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Coronavirus and personal debt: a financial recovery strategy for households

June 2020

We want to create a society free from problem debt

Summary

Compared to the Great Recession, households with low- to middle-incomes entered the present crisis more likely to be facing problem debt and struggling to pay for essentials.[i] In December 2019, 3.2 million people in the UK were in severe problem debt and 9.8 million were showing signs of financial distress.[ii]

The government has implemented a series of crucial public health measures to control the spread of coronavirus that have profound consequences for the economy and household finances. The government has also put in place a series of unprecedented measures to protect incomes and businesses during the outbreak period. However, these schemes have not protected all households against loss of income.

Many households are now facing an unprecedented and prolonged income shock. StepChange commissioned national polling at the end of May, two months after the lockdown period began, to understand how household finances have been affected by the coronavirus outbreak.[iii] We estimate that 28% of adults, or 14 million people, have experienced a direct negative effect on their income.[iv]

A broad swathe of the population has been affected but those who are younger, female, are responsible for children, or in insecure work are most likely to have experienced a negative impact. Those who are less financially resilient are more likely to have been affected: of those in severe problem debt before the outbreak, 45% have been negatively affected financially by coronavirus compared to 25% of those not in financial difficulty.

We estimate that 4.6 million people negatively affected have accumulated £6.1 billion of arrears and debt, averaging £1,076 in arrears and £997 in debt per adult affected.[v] These figures reflect the situation as of late May and are likely of increase substantially before the lockdown is fully phased out; a process that remains uncertain.

Since the beginning of the coronavirus lockdown period, 2.8 million people have fallen into arrears: most frequently utilities (1.2 million people), council tax (820,000 people) and rent (590,000 people).[vi] 4.2 million people have borrowed to make ends meet, most often using a credit card (1.7 million), an overdraft (1.6 million) or a high cost credit product (980,000). Other common financial coping strategies include using savings, asking family and friends for help, applying for Universal Credit, and selling possessions.

44% of those affected with an income of less than £30,000 have fallen behind or borrowed to make ends meet compared to 25% of those with an income of £50-60,000 (and 29% with an income of £70,000 or more). Of those who have fallen behind on essentials, two-thirds (67%) have also borrowed to make ends meet.

As of late May, our polling indicates that 2.7 million people have accessed payment holidays on mortgage and credit products – 36% of those who have accessed payment holidays expect to fall behind on regular bills before the end of June.

Government support to weather the financial impacts of the coronavirus crisis has not sheltered all households. Left unaddressed, these households face living with the financial legacy of coronavirus

for years to come. Those affected will be exposed to housing insecurity, depressed living standards and hardship, an increase in health problems, and higher levels of unemployment. In addition to the cost to individuals and families, prolonged financial difficulty will have public costs and slow economic recovery.

Policy makers should now turn their attention to preventing this outcome through a financial recovery strategy for households addressing three priorities:

- **Households struggling with arrears and debt should be provided with strong protections against housing insecurity and unaffordable repayment demands**

  Temporary measures implemented by government and regulators such as a ban on eviction for rent arrears and credit repayment holidays have provided a degree of respite, but these measures are time-limited (with varying degrees of protection in place across the UK).

  Those in difficulty are living with the threat of housing insecurity, demands for unaffordable payment and future enforcement action.

  1. The government must ensure that the pre-action protocol it has proposed to put in place for private rented housing provides a guarantee against eviction by amending ground 8 (section 8) and section 21 of the Housing Act, temporarily if necessary, to ensure the protocol cannot be circumvented.[vii] Financial support to address arrears, as outlined below, is vital to prevent subsequent housing insecurity and hardship.

  2. The government should issue new statutory guidance requiring that local authorities put in place affordable repayment plans for council tax arrears among those affected by coronavirus before resorting to enforcement action, taking into account vulnerability and financial circumstances.

  3. Utilities regulators should refresh post-coronavirus guidance to support people who are struggling, including the adequacy and effectiveness of payment help for low income households and vulnerable consumers.

  4. The Financial Conduct Authority (FCA) should extend the window for payment holidays for unsecured credit products for three months in line with mortgage payment holidays. As payment holidays come to an end, the FCA should work with stakeholders to quickly bring together a package of ‘next steps’ protections offering those negatively affected by coronavirus a safe route out of temporary difficulty, including where needed coordinated support and a repayment pathway that allows the rescheduling of repayments to an affordable level without negative credit reporting.

- **Households negatively affected by coronavirus should be provided with grants to address arrears and debt accumulated to pay for essentials during the crisis**

  Providing short-term relief against eviction, repayment demands and enforcement action is not enough. In many cases, this will simply defer dealing with arrears until a later date as financial difficulty builds. To provide effective protection against debt crisis, the government must provide financial support.

  While there are practical challenges in providing grants to households that have accumulated arrears and debt, these challenges are not insurmountable. The government should now establish a national fund to provide grants to households negatively affected by coronavirus to repay arrears and debt accumulated to pay for essentials during the crisis.

  We estimate that an effective fund would cost in the region of £5 billion. This funding would primarily benefit those who have not directly benefitted from the coronavirus income support schemes, which are expected to provide at least £50 billion in support.

- **The government should ensure the social safety net is a source of financial resilience for struggling households**

  1. Without sufficient income, struggling households will be unable to recover. Coronavirus has exacerbated poverty and insecurity: 17% of adults are now worried about paying for essentials such as a healthy diet and clothing appropriate for the weather later this year. StepChange has called, alongside the Trussell Trust and a coalition of charities, for urgent new emergency income protection measures, including:

     - an increase in local housing allowance to 50% of median local rents;
     - more help for families with additional needs such as those with children or someone with a disability or health problem in the household;
     - the lifting of caps such as the benefit cap and two child limit that prevent adequate support reaching households; and
     - additional funding for local authorities to provide crisis support grants to vulnerable households in financial crisis.

