

BSA Response to HM Treasury

Breathing Space scheme:
consultation on a policy proposal

Restricted
29th January 2019

Introduction

The Building Societies Association (BSA) represents all 43 UK building societies, as well as 4 credit unions. Building societies have total assets of over £400 billion and, together with their subsidiaries, hold residential mortgages of over £315 billion, 23% of the total outstanding in the UK. They hold almost £280 billion of retail deposits, accounting for 19% of all such deposits in the UK. Building societies account for 37% of all cash ISA balances. They employ approximately 42,500 full and part-time staff and operate through approximately 1,470 branches.

This response has been prepared by the BSA in consultation with its members. We have provided responses to only those questions that are directly relevant to our members. We have focussed our response from a mortgage lending perspective, as this is the main area of lending in the building society sector.

General Comments

The BSA and its members remain committed to supporting borrowers in financial difficulty and are supportive of initiatives that encourage people to seek debt advice early.

The sector is heavily regulated by the Financial Conduct Authority (FCA) in this regards, who set out in the lenders' handbook strict procedures to ensure that consumers are treated fairly. In recent years the FCA has conducted several thematic reviews looking at the treatment of borrowers in payment difficulty.

In December 2018 the FCA published; "management of long-term mortgage arrears and forbearance". They found that firms generally treated customers with financial difficulties well with several examples of best practice highlighted. We would echo the recommendations they made to customers which were:-

- They should not ignore the situation.
- Customers should engage with their mortgage provider about mortgage arrears – more appropriate and sustainable options are available to customers who engage early and are open with the lender.
- Early engagement may also prevent the situation from worsening.
- They should seek additional support and free, independent guidance from the Money Advice Service, which can direct them to providers of free debt advice.
- Under our rules, firms may only consider repossession as a last resort.

Mortgage arrears & possessions are at an all-time low our members tell us the key to helping customers back to financial health is early and regular communication, this would not be possible within the proposed breathing space proposals.

Whilst we welcome the mortgage principle balance and interest being excluded from breathing space we strongly believe that mortgage costs in their entirety should be excluded from breathing space.

The consultation states:-

“For example, mortgage providers should expect to receive payments for both the principal and interest on ongoing mortgage payments, as these payments are outside the protections of breathing space. However, mortgage providers would not be able to charge interest and fees and charges relating to arrears as these would be included in breathing space.”

Most lenders charge interest daily on the balance and any mortgage arrears also form part of the balance, the proposals to treat interest on arrears differently present great complexity for mortgage lenders and will cause significant disruption to existing systems and processes which are working well for the benefit of consumers.

The consultation paper leaves many unanswered questions for our members, an example would be the treatment of a joint mortgage where one of the parties enters into a breathing space agreement. Mortgage lending and administration is a complex area, engagement with the sector is key to avoiding unintended consequences and shaping a successful scheme for the customers (members) of our members. To this end we are keen to engage with Treasury to work through the finer detail around the impact of these proposals on mortgage lenders, we are more than happy to share BSA and our member expertise in this area.

Breathing Space was proposed to help customers with “short term shocks” and help them back to financial health. Existing forbearance processes often go beyond these proposals and offer lenders flexibility to agree the right solution for each individual customer. [MCOB 13.3.4A R](#) states that firms must consider the individual circumstances of the customer and determine whether it is appropriate to discuss alternative options.

Most of the recent commentary from the FCA in this area has focused on the dangers of lenders over forbearing see extract from their [2018 Business Plan](#):-

“While firms are offering more forbearance to customers in financial difficulties, in some cases providing forbearance over a long term may not always be in the customer’s best interests. This could be the case, for example where forbearance does not ultimately enable customers to pay their arrears, but only increases their debts.”

Building societies work closely with the free to consumer debt advice sector and refer customers to their services. We are aware that this sector has been under pressure for some time in terms of capacity to support the growing numbers of individuals requiring debt advice. We are concerned that the introduction of breathing space would further exacerbate this situation which could have the effect of individuals having to wait longer before they can seek the advice they need. This needs to be addressed prior to the introduction of the scheme, high standards of debt advice need to be maintained to ensure debtors are not pushed into the wrong solution.

