

Life after debt

When debt becomes a problem, we show you how to control it before it starts to control you

Recent reports show that Britain is the debt capital of Europe. Total UK personal debt was £1.25 trillion in December 2006, up almost 10 per cent on 2005. That's equivalent to almost £20,000 for every man, woman and child in the country.

In 2006, more than 120,000 people were declared bankrupt or entered an individual voluntary arrangement (IVA) in the UK, an increase of more than 50 per cent



How bankruptcies and IVAs in the UK have grown between 1995 and 2006

on the year before. And with interest rates climbing and pressure on households from increases in utility bills and council tax, the number of people who are unable to cope financially is likely to increase.

It could also be argued that banks' lenient lending policies have fuelled consumer borrowing in recent years and have therefore fed into the increase in personal insolvencies. This has been further encouraged by a more relaxed public attitude towards debt and the continued aggressive market-

ing by debt-management companies and IVA providers on daytime TV and in the press (for more, see 'Individual voluntary arrangements', below).

With the debt mountain growing, we explain debt-management plans, IVAs and bankruptcy and examine under what circumstances they could apply to you. We also help you spot the signs that your debt is getting out of control and offer advice on how to keep your debt in check (see 'Checklist', opposite).

DEBT-MANAGEMENT PLANS

An informal agreement may be a good starting point

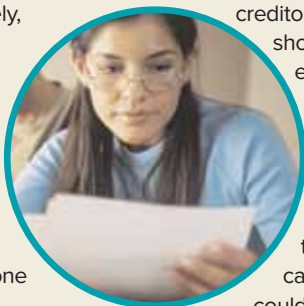
If you are in debt, you could first approach your creditors yourself and try to agree a repayment schedule. Alternatively, a debt-management plan, run by a reputable organisation such as the Consumer Credit Counselling Service (CCCS) or Citizens Advice (CA), allows you to make one payment, which is distributed to your creditors. Both of these options are agreed between the individual and the creditor, limiting possible damage to your credit rating. But neither option is legally binding. Nor does it always reduce the debt – the amount is just rescheduled.

However, if you go to CA, the CCCS or National Debtline, you can

get free advice and they will try to help you avoid further debt.

If you decide to approach your creditors independently, you should contact them and explain the situation. Your next action should be to try to pay arrears on priority debts, such as rent and utilities.

Once you've done this, you should calculate how much you could offer your unsecured creditors. Put this in writing to them and ask for charges to be frozen. If this is refused, make the payment you suggested and write again explaining that you cannot offer any more. Under the Banking Code, banks must treat people with financial difficulties sympathetically. If they don't, you should contact the Financial Ombudsman Service.



INDIVIDUAL VOLUNTARY ARRANGEMENTS

IVAs are a way out but they have their problems

An individual voluntary arrangement (IVA) is a formal arrangement through the county court and can be a way of avoiding the more onerous downsides of bankruptcy. The Scottish equivalent, a protected trust deed, works in a similar way.

IVAs are aimed at those owing more than £15,000 and with a regular income. Under an IVA, the debtor engages an insolvency practitioner (IP), who draws up a repayment schedule. Details of IPs are available from the Insolvency Service. The debtor makes a monthly payment

to the IP, who divides this among creditors. Unlike with bankruptcy, debtors will usually not lose their possessions. An IVA lasts between three and five years, after which outstanding balances on debts are written off. For an IVA to be agreed, debtors need the agreement of 75 per cent of their creditors by value, giving banks significant influence.

IVAs do have downsides.

Repayment terms are longer than under bankruptcy, IPs' fees can be expensive and IVAs stay on your credit file for six years.



NO HELP FROM THE BANK

Jane Smith 29

Jane Smith (not her real name) had credit card debts of around £25,000, from a previous abusive relationship, and was struggling to repay them. 'I was paying back my student loan and around £600 a month off my card,' she said. 'I was finding this difficult so I approached my bank for a consolidation loan.'

