1. Context of debt problems

On 14 July 1656 Dutch painter and art collector Rembrandt Harmensz van Rijn (1606–1669) made it known to the Court of Holland in Amsterdam that he could not pay his creditors due to losses suffered in business as well as damage and losses at sea. Since that day the bankruptcy of a celebrated artist has struck people as an incidence of fantastic irony. To avoid imprisonment Rembrandt applied for *cessio bonorum,* a process stipulated by the Romans whereby debtors voluntarily surrender goods to creditors. As a result of personal bankruptcy, the 50-year-old painter was forced to cede possession not only of his own works but also of a large collection of paintings and drawings by other Old Masters. In addition were ceded busts of Roman emperors, suits of Japanese armour (among many other objects from Asia) and items of natural history, including minerals. These items were offered for sale in 1657 and 1658 but the prices were disappointing. As a result, Rembrandt had to also sell his house and printing-press in Sint Anthonisbreestraat[1] and move to a small rented apartment on Rozengracht 184, where he lived in poverty until his death. The famous painter was buried in an unmarked grave, and after 20 years his remains were taken away and destroyed, as was customary with poor people at that time.

The 20th and 21st centuries have witnessed tremendous developments in terms of better health, higher incomes and stronger states to support people in need. In the Western world, epidemic diseases have been more or less conquered, and earlier causes of death have been replaced by modern and degenerative diseases linked to lifestyles, stress and excess consumption (Grand 2008). Instead of epidemics another type of disease is causing havoc by destroying people's health, taking away their incomes and possessions and undermining the state's capacity to help people in need. That epidemic is over-indebtedness.

It might sound odd to call a problem related to the economic sphere of life an epidemic. The justification is twofold. Firstly, as will be presented in this book, over-indebtedness causes serious harm to health and well-being. Secondly, over-indebtedness is also highly contagious. Of

[1] Later Jodenbreestraat, and now the location of the Rembrandt museum.

course, it does not happen through the spread of disease agents from one individual to another, but through societal structures. Therefore the connections between individual suffering and social structures will also be explored in this book.

Throughout the 1980s and 1990s a number of Western countries went through periods of economic recession resulting in unprecedented numbers of over-indebted households, that is, households no longer able to meet their financial commitments. Over-indebtedness has affected and continues to affect a substantial share of private households in all economically advanced countries. It has negative effects on debtors and their dependants in terms of health and well-being. Over-indebtedness also relates to outcomes in the labour markets, financial markets, public revenues, welfare states, health care systems and judicial systems (Heuer 2013). The debt epidemic achieved gigantic proportions during the Global economic crises. For example, in the US the Great Recession destroyed 8 million jobs between 2007 and 2009, and more than 4 million homes were foreclosed (Mian and Sufi 2015a, p. 2).

Before the onslaught of the Global economic crises in 2008, studies on the consequences of debt problems were few and far between. Only a few classic studies have dealt with debt (see Caplovitz 1963, 1974, 1979; Ford 1988 as exceptions). For example, the large body of literature on welfare state regimes or models completely ignores the regulation of consumer finance and personal insolvency (for example Esping-Andersen 1990). Even later, the study of over-indebtedness has been plagued by short-sightedness. The question of over-indebtedness has been approached from a number of quite separate and not well-connected perspectives. Economists have studied the effect of household debt on macro-economic performance. The personal traits of over-indebted individuals have been the topic of social-psychologists. Social-epidemiologists have attempted to analyse the complex relationship between health and over-indebtedness, whereas scholars of law have, among other topics, compared different insolvency regimes from a juridical perspective.

The key notion of this book is that the combination of these perspectives is necessary in order to gain a more thorough understanding of over-indebtedness. This book aims to do that through a social policy paradigm where over-indebtedness is understood as a social risk, that is, a factor endangering or preventing the full participation of individuals in society. This paradigm aims also to find remedies to prevent and alleviate the over-indebtedness epidemic. The basic assumption in this inquiry is that collective action – that is, social policies – is needed to tackle the over-indebtedness epidemic.

We will analyse households and families who default on their debts, while covering all debt types that are used for individual purposes, from credit cards to mortgages. Most of the current research focuses on consumer debts. However, as the case of Rembrandt illustrates, the distinction between consumer debts and business-related debts is sometimes difficult to draw. Entrepreneurs and self-employed persons may have assumed individual responsibility to guarantee funding or individuals given surety for family members' or friends' business loans. Consequently, we also discuss business debts to the extent they result in individual liability.

This book acknowledges that debt and its consequences are bound to existing social structures. This is illustrated, for example, by the fact that debt problems have a gendered dimension (Goode 2009). Women are at higher risk of financial strain than men due to women's weaker position in the labour market. Women have lower wages and higher poverty rates. They are also more often single heads of households with children, and tend to lose out economically in the event of divorce. As a result, we may assume that financial strain and debt burden could affect women more strongly. On the other hand, when men have sole responsibility for managing incomes constrained by over-indebtedness, they reportedly experience anxiety and depression more typically than women (Goode 2012a). However, male pride in relation to financial matters may act as a barrier to seeking advice. This effect is aggravated by the fact that male pride in relation to financial matters forms a significant component of men's identities.

This book takes a general view on over-indebtedness and reflects the role of gender only in passing. We also acknowledge that causes, consequences and correlates of over-indebtedness are also affected by other socio-economic variables such as household structure, age, education, migrant status and disability (Patel et al. 2012). Nevertheless, these dimensions will be largely ignored for the sake of clarity and brevity while, we argue, more in-depth research is needed to understand the intersectional and multidimensional nature of debt problems.

As an academic discipline, social policy analyses both the nature of the risk and its consequences in a given social context, and discusses public policies to deal with the social risk. In this paradigm identifying the risk and its special features comes before analysing policies to handle the risk. That is also the path followed in this book. The main argument of over-indebtedness as a unique social risk is presented by: first, discussing the definition of over-indebtedness; then by focusing on causes and consequences of over-indebtedness; and, finally, by analysing the policies to prevent and/or alleviate over-indebtedness. Since no survey or register study was conducted for the single purpose of this book, the contribution of this inquiry lies mostly in the conceptual and theoretical arena. The aim is to demonstrate that over-indebtedness should be tackled with a more comprehensive and integrated set of public policies than in place today.

