



Good Judgments

**The value of Judgments reaffirmed
through their use in
debt recovery and
risk assessment**

Peter Welch

December 2008

Foreword

When we were approached to help Registry Trust Limited with this research, lenders were operating in an entirely different economic climate and the desire to better understand the value of county court judgments has proved to be remarkably prescient.

The BBA has been happy to participate in Peter's study and both the analysis and findings make interesting reading for all those interested in the mechanics of credit underwriting. And, of course, it is always pleasing to see that lenders are reluctant to chase their debts through the courts and see this as a last rather than a first resort.

This report, I am sure, will provide valuable insights for lenders and policy makers as the economic cycle continues to turn.

A handwritten signature in black ink, appearing to read 'Eric Leenders', with a long horizontal line extending to the right.

Eric Leenders
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Report prepared for Registry Trust Limited and British Bankers' Association

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Executive Summary

Market context

- Recent developments in the use of judgments for both debt recovery and risk assessment need to be seen in the context of a consumer credit market undergoing significant adjustment following a decade of rapid growth. Lenders have experienced much higher arrears and write-offs since 2005, with a further deterioration in credit quality since mid-2008 following the financial crisis.

The use of judgments in debt recovery

- Lenders remain reluctant to litigate, continuing to see it as a “last resort” in debt recovery. While the number of claims and judgment registrations grew during 2005 and 2006, the increase was lower than the increase in write-offs. Judgment registrations then fell slightly during 2007, though rose during Q3 2008 as the credit crunch took hold.
- Court fees for the commencement of proceedings have changed little during recent years and were reduced from October 2007. More generally, the Government plans to eliminate the over-recovery of court costs from fees for undefended debt cases.
- The main development in the enforcement of judgments has been a rapid growth in charging orders, reflecting the increase in property prices.
- Looking ahead, the Tribunals, Courts and Enforcement Act of July 2007 makes important changes to the enforcement of judgments, notably in the regulation of bailiffs, financial thresholds for charging orders and fixed schedules for attachment of earnings orders. However, many of the crucial details will depend on secondary legislation under the Act.

The use of judgment records in risk assessment

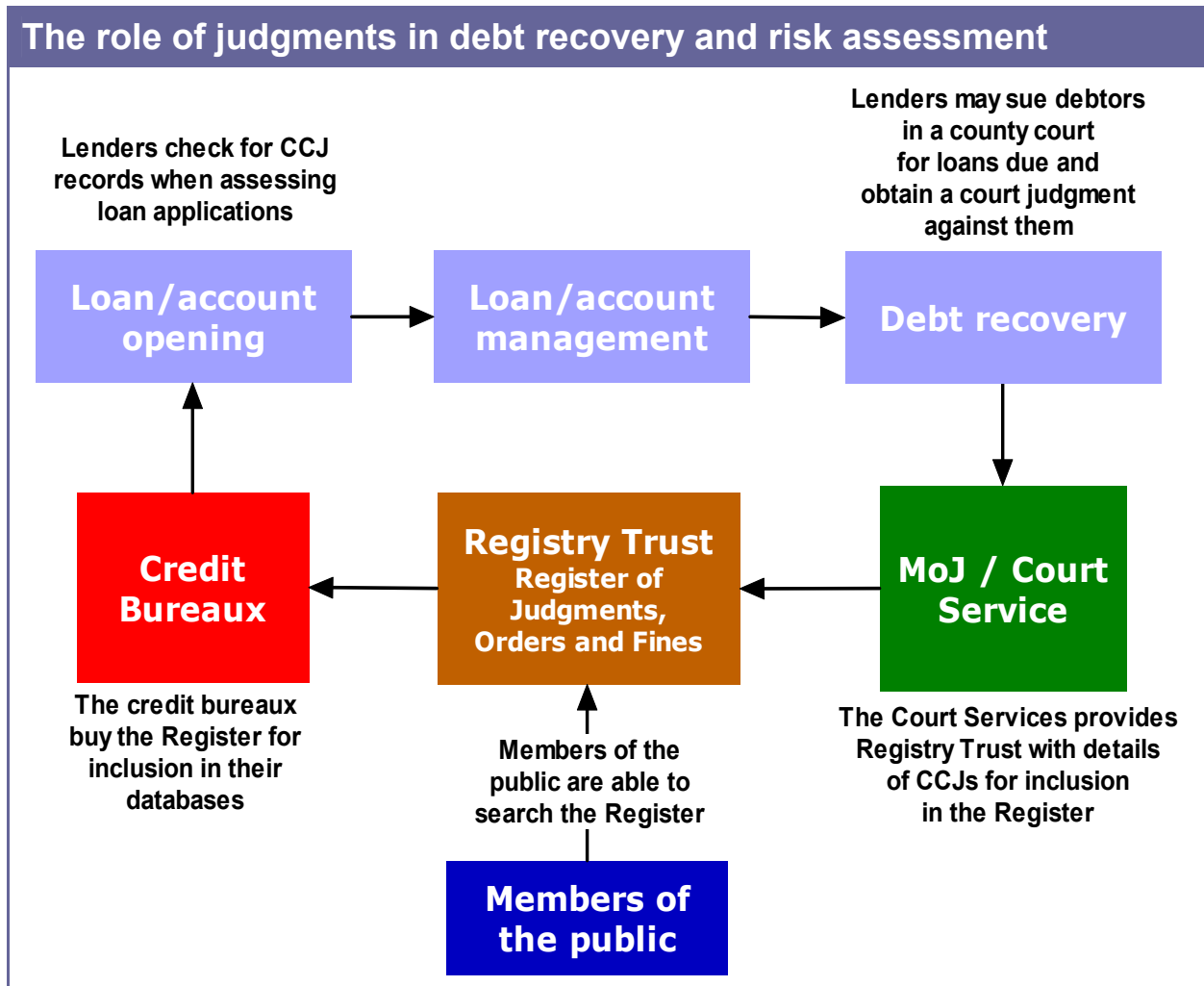
- With greater information sharing by banks and other lenders, judgment records assume a particular importance for applicants who otherwise have “thin” files at the credit bureaux.
- However, lenders and scorecard developers emphasise that judgment records remain central to risk assessment across the range of applicants despite the growth in data sharing.
- And the rise in write-offs and the current credit environment reinforce the importance of judgment records as lenders fall back on basic principles of risk assessment.

Introduction

This report examines recent trends and developments affecting lenders' use of county court judgments (CCJs).

CCJs play an important role in both the recovery of existing consumer loans and the assessment of applications for new loans:

- Lenders may take legal action against borrowers as part of their attempts to recover outstanding debts, and
- Lenders use the CCJ records that result from litigation as part of the assessment process for new loans and other credit products.



The purpose of the report is to examine recent developments in the use of litigation in debt recovery, and the role and value of the resulting judgment records in responsible lending.

The report is based on a mixture of desk research and detailed interviews with people in the credit industry with expertise in the relevant areas. The purpose is to build up an overall picture on developments in the use of judgments rather than look in depth at specific points of detail.

Given the separate trends and issues related to commercial judgments, this report only covers consumer judgments. And given the differences between England and Wales on

the one hand and Scotland on the other, the report concentrates on County Court Judgments in England and Wales.

The report is structured as follows:

1. Section one sets the context by detailing recent developments in the consumer credit market that affect lenders' use of judgments in both debt recovery and risk assessment.
2. Section two examines the factors affecting the use of litigation in debt recovery. This includes both factors that have affected the use of litigation during recent years and the possible implications on future use of the Tribunals, Courts & Enforcement Act 2007 and other recent developments.
3. Section three examines the factors affecting the use of judgment records in risk assessment.

The concluding remarks reflect on the main themes and their implications.

The author would like to thank all those who kindly took part in interviews and provided information for the preparation of the report.

