# Report of the Portfolio Committee on Trade and Industry on its study visit to the United Kingdom, dated 14 June 2018

The Portfolio Committee on Trade and Industry, having visited the United Kingdom from 30 April to 2 May 2018, reports as follows:

1. **Introduction**

The mandate of the Portfolio Committee on Trade and Industry covers trade and industry, including the regulatory and standards architecture, which requires regular and informed oversight and the development or processing of legislation that effectively balances the rights of both consumers and the private sector. In this regard, the Committee has been developing legislation to address a gap within the credit market to provide a mechanism for consumers who are over-indebted and too poor to effectively use existing debt intervention measures to escape a debt trap. It therefore, decided to undertake a comparative study visit to the United Kingdom (UK) to consider its debt relief measures, in particular its debt relief order.

This measure is of interest to the Committee, as it is comparable to the proposed measure in the draft National Credit Amendment Bill, which seeks to assist qualifying consumers who are unable to repay their debts by suspending these for up to 24 months and then extinguishing this debt if their situations fail to improve within the 24-month period. The English model uses provisions in its legislation aimed at creating an alternative and more appropriate mechanism for “No-Income-No-Assets” (NINA) debtors to apply for debt relief in the event that they are unable to pay their debt obligations. This scheme was aimed at assisting debtors with little or no assets and income.

* 1. **Purpose of the study tour**

The purpose of the English leg of the study tour was to engage relevant role players in the consumer credit regulatory regime to understand the debt relief measures that are being implemented, in particular their debt relief order. This included understanding what led to the introduction of the debt relief order; how the target group was determined; what relief is available to consumers who cannot solve after a reasonable period of time; and whether there have been any determined impacts to date. In addition, the discussions considered how consumers accessed these services. Furthermore, the Committee wanted to understand how the British government intervenes to prevent or limit unscrupulous lending and over-indebtedness.

* 1. **Delegation**

The following Members and staff undertook the study visit:

* Ms J Fubbs (ANC) (Chairperson and Leader of the delegation)
* Mr A Williams (ANC)
* Ms P Mantashe (ANC)
* Mr D Macpherson (DA)
* Ms E Ntlangwini (EFF)
* Mr A Hermans (Committee Secretary)
* Ms M Sheldon (Content Advisor).
  1. **Outline of the report**

Firstly, the report provides an overview of the South African credit regime, including an outline of the proposed measures for the National Credit Amendment Bill. Secondly, it describes the statutory framework of the UK’s debt relief regime including the role players and the different types of available debt intervention measures, and discusses other credit market regulatory matters. Thirdly, it provides the Committee’s key observations from the study tour. Fourthly, it lists its acknowledgements and sets out its recommendations to the Minister of Trade and Industry for consideration by the National Assembly.

1. **An overview of the South African Credit Regime**

Before engaging with the UK on its credit regime and debt intervention measures available for their consumers, and the statutory framework that underpins this, it is important to provide an overview of the measures currently at the disposal of over-indebted South African consumers.

In South Africa, the statutory framework primarily resides in two jurisdictions, namely the Department of Justice and Constitutional Development, where the Insolvency Act (No. 24 of 1936) and the Magistrates Court Act (No. 32 of 1944) are located; and the Department of Trade and Industry, the custodian of the National Credit Act (No. 34 of 2005). The existing debt intervention options available to consumers are:

* *Sequestration:* The Insolvency Act provides the processes that would allow for the sequestration of assets of debtors through a court order following an application by creditors. While the primary objective of the Insolvency Act is not to provide debt relief, under sequestration, part of the debt owed to creditors is settled using money generated from the sale of assets and the remainder is discharged. However, this is dependent on the possibility that the debtor’s assets can generate sufficient monetary gains to satisfy credit providers. Therefore, a debtor can be deemed too poor by credit providers to access sequestration.
* *Debt administration:* When sequestration is not viable to consumers, and the outstanding debt does not exceed R50 000, the option of an Administration Order becomes available. The consumer can apply to the Magistrate Court, and if successful, debt is restructured by the reduction of interest rates and the extension of the loan terms. A court appointed administrator will manage the order, collect payments and distribute payment to creditors. This is done at the cost of up to 12.5 per cent of payments to cover the administrator’s fees. A critique against this measure is that the process is lengthy and the high fees act as a barrier to entry.
* *Debt Review:* When a consumer is not able to meet their debt obligations but is able to pay, he/she may apply to a debt counsellor to be declared over-indebted and to have their debt restructured by lowering interest rates and extending the repayment periods. The debt counsellor develops a payment plan for the credit providers’ consideration and approval; otherwise a magistrate court may make a determination in this regard if one or more credit providers disagree with the proposal. A debt counsellor may also investigate whether any of the credit agreements were granted recklessly as part of this process. The debt review process is however not free, nor subsidized, and involves a once-off fee (including an application fee of R50, a restructuring fee which is equal to the first instalment of the payment plan, capped at R6000 and legal fees (typically a consent order costs R750 or more if the payment plan is disputed by one or more credit providers) and on-going or monthly fees (including an after-care fee of five per cent of the monthly instalment of the payment plan, capped at R400, for the first 24 months of the plan, thereafter reducing to three per cent, capped at R400). The consumer must also pay a Payment Distribution Agency (PDA) fee equal to three per cent of the monthly rehabilitation payment and capped at R500. Should a consumer choose to end the debt review process, he/she would be subject to a fee equal to 75 per cent of the restructuring fee. There have been reports from debt counsellors that consumers earning less than R7 500 a month are economically unviable for the debt review process; as the fees they would pay are less than the cost of administering the process.

Given these drawbacks and the costs associated with the three existing measures for poorer over-indebted consumers, the Portfolio Committee on Trade and Industry has embarked on developing a Committee Bill, namely the National Credit Amendment Bill, to address this gap in the debt relief regime of South Africa. The Committee had identified that a number of poor, over-indebted South Africans were unable to escape debt traps using these options due to—

* Sequestration requiring benefit to creditors (e.g. a debtor must have assets that can be realised to defray at least a portion of the total debt);
* The associated administrative costs of administration being unaffordable for poor South Africans; or
* The fees payable by the consumer being insufficient to cover the operational costs for debt review process. This often results in unwillingness by debt counsellors to assist many of these consumers (“identified consumers”).
  1. **The Committee Bill**

The Committee is thus proposing measures that would address this gap and accommodate the identified consumers. The Bill provides for the following:

* Firstly, empowering the National Credit Regulator to provide an on-going, free debt review-type process to the identified consumers. The National Credit Regulator will accordingly consider whether an identified consumer can pay their debt if the debt was rearranged. This could include a longer repayment period, a limit on costs and other fees and a reduction in the interest rate. As this is a free service, it will address the gap identified above.
* Secondly, if the National Credit Regulator finds that despite an attempt to re-arrange an identified consumer’s debt, it will simply take too long to repay (longer than e.g. five years), or the identified consumer has no income or assets that could be used to repay debt with, the National Credit Regulator will then consider that consumer for the debt intervention measure. This is a once-off application, which results in all debt recovery processes, interests, fees and charges being halted for a period of maximum two years.