We believe that the existing system works well for mortgage borrowers, the strong regulation offered by the mortgage handbook and Ministry of Justice (MOJ) pre-action protocol ensure that if all mortgage related payments are kept out of a breathing space agreement no negative effects will be felt by the customer. Exclusion from breathing space will allow lenders to continue to offer bespoke flexible forbearance solutions which would work alongside breathing space. We cannot see any cost/benefit justification for members having to completely overhaul their existing successful processes and systems.

We acknowledge that there are sectors where creditor behaviour is less tightly monitored and controlled, unregulated creditors that are outside the scope of FCA regulation are a particular area of risk. Breathing space could certainly help bring some much needed consistency in how creditors collect debt, however we should be mindful that any proposals do not negatively impact those sectors who are already working to very high standards for the benefit of customers with strong regulator oversight.

Response to Questions

1. Do you agree with the eligibility criteria for entering a breathing space, including the 12 month period?

Yes, although we feel the debt advisor should complete a full income and expenditure assessment before recommending a debtor move into breathing space. Only by completing this exercise will the debt advisor get a complete and accurate picture of the debtor's circumstances, this will also mitigate the risk of debt advisors advising a debtor to move into a breath space scheme where there may be a better alternative option. It is important that breathing space does not become the default solution to all customers in payment difficulties.

In order for the scheme to be successful the debtor must be able to access good quality debt advice quickly. It is sensible to provide examples of when breathing space protections should not be triggered. Clear and detailed guidance must be provided to ensure quality training of debt advisors can be formulated, there would also need to be consistency across providers, a common accreditation may be a method of achieving some consistency of standards across the debt advice sector.

We agree with limiting the protections of breathing space to once annually which will help mitigate the risk of gaming of the system. However, we would suggest where an individual has made use of breathing space recently say within the last 3 years there should be some onus on the debt advisor to explore why this has occurred and what steps will be taken to ensure the customer returns to financial health long-term. Breathing space could not be judged a success if large numbers of individuals are dipping in and out of the scheme every few years.

2. Do you think there should be a formal mechanism to allow creditors to object to a debtor's entry into a breathing space, given the protections already outlined above?

How could any such mechanism be best designed to minimise administrative burden?

Yes, creditors will hold lots of information on their debtors more so than a debt advisor, particularly if a detail income and expenditure exercise has not been completed. This appeal process should be as simple as possible to avoid an extra administrative burden.

3. Do you agree with the outline of the alternative access mechanism for individuals in mental health crisis care?

Yes, as long as evidence that confirmation has been given by a mental health professional on the individual condition and status.

4. Although it will be important for a professional assessment to be made of an individual's condition, do you agree that other third parties (e.g. carers) be permitted to use that professional assessment to make a referral to a debt advice agency on an individual's behalf?

Yes.

5. Do you agree with the proposed method of administering entrance into breathing space? Do you agree with the proposed role for the Insolvency Service? What kind of functionality should the Insolvency Service's notification mechanism include?

Yes, we agree that the Insolvency Service would be the most appropriate body to manage this process, however the mention of "Insolvency" may deter some individuals out of fear, stigma or misunderstanding.

We believe the best solution would be a ring-fenced and rebranded entity which sits within the Insolvency Service.

The two formal notifications of an individual's entry into breathing space and when an individual exits the protections are sensible however we would suggest a third notification at the 30 day check point informing creditors of completion of a successful review with the individual and continuation of breathing space or termination of the protections which would allow creditors to commence recovery action.

6. Do you think there should be an oversight role to ensure creditor compliance with breathing space? If so, how should this oversight role operate?

We do not feel this is necessary for regulated firms as existing regulators such as the FCA are likely to build this into their usual supervision of arrears/forbearance management. We would suggest that the Insolvency Service provide this oversight for non-regulated firms to ensure they are held to the same high standards as our members.

7. Do you think the register holding details of debtors in a breathing space should be fully public, accessible to relevant debt advice agencies and creditors or just accessible to the Insolvency Service?

We **do not** feel that a fully public register is a sensible approach, this would lead to vulnerable individuals being targeted by determined lead generators. Access should be made available to creditors via a secure portal this would help verify information provided by debt advice agencies.

8. Do you agree with the proposed approach for excluding certain debts from the protections of breathing space?

We agree in principle that some debts should be excluded however it is unclear as to the rationale of each of the debts listed in the paper. There should be a clear rationale for each of the debts excluded.