STRUCTURE OF THE BOOK

Before looking into the context of debt problems in six countries analysed in this book, we will briefly discuss a larger context of over-indebtedness among the rich countries, together with substantial issues relating to concepts and theoretical approaches. In the following section, we discuss debt collection and debt discharge; that is, the procedures relating to establishing payment default and consequent actions in six countries. We then analyse what causes people to become default-debtors. After that we focus on the consequences of over-indebtedness. Finally, we analyse public policies to prevent and/or alleviate over-indebtedness.

DEBT, REPAYMENT NORMS AND RELIGION

The essence of over-indebtedness is a breach of contract. A debt is left unpaid. This is foremost a moral problem on a individual level but one with a wide range of societal dimensions. The Latin phrase *Pacta sund servanda* is the foundation of any organized society, meaning that *agreements have to be binding*. Money and credit are inherently relational constructions operating through (tacit or explicit) contracts between people. The term “credit” (credibility → credo) reflects the moral and the legal background of the initial concept of lending money and entering into a relationship between creditor and borrower (debtor). Trust and personal responsibility are key elements in the morality of “credit”.

The legislative history of the European consumer “bankruptcy” laws is rich with references to the sanctity of contracts (Heuer 2013). The repayment norm is even present in major religions, which is reflected in the fact that there is a surprising similarity between the language of religion and the language of finance (debt). That is the case in all Indo-European languages, where debt is repeatedly associated with guilt and sin, while payment is associated with salvation. Take, for example, the English words “guilt” and “redemption”. In the German language, the words for guilt (*Schuld*) and debt (*Schulden*) carry almost similar meaning. The Lord's Prayer ("Our Father"), which has a central role in Christian worship, has even been translated to include a verse: "And forgive us our debts, as we forgive our debtors." Evidently, already during the time the Bible was written debt was a major problem underlying political and everyday life.

Given the moral norm behind the relationship between debtor and borrower, it is not surprising that religion still plays a role in over-indebtedness. Kiesel and Noth (2016) argue that while debt is discussed critically in Protestant history and writings, contrary to Catholicism, it also involves elements of a positive attitude towards debt. They find that the more widespread Catholicism is, the lower the share of over-indebted persons. In Islamic contexts, using microdata for Pakistan, Baele et al. (2014) find loans less likely to be defaulted on during Ramadan and in cities where religious-political parties receive a high share of votes.

The significance of repayment norm has been recognized since ancient times, and violation of the norm has been regulated with violent force. By default, incapable debtors are considered as "undeserving poor" (Townsend 1979). The "deserving poor" are those who are poor through no fault of their own – for example through illness, accident or age, or because of a lack of work – while the undeserving poor are poor because of laziness or personal problems including excessive debts. However, the repayment norm also reflects the power imbalance between creditors and debtors. Indeed, the Bible states that: "The rich rules over the poor, and the borrower is the slave of the lender" (Proverbs 22:7). According to the Norwegian scholar Christian Poppe (2008, p. 17), "this rule has been enforced through history with the full range of penalties for failing to repay debts, including various forms of physical punishment, enslavement and even death penalty". For example, in medieval Britain, dishonest default-debtors faced the risk of being placed in the pillory, having their ears cut off, or even being killed. In the English language, the same word, "delinquent", is used for a person who commits a felony and a person who fails to repay a debt.

Moreover, the current social order is built on repayment norm, which is of paramount importance for financial markets (Poppe 2008). If a debt is unpaid not only is a fundamental convention in society challenged but also the very existence of money economy is put in jeopardy. Evidently, the value of any currency would collapse if a large enough number of debtors announced that they were not repaying their loans. Even today those people who are deemed as neglecting their financial commitments are still subject to a variety of debt collection procedures ranging from foreclosure to imprisonment. The causes and consequences of these present-day procedures are discussed in this book.

A fundamental feature of a credit contract is indeed the fact that it is not an agreement between equally powerful parties. In essence, the contract is between a party with extra resources and a party lacking resources. To put it simply, society is divided into two distinct, largely non-overlapping categories: the haves and the have nots – that is, those who have money to lend and those who need to borrow money (see Mian and Sufi 2015a). The composition of these categories gives a measure of wealth inequality in a society.

Neglecting a due payment is obviously a breach of the social norm which dictates that agreements are binding. The studies of present-day European debtors suggest that they feel quite guilty about their inability to fulfil their obligations (Kilborn 2005). Evidently, the government is required to intervene to enforce social order and to strike a balance between the rights of the debtor and the creditor. At this point the government and society as a whole tend to side with the stronger party, the creditor. Without denying society's concerns about enforcing social commitments, this book sides with the weaker party, the debtor. We focus on individual and household level over-indebtedness from the debtor's perspective, with emphasis on social policy measures, where over-indebtedness is considered a (new) social risk – a condition which should be regulated through public policies.

WHY HAS DEBT BECOME A PROBLEM IN DEVELOPED COUNTRIES?

Credit relates to three distributive systems of modern society: namely, markets, governmental actions and informal personal networks (Polanyi 1944). Credit is an important tool for economic progress and social welfare. Credit is involved in all household financial transactions, from shopping at a grocery store to acquiring property. Through new consumer credit products and aggressive marketing practices we have witnessed a financialization and commercialization of human interactions as more and more social interactions have been transferred into the realm of the market, using credit as a central valuation metric. It is obvious that normal wage-earning households need to take out credit to afford expensive purchases such as cars or houses. Debt is increasingly used also as a tool for financing smaller consumer needs.

The developed societies encourage their citizens to make debts in order to promote economic growth. Debt is used for private consumption. It is the lubricant which keeps the economy's wheels running. Democratization of credit means that property, goods and services are distributed among the population. Credit concerns also governmental redistributive systems of taxes, benefits, fees and fines. Credit and debt may also arise from transactions between private individuals, such as borrowing money from relatives or friends. Personal networks are also involved when loans are taken from the black market or when they relate to illegal activities, for example drug trafficking.

