The Social Security (Claims and Payments) Amendment (No.2) Regulations 2006 (S.I.2006 No.3188)

Report by the Social Security Advisory Committee
under Section 174(1) of the Social Security Administration Act 1992
and the statement by the Secretary of State for Work and Pensions
in accordance with Section 174(2) of that Act.

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Presented to Parliament by the Secretary of State for Work and Pensions
by Command of Her Majesty
December 2006

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Statement by the Secretary of State for Social Security in accordance with section 174 (2) of the Social Security Administration Act 1992.

Introduction

1. The Social Security (Claims and Payments) (Amendment) Regulations 2006 were referred to the Social Security Advisory Committee on 2nd August 2006 for consultation in accordance with section 174 (1) of the Social Security Administration Act 1992.

2. These regulations amend Schedule 9 of the Social Security (Claims and Payments) Regulations 1987.

3. The purpose of these changes is to introduce a scheme where, in certain circumstances, lenders can apply for repayment to be made by deduction from benefit, where normal repayment arrangements have broken down. The changes are being introduced as part of the Government's financial inclusion strategy.

4. The scheme will be known as the Eligible Loan Deduction Scheme (ELDS), formerly known as the Affordable Credit Deductions Scheme (ACDS), and its purpose is to increase the accessibility of affordable loans for people on low incomes, encountering exclusion from mainstream financial services, by reducing the high risk levels and costs associated with lending to low-income groups.

5. Full details of the scheme are shown in the Explanatory Memorandum to the Social Security Advisory Committee.

The Regulations

6. The regulations will set out the conditions under which deductions from benefits may be made, including the lenders who will come within the scope of the scheme, the priority order of benefits from which deductions should be taken, rules on the maximum amount of deductions which should be taken and conditions on the circumstances, time of making, where deductions can be taken, and termination of deductions.

The Committee's Report and Recommendations

7. The Committee's report acknowledged that there was some support for the scheme from lenders and advice agencies. It concluded, however, that, while the Committee supported the Government's aim of increasing access to affordable sources of credit for people on low incomes, they did not feel that the proposed ELDS would achieve this aim.

8. The Committee therefore recommended:

That given its concerns the proposals should not be implemented and that the Government should look for more effective ways of improving access to low cost credit to low – income consumers.

That there should be a review of the system of deductions from benefits, including those for debts to third parties, before there is any further widening of the system. This review should consider issues of consistency in policy and efficient administration as well as the impact on claimants of deduction from benefits.

The Government Response

9. The Committee's conclusions and recommendations were based on four main areas of concern:

- The costs and inefficiency of the scheme
- The risk that it could encourage bad debt recovery practices
- The risk that it could encourage irresponsible lending
- The priority being given to third sector debts in the context of wider third party deduction policy

The Committee's conclusions are summarised and the Government's response given in the following paragraphs.

Costs and efficiency

10. The Committee concluded:

"*If take-up of the scheme among lenders turns out to be as low as suggested, then the cost becomes hard to justify. The money might be better spent on increasing the Social Fund budget*."

11. While accepting that take-up might be low initially, there has been strong interest and support for the scheme among third sector lenders and the Government believes it has potential to make a useful contribution to the availability of affordable credit for people on low incomes, as part of a package of measures including the £36 million Financial Inclusion Growth Fund. Considerable care has been taken in designing both the policy and the operation of the scheme as simply as possible. Of the £10 million originally allocated from the Financial Inclusion Fund it is now estimated that less than £3 million will be needed for the one-off cost in setting up the scheme. These resources have already been committed. The running costs are expected to be low – only around £100 – £150k per year depending on take- up.

12. The Social Fund provides an important source of interest-free credit targeted on the most vulnerable people on income-related benefits. An additional £210 million over the three years from 2006/07 to 2008/09 has been invested in the Social Fund Budgeting Loans scheme to fund significant improvements which will simplify and expand the scheme. Resources from the Financial Inclusion Fund are intended to be used to move people towards mainstream financial services. The relatively modest investment of £3million from the Financial Inclusion Fund should make a positive contribution to other measures to help expand access to more affordable credit.

Encouragement of bad arrears recovery practices

13. The Committee concluded:

"*As currently designed we believe there are inadequate safeguards in the scheme and that it could encourage debt recovery practices that are more harsh than those generally deployed by unsecured creditors. Moreover it is discriminatory as an attachment of earnings order would not be granted for only two months' arrears*."

14. The Government has considered the points made and has amended the draft regulations to provide that deductions will not be taken unless payments have not been made under the terms of the original, or re-negotiated, loan agreement for at least thirteen weeks. This should enable lenders to take positive and sympathetic action to agree suitable alternative arrangements with someone having genuine difficulties in repaying a loan before an application for benefit deductions is made.

15. The Memorandum of Understanding between the Secretary of State and eligible lender has been amended to be more explicit about the way in which lenders are expected to deal with default before a referral is made. It will include an expectation that lenders will take steps to agree alternative arrangements for re-scheduling, taking into account other financial commitments, personal factors affecting ability to repay, such as long-term health problems; and work with recognised debt-counselling agencies if appropriate. A safeguard will be built into our processes whereby, in the event of a dispute between lender and borrower about the liability for the loan and the amount owing, a referral will not be accepted.

Encouragement of irresponsible lending practices

16. The Committee concluded:

"We believe there is a danger that it could also encourage irresponsible lending and undermine steps being taken among third sector lenders to improve risk assessment techniques as they widen access to loans."

17. It is the Committee's opinion that it might have been better to require third sector lenders who use the ELDS to become signatories of the Banking Code as this provides detailed guidance on dealing with customers who are in arrears both sympathetically and responsibly and Code compliance is routinely monitored by the Banking Code Standards Board.

18. It is not possible, and neither is it the role of the benefits deductions scheme, to set rules for consumer credit practice or the credit industry generally. However, the Government has taken care to try to ensure that the scheme is only available to lenders who can demonstrate that they follow good lending and arrears management practices. The Memorandum of Understanding between the lender and Secretary of State will set out the standards lenders will be expected to follow and this will be subject to review.

19. The Department will monitor the extent to which lenders adhere to the Memorandum of Understanding ie. whether proper warnings about deductions were issued at the time the loan was taken out, whether borrowers in financial difficulty were treated sympathetically and whether adequate information about debt advice had been issued. The Memorandum of Understanding incorporates a requirement that income and expenditure risk assessments will be conducted prior to lending and, that where the borrower is experiencing difficulty, the lender is required to take steps to agree alternative arrangements for re-scheduling repayments and/or providing a source of independent free debt advice prior to referral for deductions. The lender will be required to demonstrate their adherence to these practices both as part of the assessment process before DWP enters into a Memorandum of Understanding and with each referral which will be accompanied by the signed loan agreement form. These will provide proof of the terms agreed at the time the loan was taken out. The regulations also provide that where a lender does not adhere to the terms of the Memorandum of Understanding, deductions will cease. Ongoing lender eligibility and adherence to the terms of the Memorandum of Understanding will be reviewed on an annual basis.

Diversion from main purpose of third party deductions and the priority being given to third sector debts (and the amount of deduction) in the context of wider third party deduction policy.

20. The Committee concluded:

"The proposed level of deduction is too high for a non-priority debt and the ACDS (now known as ELDS) *effectively promotes a small number of third sector lenders to the status of priority creditor.*

We are concerned that although originally set up for priority debts (housing costs and fuel) the third party deduction scheme is gradually being extended in an ad hoc fashion; and

We are concerned that the ACDS (now known as ELDS) *scheme will in effect take priority over rent and fuel for those receiving Carer's Allowance and certain other contributory benefits, and we consider that this is undesirable."*

21. For the scheme to fulfil its purpose of creating the conditions which will help lenders reduce the cost of affordable credit and lend more widely to people on low income it is important that the deduction is set at a level which could make a difference to their costs. At the same time, the Government is mindful that the deduction should not place an unreasonable burden on benefit recipients, where they are having difficulty in repaying their bills. The deduction rate is set at a standard 5% of the income support personal allowance for a person aged not less than 25. This is in line with the rate for other third party deductions, which has been accepted as being a reasonable and sustainable amount to repay debts. The Government believes that this achieves a reasonable balance between those two aims.

22. The ELDS loan is placed as the lowest of the priority order of all third party deductions, after essential costs such as housing, fuel, and water, and all the limits and safeguards that apply to the wider scheme have been applied, thus protecting the customer's benefit income. The rules ensure that no more than three deductions are taken in repayment of debts. This means that for customers with multiple debts, a loan deduction will not be taken where more essential debts take priority.

