





## The content

# Debt Advice Handbook 15th edition

## Description

With living costs and unemployment rising, budgets squeezed and problem debt on the increase, no adviser should be without this essential guide to the practice and process of giving money advice in England and Wales.

### Who's this book for?

It is essential for debt advisers, welfare rights advisers, lawyers, local authority and housing association staff, social workers and union official.

### What does it do?

The handbook provides the most comprehensive information needed by advisers on the key stages of money advice, including interviewing clients, establishing liability, prioritising debts, preparing a financial statement, negotiating with creditors and dealing with bailiffs. Fully indexed and cross-referenced to law, regulations and official guidance, and to court and tribunal decisions Includes tactical guidance and examples

### What's new?

Fully updated to cover all recent changes to legislation, caselaw and court procedure and practice Emphasis is placed on taking due care of vulnerable clients and making sure that any payment arrangements agreed are appropriate. There is a focus on sustainable credit arrangements that do not affect a client's abilities to pay essential living expenses and priority debts.

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## Voluntary charge

This section describes the available strategies for non-priority debts. They are not mutually exclusive; you may use several strategies to deal with each debt – eg, a moratorium of three months and freezing interest or charges, followed by an arrangement to make payments by equitable distribution. Alternatively, different strategies (or combinations of strategies) may be needed for individual debts – eg, some requests for write-offs, some token payments or a voluntary charge in return for a freeze of interest/charges and no payments.

Selecting a strategy is often not a single process, but may be done initially and reviewed later. The criteria described here should be equally applicable to initial or review strategies. The strategy chosen for each debt needs to be reviewed:

- if a creditor refuses to accept a particular strategy; *or*
- at the end of the time agreed by the creditor – eg, if the creditor agrees to accept no payments for six months and then to review the situation; *or*
- if the client's financial circumstances change.

Often strategies are not accepted on first application (eg, write-offs – see here) and you should always urge creditors several times to accept a realistic strategy. Second and third letters can be strengthened by details of how other creditors have come to agree to a particular strategy. If you consider a creditor is not complying with its obligations under a relevant code of practice or the Financial Conduct Authority's (FCA's) *Consumer Credit Sourcebook* (eg, it is not treating the client's individual and particular financial situation 'fairly and with forbearance and due consideration'), consider using the creditor's complaints procedure and threaten to refer the case to the Financial Ombudsman Service to resolve the matter in a fair and reasonable way.

Clients should not routinely be advised to stop payments to all their non-priority creditors while negotiations are taking place. However, in many multiple debt cases, it is appropriate for the client to reduce payments to non-priority creditors or even stop them altogether – eg, if the client does not have sufficient available income. If the client is able to make payments to non-priority creditors while still servicing their essential commitments, including priority debts, they should be

advised to do so. If not, point out that the client's default will be registered with credit reference agencies and may eventually lead to court action by the creditor, but that it is still in the client's best interests not to make these payments because there is no, or very little, available income after meeting their essential expenditure and payments to priority creditors. CONC 8.6.1R of the FCA's *Consumer Credit Sourcebook* requires any decision to reduce or stop payments to a non-priority creditor to be notified to the creditor without delay, together with an explanation that the client is following your advice (if this is the case). Although the rule refers to the notification being given by the client, it may be more appropriate for you to do this on their behalf.

A long period without any payments at all to creditors is undesirable, unless a strategy involving non-payment has been proposed in the meantime. On the other hand, a short period during which no payments are made may be inevitable while you work out a strategy with the client. <sup>1</sup>

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<sup>1</sup> *FCA Handbook*, CONC 8.6

## Debt management plans

A debt management plan is an informal arrangement under which the client agrees to repay their creditors. The term is usually used to describe an arrangement made on the client's behalf by a third party who also manages the plan. The arrangement normally involves an equitable distribution of the client's available income after priority payments have been made (see here). The client makes a single regular payment (usually monthly) to the third party, who may be:

- a debt management company, which negotiates the debt management plan, collects the payments from the client and distributes them to the creditors in return for a fee paid by the client (often referred to as 'fee chargers'); *or*
- StepChange or PayPlan, both of which can arrange a debt management plan and distribute the payments to the client's creditors, but do not charge the client a fee. They are paid by the creditors through deducting a percentage of the money recovered (known as 'fair-share' arrangements). For this reason, they are part of the free money advice sector. Both have minimum criteria for setting up a plan (eg, relating to the amount of available income) and can also help clients set up individual voluntary arrangements (IVAs – see here).

If a client's agreed strategy is to make pro rata payments to their creditors (see here), a debt management plan under which they only have to make one monthly payment, instead of a number of individual payments, may be in the client's best interests.

**Note:** some debt management companies do not deal with emergencies and/or priority debts. You must therefore assist the client to deal with these before they can be referred for a debt management plan.

The *Consumer Credit Sourcebook* requires debt management companies to signpost clients to the Money and Pensions Service's website for information about free-to-client debt advice services and to refer clients to a provider of free-to-client debt advice if the client has issues requiring urgent attention which the debt management company is either unable or unwilling to deal with. <sup>1</sup>

Debt management companies fall within the Financial Ombudsman Service's jurisdiction. If a client is dissatisfied with the service provided, they should consider making a complaint.