  2. Half (51%) of those who have applied for Universal Credit since the beginning of the outbreak are in financial difficulty or problem debt. Universal Credit does not work well for those affected by problem debt: the five week wait and advance payments burden new claimants with debt that must be repaid through deductions that reduce the value of support. It is more urgent than ever that the government address these problems by:

     - turning advance payments into grants, at minimum on a temporary basis; and

     - suspending non-priority deductions, including advances, and using the period of suspension to reform the deductions framework in line with the fairness principles and best practice in debt management to ensure that deductions are made fairly and affordably.[viii]

3. Almost one million people have turned to high cost credit to make ends meet since the beginning of the crisis. Financial support through the social security system and local crisis grants are central to preventing distress borrowing, but the need for safer alternatives to high cost credit is more pressing than ever. The government should act quickly to extend access to Universal Credit budgeting advances (while ensuring repayment terms are flexible and affordable) and accelerating work to develop a national no-interest loan scheme.

The impact of the coronavirus outbreak on problem debt

Prior to the pandemic, many UK households were not positioned to weather a sudden downturn. In 2017, the FCA's *Financial Lives* research indicated that 35% of individuals in the UK lacked financial resilience and are either 'surviving' or 'in difficulty'.[ix] Recent ONS figures suggest around 25% of working households could not cover a 25% reduction in income for three months (rising to 40% for employees in the lowest income quintile).[x] StepChange research has shown that those most exposed to problem debt as a result of income shocks are those with low levels of financial resilience.[xi]

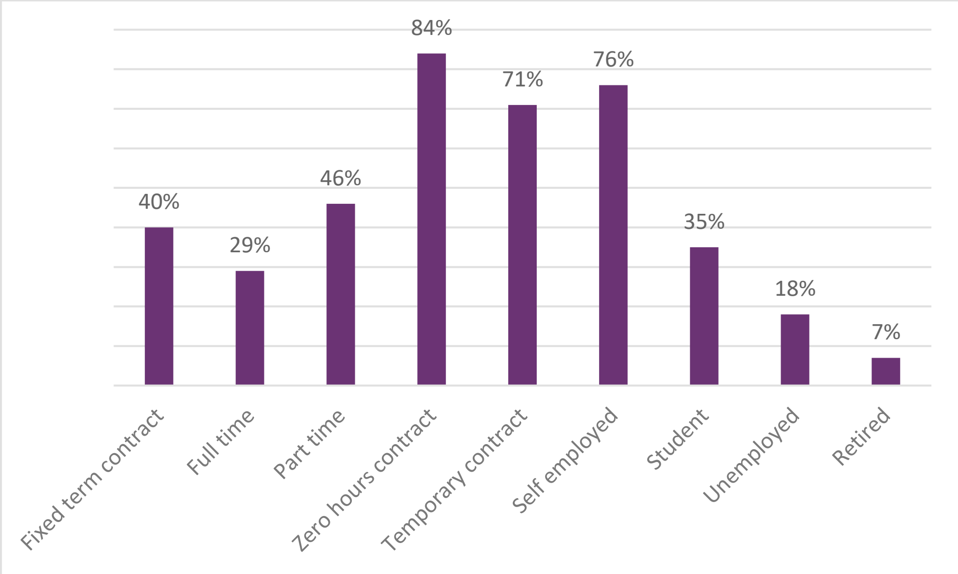
We estimate that 28% of GB adults (approximately 14 million people) have been negatively affected financially by coronavirus to date.[xii] Around one third of this group (30%) were showing one or more sign of financial distress (25%), such as missing a credit repayment, or were in severe problem debt (5%) at the onset of the pandemic. Looked at from another perspective, of those in severe problem debt before the outbreak, 45% have been negatively affected financially by coronavirus. This compares to 40% of those showing signs of financial distress and 25% of those not in financial difficulty.

This pattern reflects the greater risk of an income shock linked to the impact of coronavirus among certain groups.[xiii] Early analysis of 'shutdown' sectors and roles that cannot be continued through home working (or due to childcare responsibilities) indicates that the sectors most affected are service industries like retail, hospitality (restaurants, pubs, cafes and hotels) and wholesale. In some sectors that have not shut down, such as construction and manufacturing, some workers are nevertheless exposed to furloughing or an immediate loss of income or employment due to the effect of the shutdown on demand.

Many working parents are affected because they must provide full time home care for children.[xiv] This responsibility may fall on both fathers and mothers, but patterns of care and income (the latter of which will influence the most pragmatic choice for couple parents to make) suggest women are far more likely to take this responsibility. Parents may also be directly affected: one third of single parents and one fifth of couple parents work in a shutdown sector.[xv]

These patterns mean that, while a wide swathe of people have been affected, those who have experienced an income shock are more likely to be younger, to be in low paid and/or insecure work; and to be female. We find evidence of these patterns in our national polling: for example, 63% of those negatively affected are aged between 18-49, with 18-24 year olds nearly twice as likely to have been affected as those aged over 65. Eighty-four per cent of those working a zero hours contract, and 71% of those with a temporary contract have been negatively affected compared to 40% of those with a fixed term contract. Thirty per cent of women report being negatively affected financially compared to 26% of men.

Groups negatively affected financially by coronavirus by employment category [xvi]



There are some differences among those affected by housing tenure: 36% of private sector renters report being affected compared to 31% of those who hold a mortgage—a worrying finding given the comparative lack of protection for those who rent. Among families with dependent children, 31% of single parents and 39% of couple parents report being affected compared to 31% of single adults. Parents with non-dependent (older) children were less likely to be affected: 22% of couples and 20% of single adults.

Coping strategies

The economic dislocation caused by coronavirus is sending a shockwave through already precarious household incomes. The impact will vary depending on the starting point and the nature of the shock experienced by each household.

Our polling indicates that the most common financial coping strategy among those negatively affected is to borrow to make ends meet (26%), followed by using savings (23%), asking family and friends for help (11%), applying for Universal Credit (9%), and selling possessions (8%).