1. Market context

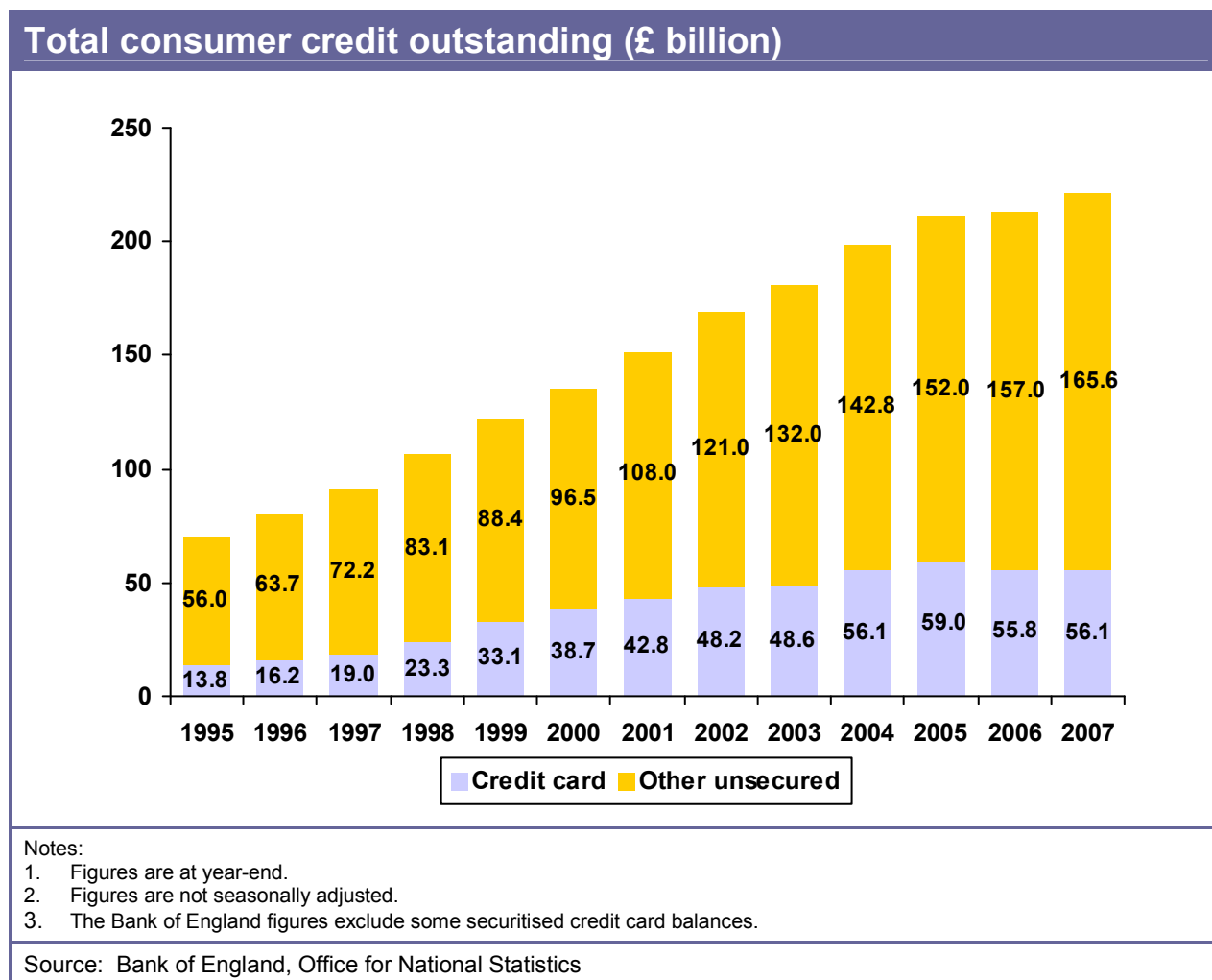
This section of the report offers a brief overview of recent developments in the consumer credit market. This helps to set in context developments in the use of litigation in debt recovery and use of judgment records in risk assessment.

The overview highlights two characteristics of the market relevant to an assessment of the role of judgments:

- The rapid growth in unsecured consumer borrowing during the decade to 2005
- The growth in arrears and write-offs in unsecured consumer borrowing since 2005

1.1 Trends in total consumer borrowing

In the decade to 2005, unsecured consumer borrowing grew at an unprecedented rate. Total consumer credit outstanding (credit cards and other unsecured consumer borrowing) trebled in nominal terms between the end of 1995 and the end of 2005, increasing from approximately £70 billion to over £210 billion.



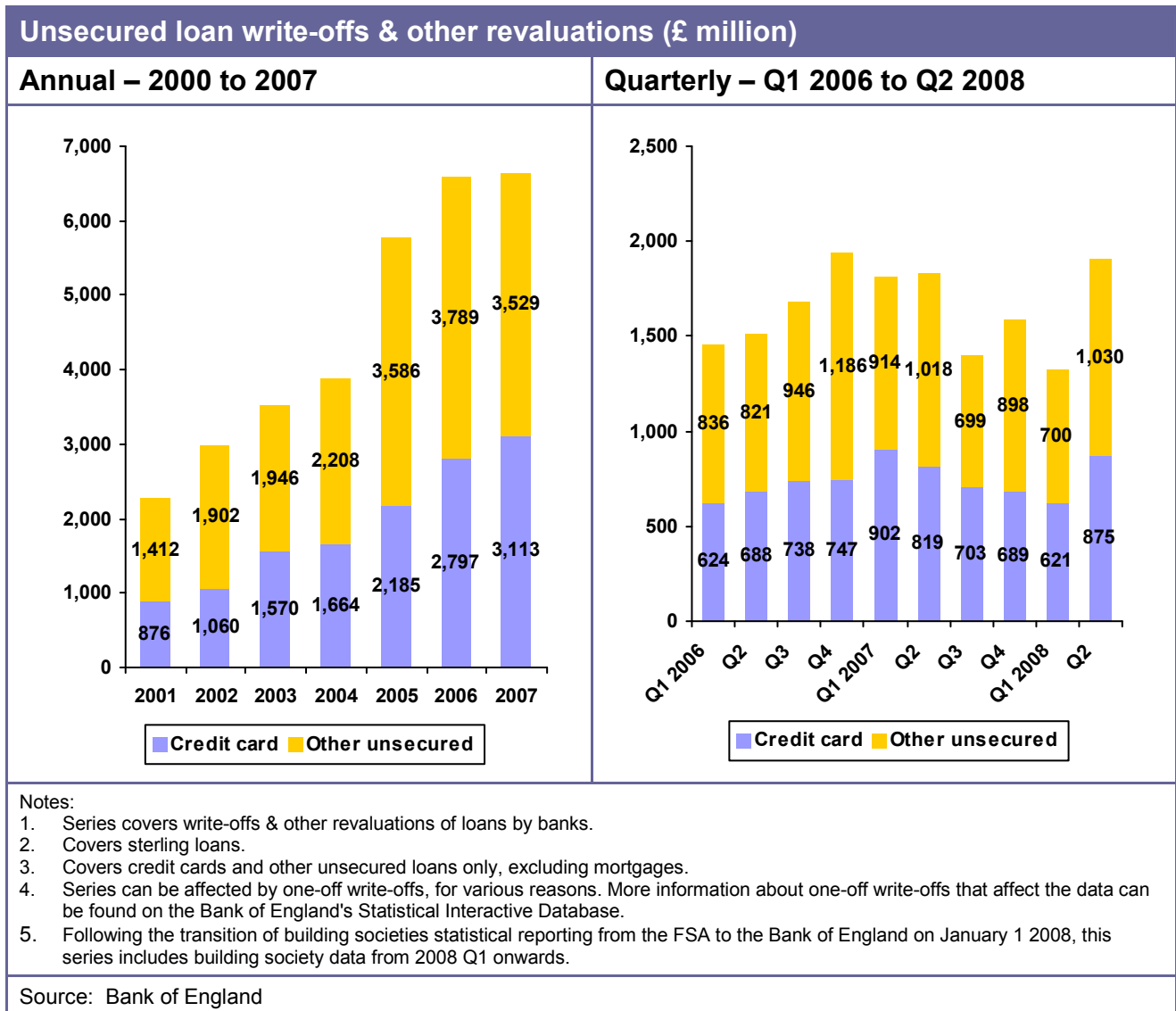
However, since early 2006 unsecured consumer borrowing has largely stabilised (though it did show increases during the third and fourth quarters of 2007). The value of credit outstanding at the end of 2007 was 5.1% higher than at end 2005.

1.2 Growth in consumer credit write-offs

Following the rapid growth in borrowing overall, the second important market characteristic has been the rapid growth during the last five years in credit losses on unsecured consumer borrowing.

Increase in write-offs from 2005

The Bank of England statistics on bank write-offs are probably the best overall publicly available indicator of trends in credit quality and credit losses on unsecured lending. The Bank of England data shows that write-offs on credit cards and other unsecured loans to individuals rose from £2.3 billion in 2001 to £6.6 billion in 2006.



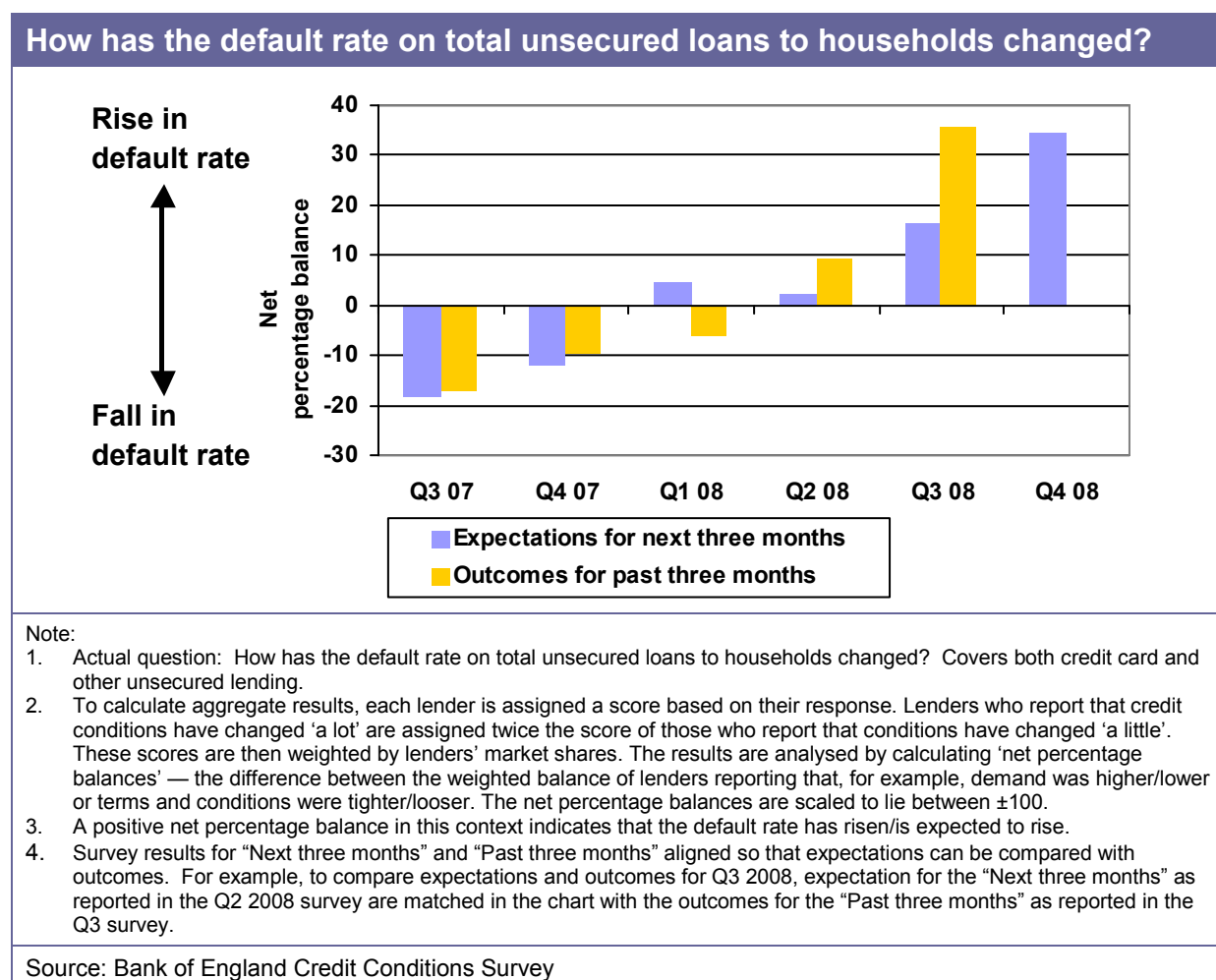
The growth in write-offs was strongest during 2005 and 2006. Write-offs increased from just under £3.9 billion in 2004 to almost £5.8 billion in 2005 and almost £6.6 billion in 2006. Overall, unsecured loan write-offs by banks in 2006 were almost three times higher than in 2001.