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<sup>1</sup> *FCA Handbook*, CONC 8.2.4R and 8.3.7(3)

## Request a write-off

Advantages

Disadvantages

Useful arguments

Checklist for action

A write-off should be considered if:

- there is no available income or capital and a client's circumstances are unlikely to improve in the foreseeable future (or may even worsen); *or*
- the debt is uneconomical for the creditor to collect – eg, a small amount is owed or the pro rata payment would be less than £1 a month; *or*
- there is some available income, but this will not repay the debt within a reasonable time (see also partial write-offs on here); *or*
- the client's circumstances are exceptional and unlikely to improve – eg, they have a terminal illness or mental health problems that affect their capacity to make a contract or make it difficult for them to manage their finances (see here).

A write-off means the creditor agrees not to collect any further payments and removes the account from its records. The client makes no further payments. If the debt is large, any realisable assets or equity in the client's home must be considered, as it is unlikely that creditors will agree to write off the debts of 'asset-rich, income-poor' clients unless the circumstances are

exceptional. It is likely that, if the creditor took court action and the client could not make payment as ordered by the court, the creditor could either apply for a charging order against the equity in the client's home (see [here](#)) or ask the court to make a bankruptcy order (see [here](#)) so that goods owned by the client, or the home, could be sold.

All creditors recognise the need to write off some debts, and they make provision for this in their accounts and the interest rates they set. The decision whether or not to request a write-off is ultimately one for the client. A client who initially says they want to pay something may change their mind in the light of creditors' responses to their financial difficulties and the realisation that their financial difficulties are not being resolved. The possibility of proposing this strategy to creditors should be kept under review.

## Advantages

- It removes the financial and emotional stress caused by that debt.
- It enables the client to make a fresh start.
- It acknowledges that further action against the client is not appropriate.

## Disadvantages

- Creditors do not agree easily to write off debts, particularly if the debt has been incurred recently.
- When creditors write off debts, they often report this to a credit reference agency. This is an agency that collects evidence, such as county court judgments and defaults on credit agreements, and shares this information with other creditors. If a debt is reported as written off, it may be difficult for a client to get credit in the future. For more details on credit reference agencies, see [here](#).
- Many creditors never formally agree to write off a debt, even when they have received a request to do so. They take no further action on it and, at some point, will write it out of their accounts. This can mean that the client is left uncertain as to whether or not the creditor has agreed to their request, and they can be vulnerable either to a change of company policy or to pursuit of a debt if their circumstances improve.

## Useful arguments

- Outline the client's circumstances and explain that they have no property or goods of significant value, no income except benefits or low wages and there is no prospect of improvement in the foreseeable future. This helps creditors to see that court action is unlikely to be successful. Explain that if bankruptcy were pursued, the outcome would be the same.

Medical evidence confirming, for example, the nature of any disability or that the client is unable to work may also be persuasive.

- Use the Money Advice Liaison Group's debt and mental health evidence form or other available evidence, if appropriate, to support the request (see here).
- Inform the creditor of the total amount of debt owing to all creditors to show the hopelessness of the client's situation.
- Most creditors have a set of criteria for deciding when to abandon debt recovery, which is determined by the cost of recovering the money. Suggest that writing off a debt is likely to be the most economic solution for the creditor. For example, *The Standards of Lending Practice*, subscribed to by banks, building societies and credit card providers (see here), suggests that creditors should take account of the client's circumstances and consider whether it would amount to a fair customer outcome to pursue or continue to pursue the debt. <sup>1</sup> The creditor must give reasons for refusing a request for a write-off and you should press for these to be provided, as this may help you to ask the creditor to reconsider its position.
- Creditors may be more willing to write off a debt after repeatedly withholding action on the account for three or six months (see here).
- It is easier to get smaller debts written off.

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<sup>1</sup> Lending Standards Board, *The Standards of Lending Practice*, p9, para 11

## Checklist for action

- Write to the creditor(s) proposing the strategy, enclosing any supporting evidence, and request written confirmation that the strategy is agreed.
- Advise the client to stop paying.
- A creditor may not initially accept a write-off. Ask the creditor to reconsider after, say, three to six months, and repeat the request at subsequent reviews.

## Request a partial write-off

Advantages

Disadvantages

Useful arguments

Checklist for action

If there is some money available to meet a creditor's demands, but this will not pay off the whole



debt in a realistic period of time, creditors can be asked to reduce the balance owing immediately or to accept agreed instalments for a set period of years, after which the balance will be written off.

Partial write-off should be seen as a means of coming to an arrangement similar to an IVA and which is broadly the same as what a court would order if an income payments order in a bankruptcy application were being considered. A period of at least three to five years, but no more than seven to 10 years, should be suggested. You should also request that further interest be stopped (see here). Partial write-off is appropriate if:

- there are no realisable assets or substantial equity that could be charged;
- the client's circumstances are such that they cannot repay the whole debt within a reasonable period of time;
- there is no expectation of capital or extra income becoming available soon.

## **Advantages**

- It reduces the amount owed and gives the client a realistic target to aim for and, therefore, a framework in which they can regain control over their financial affairs.
- The client repays less money.

## **Disadvantages**

- When creditors write off debts, they often report this to credit reference agencies and it may, therefore, be difficult for the client to get credit in the future.
- It may be difficult to get all creditors to agree to the strategy.