9. Do you think there are other debts, such as those in regulated credit agreements, or certain types of benefits, that should be excluded?

We support the list of debts included in breathing space, evidence from debt charities has increasingly shown that council tax arrears and benefit overpayments are the most common debt types. Often these debts are pursued very aggressively certainly at odds with the forbearance practices of regulated mortgage lenders. It is crucial to the success of the scheme that these debts are included.

All costs related to payment of the mortgage should be excluded, existing FCA guidance ensures any charges imposed by a firm are reasonable:-

“A firm must ensure that any regulated mortgage contract that it enters does not impose, and cannot be used to impose, a charge or charges for a payment shortfall on a customer unless the firm is able objectively to justify that the charge is equal to or lower than a reasonable calculation of the cost of the additional administration required as a result of the customer having a payment shortfall.”

Allowing debt to build up secured against a debtors property is certainly not in their best interest as it would erode equity and potentially threaten the roof over their head.

Interest on mortgage arrears should not be treated any differently to interest on the principle balance, having to separate the interest would present significant challenges and complexities for mortgage lenders. Some members have advised me that existing mortgage platforms would not be able to perform this function, manual intervention is not a safe option and would require excessive resource which would be extremely costly.

10. Do you agree with the treatment of sole traders in breathing space? In particular:

- **Do you agree with the proposed eligibility criteria and protections for sole traders in breathing space?**
- **What would be the most appropriate way of distinguishing between business and personal debts for these purposes?**

We agree that business debts the individual is responsible for should be included in the scope of protections. However, this protection should only be available to sole traders and we feel the restriction on turnover below the VAT registration threshold is sensible.

All Sole Traders should ideally have separate business bank accounts however we are aware that many individuals operate businesses via their personal account. To our knowledge the Business Debt Line operated by the Money Advice Trust is the only free to public debt advisory service that specialises in business customers. If a debt advisor were to conduct a detailed income and expenditure assessment they may be able to distinguish between business and personal debt, without this assessment it would be difficult to gain an accurate picture of the debtors circumstances. There certainly may be a knowledge gap within the debt advisory sector which would need to be plugged.

11. Do you agree with the proposed treatment of interest, fees and charges in breathing space?

No, for the reasons mentioned earlier. Apart from examples of short-term credit we do not believe collecting the contractual interest of a mortgage would disrupt the customer's journey or contribute to the failure of a breathing space scheme.

On residential mortgages, the mortgage arrears would be excluded from a debt solution such as debt management plans and Individual Voluntary Arrangements, treated separately and prioritised so that the residential home is protected.

12. Do you agree with the treatment of collections recovery action during breathing space? Should any other forms of collections and recovery action be explicitly included in the protections? How can any practical issues arising from preventing these collections and recovery actions be best mitigated?

We would caution that undue delay when pre-action protocol has been initiated may be counter to the FCA's guidance on over forbearance. Repossession is always the last resort for a lender, however in some instances it is the best solution for the customer and delay may erode their equity in the property.

13. How should creditor compliance with the scheme be monitored?

As mentioned earlier we do not feel that regulated firms require any additional oversight however non-regulated firms should have additional oversight from the Insolvency Service hopefully this would help raise the standard of debt collection across the board.

It may be worth mentioning here that the absence of a regulator for all debt collection has certainly led to major inconsistencies across creditors, we would welcome any move that improves standards across creditors and importantly brings consistency for those struggling with debt.

14. Do you agree with the proposed length of breathing space? Do you have any other comments on the operation of the check?

The ability to review after 30 days is important and the 60 days brings breathing space in line with existing forbearance timeframes. We believe creditors should receive an update notification at 30 days which could highlight debtor engagement or lack of it.

15. Do you consider that this protection is appropriate for individuals in a mental health crisis? Should there be any further protections for individuals who have accessed breathing space in this way?

Others may be better placed to answer this question.

16. Do you agree with the eligibility criteria for entering a plan? In particular, do you agree that plans lasting for a maximum of ten years is an appropriate timeframe for debt repayment?

All mortgage related costs should be excluded from a plan to enable debtors to pay off mortgage debt as soon as possible and protect their home. It is important that ten years is only used in exceptional circumstances and the aim should be to repay debts as soon as possible. Clearly, any mortgage debt would have to be repaid prior to expiry of the mortgage term.

