



# ‘Breathing Space’ from Creditor Enforcement

*Striking the right balance between  
people in debt and their creditors*

June 2015

## Executive Summary

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In any personal insolvency regime, it is paramount that people in financial difficulty are able to access the debt solution that will address their financial difficulties most appropriately. This should allow them to rehabilitate themselves financially as quickly as possible, and it should also ensure that their creditors receive the best repayment outcome possible in the circumstances, thereby achieving a balance between indebted individuals' and creditors' interests.

Financial troubles and 'insolvency' may reflect a permanent or temporary state. On a technical definition, becoming 'insolvent' means that individuals can no longer afford to repay the debts they owe; this includes both the situation where a person has been unable to pay their bills for a long period of time and has little hope of recovering financially without seeking help, as well as the situation where someone is experiencing short-term cash flow problems (such as an inability to keep up with minimum repayments on credit cards).

Such individuals will usually be provided with various notice periods before a creditor can seek to collect or enforce a debt; these vary in length depending on the kind of debt involved – for example, under the Mortgage Repossession Protocol, a mortgage lender must give a debtor six months' notice before they can enforce the security over their house. In addition to the range of notice periods provided to indebted individuals, the Financial Conduct Authority also enforces a robust regime governing how creditors can collect or enforce debts, with the ultimate aim of treating consumers fairly ('TCF') throughout the debt collection process.

Nevertheless, despite the existence of these notice periods, the FCA's TCF policies and the range of formal and informal debt solutions, R3 is concerned that these financially distressed individuals may not always access the solution best suited to their needs. This may be due to a combination of poor or incomplete debt advice, and a sense of panic that pushes them to either accept the first solution offered to them (even where it may not be the most appropriate solution for their needs) or, worse still, to 'bury their head in the sand' and do nothing at all.



**In summary, R3's proposals are:**

- A person in financial distress should be able to apply to the Insolvency Service through a qualified advisor for a **28 day moratorium**, during which no creditor action would be possible and repayments, interest and charges would be frozen. During this period, it would be **mandatory for the individual to seek debt advice from a qualified advisor in order to devise an appropriate exit strategy**.
- It should be **mandatory that the availability of this moratorium be advised to every financially distressed individual** (whether by a solution-provider, a charity, an insolvency practitioner, the Court or the Insolvency Service) before that individual is advised to enter a debt relief solution or a bankruptcy order is made. It would not be mandatory for all individuals to make use of the moratorium – this would be a matter of choice for each person.
- **Creditors would be notified** that a moratorium has been granted, and it also would be registered on a **central register**. After the 28 day period has expired, the debtor will be subject to creditor action once again (unless he/she has entered a debt solution which prohibits this or makes it redundant), and the individual's name will be removed from the register.
- **Only one moratorium should be available per individual per year**, to avoid it being used as a tool to avoid repaying their debts (rather than facilitating advice and entry into a debt solution).

This moratorium should be seen as a last resort, usually after the indebted individual has already received numerous notices of debt collection and enforcement, and would be a final opportunity to seek professional debt advice in an unpressurised environment. This would be with a view to entering the most appropriate debt solution for their financial situation, in a considered and informed manner.

**R3's 'breathing space' proposal would:**

- give individuals time to get full advice about the range of debt solutions available to them;
- enable people to make non-pressurised decisions about how to resolve their financial problems by providing the right environment, free from creditor pressure, in which they can find and enter the most appropriate solution for their needs; and
- help achieve a balanced and fairer outcome for both individuals and their creditors.



## Setting the scene – the current situation in England and Wales

The financial struggles of people in England and Wales caused by the cost of living, and the high incidence of those living at the edge of their means are well documented. Household debts have returned to their pre-financial crisis levels and an interest rate rise looms on the horizon. It is therefore unsurprising that concerns about money, in particular debts, are also rife. R3's most recent Personal Debt Snapshot<sup>1</sup> found that nearly half (46%) of British adults are at least "fairly" worried about their current level of debt, and two in five (41%) say that they struggle to get to payday.

England and Wales also saw an explosion of personal insolvencies in the opening years of the 21st century: new insolvencies quadrupled between 2002 and 2010. In 2014, nearly 100,000 people in England and Wales entered into a formal insolvency procedure and, whilst the official number of personal insolvencies has fallen over the past few years, there are potentially thousands more people unaccounted for, either in informal repayment plans or continuing to struggle on without addressing their debts.