## **Useful arguments**

- It can be argued that the creditor will receive more than if the client were made bankrupt, and it is quicker, cheaper and less stressful for the client if the creditor limits its demands to that amount now.
- A partial write-off is also very similar to a composition order in an administration order (see here) or an IVA (see here) and so creditors are only being asked to take a similar course of action to that taken in those legally binding situations, but on an informal basis. As there are no court or supervisor costs, the creditor is likely to get a higher return than in an administration order or IVA.
- The creditor may be persuaded that it is better to go for something shorter term and realisable, rather than longer term but potentially expensive to collect and unlikely to be paid.

Unless creditors reduce their demand to something the client can pay in the foreseeable future, the client is likely to lack the motivation to keep up with payments. It is unrealistic for both sides to set up repayment schemes that will last more than about seven to 10 years and it is likely that such money will eventually be written off.

- If the creditor refuses to agree to this strategy initially, it is worth requesting it again after, say, 12 months of regular payments if there is still no improvement in the client's circumstances.

## Checklist for action

- Agree with the client the amount of income available to creditors.
- Calculate offers and decide a payment period.
- Write to the creditor(s) proposing the strategy, with details of the offers and requesting written confirmation that this is accepted.
- Advise the client to start making payments. Consider direct debits or standing orders if the client has a current account.
- Request that interest or charges are stopped, using the arguments here.
- Consider whether any steps need to be taken to ensure that the arrangement is legally binding on creditors (see full and final settlements on here).

## Request that interest be frozen or reduced

Advantages

Disadvantages

Useful arguments

Checklist for action

If a client is unable to pay the contractual payments due under an agreement, adding interest and other charges, especially if they are not even repaying any capital due, only increases the total balance and the debt will never be repaid. This fact has long been recognised by county courts, and statutory interest is not charged after judgment on debts which are regulated credit agreements (but see here for when interest can be charged after a judgment).

Whenever a repayment schedule of less than the original contractual payments is envisaged, or if no payment can be afforded at present, a request should be made to stop (or freeze) all interest and any other charges accruing on the account. This strategy should always be used in conjunction with another strategy.

The request to stop interest should be made in most cases immediately the client contacts you. However, explain to the creditor why it is considered necessary – eg, the payments the client

is likely to be able to afford will not cover the ongoing interest.

*The Standards of Lending Practice* contains guidance to creditors on reducing or freezing interest and charges, <sup>1</sup> and FCA guidance on treating clients with forbearance gives as an example 'considering suspending, reducing, waiving or cancelling any further interest or charges'. Creditors often complain that advisers automatically request that they freeze interest in all cases. Requests to freeze interest should be appropriate and justified. If a creditor believes the level of the client's repayments warrants it, the creditor may refuse to freeze interest, but may instead agree to reduce it. If the loan is a regulated credit agreement, an application for a time order may be appropriate (see here).

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<sup>1</sup> Lending Standards Board, *The Standards of Lending Practice*, p9, para 9

## Advantages

- Realistic repayment schedules can be created under which debts will be repaid in a known time.
- All payments made reduce the debt. The client can see that they are repaying their debts.

## Disadvantages

- Creditors may not accept the strategy, particularly if there is substantial equity in a property or the client has realisable assets which it is reasonable to expect them to use to pay their debts.
- It is not appropriate for loans for which all interest is added at the beginning of the loan and there are no default interest/charges. In these cases, a partial write-off may achieve the desired result.

## Useful arguments

- If a county court judgment were awarded, in practice, interest would be stopped for all regulated consumer credit agreements (see here).
- Excessive default charges (ie, charges which are more than any actual or anticipated loss that the creditor has or may face as a result of the loss) are almost certainly unenforceable either as a penalty in common law or as an unfair contract term, and so the creditor should either reduce them or remove them altogether and should consider doing so retrospectively (see here).

- It is a necessary incentive to the client because otherwise they may not be prepared to lose valuable income in pursuit of a completely hopeless goal.
- Many other creditors are being asked (or have agreed) to stop interest and, therefore, fairness demands that this creditor does too.
- Make any offer of payment conditional on interest stopping.

## Checklist for action

- This strategy should always be used with another strategy.
- Write to the creditor and include a request to freeze interest and other charges, together with some justification for the request.
- Request written confirmation that this has been done.
- If the strategy is not successful initially, ask the creditor to reconsider. It may be useful to provide evidence of other creditors' agreements to freeze or reduce interest and other charges.

## Offer a reduced capital sum in full and final settlement

Advantages

Disadvantages

Useful arguments

Checklist for action

If there is available capital or saleable assets, or if the client will have such assets in the near future (eg, because they intend to sell a house or a third party, such as a friend or relative, has a lump sum they are willing to give to the creditor), the creditor may accept an offer of an amount less than that which is due, as early settlement. This is particularly likely if there is little or no available income and the client's financial position is unlikely to improve or may even worsen. Creditors are likely to recognise that acceptance of a cash lump sum makes commercial sense. When the client's income is low and unlikely to improve, it could be an attractive alternative to waiting to see if their income increases over a long period. If there is more than one creditor, lump sums should be apportioned between them in proportion to the amount owing to each.

Ask the client if there are essentials they need to purchase, or essential repairs that need to be carried out, before the lump sum is allocated to creditors.

The key to using this strategy successfully is to ensure that the lump-sum payment is not made until a creditor has agreed in writing to accept this in full and final settlement of all the money owed. Ideally, no payments should be made until all creditors have agreed and offers can

– initially at least – be made on this basis. However, be prepared to adopt a flexible approach to prevent the whole strategy from failing. For example, creditors who are reluctant to accept may be persuaded by knowing that other creditors have already agreed to accept it. Other creditors may threaten the whole strategy by demanding more than their fair share, leaving insufficient funds to tempt the remaining creditors.