17. Do you agree with the proposed criteria for creditors to object to a plan? Are there any other criteria you feel appropriate?

Yes.

18. Do you agree with the design of the proposed fair and reasonable test?

Yes, we would welcome further engagement to understand the mechanics of how this would work.

The 14 day timescale for creditors seems reasonable, however this should be explored further with creditors to fully understand the systems implications and viability of this timeframe.

19. Do you agree with the debts included within a plan? Should any other debts be excluded, or excludable on request?

All mortgage related costs should be excluded in order to protect the debtor's housing situation. Mortgage lenders should have the flexibility to follow existing recovery processes as allowing these debts to build up may not be beneficial for the debtor.

20. Do you agree with the proposed treatment of interest, fees and charges within the plan?

We disagree for the reasons mentioned earlier.

21. Do you agree with the proposed protections within the plan? Are there any unintended consequences that could arise from providing these protections to debtors?

Our members should be able to proceed with existing recovery action process, the FCA warns against delaying action which could be to the detriment of the debtor. Where payments due on a mortgage are missed, whether included in a Statutory Debt Repayment Plan (SDRP) or not, a mortgage lender should be able to initiate new court action.

22. How do you think creditor compliance with the scheme's protections can be best monitored? Should creditors who fail to comply face any sanction?

See our previous answer to question 13.

23. Do you agree that some debts should be prioritised for repayments within the plan?

Housing costs should always be prioritised to protect the debtor's home, however we would point out that in respect of mortgage arrears there is already an established principle that if the arrears are not able to be repaid before the end of the mortgage term, then the court will not suspend a possession order.

24. Do you agree with the two key plan flexibilities outlined? Should the plan offer any other flexibility that would help to make them sustainable over time?

We are supportive of annual reviews which would review income and expenditure and assess if the debtors are making appropriate levels of payments. We also believe there should be a condition that debtors contact their debt advisor when they have a change of circumstances such as pay rise, bonus or reduction in expenditure. Where there is a change of circumstances reviewing the plan earlier would be beneficial to the debtor.

We are not supportive of a payment break, up to 6 months is excessive and may discourage the motivation of individuals to get themselves back on their feet. It is also unclear what the parameters of qualification would be, for example individuals may have relevant insurance to cover for sickness so a payment holiday would not be suitable.

25. Do you have any specific comments about how these flexibilities should work? In particular, how do you think a severe, temporary, financial shock should be defined?

No, however this needs to be carefully assessed with clear guidelines.

26. Do you agree with the requirements for continued eligibility for the plan?

Yes.

27. Should the plan's funding mechanism system be based on taking a share of creditors monthly repayments?

This needs to be fair and transparent, a full cost analysis would be required before we could comment in any detail. The plans funding should be based solely on recovery of costs of administering the SDRP. The financial services sector already make significant contributions via the FCA levy supporting the Money Advice Trust/Standard Financial Guidance Body as well as large voluntary contributions to other free to consumer debt organisations such as the Money Advice Trust. Any solution should ensure that other sectors step up to the plate and contribute equally.

Deduction of a share of creditor's monthly payments would not work in respect of secured debt as this implies that an element of the debt is written off.

28. How should payment distribution in a plan be done? Should it be offered by an individual's debt advice agency, if they have appropriate handling client money permissions, or by the insolvency Service, or is there any other model that the government should consider?

For simplicity purposes it would be preferable for the distribution to be facilitated by the insolvency service rather than individual debt advice agencies, however each of these options is workable.

29. Do you have any views on how a breathing space and plan should be reflected on a debtor's credit file?

Entry into breathing space should be noted on a debtors credit file to discourage further borrowing, this is the most universal approach creditors use to provide credit. We would suggest this be removed at least one year after breathing space, which allows sufficient time for the debtor to demonstrate good financial management.

30. Do you agree with the proposed territorial scope of the scheme?

Yes.

Conclusion

We firmly believe breathing space should be limited to those sectors where consumer detriment is identified and there is a little or no regulatory or legal protections for consumers. Including mortgages within this scheme will disrupt a highly regulated arrears and forbearance process which is overseen by a strong regulator and mean unnecessary cost for our members.

We are happy to engage with Treasury on any of points raised in this response.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £387 billion, and account for 22% of the UK mortgage market and 18% of the UK savings market.