Eurodiaconia
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POLICY PAPER

HOUSEHOLD OVER-INDEBTEDNESS IN THE EUROPEAN UNION

Update - October 2015

The context

Household over-indebtedness is not a new phenomenon. European household debt has been on the rise since the 1980's. In 2007, even before the start of the financial and economic crisis, household debt in the European Union had increased on average by almost 19% since 2001[1].

Following the crisis and the subsequent rise in unemployment and public cuts to social expenditure, over-indebtedness is fated to keep rising. Eurodiaconia's monitoring of the impact of the crisis on its members as services providers confirms this analysis as it shows an unambiguous rise in the demand for services that mitigates the impact of the crisis such as food bank services and emergency financial support. However, the largest demand has been for debt-related services. A majority of our members expect this increase to continue and therefore the accompanying need for debt-related services.

Eurodiaconia's role

Eurodiaconia's members, motivated by their Christian values base, have a role to play against the current process of "financialization" of society where all exchanges (e.g. goods, services, information) are more and more reduced into financial instruments.

On the one hand, Eurodiaconia members demonstrate that human value is independent from financial success or ability of a person. On the other hand, studies have shown that credit is now becoming a common way of fulfilling needs which were previously met by state solidarity or family solidarity. In this context, Eurodiaconia members can also offer another way and provide services to the most "risky" or "unprofitable" clients, such as alternative banking or financial services, training and education skills, etc.

Additionally, Eurodiaconia monitors social policies at EU level and observes that in view of the increasing financial exclusion and unprecedented growth in personal debts, much more safeguards should be established for a better financial inclusion and the protection of individuals and families against over-indebtedness. Eurodiaconia and its members, together, can work for governments and EU officials to be reminded of the social consequences and economic benefit at stake through financial inclusion.

[1] Explaining over indebtedness in the European Union, Julia Gumy, The Research Group, July 2007

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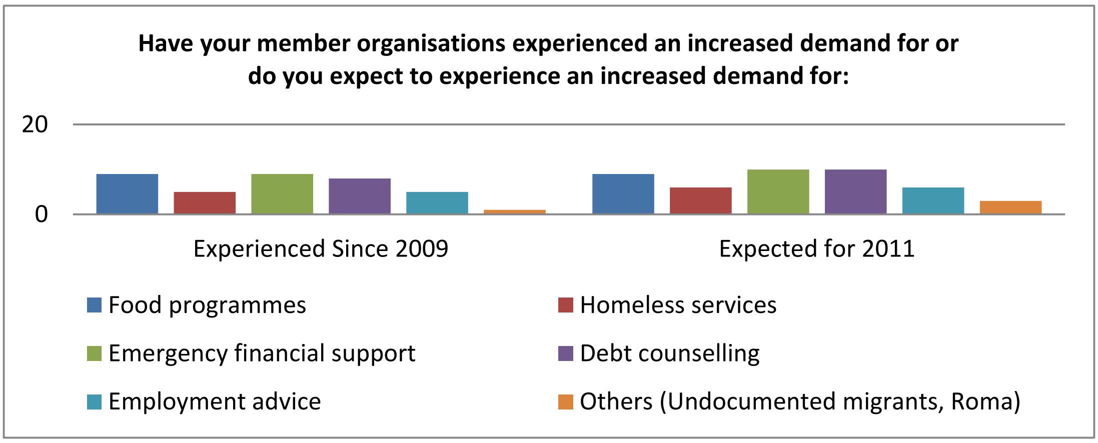
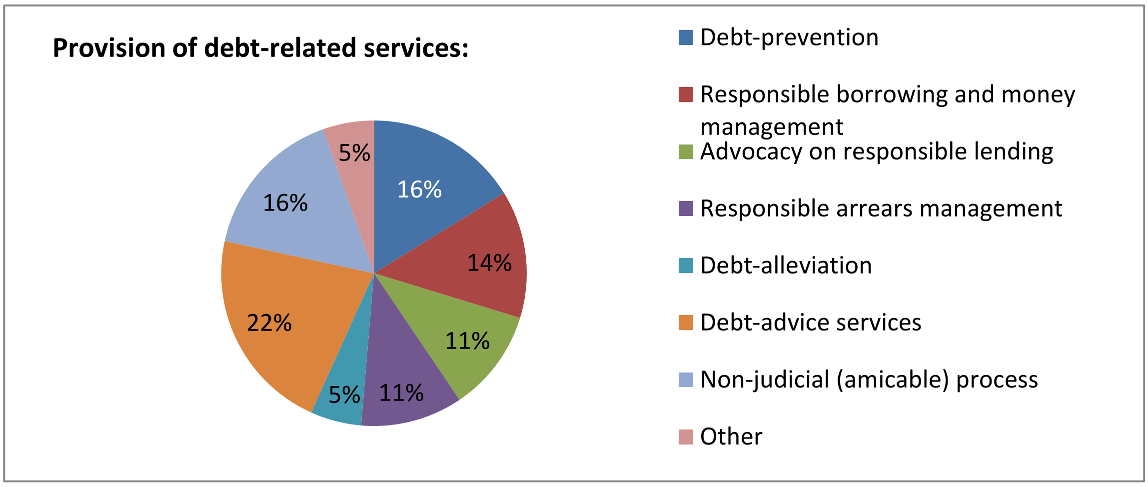
Members' experience – Increasing demand for debt-related services