During the two years, the National Credit Regulator will regularly review the identified consumers’ financial status and should the identified consumers be in a position to have their debts restructured and paid off in a reasonable period, they will then be assisted in accordance with the first step (debt review process). However, if after the two years’ period the identified consumers can still not settle their debt, the debt will be extinguished.

* Thirdly, the Bill also provides for the Minister of Trade and Industry to introduce similar debt intervention measures under circumstances such as natural disasters and exogenous shocks to the economy in the future.

England and Wales has introduced provisions in its bankruptcy legislation aimed at creating a similar measure – i.e. an alternative and more appropriate mechanism for NINA debtors to apply for debt relief in the event that they are unable to pay their debt obligations. It appears that this measure is similar to the proposal around suspending and extinguishing debts being introduced by the Committee (namely that there is no requirement for benefit to creditors and the service is provided by government); thus, the Committee had been interested in engaging the British government on this programme.

The Bill will further limit the wide-spread abuse of consumers by unscrupulous lenders and to protect the identified consumers from future over-indebtedness due to unforeseen changes in their financial situations. In this regard, the Bill proposes to introduce provisions to:

* Strengthen provisions to curb reckless lending by creditors. These include a requirement that debt counsellors, when assessing a debt review application, must always consider whether a transaction could have been reckless, and if so, must report that fact to the National Credit Regulator. At the moment, this is only done at the request of the consumer and there is no duty to report this.
* Introduce offences and penalties for prohibited conduct, such as providing credit related services without being registered or conducting reckless lending. The Act currently only provides for administrative fines. Although the Committee is aware of the criticism against criminalising commercial actions, the consequences that flow from prohibited conduct are severe and affect vulnerable consumers the most. As these practices are persisting, the Committee is of the view that a strong message should be sent to transgressors.
* Provide for compulsory life insurance for loans that are below R50 000 and are granted for a period of six months or longer. The rationale here is that most of the debtors who will qualify for the measure discussed above, will have entered into legal credit agreements but because of unforeseen circumstances, such as retrenchment, find themselves in a position where they cannot repay the debt. Compulsory credit life insurance will address this challenge. However, the Committee is cognisant of the cost associated with such insurance products and is accordingly limiting the compulsory nature thereof to a targeted level of credit. This can be expanded in future if there are tangible positive results.

1. **United Kingdom – Statutory overview of the debt intervention regime**

The UK has an array of role players in the credit regulatory space, as well as a wide number of debt intervention measures in place. This section maps out these role players, the types of debt intervention measures available in the UK, particularly in England and Wales[[1]](#footnote-2), and other relevant credit regulatory matters implemented in the UK.

* 1. **Role players in the credit regulatory regime**

*HM Treasury* is the government’s economic and finance ministry maintaining control over public spending, setting the direction of the UK’s economic policy and working to achieve strong and sustainable economic growth. In particular, they are responsible for financial services policy which includes banking and financial services regulation. HM Treasury should ensure the stability of the credit market and that consumers make good financial choices that would not lead to over-indebtedness. The necessary safety measures should be in place to prevent people falling through the cracks through the following proactive measures:

* Providing appropriate financial training – which starts at school;
* Providing sensible budget training for consumers; and
* Ensuring the availability of free debt advice service.

This approach does not necessarily ensure that people do not get into financial difficulties. According to the HM Treasury, when consumers are experiencing financial pressures or are unable to pay their debt they should be able to access free debt advice services.

The *Financial Conduct Authority (FCA)* regulates the financial services industry in the UK with a focus on protecting consumers, keeping the industry stable and promoting healthy competition between financial service providers. On the other hand, the Prudential Regulatory Authority is responsible for regulating the financial market to ensure financial stability and the efficient functioning of the economy. The FCA plays a critical role in ensuring the optimal functioning of relevant markets through the protection of consumers, the protection of financial markets and to promote competition. With respect to consumer protection, the FCA should ensure that firms become consumer centred in their business operations, provide appropriate products and services, and put the protection of the consumer above company profits. It also specifically authorises and registers organisations that offer debt counselling and debt adjustment services to consumers who may be over-indebted.

The *Money Advice Service (MAS)* was established in terms of the *Financial Services and Markets Act, 2000,* as an independent body from the FCA, to enhance public understanding of financial matters. The Money Advice Service’s statutory function is to enhance:

* The understanding and knowledge of members of the public of financial matters (including the UK financial system); and
* The ability of members of the public to manage their own financial affairs.

This includes, in particular:

* Promoting awareness of the benefits of financial planning;
* Promoting awareness of the financial advantages and disadvantages in relation to the supply of particular kinds of goods or services;
* Promoting awareness of the benefits and risks associated with different kinds of financial dealings (which includes informing the FCA and other bodies of those benefits and risks);
* Publishing educational materials or the carrying out of other educational activities;
* Providing information and advice to members of the public;
* Assisting members of the public with the management of debt;
* working with other organisations which provide debt services, with a view to improving –
* The availability to the public of those services;
* The quality of the services provided; and
* Consistency in the services available, in the way in which they are provided and in the advice given.