Credit gives access, even for those with small incomes, to a wide range of socially important items – ranging from life necessities to luxuries (Poppe 2008, p. 33). However, that is only possible as long as the debtors are able and willing to repay their loans. If a debtor is turned into a default-debtor, the process is reversed and credit will become excluding. A series of sanctions come into play, increasingly punitive up to the point where the debtors are not only blocked from further access to credit but also where they are even no longer able to guarantee basic necessities for life. They will no longer be able to engage in ordinary social activities, which will then quickly narrow and threaten to jeopardize their social identity (Poppe 2008).

So why have household debts become a problem (in developed countries) over the last few decades? The simple explanation is that credit has become ubiquitous, also described as the "democratization of credit availability". The use of credit cards has increased dramatically since the 1960s. In the mid-1960s they were largely unknown. By the second decade in the new millennium approximately 70 per cent of households participate in the credit card market in the US; 45 per cent in the mortgage market; 19 per cent in student loans; and 30 per cent in car loans (also 50 per cent hold stocks directly or indirectly) (Zinman 2015). These figures are from a cross-section of society; virtually almost everyone participates in the credit market during their life course.

However, it is worth noting that credit is not only a modern way to finance consumption. Before the dawn of the credit card industry, pawnbroking served working-class communities and helped them manage poverty (although the temperance movement preached against the pawnbroker's role in financing drinking). According to one estimate, there were nearly 1000 registered and some 50 000 unregistered moneylenders in England and in Wales in 1925. Butchers, drapers, plumbers and other traders allowed their customers to pay weeks, months and sometimes years after the goods or services were delivered (Ford 1988, pp. 15–16). Hire purchase of sewing machines, pianos, furniture and later cars, and mail order companies preceded the breakthrough of credit cards. Attitudes towards the use of credit were different, though. In the

18th and 19th centuries the wealthy and the emerging middle class expressed a dislike of credit used by poorer members of society. This attitude is visible, for example, through many proverbs, such as: “Better to go to bed supperless than rise in credit”; “He that borrows must pay again with shame and loss”; “Out of debt, out of danger”; and “Neither a borrower nor a lender be” (Ford 1988, p. 29).

During the “roaring twenties” in the US technological innovation brought new consumer products such as automobiles and radios into consumer markets (Igan et al. 2012). Financial innovations such as instalment plans made it easier for households to obtain credit to buy these coveted new items. General Motors (GM) was the first car maker to offer loans for the purchase of its automobiles. In 1991, GM established the General Motors Acceptance Corporation, and by 1927 two-thirds of new cars were purchased on instalment. Ford and Rootes followed GM’s example, as did manufacturers of electronic goods such as Pye, Electrolux and, more recently, Hitachi.

Norwegian researcher Christian Poppe (2008, p. 12) argues that most Western capitalist societies underwent a change during the 1970s and 1980s: from “save first, pay cash” to “buy now, pay later”. Credit became a device to include also those of limited means in mainstream consumer society. For the financial industry credit was no longer used as a means to finance consumption; rather, the sale of credit became an end in itself. Taking out credit was no longer connected to any negative morality. On the contrary, credit carried a promised individual advancement. Today credit is the necessary medium for a better life for all individuals with no inherited wealth.

THE CONTEXT OF DEBT PROBLEMS IN SIX COUNTRIES

The causes and consequences of debt problems, as well as policies to alleviate them, are context bound. This book adopts a comparative approach to the topic. We focus on two Anglo-Saxon countries (the US and the UK), together with two continental European countries (Germany and the Netherlands) and two Nordic countries (Finland and Norway). These six countries cover three different welfare state regimes, namely liberal, conservative and socio-democratic (Esping-Andersen 1990). These countries, as will be later demonstrated, will also fall into different categories in terms of debt collection and personal insolvency regimes and credit-based social policy orientations. While some countries get more coverage than others (for example due to specific causes of household indebtedness or availability of data and research evidence), across different chapters there will be (some) discussion on all six countries.

With its leading role among the capitalist countries the US is an obvious choice for analysis. The new innovations in consumer finance, most notably the use of credit cards, have been developed in the US and across the world from there. The US has weakly developed welfare state structures which are counterbalanced by consumer-friendly bankruptcy legislation to deal with cases of over-indebtedness. Moreover, the US credit and bankruptcy systems serve as internal models to be either emulated or avoided by other countries (Ramsay 2017, p. 7). The same holds true for the UK, or more specifically England and Wales (for more discussion see the following chapter). A number of path-breaking studies on consumer over-indebtedness have been conducted in these two countries (Caplovitz 1963, 1974, 1979; Ford 1988).

Credit has become a more central component of the German welfare state, with gradual erosion of savings promotions, the expansion of quasi-public loan schemes and the restructuring of the welfare state since the mid-1970s (Mertens 2017). Germany has a fledgling consumer insolvency legislation which emphasizes the role of debt counselling. Authorized debt counsellors have a mandated role in the German credit default legislation, and the country regularly publishes very comprehensive statistics on over-indebtedness.

With regard to over-indebtedness, the Netherlands is an interesting case among the continental European welfare states. The Dutch are the most indebted households in the euro area, in part because of tax benefits for leverage and high housing prices (OECD 2017a). At the end of 2015, almost one-third of Dutch homeowners had negative equity. As opposed to the US and the UK, the Dutch legal system provides limited options for debt restructuring. Mortgage debtors who have negative equity will not rely on the consumer insolvency procedure, which might not result in debt discharge. This regime, described as "draconian", encourages Dutch households to curb consumption and prioritize debt repayment (Klein 2016).

The decision to choose two Nordic countries relates to partly converging and partly diverging economic development and the similar scope of debt problems. The Northern European welfare states with populations ranging from 5 million (Denmark, Norway and Finland) to 10 million (Sweden) were hit by a severe economic recession in the late 1980s and early 1990s (Kiander and Vartia 2011). This was a direct result of deregulation of the economy in general and deregulation of financial markets in particular (Poppe et al. 2016). First in Norway, then Finland many people who had to sell their housing due to unemployment and/or skyrocketing mortgage interests were left with large debts when housing prices went down. For example, in Finland from 1990 to 1997 the number of people with payment default entry in the credit information register increased from 200 000 to more than 350 000 (Blomgren et al. 2016). Again, the economic collapse of 2008 led to an unprecedented period of stagnation in Finland, while similar development was not observed in Norway. In July 2017 the number of people with a payment default entry in Finland was a record almost 373 000 (Suomen Asiakastieto 2017), while there were 449 512 debtors in enforcement (Findikaattori 2017).