In total, 4.2 million people negatively affected by coronavirus report having borrowed to make ends meet since the start of the crisis, accumulating an estimated £3.3 billion in debt. The table below sets out the most common forms of credit used by those who have borrowed. Consumer credit is the most common form of borrowing, followed by family and friends and publicly supported options such as budgeting loans. While a minority have used any individual form of high cost credit, cumulatively, 980,000 people have used at least one form of high cost credit. 'Mainstream' credit such as credit and store cards can carry high interest charges and will become high cost if borrowers are not able to repay the outstanding balance promptly.[xvii]

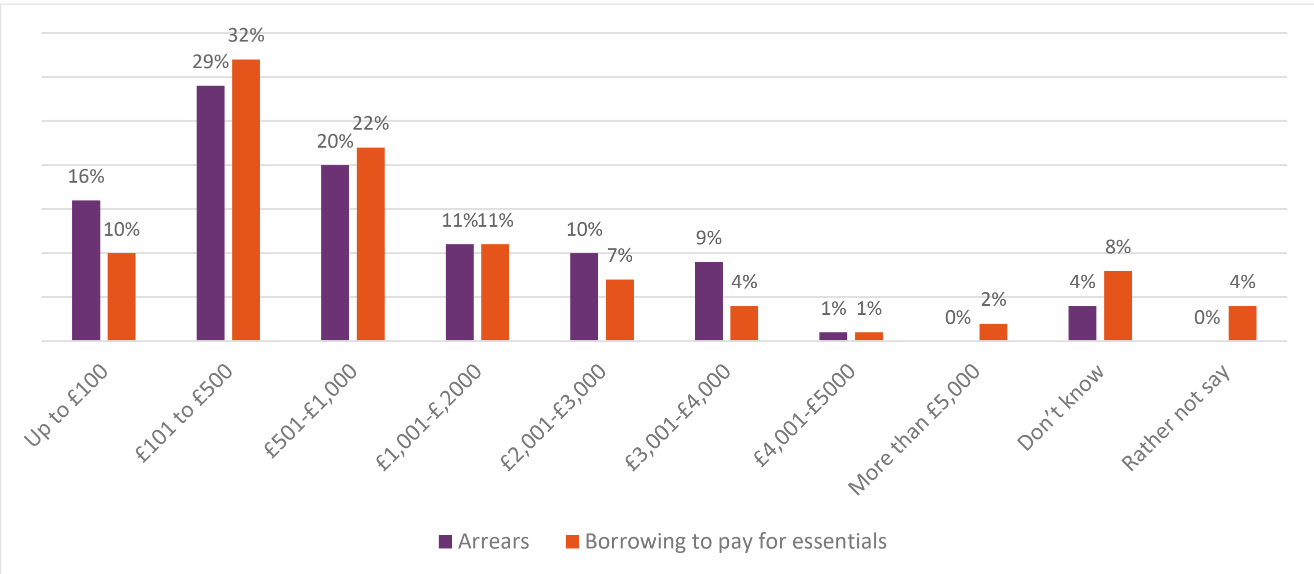
Borrowing by loan type among those affected by coronavirus

Loan type	%
Credit card	26%
Overdraft	24%
Family and friends	17%
Catalogue credit	7%
Universal Credit advance or budgeting loan	7%
Personal loan	4%
Store card	4%
Payday loans	2%
Rent to own	2%
A loan from a local authority	2%
Unlicensed lender ('loanshark')	2%
Other	2%

One if five (19%) of those negatively affected financially by coronavirus has fallen behind on regular bills: we estimate that 2.8 million people have acquired £2.8 billion of arrears. Most commonly, this is a utility bill (electricity, gas, water or telecoms – 1.18 million people), council tax (817,000 people), rent (590,000 people) or a credit card repayment (570,000 people). A further 5% of those negatively affected by coronavirus (580,000 people) who have not fallen behind expect to do so by the end of June.

The table below sets out estimates of the amount of borrowing and arrears among those affected by coronavirus who have fallen behind or borrowed to pay for essentials. We estimate that the average amount borrowed among households affected as of 19 May was £997 and the average arrears £1,076.[xviii]

Amounts of arrears and debt since the beginning of the lockdown period among those negatively affected by coronavirus



A further indicator of financial difficulty is the number of people who have taken up payment holidays. As of 19 May, our polling indicates that 2.7 million people have taken some form of payment break, with 1.5 taking a mortgage holiday and 1.2 million a consumer credit payment holiday. (Recent figures provided by UK Finance suggest payment holidays have now been provided for 1.5 million credit card and personal loan products.)[xix] In our polling, nearly half a million people report that they have asked a lender for a holiday or reduced payments but not received them.

Of those who have taken (and accessed) a payment holiday, 26% were already in problem debt at the beginning of the outbreak (and a further 12% were showing signs of financial distress). Of those who have taken a payment holiday, 36% expect to fall behind on regular bills before the end of June.

One in ten renters (11%) has fallen behind on rent since the beginning of the outbreak (this compares to less than one in twenty mortgage holders). Of this group, 27% report that their landlord has been in touch to request rent as usual, while 10% report that their landlord has offered a rent reduction. Six per cent of those behind on their rent (35,000 people) say their landlord has informed them they expect to begin eviction proceedings when this is possible.

In line with nationally reported figures, our polling indicates over two million people have applied for Universal Credit since the beginning of the outbreak. Of those who had applied for Universal Credit, 46% had applied for an advance payment; however, 29% of those who had applied for an advance had not received one.

Post-crisis financial pathways

The structure of government intervention will shape the impact of the crisis on problem debt. The government has acted to protect incomes directly through the Coronavirus Job Retention Scheme and the Self Employment Income Support Scheme, and indirectly through a number of grant and loans schemes for businesses such as the Bounce Back Loan scheme. Increases in support through Universal Credit will benefit those with low incomes, although the support offered through temporary income protection schemes has been strikingly higher than standard Universal Credit payments for many.[xx] But the government has not protected all workers, nor all of the income of those who have experienced a fall in income due to coronavirus.

Alongside direct financial support, other temporary measures have been put in place by government and regulators:

- The Financial Conduct Authority has put in place temporary guidance requiring that creditors offer three month payment holidays for those experiencing temporary difficulties.[xxi] These breaks exclude interest so charges will continue to accumulate where applicable. A shorter one month payment deferral *with* interest suspension has been put in place for short-term high cost credit loans.

- All evictions and new court actions pursuing possession have been suspended and a three month notice period imposed—further eviction proceedings could not occur until August at the earliest. (In Scotland, the notice period has been extended to six months where the reason for arrears relates to coronavirus.)

- Emergency packages have been agreed by the government with utility suppliers, including energy, water and communications, ensuring continuity of supply and supporting people experiencing financial difficulty.

- Bailiffs in England and Wales are not able to visit premises during the emergency period, although they may pursue debts remotely (through correspondence and over the phone.)

- In Scotland only, the period in which enforcement to pursue debt repayments cannot be pursued has been extended from six weeks to six months (and the restriction on benefitting from this protection more than once in a year removed). Additional flexibilities have also been agreed for Scottish debt solutions, including an increased maximum debt threshold and reduced fee for the Minimal Assets Process, and reduced bankruptcy fees.