There is no set amount that needs to be offered and, in fact, a promise by a creditor to accept part payment is not a legally binding contract unless the client has provided what the law regards as fresh 'consideration' for the creditor's promise to forgo payment of the balance. The Financial Ombudsman Service, however, may take the view that creditors who go back on their word are not behaving 'fairly and reasonably' unless the client misrepresented their true financial situation. CONC 7.14.14R of the FCA's *Consumer Credit Sourcebook* requires a creditor who accepts such an offer to communicate 'formally and unequivocally' that the offer and the payment has been accepted as settlement of the client's liability.

There is a legally binding agreement if:

- a composition is made between the client and some or all of their unsecured creditors under which the creditors mutually agree to accept a reduced sum in satisfaction of their debts on the understanding that other creditors have done the same; *or*
- the funds are made available by a third party (eg, a relative) and the offer and payment are made by them on the client's behalf; *or*
- the agreement is embodied in a formal document known as a 'deed'. The client needs to be referred to a solicitor if they want a deed drawn up – eg, if there is any doubt about the trustworthiness of a particular creditor or they want to ensure that the agreement is legally binding on the creditor.

## Advantages

- The client pays less than they would if repaying over a longer term.
- The client has the opportunity of a fresh start.
- It is a more immediate and convenient solution than setting up a repayment schedule over a number of years.
- Even if not all creditors accept, the client's total indebtedness is reduced and this may in turn enable another strategy to be adopted to deal with these.

## Disadvantages

- The client loses the advantage of having a lump sum which could have been used for other purposes.

- Even though creditors have accepted a payment in full and final settlement, they can record this on the client's credit reference file as 'partial settlement'.
- Once aware of the existence of a lump sum, the creditor may attempt court action to obtain all the money for itself.
- Creditors who have not agreed to the composition are neither included in it nor bound by it and so are free to continue pursuing their debts.
- If all available funds are distributed among only some of the client's creditors, the client may subsequently have little room to manoeuvre if put under pressure by other creditors.

## Useful arguments

- Contact the creditor before the money is available and suggest that this is the only chance that the client will have of paying a substantial amount and that because the client wants to pay their debts, they are prepared to hand all (or if there are several debts to be treated in this way, a proportionate share) of the money over to the creditor.
- It is worth pointing out that the creditor is not going to get more by refusing the offer and taking enforcement action, and that acceptance of the offer makes more commercial sense than the client continuing to make small payments over a long period of time. Such an arrangement may have to be made with senior staff in the creditor organisation and you should ensure you are writing or speaking to senior credit control managers.

## Checklist for action

- Clients who are considering accessing their pension savings to offer a full and final settlement should be signposted to Pension Wise, which offers free, impartial guidance on options to individuals older than 50 who have a work or personal pension. This service can be accessed and a free appointment arranged at [pensionwise.gov.uk/en](https://pensionwise.gov.uk/en).
- Write to the creditor(s) with details of the offer, confirming that an offer has been made on the same basis to the client's other unsecured creditors and requesting acceptance in full and final settlement to be confirmed in writing. Enclose a financial statement that includes a list of the client's creditors, the amounts owed to them and the amounts being offered to each of them in full and final settlement.
- If the money is coming from a third party, it should be made clear that the offer is being made by them on behalf of the client.
- If a creditor refuses, write back to ask them to reconsider and inform them about any other creditors who have accepted the offer under the strategy.
- Consider specialist legal help to draw up the agreement.

- Once written confirmation is received, advise the client (or third party) to send the payment(s).
- Any covering letter sent with a cheque should explain exactly what it is for and state that it is in full and final settlement. Cashing a cheque sent 'in full and final settlement' does not necessarily preclude the creditor from pursuing the balance (cashing a cheque is strong evidence of acceptance unless it is accompanied by a swift rejection of the offer).
- If money is being made available from the sale of a property, it may be necessary to obtain a solicitor's undertaking that the money will be paid to the creditor once it is sold.
- If fewer than 25 per cent in value of a client's creditors do not agree a full and final settlement, even though the remaining creditors have accepted the offer, the client could consider an IVA (see here). However, because of the costs involved, the creditors will receive less money. This could be pointed out and the creditors asked to reconsider their position.

In the unlikely event of a creditor threatening to renege on a full and final settlement or selling the account to a debt purchaser after the client has made the payment, specialist advice should be sought.

## Offer payment by a capital sum and instalments

Advantages

Disadvantages

Useful arguments

Checklist for action

When a client has capital or assets together with stable available income, but there are substantial arrears, the threat of further action can often be avoided by paying a single capital sum towards the arrears and then paying instalments towards part or all of the contractual payments. This often needs to be linked to another strategy, particularly freezing interest/charges (see here) or a partial write-off (see here). This is different from paying a capital sum in full and final settlement in that the payments will have to continue. It could be the fallback position if a full and final strategy is rejected because the amount offered is insufficient to be accepted by the client's creditors and there is a reasonable amount of surplus income available.

### Advantages

- The creditor is no longer pressing.
- Payments made towards the debt out of available income will be lower than otherwise.

### Disadvantages

- The flexibility to use the capital sum elsewhere is lost.