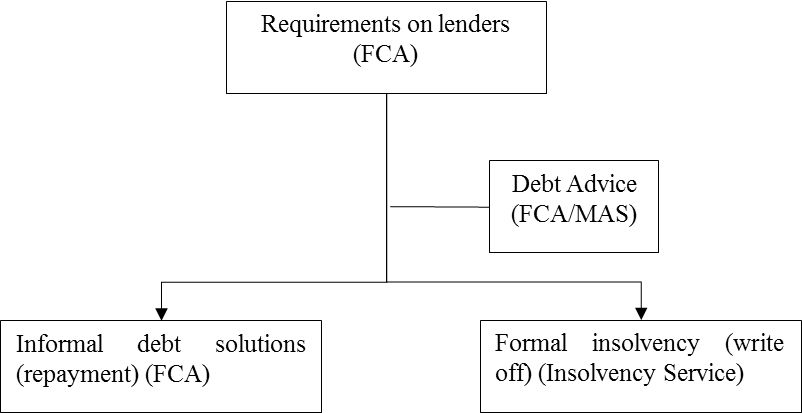
Although the MAS acts independently from the FCA, the FCA must ensure that it is able to function effectively by administering the levy from credit providers for its activities. The levy is based on a budget proposed by MAS and agreed to by credit providers. Credit providers are also allowed to annually monitor the MAS’ expenditure through a transparent process. This levy was introduced shortly after the financial crisis in 2008. StepChange Debt Charity informed the Committee that there was a recognition among credit providers that they share the responsibility of over-indebtedness. Hence, the introduction of this levy was not opposed by industry. A portion of this money is distributed to *debt advice organisations*. These debt advice organisations are registered and authorised by the FCA to provide free financial advice to consumers, which includes assessing their financial situation and proposing an appropriate debt solution when necessary. Two of the bigger debt organisations are StepChange Debt Charity and the Money Advice Trust. If a consumer accepts the recommendation regarding a debt solution, the debt advisor would refer them to an appropriate, licensed debt adjusting intermediary or insolvency practitioner.

The FCA checks debt advice organisations for compliance with the following:

* Fit and proper management;
* Right training process for debt advisors;
* Senior manager certification regime; and
* That all employees are acting in terms of the FCA’s principles.

It also conducts random testing across debt advice organisations to ensure uniform quality of debt advice.

Currently, the FCA does not require any specific qualifications for debt advisors but debt advice organisations are expected to provide the appropriate training. The FCA has introduced the Senior Manager Certification Regimes as a requirement for all senior managers. This is to ensure that all employees of the firm operate within the FCA regulatory principles to ensure fair treatment of customers.



**Figure 1: An overview of role players’ responsibilities in relation to debt intervention measures**

Source: FCA

All informal debt solutions, which require full or partial repayment of debt, are regulated by the FCA. This includes the non-statutory debt management plan (discussed in section 3.3) and the full and final settlement model, which involves offering a lump sum payment to creditors as full and final settlement of the debt.

On the other hand, formal insolvency measures, such as the individual voluntary agreement (discussed in section 3.3.4), bankruptcy (discussed in section 3.3.3) and debt relief orders (discussed in section 3.3.3), are administered by the *Insolvency Service*, an arm of the Department of Business, Energy and Industrial Strategy. They are responsible for:

* Administering bankruptcies and debt relief orders;
* Looking into the affairs of companies in liquidation, and making reports of any director misconduct;
* Investigating trading companies and taking action to wind them up and/or disqualifying the directors if there is evidence of misconduct;
* Acting as a trustee/liquidator where no private sector insolvency practitioner is in place;
* Issuing redundancy payments from the National Insurance Fund;
* Working to disqualify unfit directors in all corporate failures;
* Dealing with bankruptcy and debt relief restrictions orders and undertakings;
* Acting as an impartial source of information for the public on insolvency and redundancy matters;
* Advising the ministers of Business, Energy and Industrial Strategy and other government departments and agencies on insolvency and redundancy related issues; and
* Investigating and prosecuting breaches of company and insolvency legislation and other criminal offences on behalf of the Department of Business, Energy and Industrial Strategy.

The Insolvency Service has a subdivision, namely the Official Receiver linked to local courts that administer insolvency measures.

The insolvency profession in the UK is a regulated profession with five recognised bodies, which government ensures consistently applies regulations. These five bodies are the:

* Institute of Chartered Accountants in England and Wales (ICAEW),
* Insolvency Practitioners Association (IPA),
* Association of Chartered Certified Accountants (ACCA),
* Institute of Charted Accountants of Scotland (ICAS), and
* Chartered Accountants Ireland (CAI).

All private insolvency practitioners, liquidators or administrators must be recognised by one of these bodies to undertake these roles in the UK. About 1 200 insolvency practitioners are registered in the UK. To be a licence holder, one is required to have passed the Joint Insolvency Examination Board exams, be a fit and proper person, and have the necessary bonds/securities in place.

No insolvency practitioner may act on behalf of anyone unless there is in force security. The Insolvency Practitioners’ regulations define the requirements in which such a practitioner should operate. The Secretary of State approves such a security (bond) which makes the surety jointly liable for losses that may occur as a result of fraud of the insolvency practitioners or any person that colluded with the insolvency practitioners. This security does not cover professional negligence with most insolvency practitioners taking out additional cover against this. The bond provides two features of cover, the general penalty sum (enabling bond) and the specific penalty bond. The general penalty sum provides cover up to £250 000 (R4.46 million[[2]](#footnote-3)), renewable every 12 months. A copy is held by the authorising body and can be utilised if the insolvency practitioners failed to obtain a specific penalty sum cover in respect of an insolvency appointment. The specific penalty sum is in respect of each appointment which should not be less than the total estimated value of the insolvent’s assets.

All licensed practitioners are subject to monitoring/inspection visits which are carried out through a three-year cycle. The bodies go out and inspect Insolvency Practitioners and they look at all aspects of their work/business/practice to ensure that they are complying with all the regulatory requirements and guidelines to maintain a high standard within the profession. Failure to comply can lead to penalties being charged, deregistration and/or naming and shaming as part of disciplinary action.

* 1. **Other stakeholders**

The following stakeholders were also engaged during the study tour to the UK:

* *The All Party Parliamentary Group on Debt and Personal Finance* is one of the British Parliament’s All Party Parliamentary Groups. These are informal cross-party groups that have no official status within Parliament and are established to focus on specific areas of interest. These committees are made up of any Members of the Commons and Lords but may involve individuals and organisations from outside Parliament in their administration and activities. This Group provide a forum for MPs and peers to discuss debt and personal finance issues; to monitor legislative and other developments in this area; and to provide an opportunity for liaison between members and consumer organisations with an interest in these issues.
* *UK Finance* represents nearly 300 of the leading firms providing finance, banking, markets and payments-related services in or from the UK. It was created by combining most of the activities of the Asset Based Finance Association, the British Bankers’ Association, the Council of Mortgage Lenders, Financial Fraud Action UK, Payments UK and the UK Cards Association. Their members include large and small, national and regional, domestic and international, corporate and mutual, retail and wholesale, physical and virtual, banks and non-banks. These institutions serve individuals, corporates, charities, clubs, associations and government bodies, domestically and cross-border.