Once the period of social distancing ends, most households are likely to see a return to relative normality. However, unemployment and household incomes may recover slowly and some households will continue to struggle with ongoing payments and increased debt burdens.

Our polling indicates that a substantial number of households have already experienced serious financial difficulty linked to coronavirus. Temporary measures such as payment holidays and the ban on evictions are also delaying and disrupting the transmission of income shocks into financial difficulty. As household resources are exhausted and temporary relief measures expire, more households will experience difficulty or an increase in the severity of financial problems.

Those who have been negatively affected by coronavirus can be segmented into broad groups illustrating relative financial fragility and potential future pathways:

- **In problem debt pre-crisis** (700,000 people): Those who were in severe problem debt pre-crisis.

- **In financial difficulty pre-crisis** (3.4 million people): A wider group of people were showing some sign of difficulty pre-crisis.

- **New struggling** (970,000 people): Those who were not in financial difficulty pre-crisis but have since fallen behind (or expect to) or have borrowed to pay for essentials.

- **Growing financial fragility** (2.4 million people): This group has been affected negatively but was not in difficulty pre-crisis and has not fallen behind or borrowed; however, they are worried that they will struggle financially later this year.

- **Coping** (6.7 million people): Those who have been affected negatively by coronavirus but have not shown any indication of financial distress and do not expect to struggle later this year.

These groups will now have different needs: some will simply need limited help from individual creditors and providers through rescheduling of payments; those who have acquired multiple arrears and debts will need co-ordinated help and repayment plans; and those now in serious difficulty (or who were already in difficulty) will need debt advice.

How relief measures are phased out and what further measures are taken to support incomes will be crucial in dictating the impact of the crisis on households and the extent of financial difficulty and problem debt in the post-crisis period. The final section of the briefing note examines what more can be done to ease financial difficulty and prevent harm to the households affected.

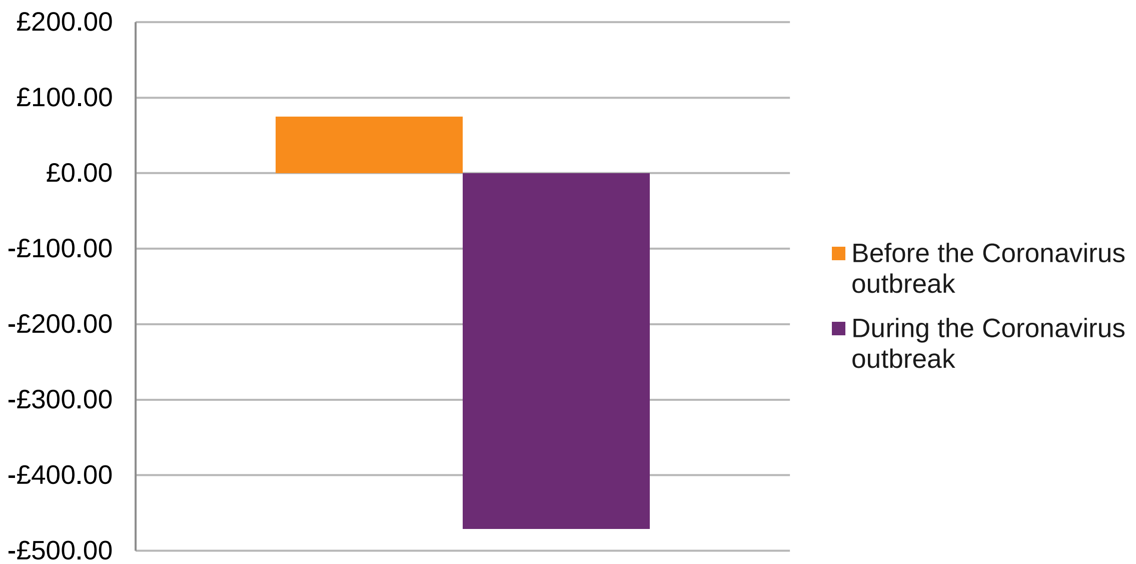
Illustrative case studies

The two following case studies examine in more detail what the reality of managing finances is for households struggling due to coronavirus.

Couple with two dependent children

Helen and Paul are a couple with two children aged 8 and 3. Paul works on a zero hours contract while Helen cares for the children. They live in a privately rented two bedroom apartment in London and receive Universal Credit. With considerable debts, their finances were in a precarious position before the crisis. Having purchased various white goods through hire purchase agreements, they have a large outstanding balance and hefty weekly payments. They make minimum payments on a credit card which they used to cover living expenses during a period when Paul was out of work. They also have water and energy arrears from this period. Paul's hours have been reduced by 75% since the outbreak. As a result of the benefit cap, their Universal Credit payment is actually reduced despite a dramatic fall in earned income.