## Useful arguments

- If this tactic is being used to prevent imminent court action, you can argue that the creditor will obtain its money more quickly than by going to court, and more money will be available to repay the debt as there will be fewer costs. An agreement such as this must be made in writing.

## Checklist for action

- Contact the creditor proposing the strategy and request acceptance in writing.
- Calculate the instalments on a pro rata basis (see here).
- Once written confirmation is received, advise the client to send payment of the capital sum, followed by regular instalments. It may be helpful for the client to set up a direct debit or standing order for these if possible.
- Ensure that interest and charges are stopped. If not, consider advising the client to withhold instalments until agreement is given to stop them.
- An IVA could be considered as an option if most, but not all, of the client's creditors accept the strategy (see here).

## Holding tactics (moratorium)

Advantages

Disadvantages

Useful arguments

Checklist for action

It may sometimes be important to gain time for the client when:

- there is some available income, but this is immediately required to deal with priority debts;
- there is no available income, but shortly there will be;
- available assets are being sold;
- the full situation is not yet known.

There could be other examples of when this tactic is appropriate – eg, when time is needed to formulate and/or implement a strategy for the client's debts.

There are a number of holding tactics (also known as 'moratoriums').

- **Asking creditors to suspend collection or enforcement action.** Section 3(f) of the *Credit*



*Services Association Code of Practice*, published in July 2017, provides a 30-day 'breathing space' if requested by an advice agency. Sections 7.3.11R and 7.3.12G of the FCA's *Consumer Credit Sourcebook* requires creditors to suspend recovery action for a 'reasonable period' (generally, 30 days, although this can be extended) if they have been informed that an adviser is assisting a client to agree a repayment plan.

It may be useful to request a short delay if you need to check a credit agreement or its enforceability. Some agencies write automatically to all creditors asking them to withhold action for a short period when their advice is first sought (a holding letter). This may not be necessary if a strategy can be formulated and/or implemented quickly or if you will be asking the creditor to write off the debt or to accept no payments for three months.

If a delay is needed because balances are required before a strategy can be implemented, ask the client to contact the creditors to obtain these if possible.

If a debt is queried or disputed, the creditor (or debt collector) should investigate/provide details (as appropriate) and should cease collection activity in the meantime. <sup>1</sup>

From 4 May 2021, the breathing space scheme potentially gives clients working with a debt advice agency protection from recovery and enforcement action for up to 60 days together with suspension of interest/charges (see here ).

- **Asking creditors to accept no payments for a specified period.** If no money is available at present to pay non-priority debts, the creditor should be asked to accept no payments for three or six months and then to review the situation.

This is invariably a temporary strategy and so is subject to review, usually after three or six months. It is always used with another strategy – eg, asking a creditor to withhold for three months and then following this with a request for a write-off. This can be useful if it is known that the creditor is unlikely to accept a write-off immediately. If a request is made to a creditor to withhold any action and accept no payments, the creditor must always be asked, at the same time, to stop interest/charges in order to prevent the debt increasing even further.

The length of time you request no payments depends on:

- any known future changes in the client's financial position which may allow payments to begin;
- the length of time needed to repay priority debts;
- the stress faced by the client and how much breathing space they need.

If the creditor agrees to withhold action and collect no payments for six months, it gives the client a substantial period of relief.

However, as this strategy can never be a permanent solution, it means that a request for a six-month delay prolongs the process of reaching one.

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**1** *FCA Handbook*, CONC 7.14.1R and 7.14.3R. *The Credit Services Association Code of Practice*, 2017, has similar provisions in s2(t).

## Advantages

- Time can give the adviser the opportunity to gather all the necessary facts and advise the client about all their available options.
- It removes the immediate pressure from the client, and enables payments to be made for priority debts.
- It gets creditors used to the idea that there are problems, but does not leave them in the dark.
- Almost as a matter of routine, many creditors accept a request from a debt advice agency to withhold action for a short period.

## Disadvantages

- It does not actually solve anything. Some creditors refuse to stop interest and so the debt grows while no action is taken.
- It can create extra work for advisers.

## Useful arguments

- Explain that considerable debts have arisen and outline the client's circumstances.
- Explain that time is required for professional debt advice.

## Checklist for action

- Contact the creditor to explain the situation and request written confirmation that the account is held in abeyance. Enclose a financial statement if requesting that more than a month's payments be withheld.
- Ensure that interest/charges will be stopped.
- Advise the client not to make payments.

## Offer token payments

Advantages

Disadvantages

Useful arguments

Checklist for action

When there is little available income, no assets or capital and the situation is unlikely to change, but it is impossible to get agreement on any other strategy, payment by instalments of a nominal or token nature may be necessary to satisfy the administrative systems of a creditor and may be the only way to prevent it from taking further action.

Clients initially seeking advice often want to make token payments rather than withholding payments or asking creditors to write off their debts, out of fear or ignorance of enforcement action, or because of previous harassment by creditors, or because they want to make some payment, however small, towards their debts. Ensure that clients do not make payments they cannot afford or at the expense of making payments towards their essential expenditure and any priority debts. A nominal or token payment is usually £1 a month. Even £5, £20 or more a month is regarded as a token payment by some creditors because, in reality, the debt will never be repaid at that rate.

The strategy need not be used for all creditors and should only be offered as a last resort if the creditor has refused to either write off the debt or accept no payments, or to freeze interest/charges and if court action by the creditor would be undesirable. The creditor must be asked to agree to take no further action and to stop interest in return for token payments being made. Token payments do not resolve the client's debt problem, so it is necessary to review the strategy later to choose a more suitable long-term option.