The Organisation for Economic Co-operation and Development's statistics on household debt (OECD 2017a, 2017b) show diverging paths of household indebtedness among the six countries (Figure 1.1).[2] The Netherlands clearly had the highest level of household debt from 1995 to 2015 as a percentage of national domestic income (NDI). In fact, the Netherlands is completely in its own league: except for 2001, its debt level increased continuously from 1995 to 2010, after which it decreased until 2016, reaching the same level as in 2007. Norway had the second highest debt level, which increased practically through the period. The UK and the US show a similar trajectory, with increase until the Global economic crisis and slow decrease in indebtedness thereafter. Germany diverges from the other countries. Household debt there increased from 1995 only to 2001, after which indebtedness began to fall continuously towards 2016. Finland shows a complete opposite trajectory, with slightly decreasing indebtedness before 2001 and continuous increase since then.

These figures also demonstrate that the effects of the Global economic crises were far from over in 2016. As a response to the crises central banks have adopted comprehensive policies to increase liquidity in the

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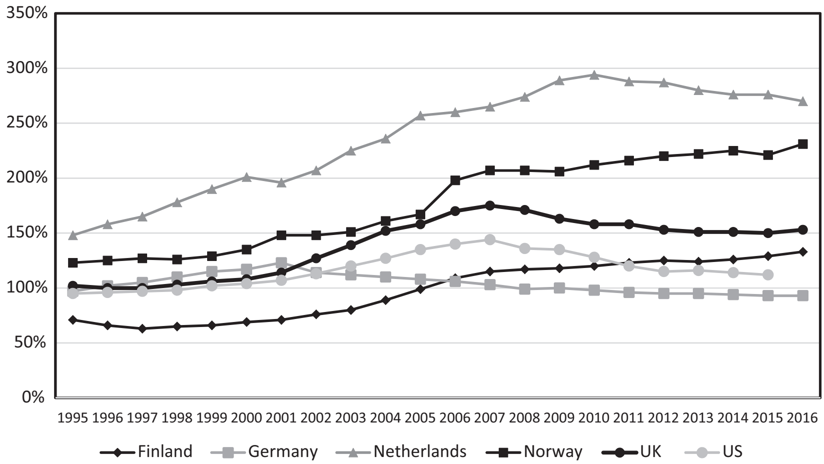
[2] The OECD defines household debt as "all liabilities that require payment or payments of interest or principal by household to the creditor at a date or dates in the future". Consequently, all debt instruments are liabilities, but some liabilities – such as shares, equity and financial derivatives – are not considered as debt. According to the 1993 System of National Accounts (SNA), debt is thus obtained as the sum of the following liability categories, whenever available in the financial balance sheet of the households and non-profit institutions serving the household sector, such as: currency and deposits; securities other than shares, except financial derivatives; loans; insurance technical reserves; and other accounts payable. For households, liabilities predominantly consist of loans, in particular mortgage loans for the purchase of houses. This indicator is measured as a percentage of NDI (for data see SNA 2008).



Source: OECD (2017a, 2017b).

Figure 1.1 Household debt as share of national domestic income in six countries between 1995 and 2015/2016

financial markets by zero level interest rates and bond purchase programmes. The record low interest rates have increased house prices and encouraged consumers to take out big loans to finance, for example, housing purchases. That is the case especially in Finland and Norway, where household indebtedness reached record levels in 2016. The near zero level interest rates have also fuelled housing investment speculation (Poppe et al. 2016). This time the development does not concern single countries but all countries where central banks have flooded the economies with cheap money. As the old cautious wisdom goes, it is not possible to spot a bubble before it bursts. If this happens, the Western countries may experience over-indebtedness to extents never experienced before.

The OECD figures for 2014–2016 shown in Table 1.1 indicate that the great majority of households had outstanding liabilities in all countries except Germany (OECD 2017b). This notion of "indebted households" excludes households having a balance on their credit card (or utility bills) on which no interest payment is paid, but includes those households that have payment arrears on their credit cards. These figures can hardly be taken as a measure of over-indebtedness; rather, they reflect payment cultures and the use of credit in different countries. A more serious measure of risk of over-indebtedness is a debt-to-asset ratio above 75 per cent of income. The United States and Norway had the highest share of households in this category (30 per cent and 21 per cent respectively), followed by the Netherlands. The column "households with debt-to-income ratio above three" in Table 1.1 indicates that the Netherlands and Norway had the highest numbers by this measure. Different measures produce slightly different country rankings, but they show that Norway, the Netherlands and the US are the countries with the highest risk of household over-indebtedness. The figures and rankings for the countries by the three measures were almost similar in 2010–2012.

Table 1.1 Share of indebted households by three different measures in six OECD countries

Country	Year	Indebted households (outstanding liabilities)	Rank	Debt-to-asset ratio above 75%	Rank	Households with debt-to-income ratio above three	Rank
Finland	2014	57.4%	5	13.6%	4	5.5%	5
Germany	2014	45.1%	6	11.0%	5	4.0%	6
Netherlands	2015	65.7%	3	17.9%	3	32.2%	1
Norway	2014	84.9%	1	29.5%	1	28.2%	2
United Kingdom	2015	61.0%	4	4.5%	6	9.6%	4
United States	2016	77.2%	2	20.9%	2	13.0%	3

Source: OECD (2017b).

It is important to note that the three types of debt that are commonly attributed to social policy area – housing (mortgages), educational (student loans) and medical (credit card) – are also associated with over-indebtedness. Therefore, access to consumer credit debt settlement or consumer bankruptcy is also an important element of credit-based social policy. Interestingly, the Anglo-liberal welfare state model has a compensatory character as opposed to continental European and Nordic welfare state models where defaulters are offered easy access to a process that guarantees a fresh new start for default-debtors. The more a credit-based social policy is promoted, the higher the risks households have to bear. These risks are socio-economically unequally distributed.