23. The third party deduction scheme is long standing, starting in the 1970s initially to safeguard benefit claimants fuel supply, and it's purpose has been primarily to safeguard the position of people receiving income-related benefits where they fall into arrears with essential bills. This remains the principal rationale for the scheme although deductions are also made under wider powers to discharge debts which help in enforcing compliance with social and financial obligations (eg. fines, Child Support). There has not been any new type of deduction since 1993, when deductions for Council Tax replaced those for Community Charge although there have been some changes in recent years to the scope and amount of existing deductions.

24.The Government takes the view that introducing a new deduction to repay a private loan in the circumstances prescribed fulfils a public policy role which, given the protections planned, should be beneficial to people on low income including people on benefits. It does not accept that the scheme is being added to in an arbitrary ad-hoc way and will continue to keep arrangements under review to ensure that new deductions are not introduced without careful consideration of the value and consequences of doing so, and to ensure they are consistent with the wider rules for deductions and take account of other debts and commitments.

25. Loans deductions may be applied to the full range of income-replacement benefits to ensure maximum impact for people on low incomes through wider access to affordable credit that the scheme is intended to support. There is no good case for excluding one or other of the benefits from this form of deduction. Other third party deductions will continue to apply only to income-related benefits as they are intended to safeguard the position of the most vulnerable from the consequences of not meeting essential financial commitments.

Conclusion

26. The Government is grateful to the Committee, and the agencies who responded to consultation, for their consideration of the scheme and resulting comments.

27. It is hoped that the amendments to the scheme and the responses provided will have reduced the concerns expressed by the Committee and those agencies who responded to consultation.

28. For the reasons outlined in this statement, the Government has decided to implement the proposals with the amendments outlined.

29. These regulations are now laid before Parliament.

The Rt Hon John Hutton MP
Secretary of State for Work and Pensions
Richmond House
70 Whitehall
London
SW1A 2NS

17 October 2006

Dear Secretary of State

REPORT OF THE SOCIAL SECURITY ADVISORY COMMITTEE MADE UNDER SECTION 174 OF THE SOCIAL SECURITY ADMINISTRATION ACT 1992

THE SOCIAL SECURITY (CLAIMS AND PAYMENTS) (AMENDMENTS) (No. xx) REGULATIONS 2006

1. Introduction

1.1 The Department of Work and Pensions proposes regulations to allow deductions from social security benefits where there has been failure to repay loans to "not for profit" (or "third sector") lenders such as credit unions and community development finance institutions (CDFIs). This scheme, known as the Affordable Credit Deductions Scheme (ACDS), would not be open to commercial lenders.

1.2 Separate regulations, similar in effect, are proposed for Northern Ireland.

1.3 The proposals were put to the Committee for consideration on 2nd August 2006 with a detailed explanatory memorandum from the Department *(Appendix 1)*. On 9th August we published a press release inviting comments on the proposals to reach us by 15th September.

1.4 We received responses from the 10 organisations listed at Appendix 2. We are grateful to those who responded and also to officials of the Department of Work and Pensions for their assistance in preparing this report.

2. Purpose and Background

2.1 In 2004 the Government published *Promoting Financial Inclusion,* setting out a strategy for tacking financial exclusion. The Department explained to us that, as part of the strategy, the Affordable Credit Deductions Scheme is intended to increase the accessibility of affordable loans for those on low incomes encountering exclusion from mainstream financial services. The aim is to achieve this by reducing the high risk levels and costs associated with lending to low-income groups.

2.2 The Department's explanatory memorandum gives the details of how the scheme would operate. There are conditions which lenders must meet to be eligible for the scheme, and they must sign a memorandum of understanding (MoU) with the Department setting out required levels of service, including the provision of information about where to get free debt advice. Only personal unsecured cash loans would qualify (i.e. not cash advances against a credit card and not business loans).

2.3 The regulations would put these deductions within the long-standing system of limits and priorities for Third Party Deductions (TPDs) from benefits (established in Schedule 9 of the Claims and Payments Regulations 1987) for payment of various debts including housing, fuel and water charges and council tax debts, and court fines.

2.4 The rate for most deductions is set at 5 per cent of the Income Support personal allowance rate for a single person aged not less than 25, rounded up to the nearest 5p. (There can also be deductions for current consumption in some cases.) For 2006/7 this is £2.90 which will rise automatically with the annual uprating of benefits. More than one deduction for debt to different creditors can be made at any one time, but the total cannot generally exceed three times the 5 per cent limit. The total amount deducted, including deductions for current consumption, cannot exceed 25 per cent of the benefit entitlement without the customer's permission. In order to keep within these limits there is a priority order for deductions (except for some Child Support deductions which are outside the priority order and are ignored) and the new deduction would be last in the priority order. These limits could mean that deductions for other third party debts could displace one for this scheme and the lender would have to make other arrangements for recovery. The generality of deductions for debts to third parties are made only from means-tested benefits (i.e. Income Support, income-based Jobseeker's Allowance and Pension Credit) and are only made from other benefits where they are paid together with those means-tested benefits, except in Northern Ireland where deductions can be made from some national insurance benefits without the need for a means-tested benefit to also be in payment. The proposed deductions would also be made from contributory Jobseeker's Allowance, Carer's Allowance, Incapacity Benefit or Retirement Pension even where there is no entitlement to a means-tested benefit.

2.5 The draft Memorandum of Understanding explains that only one deduction for affordable credit recovery could be made at any one time. The intention is that any existing or new deduction for recovery of overpaid benefit would mean that a deduction for affordable credit would be disallowed. An affordable credit deduction will not be allowed if there is a previously existing deduction for Social Fund loan recovery, but if there is a current deduction for affordable credit recovery a new Social Fund deduction would be allowed.

3. Timing

3.1 It is intended that the scheme should be introduced in December 2006.

4. Reason for consultation

4.1 The Committee had several concerns about the proposals presented to us:

i) The scheme appeared to be an over-elaborate and costly mechanism to produce a relatively minor and uncertain effect.

ii) The Department's explanation to us suggested that the reason for restricting the scheme to non-commercial lenders was that they do not have access to such effective recovery methods as are available to commercial lenders. We do not accept that non-commercial lenders are excluded from using the same recovery methods as commercial lenders.

iii) We had concerns about the resolution of disputes between lenders and borrowers.

iv) We queried whether deductions should be allowed after just two instances of default. This appeared to encourage bad arrears management by lenders who should offer ways to reschedule repayments where borrowers get into difficulties.

v) Some of us were concerned that the proposed rate of deduction might be too high in some cases.

vi) There was a suggestion that more details of the scheme should be put onto a statutory basis.

5. Responses to the consultation

The principle of the scheme

5.1 We received ten responses including two from Credit Unions and one from a local authority that offers low-cost loans. The remaining respondents were principally advice agencies or consumer bodies. The responses were divided between those who were broadly supportive of the scheme – although in all but one case this was with caveats and those who were opposed to the proposals (including one of the three lenders). The responses from those who objected to the proposals were substantial, detailed and strongly argued. However the basis for the objections varied.

5.2 Those that welcomed the proposals in principle believed that the scheme will provide incentives both for claimants to open accounts with third-sector lenders and for such lenders to intensify their efforts to attract this segment of the borrower market. Objections to the proposed ACDS included its cost and efficiency; the fact that it is a diversion from the main purpose of third party deduction; that it will encourage bad debt recovery practices; that the proposed level of deduction is too high; that it could encourage poor lending practice and/or irresponsible borrowing, and that it considerably widens the range of benefits from which money can be deducted. We set out these objections in the following paragraphs.

Costs and inefficiency of the scheme

5.3 A wide range of arguments were put forward to suggest that the scheme would not be the best use of available resources:

i) All those objecting to the ACDS felt that, as take-up will be very low, the costs of setting up the scheme could not be justified. The minutes of the Financial Inclusion Taskforce meeting in July 2006 show they are in agreement with this point of view. It is also the view of SSAC members.

ii) The number of deductions arising from the scheme is not expected to be large, and the DWP proposes to administer the scheme at its central debt management service, which should limit the cost of the operation and its impact on the rest of the organisation. Centralisation of DWP administration might also meet concerns about the possible administrative inefficiency of the scheme. Officials have told us that cost of the scheme will be about £3m – around 8 per cent of the sum set aside for the Growth Fund.

iii) There is evidence that the take-up of the scheme among third sector lenders is likely to be very low. There are over 550 credit unions, but the Department only expects 20-25 lenders to take part in the scheme in the first year building to about 50 after three years. It has been estimated that 3.3 million people live in low-income households (the lowest income quintile) and lack ready access to the mainstream credit market[1]. The National Consumer Council estimates that around 2 million people have loans from a licensed home credit company, paying interest rates (APRs) averaging 177 per cent. In contrast, the proposed ACDS would handle just 1-2,000 cases in the first year (less than 5 per cent of the credit union loans that are in arrears), rising to 5,000 after three years.

