Changes to debt relief order criteria

Lead department	Department for Business and Industrial Strategy - Insolvency Service
Summary of proposal	Make changes to the monetary eligibility criteria for debt relief orders (DRO), to ensure that the most financially-distressed consumers with debt problems can access a proportionate solution to obtain debt relief.
Submission type	Impact assessment (IA) – 15 April 2021
Legislation type	Secondary legislation
Implementation date	7 June 2021
Policy stage	Final
RPC reference	RPC-BEIS-IA-5063(1)
Opinion type	Formal
Date of issue	21 May 2021

RPC opinion

Rating[1]	**RPC opinion**
Fit for purpose	The RPC views the IA to be fit for purpose. The EANDCB can be verified and the SaMBA is proportionate. The rationale for intervention could be strengthened to clarify the desired impact of the proposed changes. The cost-benefit analysis (CBA) is well-evidenced and supported by prior consultation

Business impact target assessment

	Department assessment	**RPC validated**
Classification	Qualifying regulatory provision	Qualifying regulatory provision
Equivalent annual net direct cost to business (EANDCB)	£9.2 million	£9.2 million *(2019 prices, 2020 pv)*
Business impact target (BIT) score	£45.9 million	£46.0 million
Business net present value	£-79.0 million	
Overall net present value	£-12.3 million	

[1] The RPC opinion rating is based only on the robustness of the EANDCB and quality of the SaMBA, as set out in the Better Regulation Framework. RPC ratings are fit for purpose or not fit for purpose.

RPC summary

Category	Quality	RPC comments
EANDCB	Green	The RPC is able to verify the EANDCB figure for BIT-accounting purposes and considers the estimate to be fit for purpose.
Small and micro business assessment (SaMBA)	Green	The RPC considers the SaMBA to be proportionate and fit for purpose. The IA discusses the prevalence of small and micro businesses (SMBs) in the likely affected sectors, stating that SMBs are not expected to incur disproportionate substantive costs.
Rationale and options	**Good**	The IA argues that intervention is necessary to provide appropriate levels of debt relief for those who need it. Moreover, it states that the current system has a gap which needs addressing. The IA would be improved by making a clearer argument for changing the criteria, and the additionality they will provide in light of other debt relief initiatives being introduced.
Cost-benefit analysis	**Good**	The calculations and analysis are supported by good evidence. The IA correctly treats benefits to debtors of retained payments as transfers within the net present value calculations. It could be improved by considering the possibility that some individuals, newly-eligible for DROs, might not make use of them. It could also explore whether it is possible to monetise the wider benefits to society.
Wider impacts	**Satisfactory**	The CBA considers impacts on the public sector. The IA has included a well-considered equalities impact assessment. It would benefit from exploring other wider impacts, including innovation or competition, as well as the impact on credit markets.
Monitoring and evaluation plan	**Satisfactory**	The IA commits to undertaking a post-implementation review (PIR) for the policy. It describes an initial theory of change and discusses the data collection that will be necessary for good monitoring and evaluation.

Summary of proposal

For individuals with low levels of debt and limited ability to repay, DROs offer a proportionate debt solution, when bankruptcy or other statutory debt solutions may not be appropriate. In addition to being proportionate for debtors, a DRO may also produce better outcomes for creditors. If individuals with low levels of debt choose an alternative statutory debt solution, such as bankruptcy, their creditors might not recover anything.

The Insolvency Service (IS) is exploring how to increase the number of people able to access DROs. The IA proposes two options for consideration. The first is, non-regulatory focussing on improving the awareness of DROs among the public, aimed at increasing the uptake amongst individuals who currently meet the eligibility criteria. A second (preferred), regulatory option, of expanding the current criteria thresholds to making more people eligible for DROs, has also been considered.

The current criteria for entering a DRO arrangement focus on three key aspects:

- Level of debt – must be under £20,000.
- Assets held – cannot exceed £1,000 (with an additional exemption for cars up to a value of £1,000).
- Ability to repay – surplus income of no more than £50 a month.

These eligibility criteria were set in 2015 (a relaxation of the criteria established in 2009 when DROs were introduced) and have remained unchanged since. The regulatory option would raise the maximum limits on these criteria to a debt to £30,000, allow assets valued up to £2,000 and surplus income not to exceed £100 per month.

For the proposed regulatory option, the IA identifies the familiarisation costs associated with the changing thresholds, the cost to creditors and insolvency practitioners from the loss of fees and debt owed, and the cost to intermediaries, who process DROs, due to increased cases. Meanwhile debtors are expected to benefit from cost savings and the retainment of payments as a result of accessing DROs for the first time.

EANDCB

The direct costs to business have been identified as familiarisation costs, the costs to intermediaries as a result of increased demand for DROs, the cost to creditors from loss of potential reclaimed debt, and the cost to insolvency practitioners from a loss of fees from other forms of debt relief. The IA has estimated the percentage of creditors which are likely to be government institutions and correctly excluded their costs from the EANDCB.

SaMBA

The IA discusses the likelihood of SMBs affected by the proposals, identifying the main business groups (competent authorities, insolvency practitioners and creditors) affected by the changes.