If a creditor has already taken court action, but there is no available income and the court is unwilling to order no payments, the client should make a token offer to pay by instalments (eg, £1 a month) to try to prevent further enforcement action.

Token payments are essentially a short-term strategy. The FCA's *Consumer Credit Sourcebook* recommends accepting token payments for a reasonable period of time if the client has demonstrated that otherwise they would not be able to meet their priority debts or other essential living expenses. <sup>1</sup> This guidance reflects not only the difficulty of persuading creditors to accept no payments at all but also the belief of creditors that, firstly, people can always find some money and, secondly, that something will turn up.

All advice must be in the client's best interests. It is not generally in the client's best interests to make payments at a higher level than they can afford or to make any payments at all if the client has either no surplus income or a deficit budget. However, if a creditor does not agree, for example, to a moratorium and/or to freeze interest/charges unless token payments are made, consider whether it is nevertheless in the client's best interests to make those payments.

Many clients whose financial circumstances mean that they are only able to afford token payments may be eligible for a debt relief order or should consider bankruptcy as a debt relief option (see Chapter 10).

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**1** *FCA Handbook*, CONC 7.3.5G(3). See also *The Credit Services Association Code of Practice*, 2017, s3(g).

## Advantages

- Paying a token amount may be the only way to obtain a creditor's agreement to take no further action and stop interest/charges.
- The client feels they are paying something towards their debts and creditors can see the habit of payment being re-established.

## Disadvantages

- It uses up income that is not really available.
- It encourages creditors to take an unrealistic view of people's ability to pay.
- It can be expensive for the client as it may cost as much in postage and other charges to make the payment as the payment is worth.
- The debt will never be repaid at this rate and it hangs over the client.
- Creditors can continue to apply pressure on clients to pay more.

## Useful arguments

- A request for payments may be made by the creditor after you have made it clear there is no (or only a nominal amount of) available income as shown by the financial statement. Explain that, in fact, the only payment possible is a token payment because the client is cutting back on essential spending, such as food or fuel, in order to make the payment.
- If creditors are threatening court action, draw their attention to any recent low judgment amounts awarded by the county court.

## Checklist for action

- Contact the creditor and wait for written confirmation of the strategy.
- Ensure that further action, and interest and other charges, are stopped.

- Advise the client to make payments. Ask for a payment book if this facilitates payments without cost.
- Review at an agreed date with the client.

# Equitable distribution of available income (pro rata payments)

- Advantages
- Disadvantages
- Useful arguments
- Checklist for action

If there is available income, a number of debts, and no capital or realisable assets, this income should be distributed among all the non-priority creditors in a fair way. Apportioning the available income fairly is best done by a method known as either 'equitable distribution' or 'pro rata payments', in which the amount of each instalment is directly proportionate to the total amount owing to that particular creditor. Clients who are using the CASHflow self-help process (see here) are likely to be making offers on this basis and so may find the information in this section useful.

Calculate the amount due to each creditor each week or month, based on the following formula:

$$\text{Amount owed to creditor} \div \text{total amount owed} \times \text{total income available for distribution}$$

## Example

The client owes money to three creditors:	
Creditor A	£1,000
Creditor B	£800
Creditor C	£250

<b>Total amount owing</b>	<b>£2,050</b>
(The client's total available income is £12 a month.)	
Calculation:	
Creditor A	$1,000 \div 2,050 \times 12 = £5.85$ a month
Creditor B	$800 \div 2,050 \times 12 = £4.70$ a month
Creditor C	$250 \div 2,050 \times 12 = £1.45$ a month
<b>Total repayments to creditors</b>	<b>= £12.00 a month</b>
(Amounts may be rounded up or down for convenience, but not if this results in payments which the client cannot afford.)	

If you do not use the 'standard financial statement' (see [here](#)) or some other computer-based financial statement that automatically calculates pro rata offers, this sum must be worked out for each creditor. Even if the exact balances are not known, it may be worth calculating a distribution based on good estimates, as the weekly variation will probably be very small and may be acceptable to creditors.

If the calculation means there is a very low payment to a particular creditor (eg, less than £1 a month), you may wish to include in the offer letter a request that, in view of the high collection costs for such a small sum, the creditor should consider writing off the debt (see [here](#)) or at least

agreeing to a moratorium (see here). Any payment arrangement must be sustainable and so, when calculating the amount of available income on offer to creditors, ensure some leeway in the financial statement to cope with unexpected events (eg, short periods of sickness) so that payments can still be maintained.

In the *Consumer Credit Sourcebook*, the FCA points out that clients should not usually be advised to cancel contractual payments to their creditors before a debt repayment plan has been agreed or to make payments that do not cover ongoing interest or other charges unless it is demonstrably in their best interests – eg, if someone has insufficient available income after meeting essential expenditure and/or payments to priority creditors. <sup>1</sup>

Unless the client has sufficient available income to be able to maintain the contractual payments on these debts, as well as servicing their other debts, it is in their best interests to offer pro rata payments, provided this is accompanied by a request for any ongoing interest and any charges to be stopped so that each payment made by the client actually reduces the debt. On the other hand, if the creditor refuses to stop interest or reduce it sufficiently, pro rata payments are almost certainly not in the client's best interests and the creditor must be urged to reconsider or the strategy reviewed with the client.