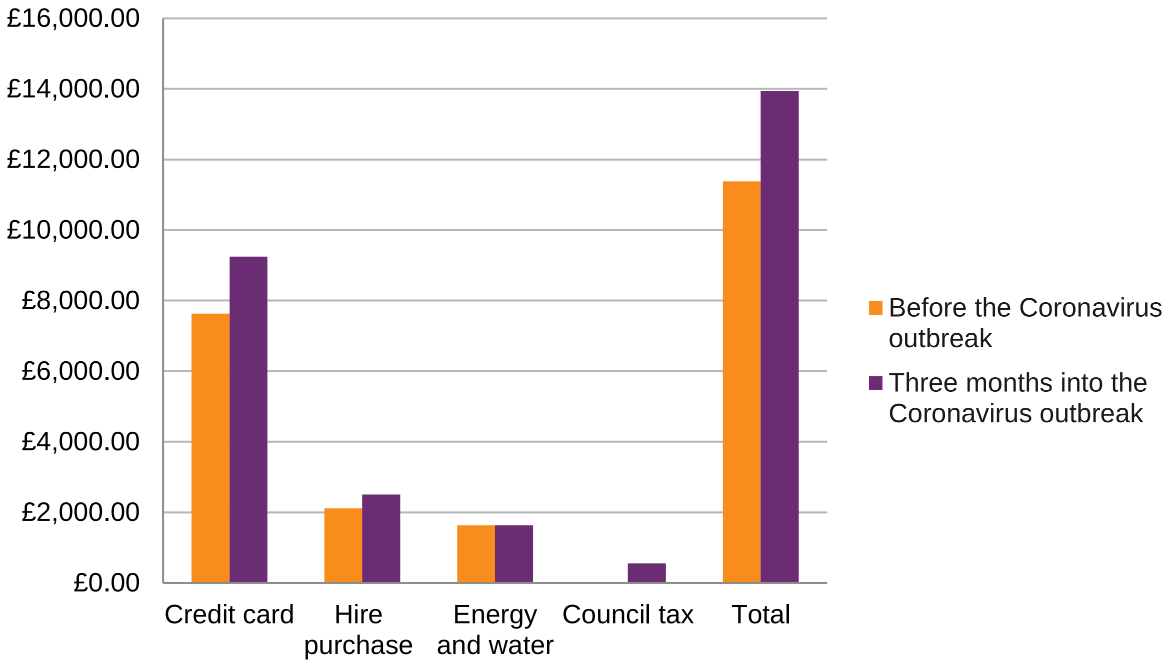
Helen and Paul's disposable income



Over a hypothetical three-month period when restrictions are in place, Helen and Paul are forced to use their credit card to pay for essentials. They benefit from the FCA's payment freezes, but interest accrues during the lockdown on all their credit products meaning they are in deeper trouble as they emerge from the crisis.

After missing a monthly council tax payment, they become liable for their full bill. As it stands, when the pause on enforcement action ends councils will be able to pursue this using their normal methods. The council gets a liability order and passes the debt onto bailiffs. The bailiff firm sends them a letter and they are charged a compliance fee. If they don't get in touch to make a payment within two weeks, bailiffs visit and further charges will be added. Although their energy and water suppliers have shown understanding, Helen and Paul are worried about being disconnected as they have been unable to make their usual token payments.

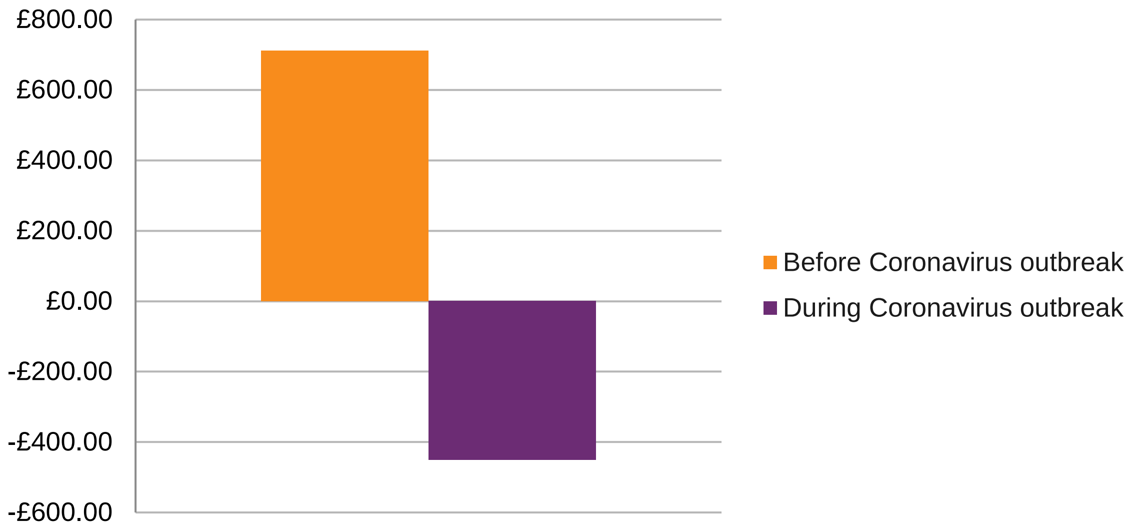
Helen and Paul's debt and arrears



Single parent with one child

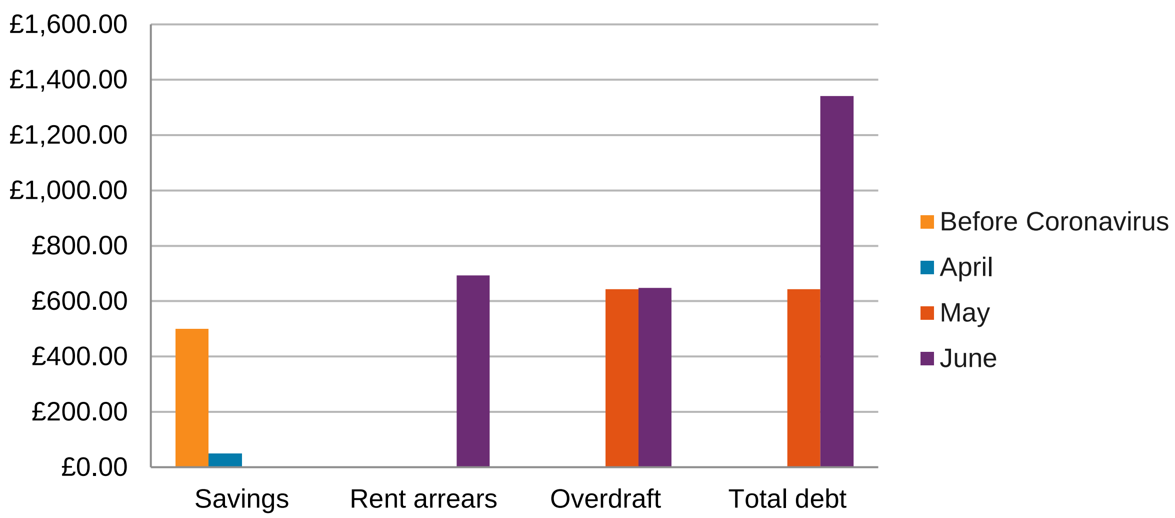
Faye is 23 and was made redundant from her job as soon as social distancing measures were implemented. She was working full time earning the National Living Wage. She claimed Universal Credit and had managed to build up a small pot of savings. She lives alone with her two-year-old daughter.