The next section describes the debt intervention measures currently available in England and Wales.

* 1. **Types of debt intervention measures**

The UK offers a number of options to assist debtors with over-indebtedness. However, most measures focus on assisting with non-priority debts, namely debts where the credit providers do not have extra powers to force consumers to pay, such as imprisonment or repossession of assets.

* + 1. **Debt Management Plans**

Debt management plans are informal agreement between a debtor and creditors to pay unsecured debts. They are used when a debtor cannot pay creditors a small amount each month or have short-term debt problems but will be able to make repayments in a few months. This option is suitable for debtors who can afford the monthly repayments on their priority debts (such as mortgage, rent and council tax) and their living costs, but are struggling to keep up with their unsecured debt.

The company will receive information about the debtor’s financial situation including assets, debts, income and creditors. It will then use this information to work out monthly payments. The affected creditors will be contacted to request their voluntary agreement to the plan. Some companies may charge a set-up fee and/or a handling fee each time a payment is made.

As this is an informal agreement, debtors are not tied into the plan for a minimum period and can cancel at any time. However, this also means It should be noted that the plan can be cancelled if agreed repayments are not up to date and unless explicitly stated in the agreement, the creditors can still ask the debtor to pay his/her full debt at a later date or take action to recover their money even if payments up to date according to the plan.

Other drawbacks are that:

* It may take longer to pay back the debt as smaller repayments are being made;
* Creditors will not necessarily freeze the interest and charges on debts.
* Creditors may refuse to co-operate or continue to contact the debtor.
* The plan may reflect on the debtor’s credit record, making future credit less accessible.
* If a licensed debt management company is used, regular payments are made to the company and it is responsible for sharing the money between the affected creditors, which removes control from the individual debtor.
  + 1. **Administration orders**

An administration order is a county court judgement or a High Court judgment for debts against an individual owing debt which should be less than £5 000 (R89 150) including any interest and charges and the capital balance owed to at least two credit providers. Debtors are required to make one monthly payment to the local court, that divide the payment among the debtors. The local court may charge a fee each time the debtor makes a payment which cannot be more than 10 per cent of the total amount owed. Debtors should be able to provide proof that they can afford regular payment. Creditors listed on the administration order cannot take further action without the court’s permission. The court determines the amount of the debt that should be repaid, the monthly repayments, and the duration of the arrangement. This arrangement is known as a ‘composition order’ where the debtor cannot pay all their debts.

The debtor is responsible for compliance with the payment agreement or the court could ask their employer to deduct money from their wages or cancel the arrangement. The administration order is added to the Registration of Judgement, Order and Fines. This is removed six years after the date the order was made.

* + 1. **Bankruptcy orders**

Insolvency procedures can be private or state implemented and can be divided into court and non-court procedures. Compulsory liquidations and bankruptcies for individuals always start in courts. The bankruptcy option is applicable for debtors who are unable to repay their debts and the equity in their assets is lower than their debts. Either the debtor can apply to be declared bankrupt or a creditor they owe at least £5 000 (R89 150) can apply to declare them bankrupt.

Most debts will be covered by bankruptcy and the remaining balance will be automatically written off at the end of the bankruptcy period. However, not all types of debt are written off and these creditors may still take action to get their money back. Debts that are not automatically written off include: (i) **magistrates court fines; (ii)** any payments a court has ordered under a **confiscation order**, for example, for drug trafficking; (iii) **maintenance payments and child support payments**; (iv) **student loans; (v) secured loans** and other secured debts, such as debts secured with a charging order; (vi) debts owed due to the **personal injury or death** of another person; (vii) **social fund loans; and (viii) some benefits and tax credits overpayments. However, an outstanding amount on a mortgage loan after the home has been sold will be covered.**

The debtor can apply online or in writing for a non-refundable fee of £680 (R12 124.40) (an adjudicator fee of £130 (R2 317.90) and a deposit of £550 (R9 806.50)), which can be paid in full or in instalments. It is a criminal offence to make false statements or deliberately withhold information about all property and a debtor can be fined or sent to prison for any intentional misrepresentation. However, the debtor bears no cost if a creditor initiates the bankruptcy application.

Once a bankruptcy order is made, the debtor’s accounts will usually be frozen and their money will come under the control of the Official Receiver. The Official Receiver will arrange an interview with them. After the interview, the Official Receiver will tell the creditors about the bankruptcy and send them a report with a summary of his/her financial situation. Assets may be sold to pay off some or all of the debt. The debtor’s name and bankruptcy details will be published on the national register of bankruptcies, called the Individual Insolvency Register.

There may be other ongoing costs that will be paid from any assets and/or spare income, called the **bankruptcy estate**, before the rest of it is distributed among creditors. These costs might include: (i) professional fees for solicitors (attorneys); (ii) expenses for any professionals, such as the trustee, engaged to act on the debtor’s behalf; (iii) any other administrative costs; and (iv) the cost of selling a home, such as estate agents' fees. **However, if the bankruptcy estate does not have enough money or belongings of value in it to cover these costs, the debtor does not have to pay them.**

The bankruptcy order normally ends after a year and will be communicated by the Official Receiver. Most debts that have not been paid will be written off with the exception of those mentioned above.

After the period, the debtor may still have a bankruptcy restriction order made against them. This can last up to 15 years and will restrict their financial affairs where the debtor has transgressed the rules during the bankruptcy period.

The benefits of going into bankruptcy are:

* The debtor may make a fresh start once the bankruptcy order is over, usually after a year.
* The pressure is taken off the debtor as they do not have to deal with their creditors.
* The debtor may retain certain possessions, like household goods and a reasonable amount to live on.
* Creditors have to stop most types of court action to get their money back following a bankruptcy order.
* The money still owed, after the bankruptcy state has paid out can usually be written off.