It is usual to send to each creditor details of the amounts owed to all creditors, together with the offers made. This should not be done if the client wishes confidentiality to be maintained. However, it is helpful for the creditors to know that they have been given the client's whole financial position as they would in an administration order or bankruptcy. If the creditor has already obtained a court order that is higher than the offer calculated, the client should consider applying to the court to vary the order (see here for how to do this).

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<sup>1</sup> *FCA Handbook*, CONC 8.6.1R, 8.6.3R and 8.6.4G

## Advantages

- Equitable distribution is widely accepted by the credit industry. Many creditors think it is the only strategy that debt advisers should use.
- It ensures that all non-priority debts are dealt with together.
- It is based on court practices. This is how money is distributed to creditors when an administration order is granted (see here).
- Many creditors automatically freeze interest/charges once an offer is accepted.

## Disadvantages

- A client may be left with little financial flexibility and money only for basics.
- Unless coupled with a partial write-off (see here), many debts may take years to clear. You should always explain to the client how many years it will take to repay the debts using this strategy, if creditors agreed to freeze interest and charges for the whole period that the client would be making payments. That can be calculated by dividing the total amount of debt by the amount of monthly surplus income and dividing this answer by 12 – eg, a client has debts totalling £24,000 and has £200 a month surplus income. It would take 10 years to clear the debts using this strategy if creditors froze interest and charges.
- If the payments do not cover ongoing interest/charges, the debt will never be repaid.

## Useful arguments

- The strongest argument in favour of this strategy is its fairness. It can be presented as a business-like response to a difficult situation, ensuring that every creditor is treated in a way which gives them the maximum possible amount.
- Sections 7.3.8G and 7.3.10R(1)–(2) of the FCA's *Consumer Credit Sourcebook* state that creditors should allow for 'alternative, affordable payment amounts to repay the debt in full where the client or an adviser makes a reasonable proposal to repay the debt', and must not pressurise a client 'to pay a debt in one single or very few repayments or in unreasonably large amounts and/or within an unreasonably short period of time'.
- It is exactly what would happen if a court were to grant an administration order or in bankruptcy, and is the kind of order which a court should make every time it makes an instalment order. The creditor cannot expect to do better.
- This strategy has often been used successfully if it can be shown that the person is starting to pay their creditors and wants to treat them all fairly. In addition, consideration should be given to asking for a partial write-off if offers will be paid for three to five years only (see here for details).
- Creditors who subscribe to the standard financial statement (see here) generally accept that a pro rata offer should be accepted (but not necessarily that interest/charges will be frozen). Non-acceptance suggests that the creditor has other information about the client, which it should be asked to disclose.
- Many creditors now have strict criteria for automatically accepting repayment offers based on a minimum payment or percentage of the debt or repayment over a maximum period in exchange for concessions on interest/charges.



## Checklist for action

- Agree with the client the amount of income available for creditors.
- Calculate offers to creditors. Consider a partial write-off if the suggested repayment period will not clear the debts within a reasonable time (see here).
- Write to the creditors with offers. Suggest a write-off if offers are low.
- Ensure that interest and other charges are stopped.
- Advise the client to make payments. Consider direct debit or standing order if the client has a current bank account. Ask for a payment book if this allows payment without cost. The client should not wait until all the creditors have accepted before starting to make payments.
- Consider whether a referral to a non-fee-charging debt management company may be in the client's best interests – ie, they would have to make one monthly payment for distribution among their creditors (see here).

## Consolidate the debts

### Advantages

### Disadvantages

Debt consolidation involves the client either taking out a new loan or increasing existing borrowing to pay off multiple debts. Debts can be consolidated by:

- an unsecured loan. These are likely to be small and so of limited potential;
- a further advance from an existing mortgage or secured lender, also secured on the client's property;
- a secured loan from a lender other than the existing mortgage provider, in addition to the existing mortgage;
- a remortgage with a new lender to replace any existing mortgage or secured loan;
- the transfer of balances to a credit card.

For many people in financial difficulties, this is likely to make the situation worse.

The *Consumer Credit Sourcebook* states that creditors must not pressurise a client into 'raising funds to repay the debt by selling their property, borrowing money or increasing existing borrowing'. <sup>1</sup>

Clients who are not in arrears and can meet their monthly commitments have the option of either carrying on with their existing agreements or refinancing them individually on more advantageous terms. However, for the average client struggling to meet their commitments, the

other options discussed in this *Handbook* are likely to be more suitable. If considering this option, the client should always be advised to obtain independent financial advice.

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1 *FCA Handbook*, CONC 7.3.10R(3) and 7.3.10AG

## Advantages

- Multiple agreements are replaced by a single agreement. The client only has to deal with one creditor.
- The consolidation loan is likely to be on better terms than the agreements it replaces, such as lower interest rates and monthly repayments.
- If the balance transfer is on the basis of a low or zero interest rate and the client can settle the balance before any balance transfer offer expires, the flexibility of a credit card enables consolidation to take place without incurring any additional costs in addition to any initial fee.
- The client's credit rating can be improved or the creditors prevented from registering defaults by the debts being repaid.