Faye's household disposable income



Faye's March paycheck will cover rent and living costs for April but after that her situation becomes more uncertain. Her Universal Credit allowance doesn't flex with her loss of earnings and she is forced to use her savings to cover rent. By May, she has had to dip into an overdraft to cover rent and living costs. Wary of this overdraft building up, in June she falls behind on her rent. Although she benefits from a £500 interest free overdraft, by the time social distancing measures are eased in June she has lost her savings and built up considerable debts. Faye is now dependent on the sympathy of her landlord to avoid being evicted from her flat and needs support to return to work quickly otherwise she won't be able to pay her rent and cover living expenses going forward.

Faye's arrears and savings



Preventing a coronavirus household debt crisis

Coronavirus has imposed an unprecedented income shock on UK households. The government's early economic measures to protect household finances during the coronavirus outbreak have not sheltered all from difficulty. There has already been a significant increase in financial difficulty as households fall behind or borrow to make ends meet; many more expect to do so in coming months.

There are significant costs to the public in worse economic and health outcomes of deep and prolonged financial difficulty. Without further support, those affected will be exposed to the negative effects linked to problem debt including housing insecurity, depressed living standards and hardship, an increase in health problems, and higher levels of unemployment.[xxii]

Further action is also imperative to ensure that those who have been negatively affected are treated fairly. The government has acted quickly to invest an unprecedented sum to prevent a much deeper economic crisis, but this support has not been distributed equally nor, unsurprisingly given the need for rapid intervention, in all cases been carefully targeted. It is now apparent that many of those who have not been protected will experience the most acute difficulty.

How the government and others treat those struggling with debt due to coronavirus will be a bellwether of the extent to which the crisis has been faced collectively. If some households face a prolonged and steep pathway to resolving arrears and debt accumulated during the crisis while others return relatively soon to 'business as usual', there is a risk of a pernicious sense of injustice in the post-crisis period.

A financial recovery strategy for households, coordinated by government, is urgently needed. This should consist of three priorities:

Households struggling with arrears and debt should be provided with strong protections against housing insecurity and unaffordable repayment demands

Repayment pressures on households come from three principle sources: rent payments, council tax and credit products:

1. ***590,000 renters have fallen behind and will be worried about eviction.*** Once the temporary ban on evictions lifts, those renting and in arrears will be faced with an acute pressure to make unaffordable repayments or lose their home.

   The government has indicated that it will put in place a pre-action protocol that would require landlords to seek to arrange repayment before pursuing eviction. As it stands, the government will be relying on landlords to show compassion and flexibility in their treatment of those who have built up arrears during the crisis. Our evidence is that this flexibility could be in short supply: 27% of renters who have fallen behind report that their landlord has been in touch to request rent as usual compared to 10% who report that their landlord has offered a rent reduction. Not all landlords can themselves afford to offer rent relief.

   The government should ensure that the pre-action protocol it puts in place for private rented housing requires affordable repayment plans and provides a guarantee against eviction by amending ground 8 (section 8) and section 21 of the Housing Act, temporarily if necessary, to ensure the protocol cannot be circumvented.[xxiii] To be effective, the government must, as noted below, combine this protocol with financial support.

2. ***820,000 people have fallen behind on their council tax bills.*** Council tax debt will form an urgent problem for those in arrears because legislation requires that arrears are referred promptly to court. While local authorities have some subsequent discretion, this is limited and relatively blunt enforcement protocols operated by many councils will lead to demands for unaffordable payment and, in England and Wales, the use of bailiffs.

   The government should now issue statutory guidance, amending regulations where necessary, requiring that local authorities put in place affordable repayment plans for council tax arrears among those affected by coronavirus before resorting to enforcement action, taking into account vulnerability and financial circumstances.

3. ***1.2 million people have fallen behind on one or more utility bills.*** We were seeing an increasing number of people seeking help with utility debts before the coronavirus crisis, highlighting the difficulties many household face meeting payments for essential services. Utility regulators will need to ensure that firms review and refresh their debt management policies to support people who are struggling, including the adequacy and effectiveness of payment help for low income households and vulnerable consumers.

4. ***2.7 million people have accessed payment holidays.*** The FCA's work to introduce temporary payment holidays has delivered accessible and effective help, reducing payment burdens without seriously impairing credit files.

   We welcome the recent extension of the window for mortgage payment holiday applications to 31 October, allowing people to extended payment holidays by up to three further months, and extending the prohibition on mortgage repossessions. The FCA should now also extend the application window, and period of help available through repayment holidays for consumer credit (including extending high cost short-term credit payment holidays).

   Even with this extension, we expect a large number of people will continue to need support when payment holidays come to an end. StepChange's recent *Life Happens* report found that without access to clear and effective help, people used coping strategies like borrowing to keep up with payments; our evidence shows many people are already doing so in response to financial pressures linked to coronavirus, significantly increasing the chance that people will fall into problem debt.

   The FCA should now support the development of the next steps of support as payment holidays come to an end. Those who come out of payment holidays before their incomes are fully recovered and with deferred repayments due will need support including:

- time to clear deferred payments and, for some, reduced payments for a temporary period;
- protection from enforcement and collection action that may otherwise destabilise their financial situation (the need for which is already embedded in FCA rules and the forthcoming Breathing Space and Statutory Dept Repayment Plan schemes);
- reassurance that their credit record will not be affected so that this is not a barrier to seeking help;
- protection to ensure further interest and charges do not create an unmanageable debt burden; and
- co-ordination for those with debts with multiple lenders.

Collectively, this means that many will benefit from the 'customer view' approach taken by debt advice providers through a debt management plan but tailored to deal with temporary financial difficulties.

None of these needs are new to credit regulation or consumer protection. The need for more time to pay is strongly embedded in existing FCA rules and consumer credit law, while the insight that collections and enforcement action can make debt problems worse and undermine recovery is embedded in the forthcoming Breathing Space and Statutory Debt Repayment Plan schemes.

The mortgage and credit payment holiday schemes have introduced a principle that credit records should not be unduly negatively affected by exceptional circumstances outside a customer's control. These circumstances and consumers' relative lack of control will not end with the payment holidays and neither should protections that are important in encouraging consumers to the right coping strategy for their temporary difficulties.

The need for protection from further interest and charges where people are in serious financial difficulties is broadly accepted (though not everywhere applied). This principle is not so clearly established (beyond initial 'breathing space' protections) where people are in temporary financial difficulties. The 'Time Order' provisions of the Consumer Credit Act provide a power for courts to re-write agreements, including interest and default charges, where it is just to do so. However, court-based consumer protection is not a practical response to the scale of coronavirus-related financial difficulties.