However, there are drawbacks, such as:

* The application fee of £680 (R12 124.40).
* Debtors with sufficiently high income will be required to make payments towards their debts for three years.
* It may be more difficult to take out credit while the debtor is bankrupt and their credit rating will be affected for six years.
* A residential home and some possessions, particularly luxury items, may have to be sold.
* Debtors that are, or are about to be, the right age to receive their pension savings, may have this taken to contribute towards debt settlement.
* There are restrictions for some professions where a person who has been declared bankrupt they may no longer carry on working in these.
* If a business is owned, it may have to be closed down and the assets sold off.
* It could affect the debtor’s immigration status by jeopardising an application to become a British citizen, or bar the debtor from acting as a sponsor for a dependent wanting to enter the UK.
* The bankruptcy will be published in a public record.
  + 1. **Individual Voluntary Arrangements (IVA)**

An individual voluntary arrangement is a formal and legally-binding agreement between a debtor and his/her creditors to pay back debts over a period of time, usually about five years and outstanding balances are written off after this period. This must be set up by an insolvency practitioner. It can be flexible to suit the debtor’s needs but it can be an expensive option and there are risks to consider. Most debts can be paid off through an IVA but there are some exceptions, namely:

* Maintenance arrears that have been ordered by a court,
* Child support arrears,
* Student loans, and
* Magistrates court fines.

In addition, creditors must agree that secured loans can be included. Furthermore, although there are no minimum or maximum limits set by the law and no minimum number of loans that must be included; in practice, creditors are unlikely to agree to an IVA if total debt is less than £10 000 (R178 300) and there are fewer than three debts and two different creditors.

IVAs are expensive, as a qualified insolvency practitioner must set them up. In addition, consumers must have long-term, steady income and assets for this to be feasible. Furthermore, an IVA may affect occupation in certain professions, as well as the security of assets and savings, including personal pensions. The IVA also allows for the refinancing of mortgages to release equity as a lump sum into the process as part of the proposal.

* + 1. **Debt Relief Orders (DROs)**

Debt relief orders were introduced under the Tribunals, Courts and Enforcement Act, 2007, and came into force on 6 April 2009. DROs are an administrative insolvency measure rather than a court-based one and are made by Official Receivers working in partnership with the professional debt advice sector.

A DRO is a cheaper option than going bankrupt and a person in financial difficulty can apply for one if they cannot afford to pay off their debts. To apply for a DRO, the applicant must satisfy strict eligibility criteria, namely:

* Debts of no more than £20 000 (R356 600) (increased from £15 000 (R267 450) from 1 October 2015);
* Less than £1 000 (R17 830) worth of assets or savings[[3]](#footnote-4),[[4]](#footnote-5) (increased from £300 (R5 349) from 1 October 2015);
* Less than £50 (R891.50) a month spare income after paying off household bills[[5]](#footnote-6);
* Has lived or worked in England and Wales within the last three years; and
* Must not have been subjected to a DRO within the last six years.

The focus is therefore on consumers who are financially excluded from other debt relief remedies, have relatively low levels of liabilities, no assets over and above a nominal amount and no surplus income with which to come to an arrangement with their creditors. Therefore, it offers to alleviate debt through a simple and relatively cheap administrative process only for consumers who cannot pay even a portion of their debt within a reasonable timeframe.

A DRO lasts for 12 months, during which time creditors cannot take debt recovery action against the debtor without court permission. At the end of the year, the debtor will be free of all the debts listed in the order provided his/her circumstances have not changed[[6]](#footnote-7). However, the debtor may only apply once every six years. The rationale for a 12-month process was linked to the need to offer consumers a fresh start and that the credit market should then reassess them on the risk to the provider and the consumer’s ability to afford the loan and its repayments while being able to meet their living expenses.

Eligible debts include: (i) credit cards, overdrafts, loans; (ii) rent, utilities, telephone, council tax; (iii) benefit overpayments and social fund loans; (iv) hire purchase or conditional sale agreements; and (v) ‘buy now-pay later’ agreements. Only debts declared at the time of the application can be covered by the DRO. However, certain types of debt cannot be included in a DRO and creditors may still pursue the collection of these. These include: (i) child maintenance, or anything owed under family proceedings; (ii) student loans, budgeting and crisis loans from the Social Fund; (iii) debts secured against an asset; (iv) fines for drug offences; (v) damages or fines a court has ordered against the debtor; (vi) unpaid TV licence fees; and (vii) any debts incurred after the DRO is granted.

An applicant can only apply for a DRO with the assistance of an ‘approved intermediary’. An approved intermediary means a trained debt advisor who has been approved to act as an intermediary by a competent authority. In practice, the debtor would apply for a DRO online, with an approved intermediary helping to complete the application form.

In the Committee discussions with the IPA, they informed the Committee that the debtor pays a fee of £90 (R1 604.70) of which payments could be made at the Post Office or a Payzone[[7]](#footnote-8) outlet. This fee may be paid in instalments and must be completed before, or on the day, that the application is submitted online via an approved intermediary to the Official Receiver. The fee is towards the administrative cost of the Official Receiver and includes a payment of £10 (R178.30) towards the costs of the intermediary. Debtors living in England, Wales and Northern Ireland can also request assistance with this fee from various charities, utility companies or trust funds.

However, StepChange Debt Charity was of the view that the £90 (R1 604.70) fee still acts as a barrier to entry for debtors to access DROs. Simultaneously, the low fee to intermediaries does not cover the operational cost of processing DROs, which may perversely incentivise intermediaries who also act as debt advisors or are part of commercial firms to steer qualifying debtor to options that may be more lucrative for them. The intermediary is also not allowed to charge a debtor an additional fee in connection with assistance provided in respect of an application for a DRO.

Upon receipt of the application and payment of a fee, an Official Receiver is able to process the DRO, without the involvement of the court. However, the Official Receiver is also able to refuse to make an order or can choose to delay the decision pending further information from the applicant.

For the duration of the DRO (usually 12 months), the debtor will be subject to similar restrictions as in bankruptcy. Such restrictions include:

* The debtor must not obtain credit of £500 (R8 915) or more, either alone or jointly with another person, without disclosing to the lender that they are subject to a DRO;
* The debtor may not carry on a business (directly or indirectly) in a name that is different from the name under which they were granted a DRO, without telling all those with whom the debtor does business the name under which they were granted a DRO; and
* The debtor may not be involved (directly or indirectly) with the promotion, management or formation of a limited company, and may not act as a company director, without the court’s permission.

In addition, the debtor’s details are published on the Insolvency Service’s Individual Insolvency Register.