[1] S. Collard and E Kempson, *Affordable credit: the way forward. Joseph Rowntree Foundation, 2005*

iv) Three respondents felt that the money would offer many more people access to affordable credit if it were added to the Social Fund Budget.

v) Two respondents (including one that was broadly supportive of the proposals) felt that a better way of opening up access to affordable credit would have been to make the ACDS an optional method of loan repayment – rather than tying it to default.

vi) One respondent (a third sector lender) felt that the scheme was against the spirit of third sector lending and that there were other (better) developments to widen access to affordable credit, which would enable lenders to be financially sustainable.

vii) Finally it was argued that credit unions already have a facility that enables state benefits (and other income) to be paid directly to a member's credit union account from which loan repayments can be deducted. In some ways this is superior to the proposed ACDS as it is open to people regardless of their source of income who can opt to pay in this way to avoid default. The scheme should be extended to become a mechanism of choice for repayment of loans from the outset, not just on default. Repayments should be allowed to continue after the loan has been paid off so that consumers can build up savings.

Diversion from main purpose of third party deductions

5.4 Three respondents argued that the third party deduction scheme was established to provide a way for claimants to repay arrears on priority debts – housing costs and fuel bills – to protect them from repossession of their home or loss of essential services. They express the view – shared by SSAC members – that adding loans from third sector lenders to the scheme essentially promotes them to the status of priority creditor and widens the scope of the TPD scheme in an ad hoc fashion. Furthermore, in cases where recipients of income-related benefits are in multiple arrears, we understand that it would be normal practice among advice agencies to offer non-priority creditors (including all loans and unsecured credit) a token £1 a month until the clients returns to work.

Encouragement of bad arrears recovery practices

5.5 Seven respondents (including three broadly positive about the scheme) expressed concerns that, as currently designed, the proposed ACDS could encourage bad arrears recovery practices and stated that they would like to see the safeguards on arrears recovery in the MoU considerably strengthened. Members of the SSAC share this view. The following gives a summary of the concerns about arrears recovery practices:

i) Permitting access to the ACDS after only two missed payments is far more draconian than is permitted by industry codes of practice such as the Banking Code and the Finance and Leasing Association

Code. These state that every attempt should be made to find out the reasons why payments have been missed and to negotiate a method of repayment. The high-cost home credit companies go further and would routinely reschedule the term of the loan (without charge) in cases of financial difficulty. Most lenders, therefore, would *not* transfer an account to arrears recovery after only two missed payments and would considering doing so as bad arrears management. SSAC members would be very unhappy for the ACDS to offer less protection than is offered under credit industry codes of practice.

ii) The MoU requires lenders to sign up to good practices such as offering information about free debt advice. Most respondents believed this to be of great importance and wanted the MoU to stress that this advice should be independent and referral should be *before* use of the ACDS.

iii) Some respondents pointed out that DWP staff would have difficulty in monitoring the extent to which lenders adhere to the MoU. If an application for a deduction is received from a lender, it will be difficult to judge whether proper warnings about deductions were issued at the time the loan was taken out, whether borrowers in financial difficulty were treated sympathetically and whether adequate information about debt advice had been issued. It is our opinion that it might, therefore, have been better to require third sector lenders who use the ACDS to become signatories of the Banking Code. A number of such lenders are exploring this possibility; the Code provides detailed guidance on dealing with customers who are in arrears both sympathetically and responsibly and Code compliance is routinely monitored by the Banking Code Standards Board.

iv) It is unclear what will happen in cases where the borrower disputes that the money is owed. Most lenders would suspend recovery until the dispute is resolved. For the generality of TPDs, claimants are referred to creditors if they dispute the amount they owe. The question of whether the deduction goes ahead pending resolution of any dispute will depend on the nature of the evidence available to the benefit decision-maker. It would be unhelpful if the MoU became a tool for borrowers to dispute deductions or a basis for appeals against deductions.

v) The DWP's explanation and the MoU state that interest on the loan balance outstanding will be "frozen at the point of referral to DWP", so that the amount of the debt referred cannot increase while deductions are in place. Two respondents supported this, saying that it is good arrears recovery practice and many commercial lenders would freeze interest on accounts that are passed to debt recovery. However, two lenders objected to interest being frozen when a loan is referred to the ACDS and the Department has since clarified that the intention is that deductions will be made in respect of the outstanding loan *including all interest that would have been payable had the loan been repaid as* *intended.* No additional charges or penalties, however, would be levied on loans referred to the ACDS – although one of the lenders thought they should be.

vi) Two respondents felt that third sector lenders should be prohibited from taking court action while payments are being made through the ACDS.

vii) SSAC members believe it is discriminatory to allow TPDs after only two missed payments as courts would be extremely unlikely to grant an application for an attachment of earnings order under such circumstances.

The level of deduction is too high

5.6 As we mention above, it would be common for a non-priority creditor (including third sector lenders) to receive an offer of a token payment of £1 a month in cases of multiple arrears being handled by a debt adviser. This being the case, SSAC members (and some of those responding to our consultation) would be opposed to lenders using the ACDS having repayments at 5 per cent of the Income Support personal allowance (or £2.90 a week).

Other respondents considered that the number and amount of deductions for debt already constitute a burden for some claimants and that the proposed deduction should be lower than 5 per cent for that reason

Possible encouragement of irresponsible lending and borrowing

5.7 Respondents were concerned that being able to request TPDs after only two missed payments may be incompatible with responsible lending:

i) One of the lenders argued that this could undermine steps being taken by third sector lenders to ensure better risk assessment. They went further and argued that lenders who have easy access to debt recovery through the ACDS could be encouraged to lend irresponsibly to people who are too high risk

ii) Two other respondents felt that lenders should not have access to the ACDS if they *have* lent irresponsibly and that this would require careful monitoring. We would agree with that point of view. The MoU does not, however, cover this point.

iii) The MoU states that lenders must explain to borrowers when they apply for a loan that on default the loan may referred to the DWP for recovery by deduction from benefit. The lender must ensure that the following statement is included on the loan application form:

"I agree that in the event of me defaulting on repayments, information about my loan may be passed on to the Department for Work and Pensions."

Some respondents felt that explaining the scheme at the point at which the loan is taken out could actually encourage default, as borrowers would know that the DWP would take care of any budgeting problems. There could be scope for argument and recourse to the statutory appeal system about whether an explanation was given at the time the loan was taken out. One lender has suggested that the details of the scheme – both statutory and non-statutory – should not be made public.

Benefits from which deductions can be made

5.8 Some respondents were unhappy at the wider range of benefits from which TPDs could be made for third sector lenders. For people receiving Carer's Allowance or contributory benefits where no means-tested benefit is in payment, this deduction would effectively become the highest priority – putting it above arrears on housing or fuel. SSAC members share the concerns of these respondents.

6. Conclusions

6.1 While we support the Government's aim of increasing access to affordable sources of credit for people on low incomes, we do not feel that the proposed ACDS would do much to achieve this aim. If take-up of the scheme among lenders turns out to be as low as suggested, then the cost becomes hard to justify. The money might be better spent on increasing the Social Fund budget.

6.2 As currently designed we believe there are inadequate safeguards in the scheme and that it could encourage debt recovery practices that are more harsh than those generally deployed by unsecured creditors. Moreover it is discriminatory as an attachment of earnings order would not be granted for only two months' arrears.

6.3 We believe there is a danger that it could also encourage irresponsible lending and undermine steps being taken among third sector lenders to improve risk assessment techniques as they widen access to loans.

6.4 The proposed level of deduction is too high for a non-priority debt and the ACDS effectively promotes a small number of third sector lenders to the status of priority creditor.

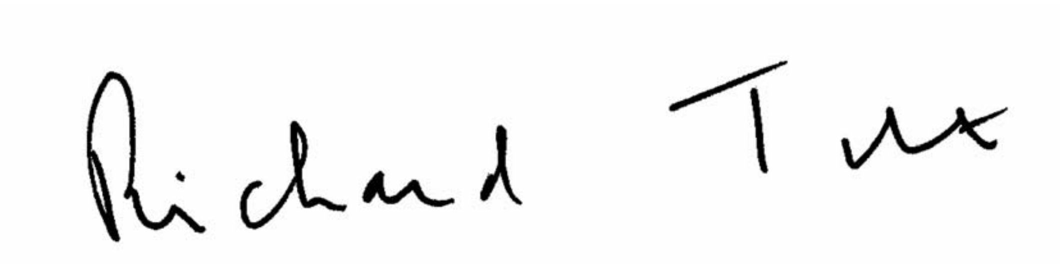
6.5 We are concerned that although originally set up for priority debts (housing costs and fuel) the TPD scheme is gradually being extended in an ad hoc fashion.