## Disadvantages

- Debt consolidation often involves replacing unsecured non-priority debts with a secured priority debt, with the client's property at risk if they default.
- Loans to clients with impaired credit ratings (non-status loans) are likely to be at higher rates of interest than those available to people with a clean credit record (status loans).
- There are usually costs associated with switching debts – eg, brokers' fees and early settlement charges.
- Although debt consolidation tends to involve lower monthly payments, it is often over an extended period, increasing the total amount payable by the client.
- Many debt consolidation loans are refinanced before running their full term (a process known as '**churning**'), which means that the client often has to borrow more as most of the repayments on the original loan will be interest rather than capital and there are early settlement charges. There may also be further costs (eg, a broker's fee), which are often added to the new loan.

## Equity release loans

### Advantages

## Disadvantages

### Checklist for action

An equity release or lifetime mortgage enables a property-owning client to release equity from their home. It is secured on the client's property and is a way of raising capital to repay debts. The term of the loan is the client's lifetime, at the end of which all the capital becomes due. The interest is rolled up and the client is not required to pay anything while they are alive. These loans are only available to clients over 55 and the older the client is the more they can borrow (depending on the amount of equity in the property). The interest rate is usually fixed. If at the time of death there is a shortfall because there is no longer equity, the lender must write off the outstanding balance and cannot pursue it from other funds the client may have in their estate.

This type of loan may involve the conversion of unsecured borrowing into secured borrowing and is only appropriate if there is plenty of equity in the property. It is most useful if the client is finding it particularly stressful owing money to a number of different creditors, or if creditors are proving difficult to negotiate with. Clients must always be advised to obtain independent financial advice.

## Advantages

- The loan prevents further action by the creditors.
- It may be a means of releasing equity from the property to use for other purposes, such as insulation or heating, which in turn can reduce living costs.

## Disadvantages

- The equity in the home is reduced by the value of the loan and will be steadily eroded by the accruing interest.
- On the client's death, the property will have to be sold to repay the loan, which may result in dependants who lived with the client being left homeless.

## Checklist for action

- Advise the client to obtain independent financial advice.
- Ensure the client obtains full details about the terms and conditions and the cost of the loan before signing any agreements.
- Inform creditors of the proposal and ask them to take no further action to enable the loan to be set up.

## Selling the home

Advantages

Disadvantages

Useful arguments

Checklist for action

When there is no available income, capital or realisable assets other than a home, sale may be considered. It should not be considered if the financial situation is likely to improve or if the sale of the home would result in homelessness. It is only appropriate as a way of dealing with non-priority debts if there is sufficient equity to satisfy most creditors' demands and to cover the costs of selling and moving, and when the stress of debts is creating unacceptable problems for the household.

The sale of a property is often recommended to people who are in debt as an easy way out of the situation, but it should be remembered that courts rarely order a property to be sold to satisfy unsecured borrowing and only after a charging order (see here) has been made and an order for sale subsequently applied for (see here), or a bankruptcy order made. If, however, an expensive house can be sold and a more modest one, which would nonetheless satisfy the client's needs, can be bought, this can be an acceptable way of coping with a debt problem and perhaps also having money left over for other purposes.

A client may have been advised (sometimes by family or friends) that they have no alternative other than to sell their property and they may, therefore, approach you only after this process has already begun. By examining the other strategies outlined in this chapter, it may be possible to demonstrate that selling the home in these circumstances is not the only option. The state of the housing market may also mean that this strategy is not easily achievable.

If a local authority or housing association rehouses people following a sale of their home, it usually only does so if it is clear that the sale is the only means to prevent eviction. Some local authorities still consider that the sale of a property makes someone intentionally homeless and, therefore, not eligible for rehousing under homelessness legislation. However, the code of guidance for local authorities states that a person should not be treated as intentionally homeless if their house was sold because of financial difficulties, and you should draw attention to this if necessary. <sup>1</sup>

In Wales, a successful mortgage rescue (see here) may mean that funds are raised for non-priority creditors.

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<sup>1</sup> Ministry of Housing, Communities and Local Government, Department *Homelessness*

*Code of Guidance for Local Authorities*, April 2019, s11.18

## **Advantages**

- It can clear the debts.
- It may raise capital for other purposes.
- The client may see it as providing the opportunity for a fresh start.

## **Disadvantages**

- It releases equity held in the property to satisfy unsecured creditors in a way a court may not order.
- It may not be possible to find alternative suitable housing.
- Moving house is a major disruption and costs a lot of money.
- The client may lose money if the housing market is depressed.
- The sale may take a long time or, in the midst of a recession, prove impossible, and the benefits of choosing this strategy may be lost.

## **Useful arguments**

- Creditors receive a lump sum, which pays the debt either in full or partially in full and final settlement (see here).

## **Checklist for action**

- Discuss the pros and cons of selling a property with the client.
- Telephone or write to creditors to inform them of the strategy and obtain written confirmation that they will take no further action.
- Advise the client to put the property on the market with a reliable estate agent.
- Check that suitable alternative accommodation is available.
- Once it has been decided to put the property on the market, write and inform the creditors of this and ask them to withhold interest charges or any other action until sale prices are available. Creditors may require a letter from an estate agent and, if a confirmation of a request to sell a property is available, this can be photocopied and sent. They may also want a letter from the client's solicitor confirming their share of the proceeds of sale to be forwarded directly to them.

## Voluntary charge

Occasionally, but only as the 'lesser of two evils', it is advisable to turn an unsecured loan into a secured one to prevent any further action being taken. This is a very high-risk strategy and should not be undertaken lightly. It is described on here.

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