Successful applicants of DROs are obliged to provide full and accurate financial information to and co-operate with the Official Receiver; and are expected to repay their creditors should their financial circumstances improve. Applicants are also not allowed to give away or sell their assets to qualify for a DRO. In addition, their credit ratings are affected and there are civil and criminal penalties if the system is abused. The Official Receiver may investigate cases independently or if an objection is raised by creditors. If it is found that a debtor has deliberately failed to disclose all information related to his/her financial affairs or fraudulently represented this, the DRO may be revoked, the restrictions can be extended up to 15 years or the debtor can be prosecuted and fined and/or sent to prison. StepChange also informed the Committee that they have an agreement with credit reference agencies to verify financial information of consumers to ensure that they comply with the necessary criteria.

In its engagement with the IPA, the Committee enquired about the impact of the introduction of the DROs and whether there was a significant uptake. The IPA informed it that there had not been a high number of applications. They were of the view that the qualification criteria addressed the moral hazard and that only those consumers who met the strict criteria were captured. Another reason was that DROs can only be applied for through approved registered intermediaries who would have had to assess the applications beforehand. These safeguards contributed to the prevention of people who did not qualify from applying for and accessing the DRO process. StepChange Debt Charity concurred that the conditions and safeguards attached, such as low income low assets; the restriction on accessing debt; and the registration of recipients; addressed the moral hazard concerns. There had also not been an increase in people seeking new debt and the cost of credit to this target group had not increased. It also should be noted that discharging of debt predates the 1914 Bankruptcy Act in the UK.This is not a new concept under Insolvency Law and therefore the reaction to the introduction of a DRO to address the market failure with respect to the provision of debt relief measures for a specific group of consumers was not significant.

* 1. **Regulation of credit market**

As mentioned above, the FCA is the main role player responsible for regulating the credit market from a consumer protection perspective. The FCA has adopted a principle-based approach to regulation, which places a bigger emphasis on credit providers to take responsibility for their actions within this framework. The principles for business are:

* *“Integrity*: A firm must conduct its business with integrity.
* *Skill, care and diligence*: A firm must conduct its business with due skill, care and diligence.
* *Management and control*: A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
* *Financial prudence*: A firm must maintain adequate financial resources.
* *Market conduct*: A firm must observe proper standards of market conduct.
* *Customers' interests*: A firm must pay due regard to the interests of its customers and treat them fairly.
* *Communications with clients*: A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.
* *Conflicts of interest*: A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client.
* *Customers’ relationships of trust*: A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.
* *Clients' assets*: A firm must arrange adequate protection for clients' assets when it is responsible for them.
* *Relations with regulators*: A firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice.”[[8]](#footnote-9)

In addition, there are principles for good regulation that the FCA must adhere to or take into consideration when regulating the market, namely:

* *Efficiency and economy*: It is committed to using its resources in the most efficient and economical way. As part of this the Treasury can commission value-for-money reviews of its operations.
* *Proportionality*: It must ensure that any burden or restriction that it imposes on a person, firm or activity is proportionate to the benefits it expects as a result. To judge this, it takes into account the costs to firms and consumers.
* *Sustainable growth*: It must ensure there is a desire for sustainable growth in the economy of the UK in the medium or long term.
* *Consumer responsibility*: Consumers should take responsibility for their decisions.
* *Senior management responsibility*: A firm’s senior management is responsible for the firm’s activities and for ensuring that its business complies with regulatory requirements. This secures an adequate but proportionate level of regulatory intervention by holding senior management responsible for the risk management and controls within firms. Firms must make it clear who has what responsibility and ensure that its business can be adequately monitored and controlled.
* *Recognising the differences in the businesses carried on by different regulated persons*: Where appropriate, it exercises its functions in a way that recognises differences in the nature of, and objectives of businesses carried on by different persons subject to requirements imposed by or under the Financial Services and Markets Act, 2000.
* *Openness and disclosure*: It should publish relevant market information about regulated persons or require them to publish it (with appropriate safeguards). This reinforces market discipline and improves consumers’ knowledge about their financial matters.
* *Transparency*: It should exercise its functions as transparently as possible. It is important that it provide appropriate information on its regulatory decisions, and that it is open and accessible to the regulated community and the general public.[[9]](#footnote-10)

The FCA informed the Committee that it recently reviewed its principles based on feedback from banks/firms. Banks and firms were calling for clear guidelines in relation to the credit-worthiness assessment processes within individual firms, and the relationship with credit scoring and with credit rating agencies. It published a consultation paper in 2017 which essentially concluded that there was no evidence that would suggest that a more prescriptive regime would be better. However, the FCA did attempt to clarify its expectations through the principle-based approach in the consultation paper.

One of the critical principles is treating customers fairly. In this regard, the FCA requires credit providers to show forbearance to customers who approach them when they are in financial difficulty or whom the credit provider suspects may have financial difficulty. For instance, the credit provider should not place undue pressure on or threaten a debtor by sending aggressive enforcement letters about taking legal action or threatening repossession of a home or a car. The credit provider should also offer the customer who cannot pay immediately some time to recover and to repay. After 60 days of non-payment, it may be fair for a firm to take some kind of enforcement action. In which case, they could approach the courts to either declare bankruptcy or issue a time order. If the creditor is awarded a time order, the consumer would be given a certain time to pay the debt within. Alternatively, the consumer may request a time order or a change in the interest rate to provide a grace period in which to settle the debt and avoid repossession of his/her assets, if he/she has fallen behind on repayments.

Furthermore, the FCA is able to set rules related to market conduct, including setting interest rates or charge caps and banning products which they view as harmful. However, this is not their preference, as this may raise the costs of doing business that is passed on to consumers.

In addition to this measure, the FCA may require credit providers to provide redress to individual consumers who fall victim to poor or prohibited market conduct. For instance, where a personal loan is granted to someone who does not have the capacity to sign due to a mental illness, action can be taken against this unfair contract. This power is considered to be more effective than strict regulations and is incorporated as part of its proactive supervisory role for large firms.

Firms must regularly report on a number of areas, such as arrears, and the FCA may engage on problem areas related to policies and processes around customer treatment. If it notices negative trends, it may randomly request to inspect a selection of case files to see how the firm has assisted debtors. Furthermore, the FCA works with the Financial Services Ombudsman and monitors complaints around customer treatment. If there are spikes in complaints in a specific area in a few firms or across a sector, then it will investigate this. It can also require firms to pay for an auditing firm to review specific areas, such as policy processes or skills of employees. If any shortcomings are found, the firms are required to address this. In response to serious challenges where consumer protection is compromised, the FCA can require firms to repay interest or the full value of the debt to debtors as redress for poor market conduct.