6.6 We are concerned that the ACDS scheme will in effect take priority over rent and fuel for those receiving Carer's Allowance and certain other contributory benefits, and we consider that this is undesirable.

7. Recommendations

7.1 Given these concerns we recommend that the proposals should not be implemented. The Government should look for more effective ways of improving access to low cost credit for low income consumers.

7.2 We also recommend that there should be a review of the system of deductions from benefits, including those for debts to third parties, before there is any further widening of the scheme. This review should consider issues of consistency in policy and efficient administration as well as the impact on claimants of deductions from benefits.



RICHARD TILT
CHAIRMAN

APPENDIX 1

AFFORDABLE CREDIT DEDUCTIONS SCHEME

LIST OF RESPONSES TO SSAC CONSULTATION

1. Leeds City Credit Union Ltd.
2. Holdfast Credit Union Ltd.
3. AdviceUK
4. Money Advice Trust
5. London Borough of Newham
6. Citizens Advice (NACAB)
7. Law Centre (Northern Ireland)
8. London Borough of Hounslow
9. Salford Welfare Rights
10. National Consumer Council

APPENDIX 2

Memorandum to the Social Security Advisory Committee

The Social Security (Claims and Payments) (Amendment) (No. xx) Regulations 2006.

The Affordable Credit Deductions Scheme

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Background

1. As part of the Pre-Budget Report 2004, the Government published *Promoting Financial Inclusion*. This set out a strategy for tackling financial exclusion and announced a Financial Inclusion Fund of £120 million to support policy initiatives in three priority areas:

- Access to banking services
- Access to affordable credit
- Access to face-to-face money advice

A Financial Inclusion Taskforce was also established to monitor Government policies and to consider what more can be done.

2. As part of a package of initiatives to increase access to affordable sources of credit for people on low incomes, it was announced that the Government would consider a scheme where, in certain circumstances, lenders could apply for repayment to be made by deduction from benefit, where normal repayment arrangements have broken down. The proposal was discussed with a range of private and third sector lenders and it was concluded that this scheme could make a useful contribution for some lenders, particularly in the third (not for profit) sector by helping to reduce the costs and levels of risk associated with lending to people on low incomes. Budget 2005 announced the Government's decision to develop a scheme. Budget 2006 announced that the scheme would be implemented by the end of 2006.

3. The scheme will be aimed at not for profit lenders from the third sector such as credit unions and community development finance institutions (CDFIs). This recognises their key role in the provision of affordable credit for people on low incomes and complements other measures to support them in tackling financial exclusion, for example the Growth Fund. The scheme will not be available to commercial lenders who will tend to have higher charges and to have recourse to effective recovery arrangements.

4. When the scheme is in operation, lenders interested in the deduction facility will be able to apply to the Department for Work and Pensions (DWP) to be included in the scheme. The scheme will only be available where eligible institutions meet defined criteria relating to good lending practice. If the lender meets the criteria, a Memorandum of Understanding signed by the lender and DWP, which will set out the lenders commitment to the various criteria and conditions and the terms on which deductions from benefit will be considered.

5. Once on the scheme, lenders may be required to demonstrate that they meet the criteria laid down and that they are participating with a view to making more loans available to those on low incomes, whilst demonstrating good lending practice.

6. A maximum of £10 million from the Financial Inclusion Fund has been allocated to DWP to support administration costs of this scheme and the operation of the Growth Fund. It is anticipated that start up costs for the

deduction scheme will be of the order of £3 million. Any monies not used for this scheme and the Growth Fund will be available for use elsewhere to support financial inclusion.

Rationale

7. The purpose of the Affordable Credit Deductions Scheme (ACDS) is to help increase the accessibility of affordable loans for those on low incomes encountering exclusion from mainstream financial services. The intention is to achieve this by reducing the high risk levels and costs associated with lending to low-income groups.

Benefit Simplification

8. Proposals for ACDS and subsequent deductions add complexity to the current system. The changes are being introduced as part of the Government's financial inclusion strategy which was first announced in PBR 2004 in *Promoting Financial Inclusion* and do not represent a simplification measure.

9. The scheme introduces a new process and form of benefit deduction, which will have an impact on delivery of a range of benefits. Although there are similarities with the existing third party deductions scheme, this form of deduction can apply to non income- related benefits. However, where possible, measures have been taken to administer the scheme in the simplest possible way within operational and policy constraints. A decision was taken to locate the major part of the work centrally within Debt Management and the Department's Debt Recovery Unit. This will enable consistency and expertise in decision – making and will provide a central service for lenders participating in the scheme. This should reduce the involvement of benefit staff to a minimum. In drawing up the rules we have modelled them on existing rules within the third party deduction scheme – for example the rates of deduction and the maximum limits which may apply.

Summary of proposed changes

10. The lenders eligible to join the scheme will be those who are eligible for bidding for Growth Fund money and would cover credit unions registered with the Financial Services Authority (FSA); Community Development Financial Institutions (CDFIs) registered with the FSA as Industrial and Provident Societies; or organisations registered as Charities, or constituted as not for profit organisations licensed by the Office of Fair Trading to provide relevant consumer credit services.

11. In order to join the ACDS, lenders will be required to sign a Memorandum of Understanding (MoU) which will set out the loan criteria, good lending practices, terms and conditions which lenders must adhere to and DWP practices (as set out below in paragraphs 16 to 17).

12. Deductions may be made where the customer has defaulted on repayment of the loan and reasonable action (short of legal action) has been taken by the lender to recover the loan.

13. The benefits from which deductions will be made are Income Support, Jobseekers Allowance (income based), Jobseekers Allowance (contribution based), Pension Credit, Incapacity Benefit, State Retirement Pension and Carer's Allowance.

Details of the proposed changes

The regulations

14. The regulations will set out the conditions under which deductions from benefits may be taken and include:

- the lenders who will come within the scope of the scheme;
- the priority order of benefits from which deductions should be taken;
- rules on the maximum amount of deductions which should be taken; and
- conditions on the circumstances, time of making and where deductions can be taken, and termination of deductions.

Eligible lenders

15. The scheme is aimed at lenders from the third sector. The regulations will set out the definition of the categories of lenders within scope – see paragraph 10 above. Lenders must have a current and valid OFT licence or be an FSA registered and approved credit union and interest charges must be frozen at the point of referral to DWP.

The Memorandum of Understanding

16. The MoU will establish the agreement between the DWP and the lender for purposes of eligibility for the scheme. The purpose of this MoU is to ensure that approved lending organisations are made aware of the levels of service required by DWP to participate in the ACDS and to confirm their commitment to continue to comply with the criteria for inclusion on the scheme. The MoU will be reviewed each year, with the first review taking place no later than 12 months from the date it comes into effect. In addition, a review may take place where there are any significant changes to policy or legislation, or where there is a change in the lenders arrangements which they should notify and which could affect their ongoing eligibility to participate in the scheme.

16.1 The loan criteria, eligibility criteria relating to good lending practices, terms and conditions, which the lender must adhere to, and DWP practices relating to operation of deductions are set out below. These cover both procedural practice and the circumstances under which deductions can be made provided for within regulations.

Loan criteria

16.2 To be eligible for deductions the loan must:

- be a personal unsecured cash loan
- not be cash advanced against a credit card
- not be a business loan.

Criteria relating to good lending practice

16.3. The Secretary of State will, by exercising his discretion conferred by S189 (6) of the SS Administration Act 1992, only enter into an agreement with a lender where he is satisfied that the lender will adhere to certain criteria related to standards of good lending practice. These will be set out in the MoU and include the following:

- Lenders must carry out an appropriate assessment of the customer's ability to repay, including an assessment of the customer's income, outgoings and any other credit commitments, as part of the loan application process
- Lenders must provide borrowers with details of a source of free debt advice where appropriate
- Lenders must offer a face-to-face interview where the customer or particular circumstances require it before, or after making a loan.
- Clear, and full information relating to the terms and costs of borrowing must be given to the customer before the loan agreement is made and must include clear information about the actual cost of the loan including full details of the APR and any additional charges that might be incurred.
- Where borrowers are experiencing difficulty in making the agreed repayments the lender will be required to take steps to agree suitable alternative arrangements, to reschedule repayments where feasible and, where appropriate, direct the customer to the services of financial advisers.

16.3.1. Whilst the full evidence set is not yet confirmed, we expect the SoS decision to exercise discretion will be based on the Lender supplying supporting documentation as follows:

- The loan application form, which includes record of income and outgoings, including other credit commitments.