Eurodiaconia has been monitoring the impact of the crisis on its members for three consecutive years[2]. The results reveal a constant increase in the demand for debt-counselling services and demonstrated that Eurodiaconia members continue to expect the demand for these types of services to keep increasing in the future.



Eurodiaconia members provide services to people in need across Europe. Among those services, they provide debt-related services. Reaching several thousands of people each year, they mainly provide debt-advice, debt-prevention and debt-alleviation (i.e. welfare support for households with debt problems) services but their assistance also goes through services of responsible money borrowing, arrears management and advocacy on responsible lending[3]. The "other" services provided by members (5%) include emergency financial assistance and assistance with taxes.



[2] Eurodiaconia 3rd report on the impact of the financial and economical crisis, Focus on over-indebtedness, 2011
[3] Eurodiaconia 3rd report on the impact of the financial and economical crisis, Focus on over-indebtedness, 2011

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Members' analysis: the causes of over indebtedness are both structural and individual

Most members identified the causes of household over-indebtedness as both structural and linked to individual behaviors.

Generally members believe that living under the strain of the financial crisis has become too difficult for families and single-parent households and that the challenges of everyday life in EU Member States have become too high, especially for families with children. They claim that over-indebtedness often appears to be a consequence of low level of income and inflexible working conditions. More generally, they denounce too much public focus on growth, low levels and complexity of social security systems, which had made itself inaccessible to the people most in need. Additionally, a lack of education and financial literacy was stressed as a main cause of over-indebtedness, leading to irresponsible spending and an inability to plan and manage households. Finally, they deplore the lack of government regulation toward what they see as a constant facilitation and encouragement of easy lending.

Overall, Eurodiaconia's members' experience matches research which distinguishes three categories of causes for over-indebtedness: change in life, gradual over-commitment, reaching a reasonable standard of living. Structural and individual causes of over-indebtedness appear to be mutually reinforcing. For instance, gradual over commitment is an individual behavior influenced and encouraged structurally. The consequences of changes of life (illness, etc.) are supposed to be softened by social security; if this does not happen timely or appropriately, this might leave people falling into further financial and/or social exclusion.

How can the EU and Member States cooperate to bring change?

Financial inclusion and over indebtedness are mostly related to national competence. However, the European Union can be involved in different ways, for instance by encouraging research in a specific area or by putting political pressure on a member state to match some minimum EU standards. The Open Method of Coordination acts as a a stimulus for Member States to learn from each other as they use it to set up common targets and follow-up on the implementation of such targets.