Furthermore, the FCA has the power to fine credit providers and to ban misleading adverts about credit. It is also a criminal offence to lend money without being authorised to do so.

* + 1. **Regulating illegal or unscrupulous lending practices**

In terms of illegal lending, the England Illegal Money Lending Team (IMLT) was set up in 2004 under the National Trading Standards. However, it has recently moved to the FCA.

Initially, it was created as a pilot scheme in Birmingham to investigate loan sharks or illegal lenders and has proven to be very effective. The English IMLT has evolved to investigate and prosecute illegal money lenders, rogue traders and internet scams while supporting those who have borrowed money from a loan shark. IMLTs in Scotland and Wales ensure that the UK is working together to stop loan sharks.

Each team is comprised of specialist investigators and Liaise Officers who have previously worked for the police, trading standards, and debt advice services. Together the investigators and Liaise Officers work to prosecute illegal money lenders while supporting people who owe money to a loan shark. Since 2004, the England IMLT have supported over 28 000 people and written off over £73 million (R1.3 billion) of debt.[[10]](#footnote-11)

It is estimated that there are 310 000 people in debt to illegal money lenders in the UK. The IMLTs within the UK work to raise awareness of what illegal money is while investigating and prosecuting loan sharks. The England IMLT work closely with education providers and partner agencies such as the police, housing associations, and debt advice service organisations to raise awareness of the problems and issues that illegal money lending causes.

HM Treasury and the FCA also reported that victims of illegal lending were supported to recover from this type of debt and are encouraged to join credit unions. The State offers them cash incentives if they do join. These incentives are funded from money seized from loan sharks.

Other unscrupulous practices are mainly among high cost lenders, such as payday lenders, which are legal, but their practices have been questionable and often contributed to over-indebtedness. High cost credit tends to be extended to consumers with poor credit records despite the fact that they are unable to pay. In the case of payday lending, Parliament had requested that the FCA sets a cap on the interest that may be charged. This was due to the lack of competition in the industry, the industry not applying affordability assessments, and recovering repayments from consumers’ accounts without consideration of their ability to live; as well as the failure by the FCA to curb payday lending.

* 1. **Credit cards**

The FCA has introduced new regulations for credit cards, as there was a trend for some consumers to consistently pay the minimum instalment while the capital balance of the credit loan was either growing or not being paid off over years due to the proportion of interest to the capital repayment. Now credit providers are required to request a consumer who has only repaid the minimum instalment over a period of 18 months to increase their repayment and to assess whether the borrower is capable of borrowing more or whether an intervention is required. This is monitored over a further 18 months and if there is no change, a credit provider must suspend the credit facilities and turn the outstanding balance into a fixed term loan to prevent persistent debt for credit cards.

* 1. **Mandatory credit life insurance**

Similar to the South African proposal, the UK had compulsory credit life insurance applied to credit agreements. It was reported that firms would enter into credit agreements and automatically add payment protection insurance to protect against job losses, as any residual liability for debt did not pass on to family beyond what the estate can settle. Various stakeholders reported that there had been a recent scandal related to this market due to misapplication as consumers were either not aware of the insurance or it was a very low risk that they could default in this regard.

Furthermore, the market had not been organized and only commercial firms were active in it charging very expensive rates to especially low income consumers, which enriched the lenders with little benefit to consumers. In spite of these difficulties, StepChange Debt Charity and the All Party Group on Debt and Personal Finance agreed that common risk could be a good thing if effectively organised and not seen as a “cash cow” by lenders.

* 1. **Funding of free debt advice**

In the Committee’s engagement with various stakeholders the issue of funding for debt advisors became a central concern. In the UK, advice charities existed for more than 80 years. They evolved to focus on debt advice to mitigate the impact of the economic crisis in the UK during the 80s and 90s driven by mass retrenchment in the mining sector. Currently, there are a number of sources for funding debt advice such as, through voluntary donations for charities, government funding, creditors through the fair share agreement for debt management plans, and an involuntary arrangement such as the levy on credit providers.

Under the fair share agreement, no direct debt service fee is charged to the consumer who pays the full repayment amount agreed. Creditors are requested, by the debt advice organisation, to contribute a percentage of the amount paid. This amount varies depending on the debt management plan.

There is general recognition that, notwithstanding other funding sources, the voluntary contributions to fund debt advice organisations are critical. These donations are mostly from private individuals, utilities, and the corporate sector. The statutory industry levy on credit providers are the other critical source of funding for free debt advice. Levies are funded by those that directly profit from lending.

With a potential increase in demand for debt advice due to the potential impact of Brexit, the question arose about who should ultimately be responsible for paying for debt advice. The debt advice sector indicated that the current contribution of free debt advice service would be insufficient if there is a significant increase in demand for debt advice due to job losses.

* 1. **Changes in legislation**

On 10 May 2018, the Financial Guidance and Claims Act received royal assent. The Act makes provision to establish a new financial guidance body (including provision about a debt respite scheme); to make provision about the funding of debt advice in Scotland, Wales and Northern Ireland; to provide powers to make regulations prohibiting unsolicited direct marketing in relation to pensions and other consumer financial products and services; and to make provision about the regulation of claims management services.

The new financial guidance body merges the existing services provided by Pension Wise, the Pensions Advisory Service and the Money Advice Service to create a clear, single financial guidance body, expected to be launched later this year. The body's aim is to ensure that savers are able to access free and impartial pensions and money guidance, as well as debt advice, in one place.