In contrast to the early 1990s when the consumer credit industry last experienced a downturn, the increase in write-offs was not due to an economic recession. Loan write-offs rose from 2005 despite strong economic growth, high employment levels and low inflation in the UK.

The most recent data suggests that write-offs stabilised during 2007. Write-offs in 2007 were only a little higher than 2006. And write-offs in the third and fourth quarters of 2007 and first quarter of 2008 were lower than during preceding quarters. Corroborating this, the large UK clearing banks reported flat or slightly lower arrears and impairments on unsecured lending during first half 2008.

Impact of financial crisis

However, the stabilisation and slight decline in write-offs from 2006-07 largely pre-dates any impact from the current crisis in the financial markets and the fall in UK house prices. Consumer lenders now appear to be experiencing a second round deterioration in the quality of their unsecured loan portfolios that is directly linked to the economic downturn and rise in mortgage problems.



This may be the reason for the increase in unsecured loan write-offs evident in the second quarter of 2008. Further, according to the latest Bank of England Credit Conditions Survey for Q3 2008: "Lenders reported a larger-than-expected increase in default rates on unsecured lending over the past three months (see chart). Losses on unsecured loans in default were also reported to have risen. Both were expected to increase further."

2. The use of litigation in debt recovery

This section of the report examines the use of litigation in debt recovery. It covers both:

- Recent developments in the use of litigation, and
- Possible changes from the Tribunals, Courts and Enforcement Act 2007, PANs and changes to time limits.

A. Recent developments

2.1 Overview

The following chart maps the trends for key indicators of creditors' use of litigation for the period from 2001 to 2007 in England and Wales. The chart covers:

- Specified "money" claims, an indicator of creditors taking legal action against debtors
- Default judgments, an indicator of judgments entered against debtors, and
- Consumer judgment registrations, reflecting the entry of judgments on the register at Registry Trust.

As one would expect, the three series show a broadly similar pattern. While volumes continued to fall in the period 2001 to 2003/04, they rose during 2005 and 2006. During 2005, specified "money" claims and default judgments showed a significant increase. This was followed by a large increase in consumer judgment registrations during 2006. However, though remaining well above the levels recorded in 2004, the number of claims, default judgments and registrations all fell during 2007 (though trends are complicated by the impact of changes in policy by DVLA and HMRC towards litigation).

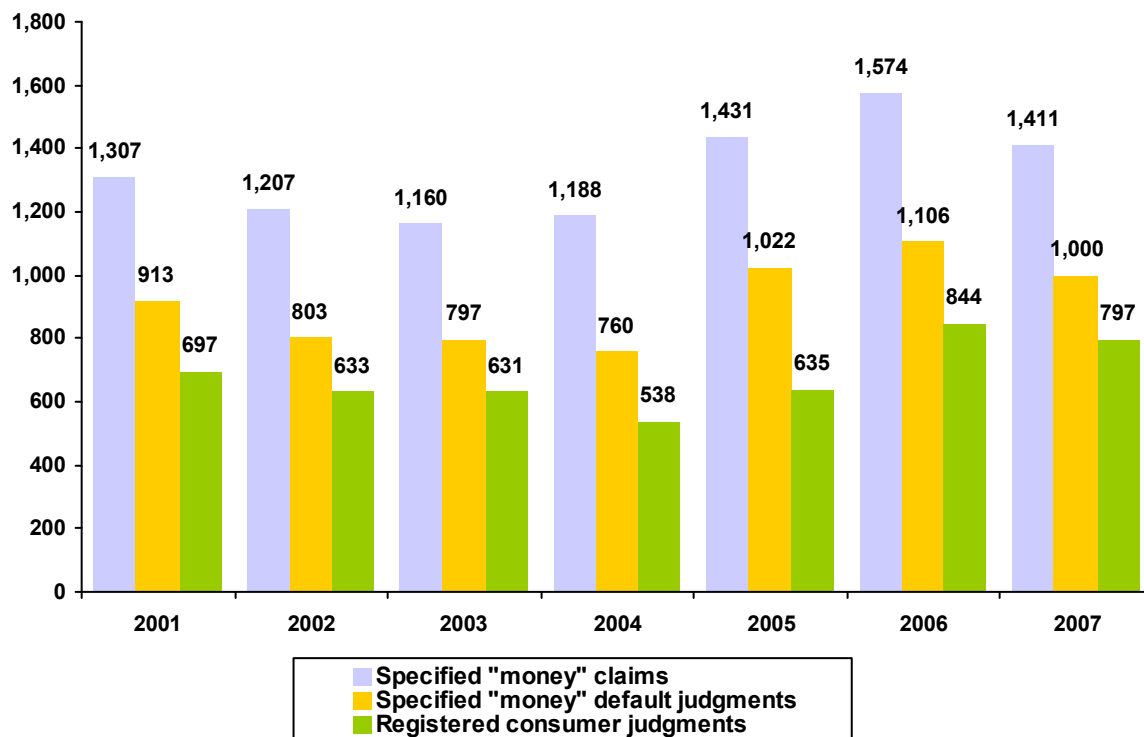
The recent trends in claims and judgment registrations need to be seen in the context of the significant increase in the volume of consumer debt under collection. The data on claims, judgments and registrations is not directly comparable with the Bank of England data on write-offs set out in the previous section. The former covers the number of claims, judgments and registrations while the latter covers the value of write-offs. However, it is noteworthy that the increase in claims and judgment registrations during 2005 and 2006 was much less in percentage terms than the increase in write-offs.

According to the Bank of England data, the value of credit card and other unsecured loan write-offs by banks in 2006 was 70% higher than in 2004 and almost three times higher than in 2000. In contrast, the number of specified "money" claims in 2006 was only 32% higher than in 2004 and 8% higher than in 2000. This suggests that the rise in problem debts only partly resulted in an increase in claims and judgments, with creditors remaining cautious about litigation and using pre-litigation approaches to recovery where possible.

Despite the fall in the number of claims in 2007, it is noteworthy that higher value claims accounted for a larger proportion of total claims than in previous years. The percentage breakdown of specified "money" claims by value band showed no significant changes between 2002 and 2006. Approximately 50% of claims by number were for a value of up to £500, with approximately 15% for a value of between £500 and £1,000, and 22-24% for a value of between £1,000 and £5,000. However, in 2007, the number of claims for a value of up to £500 fell to 41% of the total while the number for a value of between £1,000

and £5,000 rose to approximately 28%. Claims for a value of between £5,000 and £15,000 also rose from less than 9% of the total number of claims in 2006 to almost 11% in 2007.

Specified “money” claims and default judgments (000s)



Notes:

1. Statistics cover England and Wales.
2. Specified “money” claims: Claims issued for a specified amount of money, including those made through the Claim Production Centre, County Court Bulk Centre and Money Claim Online.
3. The chart does not include unspecified “money” claims. The difference between specified and unspecified is that the specified claims are issued under the default system, whereby the creditor gets judgment by default for the sum if the defendant does not defend. In the case of the unspecified cases the sum has to be proved to the satisfaction of the court, or the court actually decides the amount owing. There were 144,905 unspecified “money” claims in 2007.
4. Default judgments: Following either no response from the defendant within the allotted time period or the claimant accepting the defendant’s offer to pay all or part of the amount owed. Includes default judgments made in the County Court Bulk Centre and via Money Claim Online.

Sources: Ministry of Justice (Judicial and Court Statistics 2007), Registry Trust Ltd

Over 50% of specified “money” claims in 2007 were issued through the County Court Bulk Centre (CCBC), the central processing unit attached to Northampton County Court set up with the Claim Production Centre (CPC) to handle bulk debt collection work which is largely undefended. A further 11% were issued through Money Claim Online, part of the CCBC, through which claims up to a certain value can be issued over the internet. Use of the CPC/CCBC has significantly improved the efficiency of court action for litigators issuing large numbers of claims.