The FCA has already expressed concern over interest and charging practices in a number of recent areas: in coronavirus guidance on overdrafts and credit cards and on unauthorised overdraft charges; high cost short-term credit and rent to own (where the FCA was rightly concerned that vulnerable people were being asked to pay too much).

Concern about the affordability of interest and charges is also built into the responsible lending provisions of the consumer credit rulebook (CONC 5). Charging consumers default interest on deferred payments is effectively the same as new lending, except there is prima facie evidence of affordability problems. Public policy would not want lenders to profit from people's misfortune, so there is a balance to be struck between recognising the need to keep agreements open as consumer finances recover while ensuring that unaffordable debt and payment burdens do not build up.

We urge the FCA to work with stakeholders to quickly bring these protections together in a package of ‘next steps’ protection as payment holidays wind down. Payment holidays will not generally address the possible problems from further interest and charges accruing on deferred payments, but we urge the FCA to now do so as part of a package of next step protections.

Our evidence shows that of those taking payment holidays, 26% were in problem debt at the onset of the crisis, and 36% expect to fall behind on regular bills by the end of June. We believe there is a more general need for the FCA to ensure that borrowing through this period remains fair and affordable and that a new cohort of people do not become trapped in persistent debt. The FCA’s approach should therefore be aligned with a revised approach to persistent debt and repeat overdraft use rules, ensuring that those with significant credit card or overdraft balances linked to coronavirus have a safe, affordable and fair way to resolve debt.

The government should provide grants to households negatively affected by coronavirus to address arrears and debt accumulated during the crisis

Arrears and debt accumulated during the crisis will not simply unwind safely, even with extended protections in place to prevent eviction and enforcement action: repayments will substantially reduce income, exacerbating poverty; drive mental health problems and poor physical health, increasing the difficulty of economic recovery for many; and it will create a heightened risk of debt spirals through further borrowing to meet essentials. Even with an appropriate debt solution, dealing with problem debt is often a long and difficult journey.

Just as the government has established ‘bounce back’ loans for business, the government should now provide a fair and safe route for those who have borne the financial brunt of the crisis to get back on their feet. To provide this support, the government should set up a national financial resilience fund to provide grants to households negatively affected by coronavirus to repay arrears and debt accumulated to pay for essentials during the crisis. While there are clear challenges in operating such a scheme, these challenges are not insurmountable.

The scheme would be time-limited and bounded by the dates of lockdown conditions. Simple evidence standards can be used to assess eligibility for support: the government already has experience of establishing criteria for those affected by coronavirus for the Self-Employment Income Support Scheme. The government also has experience of making payment in arrears for qualifying essentials, for example for childcare support within Universal Credit where claimants submit receipts and invoices to evidence payments.

There is a practical imperative to extend support urgently to housing support particularly to support those at risk of eviction. So far as possible, it would be important however to include both direct debts (such as rent, council tax or utility arrears) and indirect debts, such as credit card borrowing, to pay for these essentials. In addition to a question of fairness—it would appear unfair, for example, to extend support to one household in rent arrears but not another with an overdraft of an equal size used to meet rent payments—over time such debts may crystallise into urgent financial difficulty and similar risks of housing insecurity and debt crisis. Where those seeking to access a fund have borrowed or used savings to pay for essentials, they would need to show evidence of payment and of borrowing or drawing down savings of equivalent value.

The cost of repaying all arrears and debt accumulated by those negatively affected by coronavirus would be substantial: we estimate that an effective fund for those with low incomes would cost up to £5 billion.[xxiv] There remains, however, uncertainty over the remaining lockdown period that make estimating the cost of support difficult. It is imperative to provide support in the form of grants with no subsequent repayment for those who are financially vulnerable to prevent simply deferring hardship and financial difficulty to a later time. However, support could also be extended to a wider middle-income group by operating a fund with a student loan-style structure with up front payments and deferred, income-contingent repayments set at an affordable level.

The administrative commitment to establish a scheme is significant but the government has shown it is able to act quickly where justified. In combination with protective protocols to provide households with protection from arrears and debt, it would be possible to manage claims over a period of months. With a simple application process, this would bring managing a high volume of claims within the practical constraints of recruiting or redirecting existing staff. New infrastructure would be required but the number of staff needed would, for example, be far less than that (around 25,000 people) recruited at short notice to staff the track and trace system.

The government should ensure the social safety net is a source of financial resilience for struggling households

The adequacy of support is central to supporting financial recovery among households with low incomes affected by coronavirus: StepChange has called jointly with the Trussell Trust and others for an emergency support package to support households to weather the period of social distancing.[xxv] Key measures include:

- increasing the local housing allowance to 50% of average rents in each area;
- increasing support for households with additional needs, such as those with children or in which someone has a disability;
- removing caps on assistance that prevent adequate help reaching households, such as the benefit cap and two child limit; and
- providing further funding and guidance for councils to ensure sufficient local support is in place through local welfare assistance schemes for those experiencing crisis.

Those exposed to hardship by the economic impact of coronavirus need to be supported in a way that provides reliable help and supports them to stabilise their financial situation. Universal Credit is the primary lever available to policy makers to help those not otherwise protected by the coronavirus income protection schemes, but does not currently work well for those affected by problem debt, with a system of advance payments that burdens new claimants with debt and unaffordable deductions.[xxvi]

Around half of those who have sought help during the crisis through Universal Credit have taken out an advance payment (at least one million people), and many in this group will experience difficulty as a result of substantial monthly repayments of the advance. Many new claimants will also find that additional deductions, for example for the repayment of legacy benefit overpayments, reduce the value of support.

It is more urgent than ever that the government addresses the five week wait for Universal Credit. It can achieve this by:

- turning advance payments into grants, at minimum on a temporary basis; and
- suspending non-priority deductions including advances, except where claimants opt-in, and using the period of suspension to reform the deductions framework in line with the fairness principles and best practice in debt management to ensure that deductions are made fairly and affordably.[xxvii]

Finally, over three million households have already used unsecured credit as a de facto safety net to manage financial challenges linked to coronavirus, borrowing an estimated £3.3 billion. In many cases, this borrowing will be resolved without further difficulty. However, nearly one million people have used one or more form of high cost credit. This pattern of credit use reflects the underlying lack of financial resilience among households at the outset of the crisis, with many having little (or no) disposable income and limited savings.