Against the backdrop of the high levels of debt problems being experienced by the British public, it is vital that the debt advice and personal insolvency systems operate at their optimum – so that comprehensive advice can be given to help financially distressed people enter into the most appropriate debt relief solution for their circumstances (whether informal or statutory), and so that creditors can hope to receive the maximum repayment of debts as far as possible.

Yet, for a variety of reasons, there are still individuals in financial difficulty who are entering solutions that are not appropriate for their circumstances. A large number of options, combined with poor, incomplete or ill-informed advice, often mean that people are not always aware of the various debt solutions available to them. Financially distressed people may frequently find that they do not know where to turn to resolve their situation<sup>2</sup> and they may feel pressure to enter the first solution they are given – even where this may not be the most appropriate solution for their situation. Worryingly, nearly half of R3 members (49%) who work in personal insolvency said that it typically takes an individual more than a year from first showing signs of financial distress to approaching them for advice. This demonstrates a worrying trend of individuals simply 'burying their heads in the sand', making it more difficult to establish an appropriate solution than if advice had been sought at the outset.



R3 is concerned about some aspects of the quality and range of advice being given to people with debt problems and, in particular, the lack of provision of an environment in which indebted individuals are able to make important decisions about how to resolve their financial problems. While there is certainly merit in having safeguards in place to ensure that creditors give individuals sufficient notice of debt collection and enforcement action, along with a number of debt solutions to suit a range of circumstances, individuals should be able to make a decision about which debt remedy to pursue based on full advice. They need to be able to do so in an environment which enables them to weigh up the full range of options, along with the implications for them personally, before making a decision.

<sup>1</sup> A survey of 2,011 British adults undertaken in March 2015

<sup>2</sup> Research commissioned by R3 in March 2014 suggests that 42% of British adults with debt worries are most likely to approach a family member for advice. Whilst this may be unsurprising, R3 is concerned that relatively so few people would seek the expert advice that is available – and that relatively so many British adults (21%) wouldn't know who to turn to at all for advice.

## **'Breathing space' – facilitating the space needed to take debt advice**

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The introduction of a final period of 'breathing space' in the form of a moratorium from any creditor action for 28 days would provide individuals with respite from daily creditor pressure to make a fully-informed decision. During the moratorium, individuals would be required to seek debt advice from a financial or professional advisor. At the same time, creditors would be unable to take any debt collection or enforcement action against the individual (including petitioning for their bankruptcy), and repayments, charges and interest accruing on the debts would be frozen from the date of the application for the moratorium.

The need to maintain the balance between protecting potentially vulnerable individuals on the one hand whilst maintaining the fundamental principle of repaying debts must be recognised. For this reason, R3 believes that 28 days is an adequate amount of time. A longer period would risk unduly 'dragging out' the process which would be unfair to both individuals and creditors, particularly considering the existing notice periods that apply to debt collection, whilst less time would not provide sufficient respite to allow individuals to make a sensible and appropriate decision based on proper advice.

### **Making comprehensive advice available to all indebted individuals**

Any person or organisation advising on formal debt solutions (including Debt Management Plans) should be required to inform individuals of the availability of the moratorium before recommending a particular debt solution. This requirement should also apply where a creditor petitions for an individual's bankruptcy, and the availability of the moratorium should be pointed out to an individual by the Court or the Insolvency Service before they can petition for their own bankruptcy. This would ensure that, as far as possible, all financially distressed people are aware of the opportunity to take full advice before entering any particular debt relief or repayment solution, albeit their use of the moratorium would be optional and depend on the individual's own choice.

### **Process to apply for the moratorium**

R3 suggests that only qualified debt advisors would be able to apply to the Insolvency Service to obtain a moratorium on the individual's behalf. Once granted by the Insolvency Service, the moratorium would be for a period of 28 days to enable the person to take full and appropriate advice from a qualified advisor.

Upon the moratorium being granted, the advisor would actively notify all relevant creditors of its existence, and notice of the moratorium would be also be registered in a central register which could be searched actively by creditors.

### **Developing an 'exit strategy'**

During the moratorium, debt advice must be taken from a duly qualified advisor towards devising an 'exit strategy' for the individual to resolve his or her situation or to find the most appropriate debt relief solution.