The unequal distribution can, however, be amended through a market-based insolvency regime. Angel and Heitzmann (2015) show that households in countries with no or only weak discharge possibilities are more likely to be over-indebted as their chances of exiting over-indebtedness are smaller.

WHAT IS OVER-INDEBTEDNESS?

A debt, whether small or large, is not a sign of financial problems as such. Indeed it may even indicate a high level of solvency. Actually, highly indebted households tend to have relatively high incomes and wealth. Therefore, a high level of borrowing is not necessarily an indication of inability to meet commitments. Among the wealthy, having large debts has never gone out of fashion; leveraging has been the way to riches for many present-day tycoons. A debt only becomes a problem when the debtor is unable to repay it on time.

Over-indebtedness is not a continuous variable, but rather a dichotomous variable. This notion pays attention to the particular change when individuals turn from indebted into over-indebted. Poverty is also a dichotomous or a category variable (Townsend 1979). However, a change of status from non-poor to poor, be it by absolute or relative definition of poverty, is different from a change of status from indebted to over-indebted. Objective poverty status is always tied to a certain level of resources or consumption, whether expressed in absolute or relative terms. The difference between poverty and over-indebtedness boils down to the fact that poverty is measured by income, which is a continuous variable, while over-indebtedness is exclusively a category variable.

Further clarification of the distinction between poverty and over-indebtedness is obtained by distinguishing between two types of household (Poppe 2008, p. 34; Poppe et al. 2016). The first is the "cash-flow household", which needs all available income to cover necessary daily expenses. As a consequence, this household type is largely unable to save and invest, and instead is left to consume most of the credit it takes on. In cases where the equalized incomes of this household fall below a certain amount, it is considered as suffering poverty. The second type is the "investment household", which may have income just above the bare minimum, allowing its members to take advantage of other kinds of capital than their own labour by saving money and using credit as a means to build assets such as property and education. If an "investment household" gets into financial difficulties with debts and is forced to adopt the financial career of a poor "cash-flow household", describing the household's situation through poverty would ignore the important change, typical for example among mortgage defaulters, from "investment household" to "cash-flow household".

Finally, we need to make one more distinction between poverty and over-indebtedness. The experience of poverty is related to the larger social context of where individuals and families live; and the conditions of poor individuals and households are mediated through a complex network of actors such as welfare agencies, employers and family members. That is also true for over-indebtedness; but there is also a special relationship between the debtor and the creditor, which is the single most important determinant for the experience of over-indebtedness.

It is not difficult to provide simple descriptions of over-indebtedness. Firstly, generally speaking over-indebtedness can be defined as a situation in which a debtor is permanently unable to repay a debt. Secondly, a more sophisticated definition takes into account the resources available for servicing a debt. By this definition an individual or household (assuming that resources are pooled within a household) is over-indebted if the debt cannot be sustained in relation to current earnings and any additional resources raised from the sale (under fair conditions) of real or financial assets. Thirdly, it is necessary to consider the effects of over-indebtedness. There is a theoretical case where a person has deliberately chosen to live his or her life with unpaid financial commitments, and is not harmed by that choice. Over-indebtedness becomes a problem when it is accompanied by suffering and trauma for those affected.

The critical element in defining over-indebtedness concerns the inability to pay. How then to define the instance when a person or a household is not able to pay debts? When does the situation become unbearable enough to be taken as an "inability to pay"? It is challenging to come up with an exact definition of a situation which would be both measurable and comparable across time and place. Despite decades of scholarly and administrative work there is no consensus in the literature on how to define over-indebtedness (CPEC 2013; D'Alessio and Iezzi 2013). According to D'Alessio and Iezzi, empirical studies of over-indebtedness have instead tended to converge on a common set of indicators reflecting four aspects of over-indebtedness: making high repayments relative to income; being in arrears; making heavy use of credit; and finding debt a burden (Table 1.2). Using data from the Bank of Italy's survey on Italian households the authors showed that different measures of over-indebtedness end up identifying different households with debts. About 8 per cent of households were over-indebted according to at least one indicator, but no more than 2 per cent were over-indebted according to two indicators simultaneously. The condition of over-indebtedness according to these indicators rarely coincided with the subjective condition of economic distress. The subjective measures of over-indebtedness may raise concerns of comparability. There is no reason to reject these measures, though. Subjective measures of debt burden may have an important role to play in understanding debt and its psychosocial consequences. The subjective perception of debt burden carries the direct impact of debts on individuals. Objective indicators may not give a complete picture of the pressures of debt as there are often unobserved factors that may make debt a problem (Keese 2012).

Table 1.2 Common indicators of over-indebtedness

Category	Indicator
Cost of servicing debt	Households spending more than 30% (or 50%) of their gross monthly income on total borrowing repayments (secured and unsecured)
	Households spending more than 25% of their gross monthly income on unsecured repayments
	Households whose spending on total borrowing repayments takes them below the poverty line
Arrears	Households more than 2 months in arrears on a credit commitment or household bill
Number of loans	Households with 4 or more credit commitments
Subjective perception of debt burden	Households declaring that their borrowing repayments are a "heavy burden"

Source: D'Alessio and Iezzi (2013).

After discussing the pros and cons of the measures suggested in Table 1.2, D'Alessio and Iezzi conclude that they all are, for the most part, measures of the process of becoming over-indebted, rather than measures of the outcome associated with having problems with debts (see also Haas 2006). Recognizing the ambiguities in previous definitions of over-indebtedness, a comprehensive EU study on over-indebtedness proposed a broader definition (CPEC 2013, pp. 19–31). By this definition, "over-indebted households include those who face difficulties meeting (or falling behind with) their commitments, whether these relate to servicing secured or unsecured borrowing or to payment of rent, utility or other household bills on ongoing basis". With this definition over-indebtedness may be measured, for example, through credit arrears, credit defaults, utility/rent arrears or the use of administrative procedures such as consumer insolvency proceedings.

ADMINISTRATIVE DEFINITION OF OVER-INDEBTEDNESS

Over-indebtedness can be also approached from a legal perspective. All developed societies have official legal mechanisms or institutions to collect money or property equivalent to the overdue debt (Niemi-Kiesiläinen 1999). The most obvious legal definition of debt problems or over-indebtedness is precisely the moment when a debtor is turned into a default-debtor in the eyes of the law. This is called the administrative definition of over-indebtedness.