- Promotional material, leaflets etc which specify the services provided with specific mention of access to free debt advice and provision of a face-face service to customers on request/as required both before and after making loan application.

- Loan application form/agreement showing details of the actual cost of the loan, APR and other charges clearly described.

- Details of lenders processes (including copies of standard letters) where borrower defaults on the loan.

- Application form and default letters will include certain wording as required and supplied by DWP (as part of MoU requirement)

16.3.2 The above will be in addition to the details supplied as part of the application process i.e. FSA registration number etc.

Terms and conditions for the lender

16.4 Some of the conditions below will be covered in the regulations, others which relate to administrative practice will be covered in the MoU.

- Deductions will only apply to loans taken out in GB after the scheme comes into operation and after the lender has formally been accepted onto the scheme (i.e. has signed the MoU).

- A deduction can only be made where at the time the loan agreement is entered into, the lender has explained that in the event of default on repayments the loan may be referred to DWP for recovery by deduction from benefit, and has obtained agreement for data to be shared with DWP to that effect. The borrower will not be required to give consent
to deductions.

- Interest on the loan balance outstanding will be frozen at the point of referral to DWP. This means that the amount outstanding does not increase while deductions are being made and that no other payments in respect of the same loan will be sought.

- The lender will not apply any default penalties whilst the deduction facility is in operation.

- Deductions will only be made from benefit where no other payments are being made to the lender in respect of the loan. If, after referring the case to DWP the lender subsequently receives a payment from the borrower, the lender should notify DWP and renegotiate the repayment plan with the customer.

- The lender has the right to reinstate a repayment plan with the borrower at anytime, but should give due notice to DWP to enable deductions to cease with effect from the date that payments resume.
- DWP would repay the benefit customer any payments wrongly deducted from benefit and would seek to recover from the lender normally by off-setting from scheduled payments.
- The lender must notify DWP at the earliest opportunity of any changes to their circumstances and/or the information supplied since the original application was made.

DWP action

Responsibility for debt

17. DWP will not be responsible for the loan debt and cannot guarantee deductions. Responsibility for recovery of the debt remains with the lender. Any issues relating to the loan and amounts owed raised by the borrower when the case is with DWP will be referred on to the lender.

Confidentiality

17.1 Rules of customer confidentiality will be observed. DWP will not disclose to the lender information about the customer's circumstances where deductions cannot be made. DWP will explain that it cannot make a deduction but will **not** disclose any of the borrowers' information to explain why.

Decisions and appeals

17.2 When a lender first refers a case, and deductions from benefit are possible, DWP will issue a written decision to the customer explaining that deductions will be made from benefit.

17.2.1 The normal rules relating to decisions, revisions and appeals will apply to the benefit decision relating to deductions. An appeal can be made against a decision to take deductions from benefit.

Customers moving abroad

17.3 If a customer having recovery made by deductions moves abroad, deductions will cease.

17.3.1 Deductions from benefit cannot be made from customers living in Northern Ireland. If a customer living on the mainland and having recovery made by deductions moves to NI, the case will be returned to the lender to continue recovery action.

Over-recovery of a debt

17.4 In the event of DWP making an over-recovery of a debt (and the over- recovered amount has not yet been received by the lender), an adjustment will be made by DWP before the next payment notification is issued to the lender.

Level of deductions

17.5 The amount to be deducted from a person’s benefit in respect of a loan repayment will be set at 5% of the prevailing income support personal allowance rate for a single person aged not less than 25, rounded up to the nearest 5p – currently £2.90. The rate will be up-rated annually. This is in line with other third party deductions where payments are taken in respect of arrears – e.g. for utility debts.

17.5.1 Only one deduction at a time will be made in respect of loans. Additionally a deduction will only be made from one benefit even if there is more than one eligible benefit in payment.

Priority order of benefits from which deductions will be taken

17.6 The priority order of benefits from which loan deductions will be made are as follows:

- Income based benefits, whether these are single or combined. (For the purpose of applying the deduction the income-based benefit is treated as one benefit regardless of whether there is more than one component).

- Contributory benefits

- Non-contributory benefits.

Priority and maximum amounts – income – based benefits

17.7. The loan deduction will come into line with limits set on the overall level of deductions that may be taken from benefit at one time. The intention in setting rules for this type of deduction is to ensure that the customer is left with a reasonable level of benefit after deductions have been made. Loan deductions will be lowest in the priority order after the other third party deductions to reflect the fact that other deductions are made in respect of liabilities which are essential in nature e.g. fuel, water, housing costs. Any child support deduction, which sits outside the third party deduction priority order will be ignored.

17.7.1 The rule which places a limit of a maximum of 3 times 5% of the income support personal allowance for a single person aged not less than 25 applies. So if the customer already has 3 deductions in respect of arrears for other third party deductions, the loan deduction will not be made. Another application for a deduction with higher priority, which is made at a later date, could displace a loan deduction.

17.7.2 The affordable credit deduction will be taken into account in applying the rule, which prevents the overall amount of deductions exceeding 25% without the claimant's consent.

17.8 Deductions made for overpayment and Social Fund recoveries will take priority over a potential loan deduction in order to ensure that where these are being taken the customer is not over committed.

17.8.1 In respect of loans:

- A deduction will not be made if there is a deduction in place in respect of an overpayment recovery. Any new prospect of a deduction in respect of an overpayment will displace an existing loan deduction.

- A deduction will not be made if there is an existing Social Fund loan recovery. However a new SF deduction in respect of a SF loan taken out after a loan deduction has commenced will **not** displace it. This is because the customer has the choice whether or not to take out a SF loan in addition to existing commitments. SF deduction rates are reduced for customers with existing debts.

Priority and maximum amounts – contributory and non-contributory benefits

17.8.2. The same standard rate of loan deduction will apply as for income-based benefits. Again, a deduction will not be made if there is a deduction already in place in respect of an overpayment or SF recovery and new overpayment deductions will displace an existing loan deduction.

17.8.3 Where a contributory benefit is being paid as a combined payment with an income-based benefit, all the rules in 17.7 to 17.8.1 will apply. An ACDS deduction will not be taken from a contributory or non-contributory benefit unless the *gross* amount (i.e. before any deductions are taken) of the customer's income-related benefit entitlement is insufficient to meet the deduction. "

Operational issues

18. In order to provide a more efficient service the scheme will be implemented and administered centrally by DWP Debt Management (DM). This will include:

- making decisions on benefit relating to whether deductions should be made, in liaison where appropriate with the Pension Service, Jobcentre Plus or the Disability and Carers' Service;

- lender relationship, including making potential lenders aware and explaining scheme requirements and on-going monitoring of compliance e.g. through operation of the MoU process;

- recovery by adjustment to benefit; and

- payment of deductions to lenders making the necessary accounting arrangements.

Numbers and operational impacts

19. Although it is difficult to predict the number of cases from which deductions will be made, the very speculative working assumption is that between 1000 and 2000 cases could have deductions in the first year rising to 5000 after 3 years. This is based on a prediction that the number of participating lenders will start at 20-25 in the first year and will build to 50 after 3 years.

19.1 These assumptions, whilst highly speculative, are based on information provided by the lenders with whom we have held discussions as to the likely levels of delinquency rate. This could be affected by changes in their lending patterns although at all times it will be regarded as important that the original lending decision will be based on ability to repay. Numbers will also be affected by events, which occur after a loan has been made, which could not have been predicted. For example a person may have taken a loan when in steady work and then come on to benefit at a later date.

19.2 There will be no targets for numbers of deductions and they are not expected to be high.

19.3 The additional work, which has been resourced, will be centralised within Debt Management and the impact more generally on DWP is not expected to be significant in terms of additional volumes of deductions from benefit or customer queries and can be contained within available funding (see paragraph 6). Further work will be done to ensure resources are made from the Financial Inclusion Fund where this becomes necessary.

Marketing Strategy

20. The precise detail on how the scheme will be publicised has not yet been finalised but we envisage a range of communications including an event, which will give potential lenders detailed information nearer the time. Information packs will be produced which will be used both by lenders thinking of participating and for those wishing to do so. The information pack is likely to contain:

- Background information on the deduction scheme, what constitutes an eligible lender, the type of loans we can recover by deductions, the action needed by lender prior to referral to DWP etc.

- Details of the application process and the need to enter into an MoU

- An application form with guidance notes on how to complete and the nature of supporting information required.

- A blank version of the MoU.

- A blank referral form.