The figures for 2007 pre-date the impact of the financial crisis which, even assuming lenders remain cautious in principle about litigation, is likely to push claims and judgments upwards. HMCS only publishes the data on claims and default judgments annually. However, Registry Trust’s statistics for consumer CCJs show an increase of 17.4% year-on-year in the third quarter of 2008 to 223,519, their highest level since first quarter 2007. This may be an early sign of the impact of the financial crisis.

2.2 The place of litigation in debt recovery

The slower growth in court action compared to write-offs during 2005-07 indicates that lenders continue to litigate reluctantly.

Given the rise in arrears and credit losses, there is unsurprisingly a greater urgency to collections. This is evident both in earlier contact with customers and in the greater use of debt collection and debt sale. Rather than waiting for perhaps two missed payments, banks are quicker to make contact with customers when accounts fall into arrears. Indeed, through so-called pre-delinquency management (PDM) capabilities, lenders seek to target customers showing an increased likelihood of financial stress even before any arrears (see below on discussions at SCOR on using data to improve the identification of such customers).

Despite the greater urgency, banks in particular face the reputational risk of aggressive litigation and continue to prefer informal arrangements. They are obliged to demonstrate that customers in financial difficulty are treated fairly.

The Banking Code of March 2005 already obliged subscribers to “consider cases of financial difficulty sympathetically and positively” (Section 14.1). And with borrower cooperation, Code subscribers will “develop a plan” for dealing with the financial difficulties (Section 14.2).

In 2005/06 and 2007, there were two themed reviews by the Banking Code Standards Board (the second as recently as September 2007) of the way Code subscribers treat customers who are in financial difficulties. These have been followed by a new version of the Banking Code, issued in March 2008. Section 14 of the Guidance to the Code requires banks to proactively contact customers whom the bank feels, from the information available to it, may be heading towards financial difficulty. The bank will encourage customers to make contact and provide information on sources of free independent money advice.

Further, Government policy has been to keep inappropriate cases out of court. The Practice Direction on Protocols supporting the Civil Procedure Rules (CPR) states that parties should follow “a reasonable procedure ... to avoid litigation”, and sets out in very general terms what claimants are expected to do before issuing a claim. This would ‘normally’ include sending a letter before action. Where in the view of the court the claimant has not taken the appropriate pre-action steps, cost sanctions may be imposed.

Several of those interviewed commented that the greater sharing of data through the credit reference agencies by banks (see below) improves their ability to manage accounts and identify potential cases of overcommitment by customers. SCOR (Steering Committee on Reciprocity) is currently debating access to raw positive data for consumers showing signs of early financial stress (see Section 4).

The growth in alternative arrangements – notably IVAs and Debt Management Plans (DMPs) – has also been a significant factor in limiting the growth in litigation despite the large increase in the volume of debt in recovery.

Litigation was described by one bank “as a tool to show we are serious”. Often the threat of proceedings is used to encourage a response and make arrangements with unresponsive borrowers. Debtors who are otherwise unresponsive may well respond to receiving a solicitor’s letter. However, despite its use as a threat, one lender emphasised

that litigation then has to be pursued in cases where borrowers continue to refuse contact – otherwise “word gets around and the threat has no recovery value”.

In a 2001 report for Registry Trust on debt recovery, reference was made to more sophisticated profiling of debtors by creditors to identify the most appropriate recovery procedure and so maximise the possibility of successful recovery through litigation. However, views are mixed on the extent to which recovery strategies can be tailored to borrower characteristics. In practice, the use of litigation is “still a bit of a blind business” according to one creditor. Even the additional information that may become available from implementation of the Tribunals, Courts & Enforcement Act (see below) will only be available to the courts, and will be of limited use in terms of pre-planning.

The growth in non-bank finance companies and greater use of debt collection agencies and debt sale has seen non-bank creditors become significant collectors of consumer debt. There is some suggestion that the non-bank finance companies are more likely to move to litigation, though others question this. Certainly, the judgment data for Northern Ireland, where the plaintiff is identified, shows finance companies among the most active plaintiffs. So far as debt purchase companies are concerned, a leading company in the sector emphasised that even at the end of the letter cycle it will seek an informal arrangement with a debtor ahead of initiating legal action.

In reality, data is not available to draw firm conclusions on differences in behaviour between categories of creditor. The collection of data for England and Wales on judgments by category of plaintiff would help to clarify whether there are noticeable differences between sectors in the use of litigation.

Creditor petitioned bankruptcy is an option open to creditors for unsecured debts of £750 or more (this is due to rise to £1,500 from October 1 2009). However, it remains sparingly used given the obligations under the Banking Code, the costs, the perceived complexity of the procedures and, historically, concerns about the wider reputational risks to lenders of forcing bankruptcy. Though the numbers have increased, creditor petitioned insolvency remains small in the context of the total debt recovery market.

According to the Ministry of Justice’s Judicial and Court statistics, there were only 11,327 creditor petitions for individual bankruptcy in 2007. This compares with over 49,000 debtor petitions for individual bankruptcy and over 1.4 million specified money claims. However, as with litigation, the threat of bankruptcy is sometimes used as a means of applying pressure on unresponsive borrowers.

2.3 Court fees

The level of court fees has historically been an important factor in lenders’ decisions on whether or not to litigate. Focusing in particular on fees for the commencement of proceedings, court fees have fallen in real terms during recent years, reducing the cost of initiating legal action to lenders (though, as noted above, there are other reasons why creditors remain reluctant to litigate).

The changes in court fees for the commencement of proceedings are tabulated in Appendix 2. Looking at commencing proceedings for the recovery of £1,000 to £5,000 through the Claim Production Centre, the cost changed little between 2000 and 2007. Though the fee rose from £108 to £113 in April 2003, it then fell to £110 in January 2005.

Further, in January 2005, the discount for the bulk issue of claims through the Claims Production Centre was increased to £10.

And fees for the commencement of proceedings have fallen significantly from October 1 2007 as part of the introduction of three new bands covering the range £1,000 to £5,000 (though with higher fees for hearings at debt trials). Allowing for the introduction of new claim bands, fees for commencement of proceedings were reduced for all bands for CPC cases and for all bands bar one (less than £300, which remained unchanged) for non-CPC cases.

The reduction in fees may make lower value claims more economic. For example, from October 1 2007, the fee for claims of under £300 for CPC cases has been reduced from £20 to £15. One specialist solicitor commented that there may be an increase in issuance on small value debts where creditor assesses that the customer can afford to pay.

In the large majority of cases, the court enters judgment by default. For example, default judgments accounted for just under 68% of specified “money” claims issued in 2006 (a proportion which to some creditors appears too low). However, it is worth noting that court fees remain a factor in cases where the borrower makes a token offer to pay that is accepted by the court. As one company commented, if the judge accepts an offer to pay of £1 a month, it can take 100 months to get our legal fees back.

The reductions in fees for the commencement of proceedings in October 2007 followed, and were proposed in HMCS’s Civil Court Fees Consultation Paper of April 2007 (CP 5/07) (in fact some of the fee reductions for non-CPC cases were greater than those proposed). In the paper, HMCS stated that the current fee structure for civil business “is heavily front-loaded onto the issue stage, with the fees charged at later stages of the court process covering only a small proportion of the cost of those cases that proceed to a full hearing” (CP 5/07, Chapter 3, paragraph 2, p23). As a result, the current system is heavily dependent on the volume of issue fees on undefended debt claims:

“At present, the issue fees paid in undefended debt claims are significantly subsidising the rest of the system. These are mainly paid in the first instance by bulk creditors, such as credit card and utility companies, but are then added to the defendant’s judgment debt. Most defendants in these cases are being sued for less than £500.” (CP 5/07, Chapter 3, paragraph 3, p23)

If the creditor fails to recover the judgment debt, the costs will also remain unpaid.

The Government’s objective is to re-balance the fee structure for civil business in the main civil courts to create a closer relationship between the fees charged and the cost of different stages of the process. This involves hearing fees for civil cases and adjustments to other downstream fees, and reductions in issue fees for civil business.

According to the consultation paper, overall net fee income from civil cases in 2005/06 (not just debt claims) was almost £336 million, with a surplus of more than £34 million (excluding magistrates’ courts). Fee recovery was therefore 115% compared with a target of 100%. The Government plans to eliminate any over-recovery on civil fees over the spending review period to 2010/11.

