Plan your way out of debt

By Howard Gannaway

Can you plan your way out of debt? This article will, through a series of intellectual leaps and probably rash generalisations seek to explore whether the insights and practices of Financial Planners can be of any use to debt advice practitioners. The observation that prompted these questions was that debt advisors are frequently faced with clients who are "repeat offenders", that is to say, who find themselves back in the same position of over indebtedness only a short time after having been "sorted out" by the debt advisor the first time. In a successful Financial Planning practice, on the other hand, clients moved through an established process towards long-term goals, equipping themselves with analytical tools and resources to keep them moving forward and avoid setbacks.

So what are the similarities and differences between planning clients and debt clients? Most debt advisers would have at the top of their list of differences the amount of money at their disposal. People who are the clients of Financial Planners usually have much more money than the clients of debt advisers. This is generally true but Financial Planners do work with clients with a wide range of assets and incomes. The principles of successful Financial Planning can be and are applied equally well to a client who has an annual income of €500,000 as to one who has an annual income of €50,000.

The obvious question that arises from this is whether there is an amount of income below which it is impossible to establish principles of sound personal financial management? This is a large question for another discussion elsewhere but national Governments manifestly believe there is a lower limit as they seek to keep people above it by means of welfare benefits and other social mechanisms.

Most debt advisors work on the basis that their clients are able to establish *some* principles of sound financial management. The use of a personal or household budget is established in debt advice practice both at the level of voluntary arrangements and in most compulsory arrangements as well. Indeed, most debt advisers would say that the formulation of a personal budget is one of the first steps to be taken with all clients, even those who are not yet at the stage of having to make arrangements with their creditors.

One area of similarity between many debt clients and planning clients is that of aspiration. Admittedly, many debt clients become over indebted through the need to pay for essential items such as fuel and food but there are also many whose spending is on items that imply a higher level of income than actually exists at the time and is, in effect, aspirational spending. Financial Planners would say that one of the key elements of the planning process is aspiration. The first stage of the Financial Planning journey is the setting of objectives, which involves clearly identifying and quantifying the objective and also situating it in time. To be a real objective it must also have the aspirational factor of being something the client really wants to achieve.

What are the objectives that Financial Planners normally assist with? All clients are different but most planners will agree that the following objectives are common to many of their clients in one form or another. In no particular order of priority, most would say that being financially stable in the present is crucial. This would include not only having sufficient income to meet present spending needs but also sufficient to accumulate for future needs. There must also be measures in place to provide

protection against unexpected financial shocks. Most planning clients also aspire to a time in the future when they will be able to live in a comfortable style without the need to work if they choose not to (often referred to as “retirement”!)
Along the way, many people wish to purchase a home and make provision for the expenses associated with having children. The point here is not the particular specific objectives but rather to note that the Financial Planning process is able to take any realistic objectives and put them into a framework for achievement.

Does this differ from the approach of good debt advisors? The differences are probably more of degree rather than absolute differences of style or process. The focus that debt advisers bring to stabilising the client’s current situation is of key importance and is also aspirational. The debt adviser in effect says to the client that it is possible to stabilise your present financial position if you follow the steps I shall set out – you *can* change your life. However, many debt advisers will also say that, for a variety of reasons such as pressure of work or funding restrictions, they can only really focus on stabilising the present. The question this article seeks to pose is whether the difference of aspirational and time scales between the debt advice process and the Financial Planning process could bring another valuable dimension to the debt advice process.

Financial Planners present to their clients the prospect of a longer journey and the belief that, if you stick to the plan, you can proceed systematically to achieve all your objectives. To see how this thinking can be put into service for debt advisors, let us first suggest a way of describing stages on the journey that will be meaningful to all individuals, whether they are the clients of debt advisers or Financial Planners – or just working things out on their own!

Table 1 seeks to describe four stages based around the variable of control, that is, the extent of control that an individual has over their finances.

Table 1: Four stages of control over personal finances – high level

	Chaos	**Out of Control**	**In Control**	**Wellbeing**
Objectives	X	X	?	√
Policies	X	X	?	√
Income	X	?	√	√
Expenditure	X	X	√	√
Future	X	X	X	√
Threats	X	X	?	√
Reviewed	X	X	?	√

(The titles of the stages should only be seen as working titles. Commentators who have seen this table as part of a seminar presentation[1] felt that the titles were a little abrupt. In particular, the use of the term ”Chaos” was felt to be potentially unhelpful and demotivating in a debt advice context.)

For each stage of control, the table suggests which elements of financial management/planning may be present/under control or absent/out of control. So, for example, the stage of “In Control” describes someone who may (but probably does not) have clear objectives and policies established, who does have a stabilised and sustainable pattern of income and expenditure, who has not established control over their future objectives and so on.

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[1] Seminar on Financial Education held in Utrecht in June 2007 under the auspices of the European Consumer Debt Network (ECDN)

“Objectives” refers to whether an individual has established any clear objectives for states or conditions that they have not currently achieved. “Policies” refers to whether an individual has policies or principles which they use to help them make financial decisions on an ongoing basis[2]. “Income” and “Expenditure” refer to control over currently sustainable patterns of income and expenditure. “Future” refers to whether the individual has taken steps to ensure that financial resources will be available to meet future objectives (e.g. retirement)

Table 1 looks at these stages from a fairly high-level analytical viewpoint. Table 2 suggests some actual events and situations that might apply in each stage.

Table 2: Four stages of control over personal finances – “on the ground”

	Chaos	**Out of Control**	**In Control**	**Well-being**
In work	?	?	√	√
Making ends meet	x	x	√	√
Budgeting	x	x	√	√
Saving	x	x	x	√
Debt payments manageable	x	x	√	
Assets at risk	√	√	x	x
Assets seized	√	x	x	x

How might a framework such as this be of benefit in a debt advice setting? To be of any use we do of course have to share an assumption that it is better to be in control of one’s finances than not to be in control. If so, then this framework might be of use, firstly, by showing that there are other options than either being in Chaos or about to be in Chaos. Secondly, it says that there is a progression that can lead to greater financial control and greater wellbeing and indicates specific steps along this journey. Clearly, individual debt advisers may want to tailor the content of individual steps to meet their own situations.

The framework has yet to be tested thoroughly in a practical setting. It grew partly out of some work that NIACE was doing with a debt advice agency in the UK who were keen to explore how clients could use models of learning to progress beyond a repeated cycle of over indebtedness. In this work it was recognised that not all clients could be engaged in this process and that it had to be offered as an option. At the initial interview, clients were informed that the agency offered two levels of service, one which sought to rescue the present position from impending chaos and the other service which aimed to help them avoid getting into the same situation again in the future.

It is recognised that clients faced with all the stresses of serious indebtedness will be unlikely to immediately respond warmly to a vision of future financial “Wellbeing” so the process proceeds in smaller steps, initially working only on the need to have a written budget. However, the aim is that, for those clients who are able to proceed on this path, there will be a recognisable series of steps that can be taken to help sustain financial control and ultimately wellbeing.

In the UK at the present time, there are growing moves to make links between debt advice, which is generally seen as a rescue mission and “financial capability” which is

[2] See Policy-Based Financial Planning Provides Touchstone in a Turbulent World
by David B. Yeske, CFP®, and Elissa Buie, CFP®
http://www.fpanet.org/journal/articles/2006_Issues/jfp0706-art6.cfm

a term being used to describe a more educative process of financial learning. One of the potential areas of benefit for a framework such as the one discussed here is that it can help to make links between what are currently two quite separate groups of practitioners so that clients can become learners and ultimately more financially successful.

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