20.1 The target lender group have already been engaged and advised of the Scheme and likely processes.

20.2 In addition, discussions are taking place about publicising the scheme via ABCUL (Association of British Credit Unions) and CDFA (Community Development Finance Association) websites and an article in Credit Union News and likely promotion of the Scheme via the Scottish League of Credit Unions, ACE Credit Union Services and Wales Co-operative Centre.

Monitoring/evaluation

21. A range of Management Information will be collected and used to inform evaluation of the operation of the scheme.

This will be:

- The number of lenders signed up/not accepted to the scheme.

- The number of referrals and the value of those referrals.

- The number of referrals rejected/accepted.

- The number of cases where deductions are in place and the value of those deductions.

- Prediction of expected deductions and value over given period.

- The number and value of referrals fully recovered.

- Average value of loan balance referred.

- Average recovery period of an ACDS debt.

21.1 The long term evaluation strategy has yet to be determined but is likely to consist of qualitative research. It would be difficult to evaluate the effect of this measure in isolation on the supply of affordable credit and it is likely that the impact on lenders and borrowers will be assessed alongside other financial inclusion measures, such as the Growth Fund.

21.2 The operation of the scheme will be kept under close review to assess how lenders take advantage of it and where there may be barriers to them doing so. This information will inform any future need to make changes to make the arrangements more effective.

Timing

22. It is intended that these changes will be introduced in December 2006.

Annex A

STATUTORY INSTRUMENTS

2006 No. []

SOCIAL SECURITY

The Social Security (Claims and Payments) (Amendment) (No. xx) Regulations 2006

Made - - - -	*xxx*
Laid before Parliament	*xxx*
Coming into force - -	*xxx*

The Secretary of State for Work and Pensions makes the following Regulations in exercise of the powers conferred upon him by sections 5(1)(p), 189(1), (4) and (6) and 191 of the Social Security Administration Act 1992(**a**):

[In accordance with section 173(1)(b), the Secretary of State has obtained the agreement of the Social Security Advisory Committee that proposals in respect of the Regulations need not be referred to it.]

Citation and commencement

1. These Regulations may be cited as the Social Security (Claims and Payments) (Amendment) (No. xx) Regulations 2006 and shall come into force on xxx.

Amendment of the Social Security (Claims and Payments) Regulations 1987

2.—(1) Schedule 9 (deductions from benefit and direct payment to third parties)to the Social Security (Claims and Payments) Regulations 1987(**b**) is amended in accordance with the following paragraphs.

(2) After paragraph 7C (integration loans) insert—

"**7D.**—(1) In this paragraph—

"borrower" means a person who has, either solely or jointly, entered into a loan agreement with an eligible lender in respect of an eligible loan and who is, for the time being, entitled to an eligible benefit;

"eligible lender" means one of the following which, apart from a credit union, is licensed under the Consumer Credit Act 1974(**c**)—

(a) a body registered under section 1 of the Industrial and Provident Societies Act 1965(**d**);

(b) a credit union within the meaning of section 1 the Credit Unions Act 1979(**a**);

(**a**) 1992 c.5. Section 191 is cited for the meaning given to the word "prescribe".
(**b**) S.I. 1987/1968.
(**c**) 1974 c. 39.
(**d**) 1965 c.12

(c) a housing association within the meaning of section 1 of the Housing Associations Act 1985(**b**); or

(d) a charitable institution within the meaning of section 58(1) of the Charities Act 1992(**c**)

and which is determined by the Secretary of State as an appropriate body to which payments on behalf of the borrower may be made in respect of loans made by that body.

"eligible loan" means a loan made by a lender who is, at that time, an eligible lender to a borrower except a loan—

(a) which is secured by a charge or pledge;

(b) which is for the purpose of business or self-employment; or

(c) which was made by means of a credit card.

"loan agreement" means an agreement between the eligible lender and the borrower in respect of an eligible loan;

(2) In this paragraph "eligible benefit" means—

(a) carer's allowance;

(b) the following contributory benefits—

(i) incapacity benefit;

(ii) retirement pension; or

(c) the following benefits—

(i) income support;

(ii) jobseeker's allowance;

(iii) state pension credit.

(3) Where the conditions set out in sub-paragraph (4) are met the Secretary of State may deduct a sum from an eligible benefit to which the claimant is entitled equal to 5 per cent of the personal allowance for a single claimant aged not less than 25 and pay that sum to the eligible lender towards discharge of the sum owing under the loan agreement.

(4) The conditions referred to in sub-paragraph (3) are—

(a) the borrower has twice in succession failed to make payments in respect of an eligible loan and has not resumed payment;

(b) no sum is being deducted from the claimant's eligible benefit under this paragraph;

(c) no sum is being deducted from the claimant's eligible benefit under regulation 15 (recovery by deductions from prescribed benefits) of the Social Security (Payments on account, Overpayments and Recovery) Regulations 1988(**d**); and

(d) no sum is being deducted under section 78 (recovery of social fund awards) of the Social Security Administration Act 1992(**e**).

(5) The Secretary of State shall notify the claimant and the eligible lender in writing of a decision to make a deduction under this paragraph.

(6) The Secretary of State may make deductions under this paragraph only if—

(a) the borrower is entitled to an eligible benefit throughout any benefit week; and

(b) no deduction is being made in respect of the borrower under any other application.

(7) The Secretary of State shall not make deductions from a benefit mentioned in paragraph (2)(a) where the borrower is in receipt of another eligible benefit unless that benefit is one mentioned in paragraph (2)(b) and is insufficient to enable the deduction to

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(**a**) 1979 .c34.
(**b**) 1985 c.69.
(**c**) 1992 c.41.
(**d**) S.I. 1988/664.
(**e**) 1992 c.5.

be made or is a benefit mentioned in paragraph (2)(c) and the amount is insufficient to meet the deduction plus 10 pence.

(8) The Secretary of State shall not make deductions from a benefit mentioned in paragraph (2)(b) where the claimant is in receipt of a benefit mentioned in paragraph (2)(c) unless the amount of that benefit is insufficient to meet the deduction plus 10 pence.

(9) The Secretary of State shall cease making deductions from an eligible benefit if—

(a) there is no longer sufficient entitlement to an eligible benefit to enable him to make the deduction;

(b) entitlement to all eligible benefits has ceased;

(c) a sum is deducted from the claimant's eligible benefit under regulation 15 of the Social Security (Payments on account, Overpayments and Recovery) Regulations 1988;

(d) an eligible lender notifies the Secretary of State that he no longer wishes to accept payments by deductions;

(e) the liability to make payment in respect of the eligible loan has ceased;

(f) the lender has ceased to be an eligible lender; or

(g) the claimant is not present in Great Britain.

(10) Payment of sums deducted from an eligible benefit by the Secretary of State under this paragraph shall be made to the eligible lender.

(11) The Secretary of State shall notify the borrower in writing of the total of sums deducted by him under any application—

(a) on receipt of a written request for such information from the borrower; or

(b) on the termination of deductions.".

(3) In paragraph 8(**a**) (maximum amount of payments to third parties)—

(a) in sub-paragraph (1) for "7A and 7C" substitute "7A, 7C and 7D";

(b) in sub-paragraph (2) for "and 7" substitute ", 7 and 7D". and

(c) in sub-paragraph (2A) for "and 7" substitute ", 7 and 7D".

(4) In paragraph 9(**b**) (priority as between certain debts)

(a) in sub-paragraph (1A)(a) for "or 7C" substitute ", 7C or 7D"; and

(b) in sub-paragraph (1B) after sub-paragraph (h) add—

"(i) any liability mentioned in paragraph 7D (liability in respect of loans).".

Signed by authority of the Secretary of State for Work and Pensions

Under Secretary of State,
Department for Work and Pensions

Date

(**a**) The relevant amending instruments are S.I. 1990/2208, 1991/2284, 1992/1026, 1993/495, 1996/418, 1996/1460, 1997/827, 2002/3019, 2005/777.
(**b**) The relevant amending instruments are S.I. 1993/495 and 3178, 1997/827, 2005/777.

Annex A

EXPLANATORY NOTE

(This note is not part of the Regulation)

These Regulations amend the Social Security (Claims and Payments) Regulations 1987. Regulation 2(2) amends Schedule 9 to enable the Secretary of State to make deductions from benefit on behalf on the beneficiary for the purpose of repaying certain loans made to him.

A full regulatory impact assessment has not been carried in respect of these Regulations as they do not impose a cost on business, charities or the voluntary sector.

Annex B

Details of Regulations

Citation and Commencement

Citation

1 (1) The Regulations will be called the "Social Security (Claims and Payments) (Amendment) (No. XXX) Regulations 2006."

Commencement

(2) The Regulations will come into force on 4th December 2006.