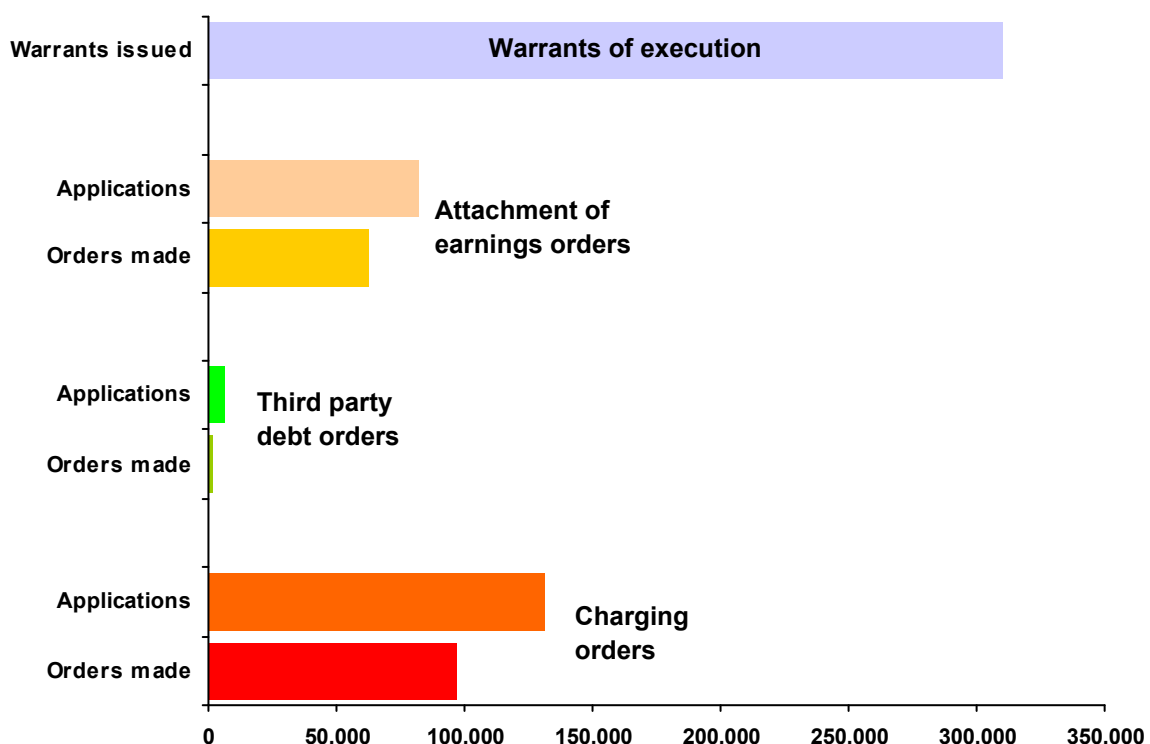
2.4 Enforcement of judgments

There are four main methods of enforcing judgments in the county court, each aimed at some aspect of the defendant's assets or income:

- **Warrants of execution** are targeted at goods owned by the defendant. They allow saleable items owned by the debtor to be sold unless the amount due under the warrant is paid.
- **Attachment of earnings orders** are targeted at the defendant's wages or salary. They oblige the debtor's employer to deduct a set sum from the debtor's pay and forward it to the court.
- **Third party debt orders** are targeted at savings of the defendant. They secure payment by freezing and then seizing money owed or payable by a third party to a debtor.
- A **charging order** prevents the defendant from selling his or her assets (such as property, land or investments) without paying what is owed.

Warrants of execution remain the most widely used means of enforcement. Numbers have fallen to below 350,000 during recent years, with some suggesting that this is partly because most judgments based on regulated agreements can still only be executed by county court bailiffs, who also collect criminal fines. However, there were still over 300,000 warrants of execution issued in 2007.

Enforcement of judgments in England and Wales (2007)



Notes:

1. Attachment of earnings orders: Includes the making of varied orders and suspended orders enabling the debtor to make payments into court directly but upon failure to do so will result in the debtor's employer being contacted.

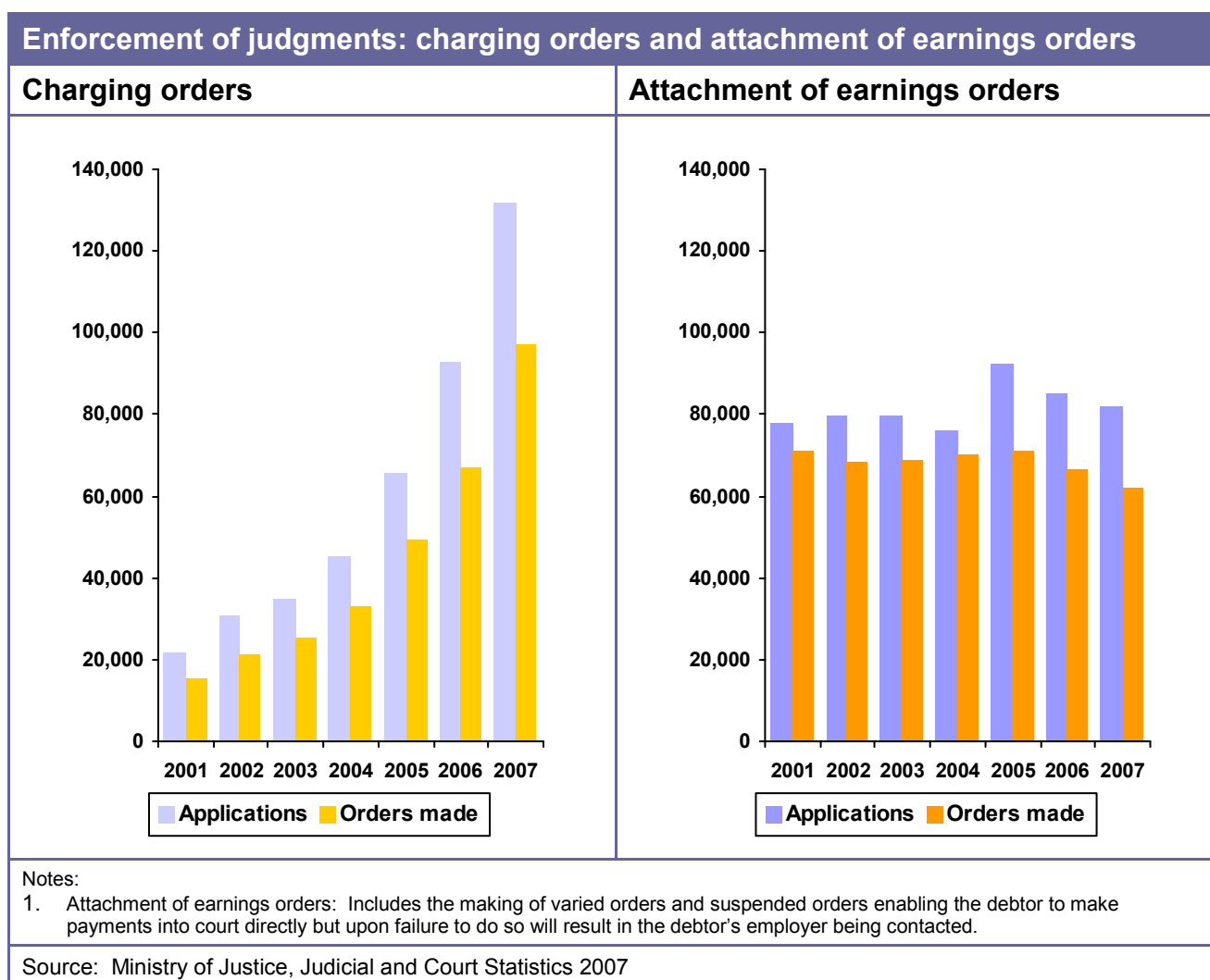
Source: Ministry of Justice, Judicial and Court Statistics 2007

However, the most striking change in enforcement during recent years is the growth in the volume of charging orders (see chart). The number of charging orders made increased sixfold between 2001 and 2007. During 2006, for the first time, there were more applications and orders made for charging orders than attachment of earnings orders. By 2007, the number of charging orders made approached 100,000, more than 50% greater than the number of attachment of earnings orders.

The growth in the use of charging orders reflects above all the rise in house prices and therefore the value of property as security. Rather than seeking to realise the security, the strategy of claimants has often been to secure a charging order and then sit on the charge as an asset, realising the value when the customer re-mortgages. However, with house prices now falling, this raises the question of how exposed some creditors with charging orders might be and whether their use as an enforcement tool is likely to fall.

In cases where the debtor is a home owner with equity in the property, there is some suggestion of competition between creditors in terms of securing their claim.

One large debt purchase company also commented that in some cases it also seeks voluntary orders with debtors. Given that debtors have to break any agreement with the court before creditors can take any enforcement action and debtor offers are accepted by the court in the great majority of cases, a voluntary order may be more effective (though see below for changes under the new Act).



B. Possible changes

2.5 Tribunals, Courts & Enforcement Act 2007

Looking at potential changes to the regulatory environment covering litigation, the most important development is the enactment in July 2007 of the Tribunals, Courts & Enforcement Act 2007.

The legislation makes important changes to the enforcement of judgments. These date back to the Lord Chancellor's Department's March 2003 White Paper *Effective Enforcement: Improved methods of recovery for civil court debt and commercial rent and a single regulatory regime for warrant enforcement agents*.

The Act is divided into eight parts. The most relevant to this review is Part 4 (Enforcement of Judgments and Orders), which covers the changes to attachment of earnings orders and charging orders, as well as the new provisions on information requests.

Part 3, which includes the changes to the regulation of bailiffs, also has some relevance, as does Part 5, which covers the various measures designed to improve and extend the current range of options available to assist debtors with relatively low levels of income and debts. Chapters 1 and 2 of Part 5 cover reform of the Administration Order (AO) and introduction of an Enforcement Restriction Order (ERO). Parts 3 and 5 of the Act are summarised in Appendix 3.

However, the full implications of the changes to be introduced under the 2007 Act are not yet clear given that many of the provisions most relevant to creditors will be implemented by secondary legislation which remains undrafted at the time of writing.

"Much will depend on the secondary legislation. Creditors need to be vigilant."
(Major retail bank)

Charging orders

The new Act makes various amendments to the Charging Orders Act 1979. Following the new Act, it will be easier for creditors to obtain charging orders (Part 4, Sections 93-94).

At the moment, creditors can only obtain charging orders when the debtor is in arrears. The judge who considers an application will not make an order unless the judgment debtor has failed to pay the amount of the judgment when it was due; or has failed to pay one or more of the instalments due under the terms of the judgment.

Following the Act, creditors can obtain charging orders whether or not the debtor is in arrears (though, if there has been no default in payment of the instalments, the court must take that into account when considering the circumstances of the case). This will move England and Wales closer to Scotland where creditors can secure a letter of inhibition (or other means of enforcement) even if the debtor has not broken a decree to pay by instalments.

