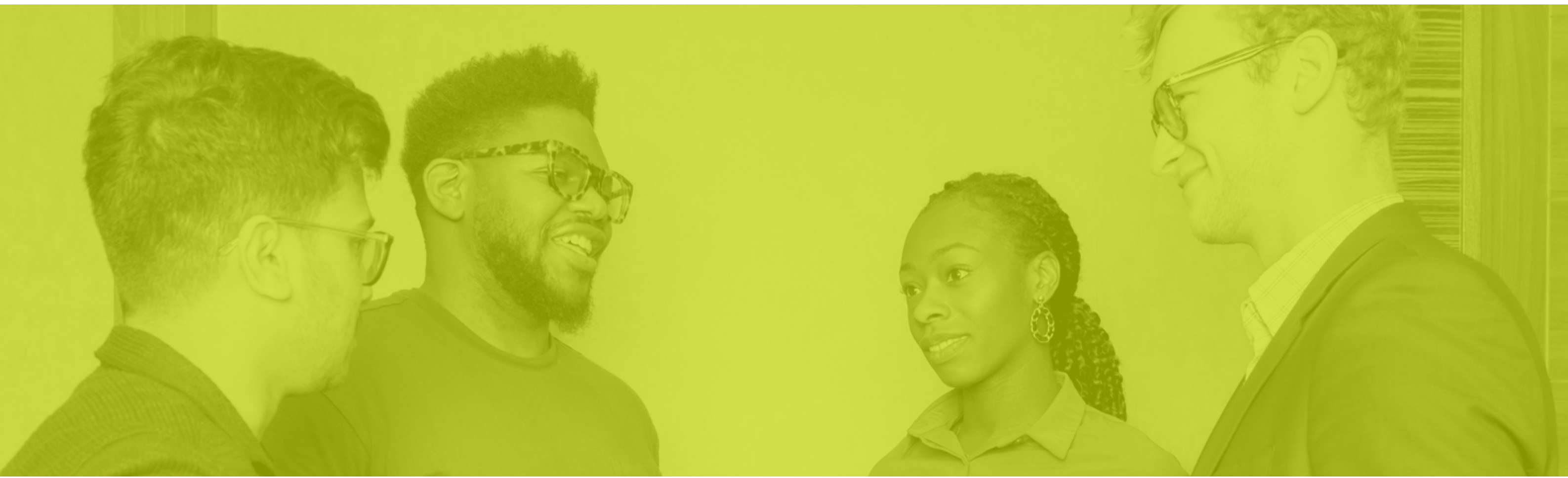
Naturally, the funding model attracts a lot of attention and scrutiny. One organisation told Arum that their initial assessment of the cost to implement the technology alone would be ~£2.5m – the same figure as StepChange arrived at in its response to the consultation.

There is also some nervousness in the market that the SDRP volumes won't be achieved, which could topple the economies of scale argument for the low fee.

"...we could find a situation whereby local authorities are paying more than the 10% fee..."

An interesting point we have heard is that the proposal to fund debt advice is not currently factored into the statutory fee structure for enforcement as set out in the Taking Control of Goods (Fees) Regulations 2014. As the fees are added to the total owed by the indebted person, the enforcement industry, which has its fees set by one part of government, could now see an erosion of those fees by another part of government.

The alternative, at least where local government enforcement is involved, is that we could find a situation whereby local authorities are paying more than the 10% fee because the debt would include enforcement fees, and the council could have to pay for the portion of the 10% that relates to enforcement action.



Getting the funding right will be a critical success factor for SDRP. As the viability of the funding model is based on economies of scale, the scheme needs to:

- **reflect the current environment to attract enough customers**
- **be inclusive**
- **be as attractive as existing debt solutions.**

CLOSING THOUGHTS

We should not underestimate SDRP. There has been a long-running campaign to achieve a statutory debt solution that encompasses a broader range of debts – and this is it – the government has listened and it has made a proposal.

Yes, many have suggested a number of changes or improvements – which is the point of running a consultation – to seek views and consider how to develop the best product.

The government should be commended for its efforts on SDRP to date and Arum, along with the vast majority across the industry, welcome the opportunity to continue providing the government with advice on SDRP as it moves forward to the next phase.

If you want to know more about the SDRP, see the following links or get in touch with us directly:

5 things you need to know about SDRP

Watch on demand - SDRP webinar

ABOUT THE AUTHOR

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Arum

Steve has been working in the debt industry for over two decades.

He has spent the majority of his career working in government, starting on the phones collecting VAT debt, and ending up being responsible for prompting policy and strategy improvements for the management of over £40bn of public sector debt.

Steve joined Arum in 2022 where he continues to contribute to the biggest conversations in the global debt market, with Credit Management Magazine recently calling him 'one of the industry’s genuine thought leaders'.

ABOUT ARUM

Arum has been helping organisations resolve problem debt for more than 23 years across 20 global territories. We provide clients with independent advice and practitioner support across collections and revenue.

Whether choosing or implementing collections technology, navigating digital business transformation, or improving customer treatments to achieve better outcomes, Arum experts are trusted by leading brands across public sector organisations, financial services (banking, lending, debt purchase), utilities, and telecommunications companies.

The Arum mission is simple: to deliver independent collections and revenue solutions globally. This is achieved by improving regulatory, credit risk and portfolio performance, whilst maximising returns on clients' technology investments.

Within the public sector, Arum aims to build better outcomes for citizens by improving the collection of local and central government revenues that fund public services. What's more, the majority of Arum's team of experts started their careers in government and financial services roles.

Arum provides a blend of practitioner-led consulting and end-to-end change and programme delivery services. Our knowledge of the creditor and software landscape is unrivalled and includes 30+ system vendors such as CGI, Equifax, Experian, Exus, C&R Software/FICO, Pega, Qualco and Tietoevry.

We're collections and revenue experts and work collaboratively with our clients to prevent and resolve problem debt.

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