It can go further by making legislative proposals, for instance when working for consumer protection. The Consumer Credit Directive[4] (last amended in 2011[5]) established some principles such as the duty to explain, duty to check if debtors can pay the credit and a compulsory delay allowing the revocation of the agreement.

The Mortgage Credit Directive[6] on credit agreements for consumers relating to residential immovable property was adopted on 4 February 2014. Member States will have to transpose its provisions into their national law by March 2016. The directive aims to create an internal market in mortgage credit with a high level of consumer protection and to promote financial stability by ensuring that mortgage credit markets operate in a responsible manner. It includes for instance provisions on consumer information requirements, a consumer creditworthiness assessment obligation, provisions on early repayment, provisions on foreign currency loans, etc.

The Bank Account Directive[7] on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features was adopted on 23 July 2014. Member states will have to transpose its provisions into their national law by September 2016. The directive aims to enable access to bank accounts for all EU consumers, irrespective of their country of residence and their financial

[4] Directive 2008/48/EC of 23rd April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC
[5] Directive 2011/90/EU of 14th November 2011, amending Part II of Annex I to the Directive on Credit Agreements for Consumers,
[6] Directive 2014/17/EU of 4th February 2014 on credit agreements for consumers relating to residential immovable property
[7] Directive 2014/92/EU of 23rd July 2914 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features

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situation, and easy accessing of information about bank account fees. Furthermore, it established a quick and simple procedure for switching bank accounts within one member state and within the European Union.

There is therefore room for action at EU level to mainstream the protection of vulnerable people against over-indebtedness, through consumer protection (education, information) but also through collection of information, monitoring and regulating of potential dangerous practices in the internal market such as irresponsible lending, advertisement, debt collection, etc.

Recommendations

Eurodiaconia members active in the provision of debt related services are facing an increasing and changing demand for services. They underline what they see as possibilities to tackle over-indebtedness in Europe.

1. Spotlight on Education

Eurodiaconia members testify of the importance for Member States to ensure accessible education to all people on financial matters, such as financial management, interest rates and the consequences of debts.

- ➔ Eurodiaconia therefore recommends the European Union to develop guidelines to encourage member states to integrate such skills in school curricula. These guidelines should particularly take into account the involvement of local authorities and the targeting of young people.

2. More restrictive regulation of lending

Eurodiaconia Members condemn the lack of strict regulation toward some abusive aggressive lending procedures and usurious interest rates, such as SMS loans still operation in e.g. Estonia, the UK, Sweden and Finland. "*Over indebtedness can also be seen in connection with loan policy of banks. There have been several bank crashes because the borrowers were not financially stables and their credit worthiness was not sustainable"* reports, for example, one of Eurodiaconia Danish members.

- ➔ Eurodiaconia therefore strongly recommends tighter regulation of lending such as a requirement to check borrower's credit worthiness (even for small loans), making the total net cost of the loan clear and visible, transparent explanation of the consequences of talking the loan to consumers, the establishment of ethical standards defined by banks and credit agencies in cooperation with NGOs and consumer organisations. Regulations have to apply as much to banks as to credit agencies.

- ➔ The European Union should reinforce sanctions and mechanisms restricting misleading advertisements as it appears that predatory lending and aggressive advertisement persists in some Member States such as Sweden and the Netherlands.

- ➔ The European Union must look at the question of the selling of debt and work to prevent usurious interest rate and abusive administration and notification fees.

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3. Address debt restructuring: support social debt restructuring and regulate existing practices

Eurodiaconia members report the devastating consequences of unregulated or badly regulated debt restructuring, when it pushes vulnerable people further into debt and exclusion. Eurodiaconia members have identified debt restructuring as key practice to be monitored and changed.