Amendment of the Social Security (Claims and Payments) Regulations 1987

2 (1) Regulation 2 (1) will amend Schedule 9 of the Social Security (Claims and Payments) Regulations 1987 as follows:

(2) Regulation 2 (2) will add Paragraph 7D to Schedule 9 of the Social Security (Claims and Payments) Regulations 1987. Paragraph 7D will allow deductions from benefit to be made on behalf of a customer for the purpose of repaying certain loans made to that customer. It will also set out the conditions under which deductions from benefits may be taken.

(3) Regulation 2 (3) will amend paragraph 8 of Schedule 9 of the Social Security (Claims and Payments) Regulations 1987 to include ACDS, when determining the maximum amount of deductions which can be taken from benefit.

(4) Regulation 2 (4) will amend paragraph 9 of Schedule 9 of the Social Security (Claims and Payments) Regulations 1987 to include ACDS when determining the priority order of types of deduction from benefit.

Annex C

DRAFT

This Memorandum of Understanding is made on …………………………..

Between

The Secretary of State for Work and Pensions [insert address] ["DWP"]

And

[insert name address and company number] ["the Lender"]

Purpose of the Memorandum

1.1 This memorandum sets out the circumstances in which the DWP will deduct from an individual's benefit payments sums due to the Lender, by way of qualifying loan repayments, in accordance with the legislation governing Affordable Credit Deductions Scheme ["the Scheme"].

1.2 This memorandum is intended to constitute ex-statutory administrative guidance to the Parties in relation to the implementation of the Scheme.

1.3 The Parties agree that this memorandum is not legally binding between them and does not create any legal rights or obligations.

The Lender's Obligations

2.1 The Lender warrants that it satisfies the criteria concerning its status and quality of service set out in Schedule 1.

2.2 The Lender acknowledges that if in the future it fails to satisfy such criteria it may be immediately excluded from the Scheme.

2.3 The Lender undertakes that in implementing this memorandum it will not do anything likely to prejudice the reputation of the DWP.

The Lender's Qualifying Loans

3 The Lender warrants that only loans which satisfy the criteria set out in Schedule 2 will be referred to the DWP under the Scheme.

The DWP's obligations

4 The DWP agrees to -

4.1 perform the administrative tasks set out in Schedule 3 subject to the specified operational requirements.

4.2 make payments as specified in Schedule 4.

Change of circumstances

5 The Lender will notify the DWP in writing of any change in their circumstances that may affect their ability to continue to participate in the Scheme.

Review of memorandum

6 The Parties will review the operation of this memorandum annually commencing from the date this memorandum is signed by the parties and at anytime at the request of the DWP.

Amendment and termination

7 The Parties may agree to amend any provision in this memorandum at any time. DWP reserves the right to amend any provision in this memorandum at any time. Lenders must then sign a new memorandum.

7.1 Either Party may notify the other that it is withdrawing from the memorandum by giving 28 days notice to the other in writing.

7.2 In the event of the memorandum being terminated (for any reason) the lender agrees to work with DWP to ensure any outstanding actions are satisfactorily resolved within a reasonable time scale.

Interpretation of the memorandum

8 The DWP may from time to time provide an interpretation of any part of the memorandum and such interpretation shall be binding on the Lender.

Applicability of related legislation

9 The Parties acknowledge that the requirements of the Data Protection Act 1998, the Freedom of Information Act 2000 and the Human Rights Act 1998 will be fully respected in connection with the transfer and retention of any information.

Signed

On behalf of the Department

On behalf of the Lender

Annex C

SCHEDULE 1

Lender Criteria

1 Must be:-

(a) a body registered under section 1 of the Industrial and Provident Societies Act 1965;

(b) a credit union within the meaning of section 1 the Credit Unions Act 1979;

(c) a housing association within the meaning of section 1 of the Housing Associations Act 1985; or

(d) a charitable institution within the meaning of section 58(1) of the Charities Act 1992 and which is determined by the Secretary of State as an appropriate body to which payments on behalf of the borrower may be made in respect of loans made by that body.

2 Must carry out an appropriate risk assessment based on the customer's ability to repay as part of the loan application process.

3 Must provide the borrower with details of a source of free debt advice where appropriate.

4 Must offer face-to-face service where the customer or particular circumstances require it before, or after making a loan.

5 Pre-sales information given to the customer before the loan agreement is made must include the actual cost of the loan including full details and other additional charges that might be incurred.

6 Post-sale practices. Where borrowers are experiencing difficulty in making the agreed repayments steps must be taken to agree alternative arrangements and where appropriate, direct the customer to the services of money advisers.

Annex C

SCHEDULE 2

Loan Criteria

1 The loan must be a personal, unsecured cash loan.

2 The loan must not be cash advanced against a credit card.

3 The loan must not be a business loan.

Annex C

SCHEDULE 3

The Repayment Process

1 DWP will make repayments of monies collected to the lender’s bank account on a four-weekly basis based on a single schedule detailing all transactions since the last statement.

2 In the event of DWP making an over-recovery of a debt (and the over-recovered amount has not yet been received by the lender), an adjustment will be made by DWP before the next payment notification is issued to the lender.

3 In the event of DWP making an over-recovery of a debt and the recovered amount has been received by the lender, DWP will reimburse the borrower and recover that amount from the lender.

Annex C

SCHEDULE 4

The Scheme

Operational requirements

1 DWP will not accept any responsibility for the debt or act as a guarantor. It is simply agreeing to offer a payment facility, where practicable, in certain circumstances such as is done for utilities. Deductions are only possible whilst customer is in receipt of a prescribed benefit. In the event benefit ceases the case will be returned to the lender.

2 The lender will not apply any default penalties whilst the deduction facility is in operation.

3 DWP will return, without explanation, any case that cannot be recovered by deductions from benefit.

4 Deductions will only apply to loans taken out in GB after the scheme comes into operation and when the lender has formally been accepted onto the scheme (i.e. has signed the MoU).

5 Deductions from benefit cannot be made from customers living in Northern Ireland (NI). If a customer living on the mainland and having recovery made by deductions moves to NI, the case will be returned to the lender to continue recovery action even if an eligible benefit continues in payment.

6.1 DWP is limited by law to the amount that can be deducted from a persons benefit. The flat rate amount prescribed in regulations is 5% of the prevailing income support rate for a single person aged 25 or over, rounded up to the nearest 5p. This equates to £2.90 for 2006/2007. More than one such deduction can be made but the total should (with Third Party Deductions (TPDs)) not exceed the 3X5% limit and the 25% of benefit overall limit.

6.2 Private loan deductions will sit outside of the priority order but last after all other deductions – TPDs, social fund, child support and overpayment recovery. A new deduction of higher priority would displace a private loan deduction.

6.3 Deductions can only be made in respect of one loan at a time.

7 If, after referring the case to DWP the lender subsequently receives a payment from the borrower, the lender should recall the case from DWP and renegotiate the repayment plan with the customer.

8 The lender has the right to reinstate a repayment plan with the borrower at any time, but deductions will cease with effect from the date that payments resume.

9 When a borrower applies for a loan, the lender will explain that in the event of default on repayments the loan may be referred to DWP for recovery by deduction from benefit.

10 The lender must ensure that the following statement is included on the loan application form:

> *"I agree that in the event of me defaulting on repayments, information about my loan may be passed on to the Department for Work and Pensions"*

Responsibilities

11 Deductions can only be considered where loan repayments are in arrears (this means more than two missed payments) and reasonable action, short of going to court, to reinstate payment has been unsuccessful. Lenders should have carried out their usual trace procedures before referring the case to DWP.

12 Before referring a case to DWP the lender will have taken steps to contact the borrower to discuss the debt and to broker alternative repayment arrangements and arrive at possible solutions to the problem. This should include as a minimum:

(a) A letter outlining the arrears position will have been issued by the lender.

(b) If no response to the letter is received then a second letter will have been issued by the lender.

(c) If still no response, a third and final letter will have been issued confirming referral to DWP (for consideration of deductions from benefit) 14 days from the date of the third letter, provided there has been no response and/or repayments have not been reinstated.

13 When a lender first refers a case, and deductions from benefit are possible, DWP will issue a notification to the customer explaining that recovery will be made from their benefit. DWP will be responsible for discussing with the customer matters relating to deductions from benefits and payments to the lender. Any subsequent contact with the customer regarding the loan arrangements will be the responsibility of the lender.

14 Interest on the loan balance outstanding will be frozen at the point of referral to DWP. This means that the amount you tell us is outstanding does not increase while deductions are being made and that no other payments in respect of the same loan will be sought.

15 In the event of a borrower lodging an appeal against the amount of the loan outstanding, the borrower will be advised to contact the lender. In the meantime recovery by deduction will continue.