The 'exit strategy' could include the individual's affairs being sorted out informally (for example by negotiating with creditors or arranging a debt repayment plan), or it could mean identifying an appropriate formal insolvency procedure/solution. A requirement to prove that advice is being taken should be built into the process, to stop individuals from using it as a time-wasting tool or a delay tactic to prevent creditors from enforcing their rights to seek repayment of a debt. This would ensure that the moratorium could not be used to delay the inevitable – it is intended to be a final period of time for advice to be taken and an appropriate exit plan to be made, rather than a remedy in itself.

In R3's view, a maximum of 28 days' moratorium is sufficient to give an individual time to consult a debt advisor and to determine whether an informal or more long-term debt solution is needed. This time period is also likely to be less objectionable to creditors, as it is a reasonable, finite period during which they would be required to stop interest, charges and enforcement action to give the person the 'breathing space' that they need. This achieves a balance between both creditors' and the individual's interests.

Where a company is going through an insolvency procedure, involvement of an insolvency practitioner throughout the process provides comfort to creditors that the company has received the most appropriate advice for its circumstances and is entering an insolvency solution designed to provide the best return to creditors, where possible. Similarly, in the case of breathing space for individuals, R3 envisages that the entire process of applying for a moratorium and devising an appropriate exit strategy during its existence would be managed by a qualified advisor, thus providing similar reassurance to creditors and the best outcome possible for the individuals involved.

### Creditor challenge

Where they believe that it is being used as a time wasting tactic, there should be a method for creditors to challenge a moratorium by appeal to the Insolvency Service, with ultimate recourse to the court. This could be, for example, where a debtor is unable to provide proof that advice is being sought. Where this is the case, all previously-frozen repayments, charges and interest would be backdated to the beginning of the moratorium period, and it would then be open to creditors to re-start debt collection action as usual.

### Completion of moratorium

Once the moratorium has expired, the person would be subject to creditor action again, provided that he or she has not already entered an insolvency or debt repayment solution which prohibits this.

R3 suggests that an individual should only be entitled to one moratorium per year, to avoid it being used as a temporary escape route rather than a method of finding an appropriate, permanent solution to resolve their financial situation.

### Funding

The system should be funded by a one-off, non-refundable fee paid by the debtor on application for the moratorium. This fee would not be so high as to prevent access to the breathing space, but is necessary to further ensure that the moratorium is not used as a time-wasting tactic simply to delay the inevitable.

## The bigger picture – the wider personal insolvency landscape

In addition to addressing the need for individuals to be able to seek expert advice about their financial situation free from the pressure of creditor action, R3 also believes that clear, uniform personal insolvency regulations would assist in ensuring that debtors enter the correct solution for their needs. While the UK is home to one of the world's most effective insolvency regimes, according to the World Bank, the scale and nature of personal debt in England and Wales has changed rapidly in the past decade, with insolvency numbers more than trebling in a short space of time; it is therefore important that the insolvency regime changes with it. Without reform, indebted individuals will struggle to access a debt solution that is right for their situation – this exacerbates the debtor's problems and is of no benefit to creditors.

R3's suggestions for a unified approach to the personal insolvency regime are laid out in our **Personal Insolvency Landscape paper**<sup>3</sup> and our most recent update on bankruptcy<sup>4</sup>. If all of these proposals were to be implemented, in addition to R3's proposals for 'breathing space' set out in this paper, identification of a clear and suitable debt advice approach for each individual would be far more accessible, which would ultimately have a significant positive impact on indebted individuals' ability to resolve their debts and on creditors' chances of seeing their money repaid.

<sup>3</sup> [https://www.r3.org.uk/media/documents/policy/policy\\_papers/personal\\_insolvency/R3\\_Personal\\_Insolvency\\_Landscape\\_Jan\\_2014.pdf](https://www.r3.org.uk/media/documents/policy/policy_papers/personal_insolvency/R3_Personal_Insolvency_Landscape_Jan_2014.pdf)

<sup>4</sup> [https://www.r3.org.uk/media/documents/policy/policy\\_papers/personal\\_insolvency/R3\\_Personal\\_Insolvency\\_Landscape\\_D2.pdf](https://www.r3.org.uk/media/documents/policy/policy_papers/personal_insolvency/R3_Personal_Insolvency_Landscape_D2.pdf)

## ANNEX – Comparison of R3's proposals to provisions in other regimes

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In other jurisdictions, mandatory debt advice and 'breathing space' provisions already exist in various forms.