➔ The European Commission should develop its understanding of debt restructuring and its social consequences and encourage Member States to develop their regulation of this practice. There should be a requirement for the creditor to come forward to identify himself early in the process. The fines should be clearly limited to a maximum reasonable ceiling.

➔ The European Commission should support NGOs wanting to provide "social" debt restructuring by providing interest free grants or encouraging public authorities or banks to provide such interest free loans to NGOs practicing social debt restructuring.

4. A European minimum standard for debt settlement

Eurodiaconia members have observed that service users are very often unable to access the existing processes for debt settlement as they are based on stringent criterions (e.g. being in employment or having a certain income). The result is that debt settlement is unavailable for people who need it most.

➔ Eurodiaconia calls on the European Commission to study the different national legislations and practice of debt settlement and their accessibility for the most vulnerable. Then the European Commission should propose a minimum standard procedure of debt settlement available in all EU Member States for the most vulnerable.

5. Monitoring and strictly regulating credit cards ("revolving credit")

Legislation, definitions and habits on credit cards vary greatly between countries. The common trend is that Eurodiaconia members have reported on the danger of ("revolving") credit cards as they see vulnerable people falling easily into over-indebtedness through this facility. "Credit cards" allow the consumers a continuing balance of debt, subject to interest being charged. If the full credit card balance is not paid at the end of the month, the bank will charge interest on the amount still owed. Carrying a balance from month to month is called revolving the debt. This can be very convenient and is a very common practice in some Member States (as the UK), however it can also be dangerous due to high accumulating interest rates.

The 2011 over-indebtedness analysis by the Banque de France (*Baromètre du surendettement 2011)* confirms the danger of this service as it reports that revolving credit are linked to 76,9% of the cases it has been dealing with between October 2006 and September 2011. In average, there are about 4 revolving credit per file, amounting to 16.100 euros (the average total amount of the debt per case dealt with is 36.000 euros)[8].

➔ The European Union should monitor the social impact of revolving credit and credit cards and encourage Member States to regulate these services more strictly by looking at the issues of limits for credit on cards, multiple cards and financial education through legislation or code of conducts.

[8] Baromètre du surendettement, Banque de France, http://www.banque-france.fr/fr/instit/protection_consommateur/secretariat_des_commissions_de_surendettement_barometre.htm

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6. Independent advice on borrowing and money management

➔ Advice on loans and selling of loans should be separated. Banks should provide borrowing and money management advice, independent from their own interest. This could been done through a compulsory contribution to a debt-counselling or debt-relief fund, on the model of the slot machine association funding the Guarantee Foundation in Finland.

Several Eurodiaconia organisation offer free debt counseling. In Denmark, Copenhagen, the needs were so great that a waiting list for several months had to be established. Similarly, the municipality of Copenhagen gave counseling on debt, budgeting, advice on debt relief or remission of debt.

7. Higher level and simplified social security mechanisms

As over-indebtedness appears to be both a cause and a consequence of poverty and social exclusion, simplified and higher levels of social security are both a preventative measure and an action to support people who have fall into debts.

Eurodiaconia members denounce the level of complexity of the social security system in their country which sometimes makes itself inaccessible to people most in need. For instance, Kerk in Actie witnesses that often people in situation of over-indebtedness "*do not take advantage of income support such as housing or health care benefit. (…) They do not know what the possibilities are or where to find information*".

➔ The access to social security support should be rationalised and simplified to be fully accessible.

➔ The European Union should encourage member states to increase their levels of social security as an investment warding off the future cost of today's non-inclusion.

8. Beyond economic growth, consumption and ownership

Members advocate for Member States and the European Union not to forget core values such as solidarity and environmental sustainability at the expense of economic growth, consumption and ownership. The public debt crisis has demonstrated that the current society rests on unsustainable values and actions.

➔ The European Union should work toward an analysis of the consequence of a mindset change questioning current cultural trends in which unnecessary consumption and greed are encouraged and valued and promote instead alternative values such as moderation and generosity.