However, by regulation, HMCS will be able to set the amounts on which creditors can issue charging orders. Section 94 of the new Act gives the Lord Chancellor the power to set by statutory instrument financial thresholds for charging orders.

There is currently no minimum balance for charging orders in contrast with the £750 minimum balance for bankruptcy (with this due to rise to £1,500 from October 1 2009), with considerable District Judge discretion. If the minimum balance is too high on charging orders, the fear is that it might push creditors towards bankruptcies and/or be more aggressive in seeking the sale of the debtor's property to crystallise the charge or encourage the debtor to pay.

Much will depend on the detail of the regulations. One creditor suggested that the regulations may allow charging orders for a relatively small sum in the case of utilities which have to supply. In contrast, banks may be faced with a higher threshold above which charging orders are permitted.

Attachment of earnings orders

The new Act also affects attachment of earnings orders (Part 4, Sections 91-92), with various amendments to the existing Attachment of Earnings Act 1971.

Orders will be based on rates set in bands (Section 91 Attachment of earnings orders: deductions at fixed rates), which should be easier for the Court to calculate.

Attachment of earnings orders will also be movable to new employers under the legislation (Section 92 Attachment of earnings orders: finding the debtor's current employer), making them more attractive to creditors.

Information requests and orders

The Act also contains provisions for the Court to obtain information from relevant Government departments when a creditor seeks enforcement (Part 4, Sections 95-105).

If a creditor in relation to a judgment debt makes an application for information under the new Act, the relevant court may, in relation to the debtor, make one or more of:

- A departmental information request
- An information order

Creditors are already able to seek an order to obtain information ahead of taking any enforcement action. Under this procedure, the judgment debtor is ordered to come to the court to be questioned, on oath, by a court officer on their employment status, income and other relevant financial information.

The new Act also introduces a departmental information request – a request for the disclosure of information held by, or on behalf of, a government department.

A power of the court to seek relevant information on the debtor from government departments (for example, information on income tax, VAT, utility bills) might be potentially helpful in the enforcement of judgments. However, according to the Ministry of Justice, there will be tight controls on departmental information requests. The courts will not obtain this kind of information as standard, and will be limited in what they will be able to obtain.

2.6 PANs

Among other important developments, one of the ideas piloted by HMCS has been a Pre-Action Notice (PAN) intended to encourage engagement by debtors in advance of litigation. The PAN was piloted nationally for 12 months, from October 2005.

However, in the words of one creditor, PANs appear to have “died a death”. Given the overall lack of increased engagement compared to the current procedures followed by those creditors taking part in the pilot, and the additional potential costs, the HMCS concluded that “we do not feel that there is any justification for the introduction of this mandatory system” (see Ministry of Justice & HMCS Consultation Paper CP 22/07, *The debt claim process: helping people in debt to engage with the problem*).

According to one leading solicitor in the field, PANs were based on the false premise that creditors are desperate to sue and failed to recognize the work already undertaken to engage the debtor prior to litigation. In August 2008, the Ministry of Justice announced it is pressing ahead with plans for creditors to give people owing them money information on how to contact them to discuss problems, including details of independent free advice providers in a letter before taking legal action.

2.7 Time limits

A potentially much more serious development floated by HMCS is reducing the time permitted for the recovery of debts from six to three years.

If the limitation came in, the consensus is that it would have a drastic effect, with lenders using collection agencies earlier, selling debt earlier and suing earlier in the collections process. A three year statute of limitation on debt recovery also raises the prospect of a corresponding reduction in the time judgment records are held by Registry Trust and the credit bureaux.

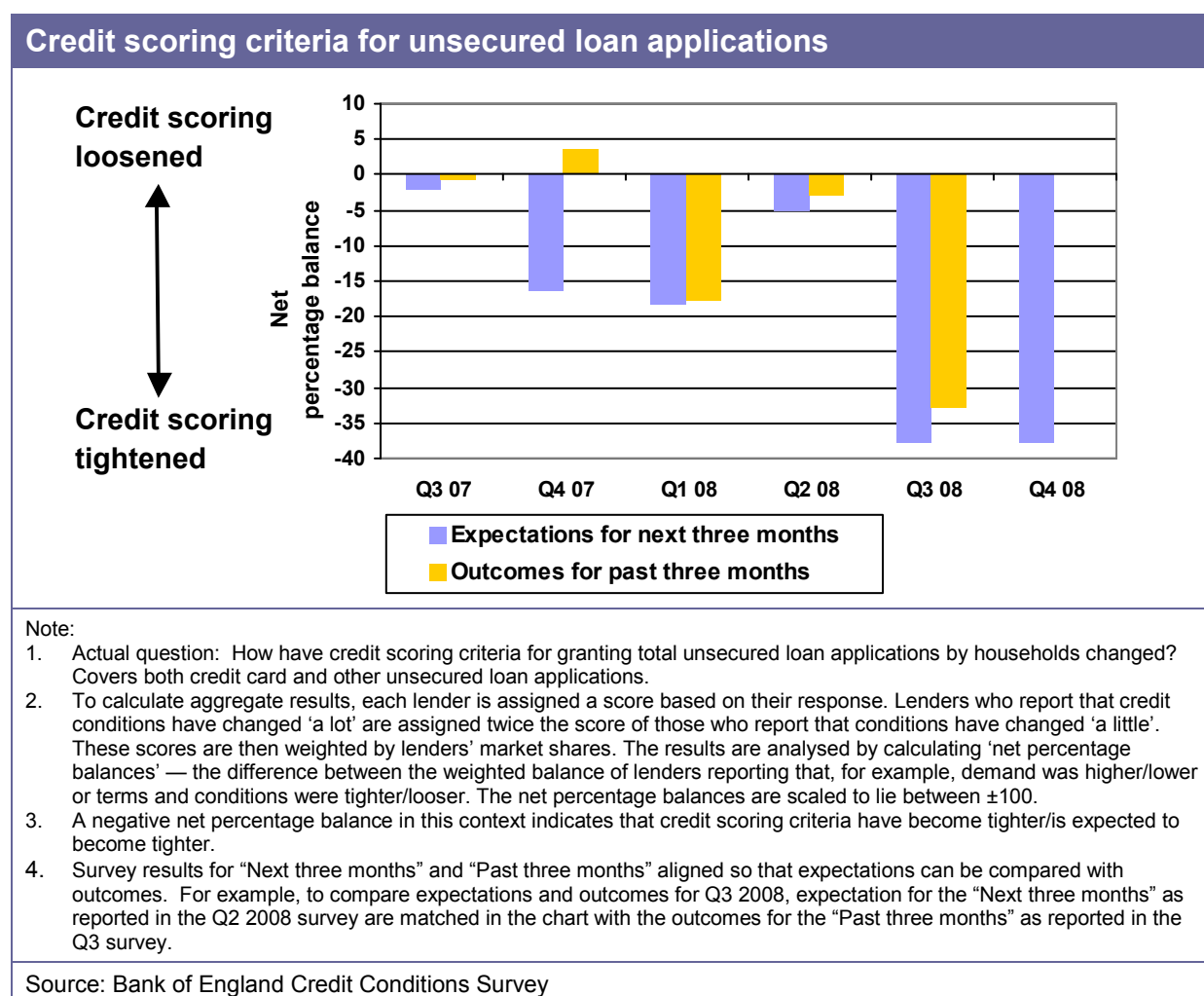
However, there remains an air of uncertainty about the proposal with lenders more relaxed than when they were first voiced. Latest reports indicate that a consultation by HMCS is still planned, though the date and content are not yet known.

3. The use of judgment records in risk assessment

This section of the report examines developments in the use of judgment records in risk assessment. Despite all the recent changes in the consumer credit market, it is clear from those interviewed that CCJs remain central to the assessment of applications for credit.

3.1 More risk averse environment

The current environment supports the continuing importance of CCJs to risk assessment. Following the rise in consumers' credit commitments and subsequent rise in credit losses documented in Section 1 of the report, lenders have understandably become more risk averse and tightened criteria for new lending. The "credit crunch" in financial markets and decline in UK house prices is only adding to a more cautious approach to lending.



For example, according to the latest Bank of England Credit Conditions Survey for Q3 2008: "In line with their expectations three months ago, lenders reported a reduction in the amount of unsecured credit they were prepared to make available to households and small businesses. Lenders reported that they had implemented the tightening through stricter lending criteria for both credit card and non-credit card borrowers (see chart). These changes were associated with a decline in the proportion of unsecured loan and credit card applications being approved.... Looking ahead, lenders expected a further reduction in overall unsecured credit availability, which would be associated with a further tightening in credit scoring criteria and declines in approval rates."

Lenders are also under greater pressure from policymakers and the media to demonstrate that they are lending responsibly.

For example, the Consumer Credit Act 2006 gives the Office of Fair Trading (OFT) greater powers to consider practices which appear to involve irresponsible lending in its decisions on consumer credit licences. In August 2008, the OFT launched a public consultation on the scope of its project looking at irresponsible lending in UK consumer credit markets. The consultation is the first stage of the OFT's irresponsible lending project. The OFT says one of the key outcomes of the project is expected to be clear guidance on lending behaviours and practices which the OFT considers to be irresponsible.

Section 13 of the Guidance to the latest version of the Banking Code, published in March 2008, requires banks to consider credit reference agency data in assessing all applications for credit. Banks must also consider at least one of:

- income and financial commitments
- the customer's previous financial behaviour; and
- internal credit scoring techniques.

All these factors have encouraged the industry to pay greater attention to indebtedness and affordability in making lending decisions.