### a) Scotland

Scotland's personal insolvency regime provides for a form of 'breathing space' from creditor action under the Debt Arrangement Scheme (DAS). This scheme allows individuals to repay their debts under a 'debt payment programme' (DPP) which is based on their disposable income. Under this scheme, it is possible to apply for an 'intimation' – by notifying the DAS Administrator of an intention to apply for a DPP, an individual is entitled to six weeks' 'breathing space' from creditor action while the DPP is being put together. Once approved, the DPP freezes all interest, fees and charges on the debts included from the date that the DPP application was submitted, resulting in those charges being written off once the debtor completes the DPP (which can last for 'any reasonable length of time').

By way of comparison, this scheme is somewhat narrower than what R3 is proposing in England and Wales, as R3 believes that debt enforcement action and associated interest and charges should be frozen for 28 days in order to allow an individual to receive full advice about the appropriate debt solution for their circumstances, whether this is a form of debt repayment plan or a formal insolvency procedure. Thus, R3's suggestion of a moratorium is for a wider purpose than the Scottish intimation – it would precede any insolvency or debt relief procedure, not just a debt repayment plan. R3 believes that this would ensure a more holistic and balanced approach to the issue, as the moratorium would be available to all people who need to obtain debt advice about their options and not just those who may enter a specific debt repayment plan.

### b) Australia

In Australia, the current regime allows an individual to apply for a declaration under S.54 of the Bankruptcy Act 1966, which then gives them a period of 21 days to consider their options where no creditor enforcement action is possible. There is, however, no specific requirement for the individual to seek advice during this time. Thus, the Australian regime is slightly more favourable to individuals than the moratorium R3 is suggesting for England and Wales, where proof of professional advice would be required. R3 believes that making debt advice a mandatory condition of the moratorium will ensure that there is a well-balanced approach to ensuring that people are given appropriate time to take full advice with a view to entering a solution best suited to their financial needs, while also balancing creditors' interests in ensuring that there are no time wasting or delay tactics by individuals trying to avoid repaying their debts. It is important that the 'breathing space' period is used to assist financially distressed people to enter the most appropriate solution for their circumstances; this is particularly true where this may allow them to undertake repayment of some or all of their debts in a structured way (for example, via an Individual Voluntary Arrangement (IVA)).



### c) Canada

The situation is slightly different in Canada. At the point at which an individual is considering bankruptcy and has visited an advisor (called a 'trustee'), that trustee is required to make a pre-bankruptcy assessment of that person. This includes an outline of their financial affairs, a discussion of their options (including the option of a consumer proposal<sup>5</sup>) and the various rights and responsibilities of the individual. This requirement was introduced in response to concerns that individuals were being processed through bankruptcy without being provided with a full explanation of their options and without an opportunity to meet a trustee (clerical staff were responsible for processing the bankruptcy).

However, the regime does not provide a moratorium from creditor action while this advice is being taken (and charges and interest will still accrue), thus the effectiveness of this advice may be limited – it is possible that the person will still feel the sense of panic pushing him or her to accept the bankruptcy option quickly, without the time or space to consider any other options fully. R3 believes that the 28 day 'breathing space' provisions we are proposing in England and Wales will be better suited to addressing the issue: not only will the proposals make comprehensive advice on the various debt solutions mandatory, they will also allow a financially distressed person to make an informed and careful decision based on this advice by removing the pressure from creditors during the advice period by freezing accruing interest and charges and preventing any enforcement action.



### About R3:

R3, the insolvency trade body, represents the UK's insolvency practitioners. R3's full members are all regulated by their recognised professional bodies, they can be licensed insolvency practitioners, solicitors, chartered accountants or certified accountants. They have extensive experience of helping businesses and individuals in financial distress.

<sup>5</sup> A 'consumer proposal' is when an offer is arranged through a trustee to pay the insolvent's creditors a percentage of what is owed over a specific period of time (up to five years). Payments are made from the consumer debtor to the trustee, and the trustee uses that money to pay each affected creditor.