

# **Call for evidence: Review of the personal insolvency framework (The Insolvency Service)**

**AdviceUK response**

October 2022



Thank you for giving AdviceUK the opportunity to respond to Call for evidence: Review of the personal insolvency framework.

**Section 1** of our response includes background information on AdviceUK. **Section 2** details our response to the call for evidence.

## **SECTION 1: BACKGROUND AND OVERVIEW**

### **About AdviceUK**

We would like to take this opportunity to provide you with some background information about AdviceUK: -

- AdviceUK is the largest network of independent advice centres in the UK, with (at the time of writing) over 650 member organisations in England, Scotland and Wales.
- Our members are very diverse both in terms of size and nature. Some are large organisations with predominantly paid staff. However, many are small community-based organisations, some of whom are staffed and managed by part-time volunteers.
- For many AdviceUK members, the provision of advice is their core business activity. However, for a significant minority advice is only one of a range of services provided, e.g. our members include housing associations, student unions, and women's refuges.
- Some of our members provide advice across a range of areas of social welfare law, e.g. housing, debt and benefits. Others only provide advice in one area of law, e.g. immigration or employment.
- More than 250 of AdviceUK's members provide debt advice to the general public. The Money Advice Trust has estimated that they account for 25% of free- to-client face to face money advice provision in the UK.
- Most of our members work in areas with high levels of multiple deprivation and over a quarter specifically serve niche communities, e.g. defined ethnic minority groups (very often where English is not the first language), or disabled people.
- Debt advice was first developed by AdviceUK member the Birmingham Settlement in the 1970s and since then our money advice members have been

at the forefront of innovation in the sector. This continues to be the case today as members have responded to the COVID-19 pandemic and the current cost of living crisis.

- AdviceUK has been designated as a Competent Authority under the Debt Relief Order regulations.

## **SECTION 2: ADVICEUK'S RESPONSE TO THE CALL FOR EVIDENCE**

### **Introduction**

We welcome the call for evidence on the personal insolvency framework. There have been major societal and economic changes in the UK since the introduction of the Insolvency Act in 1986 and, as a result, we believe that significant changes are needed in the area of personal insolvency.

Because we have limited capacity, it has only been possible for us to provide our views on the main changes that we think are needed to the personal insolvency framework. Our views have been informed by a sector-wide survey of advisers working in the not-for-profit debt advice sector. Over 500 responses were received from advisers, including many from advisers working for members of the AdviceUK network.<sup>1</sup> That said, the views expressed in this response to the call for evidence are AdviceUK's and may not necessarily reflect the views of all of our members.

We think that six major changes are needed to the current framework for personal insolvency. These changes are detailed below.

### **1. The Insolvency Service should have a stronger consumer protection role**

The description of The Insolvency Service on the GOV.UK website states:

We are a government agency that helps to deliver economic confidence by supporting those in financial distress, tackling financial wrongdoing and maximising returns to creditors.

In achieving this purpose, The Insolvency Service aims to balance the interests of people in debt with the interests of creditors.

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<sup>1</sup> We are happy to share the results of this survey on request

However, we believe that there is a power imbalance between creditors and people in debt and that The Insolvency Service should take a more active role in addressing that imbalance. We would like to see The Insolvency Service have a much stronger consumer protection focus, ideally one aligned with the Financial Conduct Authority's (FCA's) new consumer duty.

There is still a great deal of stigma associated with insolvency, and we think it is important that, both in its actions and its language, The Insolvency Service offers people in debt a fresh start and avoids any suggestion that people should be punished for their financial problems.

## **2. The insolvency framework should be more flexible**

More than ever before, people's circumstances are changing. In part, this is a reflection of changes in the employment landscape since the 1980s, with more people working in more flexible ways and with a greater number of people having incomes that fluctuate. Examples of this trend include the growth of the gig economy, the emergence of zero hours contracts and an increase in the number of self-employed people. This means that some people enter into an insolvency option that subsequently is no longer suitable for them.

However, the current insolvency framework does not make it easy for people to move from one insolvency option to another when their circumstances have changed. It is therefore important that the framework is amended to facilitate movement from one option to another where there has been a change in someone's circumstances.

In addition, there should be greater flexibility within the different insolvency options, so that they can better accommodate changes in people's circumstances. Debt Relief Orders (DROs), for example, are very inflexible to the extent that a DRO can be revoked if the individual's circumstances change during the moratorium period.

## **3. There should be a single insolvency portal**

Under the current insolvency framework, there are different ways in which people in debt can access an insolvency option, e.g. DROs can only be accessed through an approved DRO intermediary, Individual Voluntary Arrangements (IVAs) through an insolvency practitioner, and bankruptcy online via GOV.UK.

We think that this is confusing for people in debt and that creating a single portal as the only way in which someone can access an insolvency option will simplify the landscape and make people's journeys into insolvency easier.