A key element in/of the administrative definition of over-indebtedness is the official recognition of a debtor's failure to pay a certain debt. That may happen through the courts or by the nature of the claim (Betti et al. 2001). The latter category includes those obligations which can be collected through legal means (forced sale of property, wage attachments and so on) without court procedures. Depending on jurisdiction these items include, for example, taxes, rates, fines, alimony, child maintenance and insurance payments.

A precondition for administrative over-indebtedness is that the creditor will take legal action to collect the debt. Creditors have their own actions, measures and definitions for default before they decide to go to court (Ford 1988). The creditor will normally apply soft measures to enforce payment before initiating legal actions. When an invoice or a loan is left unpaid after the due date the creditors will send a reminder letter and, in most cases, will charge extra interest on the overdue payment. Sometimes they call up the debtor or send another, this time more angry letter. What is relevant here is that the creditors cannot take any serious action (for example garnishing wages, selling property, evicting tenants) before the overdue payment is processed through the courts. The situation changes dramatically after the court has confirmed an unpaid debt.

A key feature of the administrative definition of over-indebtedness is the qualitatively negative change in people's economic conditions once a debt is confirmed through the courts. This is most clearly visible among those who had large debts and large assets before insolvency and among those who face losing their homes. Janet Ford (1988, pp. 109–111), who interviewed 40 households with mortgage arrears in the UK, notes a qualitative change in defaulter conditions after they realized that they could lose their homes. The initial situation of arrears was described with words such as "shock", "panic", "frightened", "scared". According to Ford (1988, p. 129), the borrowers saw their situation not only as difficult but also as qualitatively changed:

> By "not paying" they believed they were perceived and judged differently and more harshly, they faced a set of circumstances whose outcomes were unknown and where they had very limited ideas and knowledge as to the best or appropriate course of action. They found it hard to convey their position to others.

The category of most affected debtors includes also misfortune entrepreneurs and investors who risk losing their lifetime achievements in terms of assets and savings. It is important to note, however, that even for poor individuals and households with small debts and no assets the administrative decision to determine payment liability is a qualitative change towards more serious financial difficulties. However, "judgment debt" as such does not amount to insolvency. The process concerning judgment debt is simply a legal determination of payment liability, and does not concern a debtor's ability to pay.

We may assess the relevance of the administrative definition of over-indebtedness by contrasting it with the five criteria for defining over-indebtedness presented in a study carried out for the European Commission (Fondeville et al. 2010):

1. The unit of measurement should be the household because the incomes of individuals are usually pooled within the same household.
2. Indicators need to cover all aspects of households' financial commitments: borrowing for housing purposes, consumer credit, to pay utility bills, to meet rent and mortgage payments and so on.
3. Over-indebtedness implies an inability to meet recurrent expenses, and therefore should be seen as a structural rather than a temporary state.
4. It is not possible to resolve the problem simply by borrowing more.
5. For a household to meet its commitments, it must reduce its expenses substantially or find ways of increasing its income.

As to the first criterion, administrative definition, at first sight, seems to fail the test. The procedures to determine payment defaults concern individuals, not households. However, the consequences of one household member's insolvency affect everyone in the household. The same applies to the second criterion. While the court determines the validity of individual claims, a possible payment default has potential consequences for all the household's financial commitments.

The third criterion recognizes the fact that the term over-indebtedness refers to severe debt problems. That is the case with the administrative definition of over-indebtedness. Consequences of payment default, for example, follow individuals for a long time in terms of default entries in credit reports. They may limit individuals and households' capability to participate in a normal way of life/living for several years even if the overdue payment is subsequently settled (CPEC 2013). The benefit of the administrative definition of over-indebtedness is that it is not necessary to give a definite amount of deficit either in absolute or relative terms to determine a severe debt problem.

The fourth and fifth criteria are fully covered in the administrative definition of over-indebtedness. The consequences of payment default are so severe, including possible loss of home and all other properties, that households are likely to exhaust all options to borrow more money and/or reduce expenses and/or increase incomes to avoid payment default.

MODIFIED ADMINISTRATIVE DEFINITION OF OVER-INDEBTEDNESS

In the following, we will take the administrative definition of over-indebtedness as a starting point while acknowledging five major limitations in this approach. Firstly, as stated earlier, some claims can be collected through forceful measures even if they are not litigated. Secondly, there are also other claims which, before court proceedings, may result in serious consequences for everyday life if they are left unpaid. For example, a household may lose access to water, heating and electricity if utility bills are left unpaid. Disconnecting vital utility services can also have critical consequences, especially in extreme climate conditions. The service providers do not need a court decision to discontinue service delivery. The same goes for phone lines and internet subscriptions (although prepaid options are currently available). In the absence of universal health care patients with serious illnesses may lose their lives if they cannot pay for their vital treatment. This situation can, no doubt, be characterized in terms of over-indebtedness even if there is no court decision to claim back the overdue medical debts.

We may, however, include these instances in an administrative definition of over-indebtedness since consumer law and similar provisions regulate the conditions under which a utility service company can stop their services. Given the compounded nature of default consequences and the regulated procedures to discontinue services it is reasonable to assume that households would not leave these types of claims unpaid as a result of forgetfulness, even if the overdue amount is small.

Thirdly, the consequences of unpaid claims are bound to a specific welfare state and legal context. In some contexts, non-payment can have life-threatening consequences if vital medical treatment is discontinued as a result of payment neglect. That would not be possible in countries providing universal access to health care. The health care providers' practices with regard to unpaid medical debt may not be regulated in consumer law or similar provisions. In addition, many countries provide means-tested social assistance for individuals and/or households with difficulties paying utility and/or medical bills. These practices may be regulated in law or they may be discretionary.