Annex C

The borrower can only appeal against the decision to make deductions from benefit, not against the amount of the loan. Any issues underlying an appeal which relate to liability for the loan will be referred to the lender.

Deductions will continue, but not be paid to the lender, until the outcome of the appeal is known.

16 From the outset, lenders must provide borrowers with information about the scheme and how deductions from benefit may be implemented in the case of a default on repayments.

Cases eligible for referral to the DWP

17 Deductions from benefit can only be made if the customer is in receipt of one or more of the following benefits:

(a) Income Support

(b) Jobseekers Allowance

(c) Carers Allowance

(d) State Pension

(e) Pension Credit

(f) Incapacity Benefit

18 To make a referral to DWP the lender must send a DWP referral form signed by a suitably authorised person for the lender [insert CRU address (Central PO BOX address once agreed)].

APPENDIX 3

STATUTORY INSTRUMENTS

2006 No. []

SOCIAL SECURITY

The Social Security (Claims and Payments) Amendment (No. 2) Regulations 2006

Made - - - -	*xxx*
Laid before Parliament	*xxx*
Coming into force - -	*27th December 2006*

The Secretary of State for Work and Pensions makes the following Regulations in exercise of the powers conferred by sections 5(1)(p), 189(1), (4) and (6) and 191 of the Social Security Administration Act 1992(**a**) after consultation with the Social Security Advisory Committee(**b**).

Citation and commencement

1. These Regulations may be cited as the Social Security (Claims and Payments) Amendment (No. 2) Regulations 2006 and shall come into force on 27th December 2006.

Amendment of the Social Security (Claims and Payments) Regulations 1987

2.—(1) The Social Security (Claims and Payments) Regulations 1987(**c**) are amended as follows.

(2) In regulation 2(1) (interpretation), before the definition of "the 2000 Act" insert—

""the 1992 Act" means the Social Security Administration Act 1992;".

(3) In Schedule 9 (deductions from benefit and direct payment to third parties)—

(a) after paragraph 7B(**d**) (arrears of child support maintenance) insert—

"Eligible loans

7C.—(1) In this paragraph—

"borrower" means a person who has, either solely or jointly, entered into a loan agreement with an eligible lender in respect of an eligible loan and who is, for the time being, entitled to an eligible benefit;

"eligible lender" means—

(a) a body registered under section 1 of the Industrial and Provident Societies Act 1965(**e**) (societies which may be registered);

(**a**) 1992 c. 5. Section 191 is cited for the meaning given to the word "prescribe".
(**b**) *See* section 170 of the Social Security Administration Act 1992.
(**c**) S.I. 1987/1968.
(**d**) Paragraph 7B was inserted by S.I. 1996/2344.
(**e**) 1965 c. 12.

(b) a credit union within the meaning of section 1 of the Credit Unions Act 1979(**a**) (registration under the Industrial and Provident Societies Act 1965);

(c) a charitable institution within the meaning of section 58(1) of the Charities Act 1992(**b**) (interpretation of Part II);

(d) a body entered on the Scottish Charity Register under section 3 of the Charities and Trustee Investment (Scotland) Act 2005(**c**) (Scottish Charities Register),

which, except for a credit union, is licensed under the Consumer Credit Act 1974(**d**) and which may be determined by the Secretary of State as an appropriate body to which payments on behalf of the borrower may be made in respect of loans made by that body;

"eligible loan" means a loan made by a lender, who is at that time an eligible lender, to a borrower except a loan—

(a) which is secured by a charge or pledge;

(b) which is for the purpose of business or self-employment; or

(c) which was made by means of a credit card;

"loan agreement" means an agreement between the eligible lender and the borrower in respect of an eligible loan.

(2) In this paragraph "eligible benefit" means—

(a) carer's allowance;

(b) the following contributory benefits—

(i) incapacity benefit;

(ii) retirement pension; or

(c) the following benefits—

(i) income support;

(ii) jobseeker's allowance;

(iii) state pension credit.

(3) Where the conditions set out in sub-paragraph (4) are met the Secretary of State may deduct a sum from an eligible benefit to which the borrower is entitled equal to 5 per cent. of the personal allowance for a single borrower aged not less than 25 and pay that sum to the eligible lender towards discharge of the sum owing under the loan agreement at the date of the application.

(4) The conditions referred to in sub-paragraph (3) are—

(a) the borrower has failed to make payments as agreed with the eligible lender for a period of 13 weeks before the date of the application and has not resumed making payments;

(b) the borrower has given his written permission to the eligible lender to provide to the Secretary of State personal data within the meaning of section 1 of the Data Protection Act 1998(**e**) (basic interpretive provisions);

(c) the eligible lender has agreed that no interest or other charge will be added to the amount owed at the date of the application;

(d) no sum is being deducted under this paragraph;

(e) no sum is being deducted from the borrower's eligible benefit under section 71(8) of the 1992 Act (overpayments-general) at the date of the application; and

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(**a**) 1979 c. 34.
(**b**) 1992 c. 41.
(**c**) 2005 asp 10.
(**d**) 1974 c. 39.
(**e**) 1998 c. 29.

(f) no sum is being deducted from the borrower's eligible benefit under section 78 of the 1992 Act (recovery of social fund awards) at the date of the application.

(5) The Secretary of State shall notify the borrower and the eligible lender in writing of a decision to make a deduction under this paragraph.

(6) The Secretary of State may make deductions under this paragraph only if the borrower is entitled to an eligible benefit throughout any benefit week.

(7) The Secretary of State shall not make deductions from a benefit mentioned in sub-paragraph (2)(a) where the borrower is in receipt of another eligible benefit unless that benefit is one mentioned in sub-paragraph (2)(b) and is insufficient to enable the deduction to be made or is a benefit mentioned in sub-paragraph (2)(c) and the amount is insufficient to meet the deduction plus 10 pence.

(8) The Secretary of State shall not make deductions from a benefit mentioned in sub-paragraph (2)(b) where the borrower is in receipt of a benefit mentioned in sub-paragraph (2)(c) unless the amount of that benefit is insufficient to meet the deduction plus 10 pence.

(9) The Secretary of State shall cease making deductions from an eligible benefit if—

(a) there is no longer sufficient entitlement to an eligible benefit to enable him to make the deduction;

(b) entitlement to all eligible benefits has ceased;

(c) a sum is deducted from the borrower's eligible benefit under section 71(8) of the 1992 Act;

(d) an eligible lender notifies the Secretary of State that he no longer wishes to accept payments by deductions;

(e) the borrower's liability to make payment in respect of the eligible loan has ceased;

(f) the lender has ceased to be an eligible lender; or

(g) the borrower no longer resides in Great Britain.

(10) The sums deducted from an eligible benefit by the Secretary of State under this paragraph shall be paid to the eligible lender.

(11) The Secretary of State shall notify the borrower in writing of the total of sums deducted by him under any application—

(a) on receipt of a written request for such information from the borrower; or

(b) on the termination of deductions.

(12) Where a deduction is made under this paragraph from a specified benefit, paragraph 8(**a**) (maximum amount of payment to third parties) is to have effect as if—

(a) in sub-paragraph (1) for "and 7A" there were substituted ", 7A and 7C"; and

(b) in sub-paragraph (2) for "and 7" there were substituted ", 7 and 7C"."; and

(b) in paragraph 9(**b**) (priority as between certain debts)—

(i) in sub-paragraph (1A)(a) after "7A" add "or 7C"; and

(ii) in sub-paragraph (1B) after sub-paragraph (g) add—

"(h) any liability mentioned in paragraph 7C (liability in respect of loans).".

Signed by authority of the Secretary of State for Work and Pensions

Under Secretary of State,
Date Department for Work and Pensions

(**a**) The relevant amending instruments are S.I. 1990/2208, 1991/2284, 1992/1026, 1993/495, 1996/481, 1997/827, 2005/777 and 2006/2377.

(**b**) The relevant amending instruments are S.I. 1993/495, 1997/827 and 2005/777.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Social Security (Claims and Payments) Regulations 1987.

Regulation 2(2) inserts a new definition into regulation 2. Paragraph (3) amends Schedule 9 to enable the Secretary of State to make deductions from benefit and make payments, on behalf of the beneficiary, for the purpose of repaying certain loans.

The Report of the Social Security Advisory Committee dated 17th October 2006 on the proposals referred to them in respect of these Regulations together with a statement showing the extent to which these Regulations give effect to the Recommendations of the Committee, and in so far as they do not give effect to them, the reasons why not, are contained in Command Paper Cm. 6974 published by the Stationery Office Ltd.

A full regulatory impact assessment has not been carried out in respect of these Regulations as they do not impose a cost on business, charities or the voluntary sector.

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