We believe that a single portal will have other advantages. At present, anyone searching for an insolvency solution on the internet will be met with a confusing array of information sources, many of which are unreliable and many of which are commercially driven. This makes it very difficult for an individual to make an informed decision about the most appropriate insolvency option for their particular circumstances. Where the internet is concerned, insolvency is very much the Wild West with many unscrupulous cowboys seeking commercial advantage from people's financial difficulties. A single portal will protect people from this potential exploitation, and in particular people in vulnerable circumstances.

We think that the portal should be hosted by GOV.UK and should include access to Breathing Space, DROs, IVAs, bankruptcy and Statutory Debt Repayment Plans (when the latter are implemented).

The portal will provide reliable information about insolvency options.

We think that the portal could incorporate some decision trees that would narrow down the range of available options for an individual in financial difficulty, e.g. if someone had debts in excess of £30,000 for DRO option would not appear.

The portal could also provide referrals to providers. Ideally, though, we think that people should receive free, impartial, independent debt advice before proceeding with a particular insolvency option. Something along these lines already exists in Scotland where an individual cannot access the Scottish Debt Arrangement Scheme until they have received budgeting advice from a debt adviser. Adopting a similar approach would avoid the Wild West situation described above and ensure that people in debt entered the insolvency option most appropriate to their individual circumstances and in their best interests. There are clear benefits, in our view, in separating advice from delivery. However, we recognise that this could increase demand for not-for-profit debt advice and therefore has resource implications.

#### **4. The FCA should regulate insolvency practitioners**

In our opinion, the current IVA market is a largely dysfunctional one. Advisers working for AdviceUK members see far too many people who have entered into an IVA when it was not in their best interests to do so.

For example, one of our members recently wrote the following to us:

... the mis-selling of IVA's is becoming more common. Clients on benefits, less than £30k debt hooked in to an expensive IVA when they should have been on a DRO come to us in a worse position than they were when they first needed debt advice.... Some IVA companies will not release clients who are on benefits from their IVA and then we end up in a complaint process with them, in order to protect the client as best as we can. These companies advertise on TikTok etc., so get to people when they can be quite vulnerable.

There are far too many failed IVAs. We think that this unacceptably high failure rate provides further evidence of the widespread mis-selling of IVAs. The business model adopted by a firm drives its behaviour and fatally compromises the impartiality of the advice that people in debt receive. This was also the case with informal debt management plans prior to the FCA assuming responsibility for the regulation of consumer credit in 2014. However, the problem with this market has largely disappeared since then due to the effectiveness of the FCA's regulatory regime. In our view, the bodies currently responsible for regulating insolvency practitioners have failed and we believe that the FCA should assume responsibility for regulating insolvency profession in the same way that they now regulate commercial debt management. FCA regulation would allow for the proper monitoring of consumer outcomes and address the risk of consumer detriment. It would have the added advantage of further simplifying the insolvency landscape.

## **5. Insolvency fees should be means-tested**

People who would benefit from an insolvency option should not be prevented from accessing it because they cannot afford to do so.

At present, many people seen by AdviceUK members cannot apply for bankruptcy because they cannot afford the £680 fee. This is also true, although to a lesser extent, in relation to DROs, even though it is possible to pay the £90 fee in instalments. For people living on very low incomes, £90 is a lot to have to pay at a time when they are struggling to meet even their essential daily living needs. For most, the £680 need for bankruptcy is simply impossible.

Advisers have traditionally sought to raise insolvency fees for clients by applying to charitable trusts. However, not only does this take up valuable adviser time, it is also now becoming increasingly difficult to raise the fee in this way, given that

many charitable trusts are now experiencing significantly increased demand for help.

Fees should never be a barrier to accessing an insolvency option. We therefore believe that means-testing should be introduced in relation to insolvency fees to ensure that people on low incomes are able to access the insolvency option that best meets their needs.

## **6. DROs should be simpler and more flexible**

We welcomed the introduction of DROs in 2009. The scheme was intended to provide a simple and affordable alternative to bankruptcy for people with low incomes and few assets. We know that many people in financial difficulty have benefitted from the scheme in the thirteen years since then.

However, from an adviser's perspective the scheme is neither simple nor affordable. DROs are time-consuming and complex. It is telling, we think, that over a third of all the enquiries that Shelter's Specialist Debt Advice Service receive from advisers are about DROs. In our view, this indicates that there are systemic problems with the scheme. It is also very resource-intensive which means that, in effect, not-for-profit charities are subsidising the delivery of a Government scheme. We think that this is unacceptable and ultimately unsustainable.

The DRO scheme is also lacking in flexibility, as we have noted earlier in our response.

We are therefore of the view that the scheme should be reviewed with the aim of making it simpler for advisers and more flexible for people in debt.

## **CONCLUSION**

Thank you once again for giving us the opportunity to respond to the call for evidence. We hope you have found our response to be both helpful and useful.

If you have any questions or require further clarification on any of the points that we have raised then please contact: -

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