Fourthly, sometimes the negative consequences of indebtedness set in before payment default. People may try to meet their financial obligations to an extent that seriously affects their essential consumption. Take an example of a tenant who gives nearly 90 per cent of her welfare allowance to a landlord to repay overdue rent and to avoid eviction. In that case it would be feasible to agree on a debt/income ratio which could be used as a yardstick analogous to the definition of relative poverty (40, 50 or 60 per cent of median income). Private individuals service their debts with incomes from their work input, entrepreneurial activities or from social security payments. We may try to define over-indebtedness through setting a threshold for debt/income ratio. The definition is valuable in identifying persons/households that are about to live beyond their means. But even this definition would end up in difficulties with very high incomes and debts. In addition, this approach does not fully capture the impact of debt collection procedures.

Finally, we need to consider whether or not over-indebted individuals have positive assets. The strength of over-indebtedness as a social measure is the very fact that it concerns not only income but also wealth. In many cases over-indebtedness indicates that people have negative assets. However, it does not follow from the administrative definition of over-indebtedness that it could be equated with no assets. Under some circumstances people are ready to face debt judgment even if they hold some assets, for example a family home. Many jurisdictions divide debtors in insolvency proceedings into two categories, as will be later discussed, on the basis of whether or not they have any remaining assets.

In the following we will use a modified administrative definition of over-indebtedness. By this definition *over-indebted persons are those who have defaulted on claims which have been confirmed through court and which are collected by creditors – including claims which can be distrained without litigation (for example unpaid taxes) – or which through an administrative regulated process or otherwise lead to serious consequences (for example the household has no electricity, heating or* *water*). This book is based on the hypothesis that the social consequences of over-indebtedness are related to the qualitative changes taking place when debt collection actions are initiated and/or when the serious consequences covered by the definition set in.

Of course, even using this modified administrative definition of over-indebtedness we need to consider the possibility of false positives and false negatives. False positives would relate to cases where relatively well-off individuals or households (would) end up with payment defaults, for example, as a result of irresponsibility or determined decision not to pay a certain claim (for example alimony or child maintenance). This problem could be avoided by using a narrower legal definition – for example, personal insolvency, debt settlement or debt discharge – as an indicator of over-indebtedness. However, that would create more problems since not all unpaid claims end up being discharged, and not all debtors seek and/or are granted debt settlement.

In any case, payment default, whether caused by lack of funds or lack of motivation to pay, comes with a number of negative consequences for the debtor, including bad credit reports with ensuing problems in getting insurance, renting accommodation or getting a job. In the US, for example, landlords may docket a money judgment which could appear in tenants' credit reports for many years, accruing 12 per cent interest (Desmond 2016). It will be a real barrier to self-reliance and security for those who try to take a step forward and apply for a student loan or purchase a first house, for example.

Payment default as a definition of over-indebtedness may also lead to false negatives. It is possible that there are people struggling with insurmountable debts who never end up in administrative records. The most obvious example is underwater mortgage debtors who have lost all their equity but continue to service their debts in an effort to avoid foreclosure. False negatives may also stem from more unusual circumstances, such as private debts (for example drug debts). Lastly, the problem with an objective measure such as payment default is that the rules governing such procedures, and the policies and practices can vary between countries, and perhaps between regions within countries. This topic is further discussed in the next chapter.

Finally, we need to make a distinction between a *definition* of over-indebtedness and an *indicator* of over-indebtedness. For theoretical and analytical purposes, it is imperative to define over-indebtedness. However, as described above, previous research has convincingly demonstrated that there is no single valid definition of over-indebtedness which could be translated into a single quantitative indicator; nor is there a quantitative measure which could effectively capture all the necessary dimensions of over-indebtedness. Over-indebtedness is complex and multi-dimensional, and therefore to measure the quantity and the quality of over-indebtedness multiple indicators must be assessed, collected and analysed.

CREDIT-BASED SOCIAL POLICY

The notion of credit-based social policy adds a new dimension to discussion on the role of welfare states and over-indebtedness. The terms "credit-based social policy" or "asset-based welfare" denote a policy paradigm which emphasizes the regulation and promotion of private assets as a means of social security (Mertens 2017). The paradigm is based on the assumption that the ownership of property and shares acts as a buffer for individuals and households facing social risks, particularly during illness, unemployment and retirement, over their life cycle. The welfare state should then support and incentivize economic behaviour that facilitates ownership and investment in order to protect individuals and households from social risks. Within this paradigm over-indebtedness is a situation which seriously endangers the capacity of personal assets to act as a buffer against social risks.

Traditionally the role of markets in providing social protection has been understood through wages and business income, which are then used as savings, sometimes through private insurances acting as buffers against social risks. In terms of welfare state classification, where social risks are pooled by the state, by employers or in the market, credit-based social policy is connected with the role of private wealth and financial markets. Prasad (2012) adds a new dimension to the role of markets and credit by arguing that differences in debt levels between different countries originate from the compensatory character of credit. In the credit-based paradigm is it believed that credit may also compensate for the lack of life cycle-specific public benefits, such as child allowances or housing benefits, and may serve as an instrument for social mobility when allowing both property investments (homeownership) and human capital investment (educational loans) (Logemann 2012, p. 203).

Credit-based social policy has been pursued to enhance social and political stability, or discipline endorsed to promote neoliberal capitalism (Soederberg 2014). As Harvey (1978, p. 15) already notes: "a worker mortgaged up to the hilt is, for the most part, a pillar of social stability". During times of labour shortages, employers preferred to hire married men with mortgages who were tied down by debt and responsibility. Already the instalment plans used to sell cars and household appliances forced the workers to adjust their lives to the discipline of monthly payments (Ramsay 2017, p. 27). With financial deregulation and economic and political pressure on welfare state finances, homeownership has become an increasingly important tool in risk protection. Mortgages appear as an individual strategy for attaining economic security. Home equity can be used to finance current and future consumption as well as emergency cash and disguised retirement saving (Schwartz 2012, p. 48). During crises, the value of a home can be realized through specific financial vehicles.

Borrowing ideas from Foucault, Lazzarato (2012) argues that a debt-dominated economy has created the "indebted man" who is supposed to learn to exploit credit markets appropriately and develop a way of life, discipline, attitudes and conduct which fits into the logic of the markets. Individuals are expected to take into account the credit scoring technologies and teachings from the financial literacy education movement in their daily lives. According to Lazzarato, debt is not only an economic mechanism but also a technique of "public safety" through which individual and collective subjectivities are governed and controlled. Soederberg (2014) takes a step even further when arguing that capital exploits workers through the credit system, where stagnant wages are compensated with high-cost credit. According to Soederberg the rhetoric of democratization of credit, financial inclusion and consumer protection is used to normalize credit as a disciplining instrument of the neoliberal state. Soederberg has coined the term "debtfare". The debtfare state imposes the market discipline of high-cost credit to the poor and serves the interests of the "poverty industry".