It was willing to lend her £25,000 at 7.4 per cent, but told her she would have to take out payment protection (see 'Protection or rejection', *Which?*, May 2007, p30), adding £7,660 to the loan. With interest, the total repayable was around £43,000.

When Jane's rent went up, she found it harder to cope. She went to her



bank to ask whether it would increase her overdraft by £250, as she was attracting charges. It refused but suggested that Jane use her now-cleared credit card to pay for living costs – a clear example of irresponsible lending. Her debts led to stress and illness, so she decided on insolvency.

Declared bankrupt last year, she is now paying her creditors an affordable £180 a month. But the damage to her credit rating will last a good deal longer.

Checklist

Signs that debt is out of control

- Taking out loans to pay off credit cards and then spending on the credit card again.
- Using cards to pay off your loans.
- Taking out new credit cards because you have reached the credit limit on another card.
- Never getting out of an overdraft.
- Making the minimum payments on your credit card balance and continuing to use the card.
- Regularly withdrawing cash on your credit card.
- Regularly dipping into savings or using your credit card to pay day-to-day costs, without paying it back.
- Borrowing from family and friends with no way to pay it back.
- Missing payments for bills.
- Applying for credit with less reputable lenders after being turned down by high-street banks.
- Making use of cheque-cashing agencies offering an advance on next month's paycheck.

Controlling your debt

- Always pay secured and priority creditors in full. Secured debts include loans and credit agreements under which the creditor has a hold over an asset.
- Try not to obtain further credit while experiencing difficulties.
- Maximise your income and claim all the benefits and grants to which you are entitled.
- Try to make lifestyle changes to cut spending.
- Check that your employer is using the correct tax code and that you have taken advantage of all available tax allowances, including the child and working tax credits.
- Consider remortgaging your home.
- Minimise other costs (use www.switchwithwhich.co.uk to switch utility suppliers, for example).
- Get independent advice early from Citizens Advice, National Debtline or the CCCS.

BANKRUPTCY

If debt is overwhelming you, bankruptcy is the last resort

Bankruptcy is a court order that you can apply for if you are unable to pay your debts. Alternatively, any creditor to whom you owe more than £750 can apply to have you declared bankrupt.

Under a bankruptcy order, the Official Receiver takes control of your money and property, and deals with your creditors on your behalf. Once discharged from bankruptcy, the debtor no longer has to pay any outstanding debts detailed in the proceedings.

Bankruptcy has become more socially acceptable since changes in the law, which took effect in April 2004, made it easier to go bankrupt. To encourage entrepreneurs to try again after a company failure, the

period bankruptcy lasts was reduced from three years to one. However, the Scottish equivalent of bankruptcy, sequestration, still lasts for three years. Bankruptcy remains on your credit reference file for six years and may prevent you from getting credit during that time. But in some cases, it can be the best option, especially

if you owe a lot, have few assets and no way of repaying the debts.

However, the Official Receiver can sell most of your assets, and you may have to make monthly payments from your income for three years from the date of the agreement. Furthermore, some debts are not written off, including court fines and student loans.



Bankruptcy has become more socially acceptable since changes in the law in 2004

Contacts

Business Debtline

0800 197 6026

www.bdl.org.uk**Child Support Agency**

0845 713 3133

Citizens Advice England and Waleswww.citizensadvice.org.uk**Citizens Advice Scotland**www.cas.org.uk**Citizens Advice Northern Ireland**www.citizensadvice.co.uk**Consumer Credit Counselling Service**

0800 138 1111

www.cccs.co.uk**Financial Ombudsman Service**

0845 080 1800

www.financial-ombudsman.org.uk**The Insolvency Service**

0845 602 9848

www.insolvency.gov.uk**Jobcentre Plus**www.jobcentreplus.gov.uk**National Debtline**

0808 808 4000

www.nationaldebtline.co.uk**The Pensions Agency**

0845 606 0265

www.pensions.gov.uk**Samaritans National Helpline**

0845 790 9090