Addressing the use of credit to pay for essentials is foremost about supporting households to build financial resilience through sufficient income and manageable costs. However, credit remains an important tool for households to manage and smooth unexpected or unpredictable expenses. The scale of use of high cost credit speaks of the need to provide better alternatives at greater scale.

The government has recently released £65 million from the dormant assets fund to Fair4All Finance to accelerate its programme to improve access to affordable credit (and meet other objectives to improve financial support for vulnerable people). This funding is welcome but will take time to support expanded access to credit and must be seen in the context of demand for high cost credit, which accounts for billions of pounds in lending annually.

The current crisis demands a more urgent response: the government can act quickly on its recent scoping work to develop a national no interest loan scheme, which would provide a mechanism to more directly influence access to affordable credit: the scale of borrowing during the lockdown period illustrates the scale of the potential demand for a more affordable alternative to commercial credit.

The government can also use the existing mechanism of budgeting advances within Universal Credit to extend access to interest-free loans for those with low incomes. Budgeting advances should only be extended where grants are not appropriate and must be managed carefully to avoid creating unsustainable debt burden for those who are financially vulnerable. This can be achieved by changing the way that budgeting advances are provided so that they are better suited to the needs of households with low incomes through more flexible borrowing and repayment terms. This includes removing restrictive eligibility criteria unrelated to affordability (the maximum income cap of £2,600, or £3,600 jointly for couples), allowing multiple loans (up to a maximum amount) so that the scheme can be used to pay for low value items, and extending the maximum repayment period to at least 24 months to ensure repayments are set at an affordable level.

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[i] Ahmed, J. and Henehan, K. (2020) *An outstanding balance? Inequalities in the use – and burden – of consumer credit in the UK*. London: Resolution Foundation; Sturrock, D. (2020) 'Despite short-term relief, households could face debt problems as a result of the coronavirus (COVID-19) pandemic', IFS Observation.

[ii] Large national poll conducted by YouGov Plc. Total sample size was 4,972 adults. Fieldwork was undertaken between 28th November - 2nd December 2019. The survey was carried out online. The figures have been weighted and are representative of all GB adults (aged 18+).

[iii] Large national poll conducted by YouGov Plc. Total sample size was 3,796 adults. Fieldwork was undertaken between 15 and 19 May 2020. The survey was carried out online. The figures have been weighted and are representative of all GB adults (aged 18+).

[iv] This includes negative impacts that are felt now, such as unemployment or a reduction in income from work, but not indirect effects such as the reduced value of pensions or investments.

[v] This figure is a mid-bound estimate, with an upper bound of £7.8 billion and a lower bound of £4.5 billion.

[vi] Rent arrears include those renting in the private sector or from a local authority or housing association (but not those making a board payment); utilities include electricity, gas, water and telecoms.

[vii] Ground 8 (section 8) provides mandatory grounds for eviction where tenants are in arrears and would need to be suspended; section 21 would also need to be amended so that judges are not required to grant a 'no fault' possession order where a landlord has applied to the court rather than pursue steps in a pre-action protocol.

[viii] A small number of 'priority' deductions may need to be applied to protect a claimant against hardship or negative legal consequences (such as court fines). Claimants should also be free to opt-in to repayments where they wish to do so, for example to repay pre-existing arrears.

[ix] Financial Conduct Authority (2017) *The financial lives of consumers across the UK: Key findings from the FCA's Financial Lives Survey 2017*.

[x] ONS (2020) *Financial resilience of households; the extent to which financial assets can cover an income shock*

[xi] StepChange (2019) *Life happens Understanding financial resilience in a world of uncertainty*

[xii] This includes being furloughed with a reduction in salary, a fall in income from self-employment, a reduction in hours worked, unemployment or redundancy, a fall in income due to self-isolation or care responsibilities (for adults or children). A small proportion of respondents also cited a range of 'other' reasons such as reduced income from a lodger and reduced share dividends or income from savings.

[xiii] Gustafsson, M. & McCurdy, C. (2020) *Risky business: economic impacts of the coronavirus crisis on different groups of workers*. London: Resolution Foundation.

[xiv] McNeil, C. (2020) *Children of the Pandemic*. London: IPPR.

[xv] Gustafsson, M. & McCurdy, C. (2020)

[xvi] YouGov polling. See note iii for details.

[xvii] StepChange (2019) *Red Card: Subprime credit cards and problem debt*

[xviii] This is a mid-bound estimate, with a lower bound of £729 (borrowing) and £793 (arrears) and an upper bound of £1,266 (borrowing) and £1,360 (arrears).

[xix] UK Finance, 29 May 2020, 'Lenders approve almost 1.5 million payment holidays on credit cards and personal loans'

[xx] Support through the social safety net includes an increase in the Universal Credit standard allowance of around £20 each week, and increase in local housing allowance to 30% of average rents and a £500 million hardship fund for local authorities, the majority of which must be used to extend local council tax support schemes.

[xxi] www.fca.org.uk/coronavirus-support.

[xxii] Royal Society for Public Health (2018) *Life on Debt Row*; National Audit Office (2018) *Tackling Problem Debt*.

[xxiii] Ground 8 (section 8) provides mandatory grounds for eviction where tenants are in arrears and would need to be suspended; section 21 would also need to be amended so that judges are not required to grant a 'no fault' possession order where a landlord has applied to the court rather than pursue steps in a pre-action protocol.

[xxiv] We make a simplified estimate of the cost of extending grants to those who have fallen behind or borrowed to pay for essentials with an individual income of less than £26,000. The actual cost may be lower due to take-up less than 100% and the exclusion of borrowing not directly linked to essentials.
[xxv] Trussell Trust (2020) 'Joint call to Government for a Coronavirus Emergency Income Support Scheme that can help us all weather this storm'
[xxvi] StepChange (2020) *Problem debt and the social security system*.
[xxvii] A small number of 'priority' deductions may need to be applied to protect a claimant against hardship or negative legal consequences (such as court fines). Claimants should also be free to opt-in to repayments where they wish to do so, for example to repay pre-existing arrears. In May last year, the government published a statement articulating that good practice fairness principles agreed with the debt advice sector are embedded in a cross-government debt management strategy.