In short, credit-based social policy has three dimensions. Firstly, it is about the use of loans as a means of social policy, for instance, through public loan programmes and repayment subsidies. The idea is to help individuals and households accumulate capital which could be used to face social risks. Secondly, it entails using loans as a substitute for social policy, as is the case when households make use of commercial credit offers in order to obtain social or health care services or when they use credit to finance everyday consumption needs emerging from social risks such as unemployment or work disability. Thirdly, and most importantly for the context of this book, credit-based social policy deals with the rules and regulations concerning consumer credit defaults.

In many respects, our six countries provide interesting avenues to study credit-based social policy. The policies facilitating credit-based social policy can be traced back to the Reagan era in the US and the Thatcher era in the UK. The US has promoted homeownership through mortgage interest deduction and the UK with mortgage interest relief at source (Ford 1988; Mian and Sufi 2015a). In the US, government-sponsored enterprises (GSEs) – such as Fannie Mae (the Federal National Mortgage Association, FNMA), Freddie Mac (the Federal Home Loan Mortgage Corporation, FHLMC) and Ginnie Mae (the Government National Mortgage Association, GNMA) – improved low- and middle-income households' access to homeownership by lowering the cost of mortgages by extending guarantees and building a secondary market for mortgage-backed securities (Fligstein and Goldstein 2012). Most importantly, that happened without any additional burden on the taxpayer at the time. The same holds true for the growing student loans markets in the US which have been accompanied by a gradual reduction in public support for higher education. Instead of trying to fight the massive increase in tuition fees with direct support to higher education institutions, the US has allowed the shift from grants to loans (Quinterno 2012; Williams 2006).

The US welfare state demonstrates that credit may cushion social risks such as unemployment and illness, serving as a "debt safety-net" (Montgomerie 2013; Trumbull 2012). For example, if a worker loses his job but can skip mortgage payment without foreclosure, he can seek work without selling the house. In this case, the mortgage has a feature resembling unemployment insurance (Mian and Sufi 2015a, p. 69). Credit can also compensate for stagnant wages, as the US case demonstrates. In the US, mortgage-credit growth between 2002 and 2005 was negatively correlated with income growth (Mian and Sufi 2015a, p. 79).

Public policies concerning credit access, taxation and debtor protection are central features of the Anglo-liberal welfare state model (Crouch 2009; Hay 2011, 2013; Montgomerie 2013). Also, Germany, the Netherlands and the Nordic countries have a long history in promoting household savings, especially homeownership (Mertens 2017; Poppe 2008; Poppe et al. 2016). It can be also argued that welfare state interventions such as sickness and unemployment insurance have been supporting the use of credit by underwriting potential risks or problems with its use. As Janet Ford (1988, p. 39) observed, sick pay, health care provisions, unemployment benefits and pensions reduce the uncertainties relating to income continuity or the need to set money aside for cases of emergency and make credit a possibility.

As opposed to mortgages and student loans, credit-based social policy has not been actively promoting the use of credit to finance health care (Mertens 2017). However, unlike the health care systems in Europe, the US welfare state does not provide universal coverage. That leaves a gap to be filled through accumulation of medical debt. Given the catastrophic nature of health care costs for the uninsured, medical debt can amount to substantial volumes. In the absence of universal health care or employer-sponsored health care provision, the cost of treatment for many households is too high to be paid out of current incomes, inducing the use of credit and particularly high-limit credit cards. Private consumer spending on health care – which constitutes the main difference between American and European expenditure patterns – is a compensatory feature resulting from an underdeveloped public system of health provision. A series of empirical studies on bankruptcies in the US in the 1980s and 1990s showed that bankruptcy is a middle-class phenomenon representing a pragmatic response to a high debt economy where people have little public support in the event of unemployment or sickness (Ramsay 2017, pp. 31–32). More generally, the use of credit, for example with credit cards, to finance everyday consumption can be seen as a strategy to adapt to social risks which are not covered by the welfare state.

METHOD AND DATA SOURCES

We use a comparative policy analysis to describe how policies pertaining to over-indebtedness, causes of over-indebtedness and consequences of over-indebtedness differ across countries. With regard to data sources we rely mostly on published data and literature from various fields, including legal studies, economics, social epidemiology and comparative welfare state research. A key source of illustrative examples is the 2013 Civic Consulting of the Consumer Policy Evaluation Consortium report (CPEC 2013). This report, produced at the request of the Directorate General Health and Consumers (DG SANCO), included analysis of 277 stakeholder interviews in all European Union (EU) Member States (covering the financial industry, civil society organizations, public authorities and independent experts) and a total of 120 face-to-face interviews with over-indebted households in six countries (France, Hungary, Germany, Slovenia, Spain and the UK). It also involved desk research and analysis of available statistical data; an analysis of specific aspects in selected Member States through country experts; and an EU27 survey of organizations active in addressing instances of over-indebtedness, debt counselling and guidance services.

With regard to debt collection procedures and personal insolvency regimes we rely on the rich, mostly juridical, literature in the field. We also utilize German credit insurance company Euler Hermes' open online database of debt collection systems in 44 countries. The country profiles compiled by the company's debt collecting experts review factors such as collection practices, court proceedings and insolvency proceedings that will impact collection of debts in a country (Euler Hermes 2017).

In studying the causes and consequences of over-indebtedness we would have liked to rely on national or comparative register data. While register data produced for administrative purposes has shortcomings, it does not suffer from self-reporting biases. As a country with a long tradition of public registers, Finland has excellent data sources for conducting social epidemiological studies on over-indebtedness. The availability of excellent registers and the possibility of merging them allows, for example, study of the intergenerational effects of over-indebtedness. Unfortunately, similar registers are not available for all countries. A few previously unpublished examples from the Finnish register studies are given.