Furthermore, a proposal around a debt respite (or “breathing space”) scheme should be developed by this new body. The intention of such a scheme is to provide for one or more of the following: (i) protect individuals in debt from the accrual of further interest or charges on their debts during the period specified by the scheme; (ii) protect individuals in debt from enforcement action from their creditors during that period; and (iii) help individuals in debt and their creditors to devise a realistic plan for the repayment of some or all of the debts.[[11]](#footnote-12)

1. **Key observations**

Based on its engagements, the Committee made the following key observations:

* 1. Credit regulation in the United Kingdom appears to be more debtor-friendly than in South Africa, as the Financial Conduct Authority’s expectation of credit providers is to show forbearance when a consumer has approached them regarding financial difficulty or appears to be in financial difficulty. They should refer the consumer to sources of free debt advice without placing undue pressure on them to pay or taking disproportionate action against the consumer in the short term. This expectation is possible given the principle-based regulatory approach the regulator follows, as credit providers are expected to apply a set of principles while taking responsibility for their actions. South Africa, on the other hand, has a more rigid, rules-based approach. The rules-based approach may disincentivise credit providers to inherently act in a manner that treats consumers fairly, as long as they can show that they have applied the rules.
  2. The English and Welsh debt relief system is set up to honour ‘prioritised’ debt, namely those that have assets underlying them or have secondary consequences for the consumer should they default. It is also purported that most consumers want to repay their debts, as most of the debt relief interventions, while providing a fresh start, affects the consumer’s credit record and the likelihood that they can access credit in future. Therefore, the options available to them are rarely abused.
  3. The United Kingdom has a long history of insolvency measures that involve the discharge of debt after settling debt with the debtor’s assets and/or available income as far as possible. Therefore, the introduction of the debt relief order, which fills a gap for individuals who would otherwise not be able to qualify for or afford a bankruptcy or administration order, did not have an adverse effect, as there was a clear gap in the market.
  4. The Committee was concerned about the link between the debt advisors and debt adjusters/intermediaries in the English and Welsh system, as there may be an incentive, particularly in the commercial sector, to favour interventions that provided more fees to the debt advice organisation even when the option recommended is not the most suitable for the consumer’s circumstances. Currently, interventions that target the most vulnerable consumers offered the lowest fees to intermediaries and did not cover the cost of administering these interventions. This may increase the cost for consumers or keep them indebted for longer than necessary.
  5. The English and Welsh debt relief order option for low income, low assets consumers with only unsecured debt (non-prioritised debt) has not presented any significant moral hazard, as the target group is fairly small and there are grave consequences if a consumer deliberately altered their finances to meet the strict criteria.
  6. Key economic crises in the United Kingdom, such as the mining closure in the mid-80s, the credit booms in the 90s and the 2008 economic crisis, saw a significant number of people becoming over-indebted. These phenomena resulted in the establishment and evolution of the debt advice sector.
  7. One of the mechanisms that enable free debt advice and financial literacy for consumers and scholars was the introduction of a levy on credit providers. Credit providers are represented through a Financial Conduct Authority panel that monitor the management of the funds in a transparent and accountable manner. However, there was concern that financial literacy training at school level was still fragmented, as teachers were not always confident in teaching the subject matter and the curriculum not always being uniformly implemented.
  8. The business model of most payday lenders in the United Kingdom was based on the premise that debtors would default on their repayment. This was mainly marketed to low-income consumers, with no affordability assessments and high interest rates being applied in an uncompetitive manner leading to a rise in over-indebtedness amongst this group. Therefore, the legislature[[12]](#footnote-13) decided that a cap on interest rates should be introduced in spite of the more flexible regulatory approach of the Financial Conduct Authority. This cap on interest rates made it less profitable for payday lenders to maintain this model; however, responsible payday lenders have subsequently managed to operate at profitable levels.
  9. The measures to address illegal lending were quite extensive and decisive. They provided a disincentive to illegal lenders to continue as they could be prosecuted and their proceeds would be confiscated if caught; while assisting victims of illegal lending by offering a rehabilitation option to establish a savings fund through credit unions to curb future financial challenges.

1. **Acknowledgements**

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The Committee wants to express its deep appreciation to HM Treasury, the Financial Conduct Authority, the Insolvency Service, the Insolvency Practitioners Association, the All Party Group on Debt and Personal Finance, StepChange Debt Charity, the Money Advice Trust and United Kingdom Finance for their valuable contribution to the discussion. The Committee also wishes to thank its support staff, in particular the Committee Secretary, Mr A Hermans, and the Content Advisor, Ms M Sheldon, for their professional support and conscientious commitment to their work.

The Chairperson of the delegation thanks all Members for their active participation during the process of engagement and deliberations and their constructive recommendations made in this report.

1. **Recommendations**

Informed by its deliberations, the Committee recommends that the House requests that the Minister of Trade and Industry should consider:

* 1. Engaging with the Minister of Finance to consider introducing a levy on credit providers for the National Credit Regulator to facilitate financial literacy training and free debt advice for consumers.
  2. Engaging with the Minister of Basic Education to consider including financial literacy and budget management as a compulsory part of the curriculum.
  3. Improving the distribution of consumer education information by the National Credit Regulator in all official languages.
  4. Expediting the review of the National Credit Act, 2005, including the implementation of measures to confiscate the proceeds from convicted illegal lenders and providing more accessible debt advice/counselling to lower income consumers.

Report to be considered.

1. The debt interventions that were considered are specifically applied in England and Wales, as different jurisdiction are permitted to vary their legislation. It was indicated that Scotland and Northern Ireland have fundamentally different legislation in this regard. [↑](#footnote-ref-2)
2. The conversion is based on the ZAR/GBP exchange rate as on 14 June 2018 of R17.83/GBP (Business Day website). [↑](#footnote-ref-3)
3. This does not include pension schemes since April 2011. [↑](#footnote-ref-4)
4. The asset value is based on Section 283(2) of the Insolvency Act of 1986 which defines the bankruptcy estate outlines which assets should not be included, such as clothing, bedding, furniture, household equipment and provisions as are necessary for satisfying the basic domestic needs of the bankrupt and his family. [↑](#footnote-ref-5)
5. The rationale for the £50 is to allow the consumers to be able to save and rebuild the savings culture. [↑](#footnote-ref-6)
6. Changed circumstances would include an increase in income, an inheritance received or errors or omissions that were erroneously missed. [↑](#footnote-ref-7)
7. Payzone is a consumer payment company founded in 1995 in the UK. It rents payment terminals to retailers (outlets) including web traders, to accept credit card payments both for goods sold onsite, utilities, bridge tolls, lottery tickets and the like. [↑](#footnote-ref-8)
8. FCA (2016) [↑](#footnote-ref-9)
9. Ibid [↑](#footnote-ref-10)
10. StopLoanSharks website, accessed on 14 June 2018. [↑](#footnote-ref-11)
11. Financial Guidance and Claims Act, 2008 Section 6(2) [↑](#footnote-ref-12)
12. The UK legislature consists of the House of Lords and the House of Commons. [↑](#footnote-ref-13)