3.2 Greater information sharing

There has been a step change in information sharing by banks. Historically cautious about sharing positive data, banks have become strong advocates of its merits. There is now comprehensive data sharing across most main lending sectors. In part, the greater enthusiasm for information sharing reflects the wider array of lenders and growth in non-bank lending, with access to positive data often essential to securing a comprehensive overview of an applicant's existing credit commitments.

To summarise the main developments:

- From end 2003, there has been full sharing of data by banks on card and loan portfolios.
- All banks now share current account data for overdrafts above £1,250, with nearly all banks now sharing data below £1,250 (see Section 8 of the Principles of Reciprocity, version 30, November 2008, for details on the sharing of current account data).
- The big 5 banks now share data which highlights consumers who are in danger of becoming over indebted, which may include income data.
- From December 2008, five major lenders (Barclaycard, Capital One, GE Money, HBOS and MBNA) are to begin sharing behavioural data on credit card use, with other lenders to follow (see Section 9 of the Principles of Reciprocity, version 30, November 2008, for details on the sharing of additional positive data on credit & store cards).
- Also from 2008, data sharing will be extended to encompass home credit (a remedy from the recently completed Competition Commission investigation into the sector).
- Discussions are now taking place on sharing data on equity release loans.

In addition to greater data sharing, there is also greater use of shared data. The use of different categories of data under SCOR (Steering Committee on Reciprocity) rules is summarised in Section 2 of the latest version of the Principles of Reciprocity (version 30, November 2008).

SCOR is now debating access to data as consumers show signs of early stress. This will, if agreed, allow access to raw positive data in specially developed teams, such as money management teams, to deal with individuals that do not necessarily have arrears or CCJs but can be recognised at an aggregated level of showing signs of stress and becoming over indebted.

The improvements in data sharing clearly improve credit assessment. For example, the May 2007 report of the Independent Reviewer to the sponsors of the Banking Codes' Review 2007 quotes one bank as saying that that recent developments in data sharing showed that average unsecured debt for their customers was previously understated by 20-25% and that 40% more of their customers now met their 'highly indebted' criteria. Lloyds TSB commented in its 2006 results release that the increased sharing of industry-wide customer data, particularly with regard to credit card use, had improved its customer understanding and led to a reduction in some credit limits.

The Banking Code Guidance on what factors subscribers should consider in their credit assessments (set out in Section 13 of the Code which covers Lending) was tightened from July 2006. The May 2007 review recommends further strengthening of the Guidance, with Section 13 amended to require all subscribers to share all positive data that may legally be shared.

This recommendation only applies where customer consent to data sharing already exists. Discussions also continue with the Department for Business, Enterprise and Regulatory Reform (BERR, previously the DTI) on sharing non-consenting data following the DTI's consultation of October 2006. However, legislation will be required for this to proceed.

The growth in data sharing greatly increases the volume of information available on credit applicants and raises the question of whether the new data might substitute for existing sources of data such as CCJ records.

3.3 CCJ records and “thin” files

Given this deepening of data sharing, it follows that CCJ records assume a particular importance for applicants who otherwise have “thin” files at the credit bureaux. Greater information sharing increases the gap between data rich and data thin records. For “thin” populations, a leading scorecard developer commented that there is now a huge number of characteristics that you cannot use. In this environment, any CCJ record is particularly important, and there remains a significant population of people with CCJs but not defaults. This is especially the case for younger people with a short credit record.

For example, one of the credit reference agencies supplied Registry Trust with data for the study based on a recent sample of just over 11,000 credit applications. Some 13% of these had one or more defaults and just under 7% had one or more CCJs.

- Of the population having a CCJ, 73% of these also had a default.
- Of the population having a default, 35% of these also had a CCJ.

Due to the more transient nature of individuals with adverse credit histories, the agency used all known linked addresses rather than just their current addresses to search for records. All CCJ records remain registered at the address the individual lived at when the CCJ was originally registered, though unsatisfied defaults can move to a customer's new address should the lender wish to do so. Defaults and CCJs relating to the same debt

may therefore be registered at different addresses.

The credit reference agency emphasised that this data was only indicative. No work was performed to fully validate the findings or fully test the appropriateness of the (relatively small) sample used. Due to the complexity of the work, it had not tried to match CCJs with their corresponding default(s), or vice versa. Complications include the fact that multiple defaults from one lender may result in just one CCJ. Nonetheless, the data does help to illustrate that there remains a significant population, perhaps several hundred thousand, of bureaux files with CCJs but not defaults.

3.4 CCJ records and wider risk assessment

Continuing value

Despite the deepening of data sharing, the clear message from the banking sector and scorecard developers is that CCJ records remain vital across the range of applicants and not just for those with “thin” files.

A leading scorecard developer commented that he has not noticed a decrease in their value, with CCJs still contributing strongly to the discrimination of scorecards.

“In my experience, 10-15% of the predictive power of scorecards comes from judgment data, depending on product and target population. And this hasn't changed significantly over the last 10 years.” (Leading scorecard developer)

The message from the banking sector is the same.

“Banks are now looking at every bit of data they can get. But this doesn't affect anything around how we value CCJs.” (Major retail bank)

The greater volume of data gives lenders a much fuller picture when managing existing accounts. They can see earlier when customers are at risk of becoming indebted. However, CCJs still remain essential to assessing first time applications.

Judgment and default records

Despite the much greater availability of shared data on people in arrears through to default, it was emphasised that people may still recover from 3-4 payments down. In most cases, a CCJ may be preceded by a default (though see above on the significant minority of files with a CCJ but no default). But a default record compared to a satisfied CCJ record and unsatisfied CCJ record continue to capture different levels of risk and so help the discrimination of scorecards.

The term “default” is used to refer to a situation where the lender in a standard business relationship with an individual decides the relationship has “broken down”. However, it was noted that in practice this still may result in differences between lenders on when a loan or account has fallen into default, so affecting its scoring efficiency. In contrast, CCJs tend to be more consistent. In August 2007, the Information Commissioner's Office (ICO) released a new set of best practice guidelines to encourage greater consistency among creditors when filing default information.

The continuing value of CCJ records even with an accompanying default indicates that judgment records remain vital in typifying and identifying a particular kind of customer behaviour. Specifically, judgment records continue to identify customers that wilfully

ignore communication with their creditors and/or have a complete “head in the sand” mentality when faced with repayment problems (as evident from the fact that the majority of judgments are entered in default), but whose circumstances (for example, earnings or ownership of a property or other assets) justify litigation by creditors. In capturing this behaviour, judgment records continue to provide additional discrimination in lenders’ scorecards.

Lending policy to those with CCJ records

Previous research for Registry Trust highlighted that many lenders had become more sophisticated in their use of judgment information. While in some circumstances a judgment might still be grounds for a policy reject, in others the Judgment may be scored depending on factors such as its age, value and any satisfaction.

This latest exercise indicates that each lender’s approach depends on its position in the market and tolerance of risk. However, the rise in risk aversion and pressure on lenders to demonstrate responsible lending is likely to have increased the proportion again treating a CCJ record, and particularly an unsatisfied record, as grounds for rejection. A major retail bank commented that the only circumstances in which further lending to an applicant with a CCJ might be deemed responsible would be a consolidation loan, with the CCJ then used to assess what level of debt and what type of loan are appropriate (under the Banking Code Guidance, where a consolidation loan is being provided and the subscriber considers the customer to be in financial difficulties, the subscriber should reduce or pay off the existing in-house borrowing that it is aware is being consolidated).

However, for those operating in the near-prime and sub-prime segments, CCJ records (as public records unlike most of the other data held by the credit bureaux) remain important as a possible means of *identifying* potential customers. For example, customers with an old CCJ record on their file (particularly those close to the somewhat arbitrary six-year expiry date for judgment records) but subsequent evidence of recovery (eg a satisfaction) may actually be good prospects for those in the near-prime and sub-prime segments. In the more risk-averse conditions now characterising the consumer credit market, it will be important both that:

- credit from reputable providers remains accessible to such customers as part of their economic rehabilitation, and that
- lenders operating in this segment assess applicants with old CCJ records intelligently and responsibly.

Other findings

One further specific point worth noting from the research is an observation that the gap between those people with CCJ records and those with insolvencies/bankruptcies has narrowed. Historically, candidates with insolvencies/bankruptcies were higher risk than those with CCJs. However, according to a leading scorecard developer, this gap has decreased over recent years to the point where there is now very little difference in the UK population. Indeed, in some sub populations, the risk associated with CCJs is now even higher.

4. Conclusions

Summing up, there are two main points to make in conclusion.

First, the research confirms that litigation is something that lenders pursue reluctantly at the end of the debt recovery process. This is evident from the fact that judgment registrations grew much more slowly during 2005 and 2006 than the rise in consumer credit write-offs.

But this reluctance gives sharp definition to the role of litigation in the recovery process. In the words of one retail bank, the value of a judgment against someone is very clear – namely that a creditor had to go so far as to sue you to recover their money.

Second, a more discriminatory use of litigation in the recovery process translates into a continuing value for judgment records in the assessment of credit applications. Despite the growth in data sharing, it is noteworthy that those consulted remain unequivocal about the continuing importance of judgment records to risk assessment.

Secondary legislation drafted under the new Tribunals, Courts & Enforcement Act may affect lenders' overall approach to litigation as well as specific decisions on enforcement. However, this is unlikely to change the continuing importance of judgment records to risk assessment. Indeed, in the current climate, with credit scoring criteria tightened further in response to the financial crisis, judgment records are likely to assume even greater importance.