The IA provides evidence to show that the majority of DRO cases are handled by large competent authorities. Therefore, the impact of new DRO cases is expected to fall, primarily, on large businesses. Although almost half of insolvency practitioners are estimated to be SMBs, the IA asserts that the impact on these firms is not disproportionate, taking into consideration how low their costs are likely to be. With respect to creditors, the IA claims that in value terms most creditors are large financial institutions and government bodies, so the impact on SMBs will be minimal.

Rationale and options

Rationale

The IA establishes the number of people who are currently eligible and utilising DROs. It argues that the main justification for intervention is one of equity: looking to provide a proportionate debt solution for individuals with low levels of debt and little ability to pay it. In response to a previous consultation, stakeholder groups, including creditors and insolvency professionals, supported expanding the criteria.

The IA argues that a ‘gap in the market’ exists, where debtors have too-few assets or too-little surplus income, and so are either unable to settle their debts or obtain a DRO. In such situations, creditors’ costs of recovery are often disproportionate to the value of what they can recover. The IA would benefit from discussing and highlighting this rationale in more detail, particularly as it could be used to substantiate clearly, the need to raise the criteria thresholds to the levels proposed.

However, the IA discusses the introduction of the ‘Breathing Space’ policy this year and suggests that this may increase demand for DROs due to increased likelihood of debtors receiving professional debt advice. It is therefore not clear how much impact the proposals would have on increasing the demand for DROs as a form of debt relief, on top of that which is expected as a result of *Breathing Space*. The IA would benefit from establishing clearly whether the potential increase from *Breathing Space*, and other options being considered, will impact on the need for the proposed changes achieving the stated policy objectives.

Options

The IA considers both non-regulatory and regulatory options, both of which would seem to address the policy objective of increasing the number of individuals choosing DROs instead of other debt solutions. The RPC welcomes the use of consultation to help shape the regulatory option that has been considered.

For the regulatory option, the IA does not discuss how increased awareness might change the demand for, and impact of, DROs. The IA would be improved from considering whether the actions covered by option 1 (non-regulatory) will also be carried out as part of option 2 (regulatory).

Furthermore, the IA discusses the potential for encouraging increased usage of forbearance without explicitly evaluating this as an additional non-regulatory option. It suggests that this is not a long-term solution. The IA would, however, benefit from exploring this possibility in more detail.

Cost-benefit analysis

Evidence and data

The CBA is well-supported by evidence. The IS informed the initial policy development of the regulatory option using consultation and supporting data. The figures used for calculations are well-evidenced, drawing on current data collected by the IS.

Modelling

The CBA includes the costs, to both creditors and insolvency practitioners, of lost reclaimed debt, and the benefits to debtors of retained repayments. The RPC is pleased to see that the IA considers the benefits to debtors. It treats correctly the benefit to debtors of retained payment and debt relief, as a transfer with offsetting costs experienced by business in NPV calculations.

The IA could be improved through consideration of the costs to the debt advice sector arising from the preferred option. Many of the organisations in this sector are civil society organisations, where advice may be distributed centrally to volunteers and, therefore, may incur costs as a result of these proposals.

Uncertainty, risks and assumptions

The IA estimates the number of debtors who would become newly eligible for DROs under the proposed changes to the criteria. However, as highlighted by current debtor behaviour, not all individuals eligible for DROs are likely to make use of them. Therefore, the IA would benefit from considering the impact of the assumption that those newly eligible for DROs would display similar rates of usage to those currently qualifying. This analysis could use additional sensitivity analysis to assess the reduction in costs from changes to the take-up rate of DROs among newly eligible debtors, or an analysis of the probability of application as a function of the applicants' income, indebtedness and assets.

When estimating the time cost for business, the IA assumes that the wage rate for all administrative occupations is representative of individuals working in the debt sector. However, the IA would be improved by considering whether a more-specific wage rate could be used for these calculations.

Wider impacts

The IA has assessed potential impacts on the IS and other public sector organisations and, where possible, monetises them as part of the main CBA. The RPC commends the very well-considered and detailed equalities impact assessment, which includes looking at the prevalence of individuals with protected characteristics who require debt relief. This assessment illustrates that the proposed changes do not give rise to any new equity issues.

However, the IA does not comment on potential competition or innovation impacts. The IA could be improved by stating on whether or not such impacts have been considered. If the IS believes there to be no impacts, this should be stated clearly.

Monitoring and evaluation plan

The IA commits to undertaking a PIR, which will be carried out to establish how successful the policy has been. The RPC is pleased to see the inclusion of a theory of change which establishes the expected outputs and outcomes of the policy, and from which the IS will develop the monitoring and evaluation (M&E) plan. In addition, the IA discusses potentially undertaking further sensitivity analysis as part of this M&E plan, to understand the rate of flow of debtors into the expanded DRO scheme. It also discusses the data collection that will be necessary for the M&E plan, and how it will be sourced. The IA would benefit from considering whether debtor experiences can be used to identify improvements in their own situation, as a result of these proposals.

Other comments

Discussion of Covid's impacts on debt repayment

The RPC acknowledges the difficulty in accounting for the impacts of Covid on the economy. However, the IA would benefit from discussing the expected impacts on the rate of individuals falling into debt and the impacts on debtors' ability to repay debt.

Regulatory Policy Committee

For further information, please contact regulatoryenquiries@rpc.gov.uk. Follow us on Twitter @RPC_Gov_UK, LinkedIn or consult our website www.gov.uk/rpc.