9. More support for diaconal organisation offering debt related services

Preventative measures against over-indebtedness are the ideal for social policy and society. However, at the moment, over-indebtedness persists and measures of support are essential for social inclusion.

➔ Eurodiaconia recommends a consistent and increased support to diaconal organisation offering debt related services, independent advice and social lending.

➔ Best practice examples such as the SchuldHulpMaatje project by Kerk in Actie should be promoted and supported at EU level.

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10. Integrated approach (health, legal, social and economic)

People in situations of over-indebtedness are often dealing with intertwined circumstances, touching on legal, health, economic and social issues. That is why researchers and Eurodiaconia members agree on the need to develop more integrated approaches, responding to a greater extent to the full problem of individuals in situations of over-indebtedness and looking at the broader needs of the individual in situation of over-indebtedness. Researchers have found it hard to come across good practices of such integration in the EU, as noted by Eurofound[9].

- ➔ Member States should be encouraged to support local authorities in engaging in the development of integrated approaches.

- ➔ The European Union should promote integrated approaches such as the Kerk in Actie, YMCA and Christian against Poverty UK models through best practice exchanges, access to EU funding, and the facilitation of staff exchange programs between legal, health, economic and social actors.

11. Enhance dialogue between NGOs, banks and public authorities

Eurodiaconia members reported their interest for further cooperation with different actors, on the model of the SchuldHulpMaatje. Banks, public authorities and NGOs have a strong interest in working together to tackle the issue of over-indebtedness.

- ➔ Member States and/or the European Union could facilitate this dialogue through the establishment of formal platforms or task forces for cooperation.

- ➔ This cooperation could touch on prevention and intervention through different actions such as an exchange of volunteers between banks and NGOs and talks about self-regulation of credit, consumer credit and revolving credit. When existing in their country, Eurodiaconia members would like to start a dialogue with church banks on the question of self-regulation of credit.

12. Work toward adequate minimum income

As recognised by the Active Inclusion Recommendation endorsed by the Employment, Social Policy, Health and Consumer Affairs (EPSCO) Council on 17 December 2008, and reaffirmed by the EPSCO since then, minimum income schemes can play a decisive role in lifting people out of poverty and enabling a greater inclusion of people at the margins of society. Minimum income would protect the most vulnerable people from the need to borrow money to meet their needs.

Most Member States in the EU have some form of minimum income, nevertheless "[*m]ost Member States fall short of having minimum income schemes which allow all people to live life with dignity and many fall very far short"*[10], as stated by the coordinators of the European Network of National Independent Experts on Social Inclusion, in their report on minimum income schemes across EU Member States.

- ➔ Eurodiaconia call on Member States to work toward adequate minimum income schemes, allowing empowerment and full participation of all individuals.

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[9] "Eurofound (2012, forthcoming) *Household debt advisory services in the European Union*. Dublin: Eurofound."

[10] Hugh Frazer and Eric Marlier (2009) *Minimum Income Schemes Across EU Member States.* Brussels: European Network of National Independent Experts on Social Inclusion

- ➔ Eurodiaconia asks the European Commission to intensify its support to Member States by facilitating exchange of best practice and policies.

13. Universal access to a bank account

Financial exclusion and over-indebtedness are two sides of the same coin as they both relate to banking problems and both have as a consequence the deprivation of all or part of financial services.

Access to a bank account determines the ability for full participation in society and social inclusion, through for instance the opportunity to manage the paying of bills and the possibility to receive social benefits from public authorities. It is therefore a necessary element of social cohesion and should be protected at European level.

- ➔ On the 23 July 2014, the directive on the transparency and comparability of payment account fees, payment account switching and access to a basic payment account was formally adopted. Eurodiaconia calls on the European Commission to closely monitor the implementation of the directive on access to a basic bank account, especially as to its implementation for the most vulnerable consumers.