Appendix 1: Policy and regulatory developments

November 2008	<ul style="list-style-type: none"> • Five credit card issuers (Barclaycard, Capital One, GE Money, HBOS and MBNA) announce the sharing of 'behavioural data' on their customers' accounts from December • Latest version of the Principles of Reciprocity (version 30)
August 2008	<ul style="list-style-type: none"> • OFT launches a public consultation on the scope of its project looking at irresponsible lending in UK consumer credit markets • FSA publishes results of review of responsible lending practices in the mortgage sector
July 2008	Publication of Data Sharing Review Report by Richard Thomas, the Information Commissioner, and Dr Mark Walport, Director of the Wellcome Trust
April 2008	Reforms introduced by the Consumer Credit Act 2006 (CCA06) come into force. Changes include identifying irresponsible lending as an unfair business practice.
March 2008	<ul style="list-style-type: none"> • New version of Banking Code launched, including strengthened credit assessment practices to enhance responsible lending (Section 13) and more help for customers who may be heading towards financial difficulties (Section 14) • Government publishes response to January 2007 consultation paper on the regulation of enforcement agents
January 2008	Ministry of Justice consults on both the revised Administration Order scheme and the Enforcement Restriction Order scheme
January 2008	OFT publishes revised guidance on fitness and requirements for Consumer Credit licence holders and applicants
November 2007	<ul style="list-style-type: none"> • Ministry of Justice announces terms of reference for a review of the scope of sharing of personal information and the protections that apply when personal information is shared in the public and private sectors • FSA begins thematic review of responsible lending in the mortgage market
September 2007	<ul style="list-style-type: none"> • Ministry of Justice & HMCS publish Consultation Paper CP 22/07 "The debt claim process: helping people in debt to engage with the problem" • Banking Code Standards Board publishes second themed review of the way subscribers treat customers who are in financial difficulties
August 2007	The Information Commissioner's Office (ICO) releases set of best practice guidelines to encourage consistency among creditors when filing default information on consumers
July 2007	Tribunals, Courts and Enforcement Act 2007 receives Royal Assent
May 2007	Report of the Independent Reviewer to the sponsors of the Banking Codes' Review 2007
April 2007	HMCS consults on civil court fees (Consultation Paper 5/07)
January 2007	Government consults on longer-term options for the regulation of enforcement agents
October 2006	DTI consultation on the removal of barriers to the sharing of nonconsensual credit data
May 2006	Department of Trade and Industry (DTI) sets out plans for implementing new consumer credit law
April 2006	Amendments to Banking Code strengthening Sections 13 (Lending) and 14 (Financial difficulties – how we can help)
March 2006	<ul style="list-style-type: none"> • Banking Code Standards Board publishes themed review of the way subscribers treat customers who are in financial difficulties • Consumer Credit Act 2006 receives Royal Assent
March 2005	New version of Banking Code launched

Source: Relevant organisations, author's research

Appendix 2: Court fees

Starting Proceedings										
Value of Claim	Prior to April 1999	April 1999	April 2000	From April 1 2003	From January 4 2005	From January 10 2006	From April 6 2006	From April 6 2007	From October 1 2007	From May 1 2008
< £200	£10-20	£20	£27							
£200-£300	£30	£30	£38							
< £300				£30	£30	£30	£30	£30	£30	£30
£300-£400	£40	£40	£50							
£400-£500	£50	£50	£60							
£300-£500				£50	£50	£50	£50	£50	£45	£45
£500-£1,000	£60	£70	£80	£80	£80	£80	£80	£80	£65	£65
£1,000-£5,000	£80	£100	£115	£120	£120	£120	£120	£120		
£1,000-£1,500									£75	£75
£1,500-£3,000									£85	£85
£3,000-£5,000									£108	£108
£5,000-£15,000	£100-150	£200	£230	£250	£250	£250	£250	£250	£225	£225
£15,000-£50,000	£150	£300	£350	£400	£400	£400	£400	£400	£360	£360
>£50,000	£300-500	£400	£500							
£50,000-£100,000				£600	£700	£700	£700	£700	£630	£630
£100,000-£150,000				£700	£900	£900	£900	£900	£810	£810
> £150,000				£800						
£150,000-£200,000					£1,100	£1,100	£1,100	£1,100	£990	£990
£200,000-£250,000					£1,300	£1,300	£1,300	£1,300	£1,170	£1,170
£250,000-£300,000					£1,500	£1,500	£1,500	£1,500	£1,350	£1,350
>£300,000					£1,700	£1,700	£1,700	£1,700	£1,530	£1,530

Note:
 Figures in red signify changes, figures in blue signify fees for new bands.
 Source: Ministry of Justice / HMCS

Starting Proceedings - Claim Production Centre Cases

Value of Claim	Prior to April 1999	April 1999	April 2000	From April 1 2003	From January 4 2005	From January 10 2006	From April 6 2006	From April 6 2007	From October 1 2007	From May 1 2008
Less than £200	£10-15	£15	£20							
£200-£300	£25	£25	£31							
Less than £300				£23	£20	£20	£20	£20	£15	£15
£300-£400	£35	£35	£43							
£400-£500	£45	£45	£53							
£300-£500				£43	£40	£40	£40	£40	£30	£30
£500-£1,000	£55	£65	£73	£73	£70	£70	£70	£70	£55	£55
£1,000-£5,000	£65	£95	£108	£113	£110	£110	£110	£110		
£1,000-£1,500									£65	£65
£1,500-£3,000									£75	£75
£3,000-£5,000									£85	£85
£5,000-£15,000	£75	£195	£223	£243	£240	£240	£240	£240	£190	£190
£15,000-£50,000	£75	£295	£343	£393	£390	£390	£390	£390	£310	£310
>£50,000	£75	£395	£493							
£50,000-£100,000				£593	£690	£690	£690	£690	£550	£550
£100,000-£150,000				£693						
> £150,000				£793						

Notes:

1. Figures in red signify changes, figures in blue signify fees for new bands.
2. With effect from January 4 2005, the discount for claims issued out of the Claims Production Centre was increased to £10. The discount applies to all fees up to £100,000.
3. Claims above £99,999.99 cannot be issued through the Claim Production Centre

Source: Ministry of Justice / HMCS

Appendix 3: Tribunals, Courts & Enforcement Act 2007 – further details

The discussion of the Act in the main body of the report focused on Part 4, which covers the changes to attachment of earnings orders and charging orders, as well as the new provisions on information requests.

However, both Part 3 (Enforcement by Taking Control of Goods) and Part 5 (Debt Management and Relief) also have some relevance. Part 3 includes the changes to the regulation of bailiffs. Part 5 covers the various measures designed to improve and extend the current range of options available to assist debtors with relatively low levels of income and debts. Some of the main points from Parts 3 and 5 are summarised in this appendix.

Part 3: Enforcement by taking control of goods (regulation of bailiffs)

The changes to the regulation of bailiffs (Part 3, Chapter 1, Sections 62-70 of the Act) have attracted the most attention. The Act brings together in one place the laws regarding seizure and sale of goods. Enforcement agent law was previously a mix of statute law, secondary legislation, case law, guidance and codes of practice.

The Act strengthens the regulation of enforcement agents. In future, nobody will be able to act as a bailiff unless they are personally certificated to do so by a county court judge (or in prescribed circumstances a district judge). They will each have to pass a training programme, deposit a bond, which can be forfeited for misconduct, and demonstrate to the judge that they are fit and proper. In due course, the Government wants to move licensing and regulation into the hands of the Security Industries Authority (SIA).

In March 2008, the Government published its response to the consultation paper of January 2007 on longer-term options for the regulation of enforcement agents confirming strengthened regulation of bailiffs. The document recommends that bailiffs in England and Wales should be regulated by the Security Industry Authority. The Government says extended powers of entry under the new Act will not be brought in to force until the statutory regulation of the industry is in place.

The procedures necessary for taking control of goods under the new Act are more prescriptive than at present. One suggestion is that this may encourage bailiffs to remove goods at the earliest opportunity. Alternatively, they may deter companies from using bailiffs. Critics point to Scotland where the new enforcement law inadvertently curtailed seizure at homes.

Part 5: Debt Management and Relief

In considering the changes introduced by the Act, it is also worth noting that Part 5 covers measures designed to improve and extend the range of options available to assist the over-indebted. It is aimed at those with multiple debts but with relatively low levels of overall debt. The measures include reform of the Administration Order (AO), and the introduction of Enforcement Restriction Orders (ERO).

The Act provides for secondary legislation to define the parameters for each scheme. The Ministry of Justice and HMCS issued a consultation document on the parameters in January 2008.

The AO scheme is a court administered debt management scheme currently restricted to those with maximum debts of £5,000, one of which must be a judgment debt. Once an order is made creditors named in the order cannot enforce their debts without leave of the court nor add interest or other charges to the debt. However, the lack of clarity about the nature of debts that can be included has led to differences of approach between courts. Further, the current AO scheme has little support from either the advice sector or the credit industry.

Though the number of Administration Orders has increased during recent years, the 7,407 AOs registered with Registry Trust during 2007 compares with almost 800,000 consumer CCJs.

Among the changes proposed to the AO scheme to make it more attractive are:

- No need for there to be a judgment debt
- Greater clarity on debts that can and cannot be included in an order
- A maximum five year limit on the duration of orders
- An increase in the total debt limit to £15,000

Enforcement Restriction Orders (ERO) are intended to provide short-term assistance via enforcement relief to those who experience a sudden and unforeseen change to their financial circumstances from which they are likely to recover within a relatively short period. Orders will be limited to a maximum of 12 months during which enforcement action by creditors will be barred, except with the permission of the court. EROs date back to the 1990 Courts and Legal Services Act, though because of operational issues were never implemented.