

Resume

Debt as a shared responsibility:
A present-day application of the *debt jubilee*.

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Resume of a position paper written as part of the three-year programme Finance and the Common Good (2019-2021) of Socires and the Sustainable Finance Lab.

June 2020

Finance
and the
Common
Good



Towards relational finance

Introduction

Debts have always been a moral issue. They are laden with norms and values. Being in debt brings value judgments. Creating debt creates responsibility. The question is: are we treating debt properly today? Do debts and the relationships they imply need to be reassessed?

Debts have been increasing rapidly, even more so after the warning calls of the financial crisis that started in 2008. Since then debt worldwide increased with an additional 80 percent. This debt mountain is looming as a big threat over the world-economy. In addition, it augurs serious troubles for numerous individuals in debt as well as countries that are in debt.

Households, companies and governments take on debts to finance activities and investments. As long as the activities financed by debt are productive and as long as this increases incomes, debts contribute to the development of society and its economy and can be repaid with the newly generated income. When general trends become negative, as now during the corona crisis, debts tend to become unproductive. They can even turn into a lead weight that draws people, companies, organizations and countries down. The question then is: who will take responsibility?

In today's Western world, and certainly in the Netherlands, debtors bear the greatest guilt. If a debt can no longer be repaid, they are held responsible. Their inability to pay interest and principal is seen as negligence. Lenders have rights, often supported by law and courts, to recover their debts, including collection costs and penalties.

Ironically, when really large creditors (the banks) get into trouble, governments step up to rescue them.

Likewise, when countries are unable to pay their debts, such as Greece recently, they are considered guilty and must pay up; they are expected to meet their obligations or, if they are unable to do so, take far-reaching measures, such as retrenchment, privatisation, liberalisation, and added flexibility in the labour market. At present, Italy, with its high level of debt, is in the dock as far as the Netherlands is concerned. If it wants aid, it will 'ultimately' have to take measures to better its behaviour.

For the greatest part of our history this was different. Creditors were suspect and held morally responsible for bad debts. Rulers in the Babylonian Empire (1100 BC) recognized that it was undesirable to hold subjects to their debt obligations 'to the last dime'. They devised the debt jubilee, a cancellation of debt, liberation from slavery and the return of confiscated land once every seven years or once every seven times seven years. The objective was to have the debtors participating fully in the economy again.

In many ancient writings, including the Bible and the Koran, creditors face moral suspicion, and charging interest on a loan is condemned. We can conclude that value judgments and attributions of guilt change over time. This is a good time to alter value judgments and attributions of guilt once again, and re-evaluate the moral characterizations of debt, debtors and creditors.

In this position paper, based on the principle of the debt jubilee and applying theological, anthropological, philosophical as well as economic perspectives, we call for a new moral characterization of debt, debtors and creditors, and propose institutions that do justice to this moral reevaluation.

We focus mainly on household debt, individual debt and country debt. Corporate debt is excluded from this consideration.

Debt is more than a transaction between two parties; it also signifies a relationship between those parties. We propose that debt is not only the fault of the borrower. It is a shared responsibility. And in exceptional cases, also a common responsibility.

Debt is the responsibility of both the debtor and the creditor: they share the responsibility when debt becomes problematic and stands in the way of a full and healthy life of either party. That is the shared responsibility.

If externalities for which neither the debtor nor the creditor is to blame, such as the corona crisis, are the cause of unproductive debts, the community also shares in the responsibility. Then we speak of a common responsibility.

Should cancellation be necessary at a given time for both prudent and moral reasons, the question becomes how to identify and express shared and common responsibilities in a concrete distribution of the loss. The aim is that everyone, including people and countries in debt, can participate fully in society. Debt resolution, including debt cancellation, should be the norm when debt prevents full participation in society.

We propose a moral paragraph in debt contracts to express those shared responsibilities. Such a paragraph incorporates conditions for cancellation. We also propose an international approach to unproductive national debt.

Inspired by theological, philosophical and anthropological perspectives, we advocate a re-evaluation of debt and the question of debt. In doing so, we support the findings of the anthology ‘Verlossing van Schuld en Boete’ (‘Redemption of Debt and Penalty’, edited by Stijn Verhagen, Lilian Linders and Marcel van Dam 2014). Just as the authors of this book, we are concerned with a change in attitude towards debt and the relationship between creditors and debtors. This change is reflected in a proposed institutional innovation. A debt-free economy is neither conceivable nor desirable, but a society free of the current heavy moral burden of debt should be possible.

We draw the following conclusions and make the following concrete recommendations for realising new debt practices.

Conclusions and recommendations

1. **The mountain of debt must be drastically reduced for the sake of a sustainable society. That is a society without excessive differences between rich and poor, without disruptive financial instability, and without people and countries succumbing to the burden of debt.**

Debts are good and useful when they enable productive activities. Debts become problematic when they take people, businesses and economies down. The current debt mountain is becoming unsustainable. It undermines the financial system, increases inequality between individuals and between countries, and incapacitates numerous individuals and countries.

The debt mountain must be drastically reduced. Numerous measures are currently being proposed and taken to address the problem of debt, prompted, amongst other things, by the corona crisis. We embrace many of these measures - anything that reduces the mountain of debt and alleviates problematic debt is fine as far as we are concerned. It is good to reverse the tax benefits of debt financing. It is good to relieve young people of their debts, and to offer more help to debtors. It is good to restrict consumer credit, and to lower the maximum interest rate on consumer credit significantly. It is good to relief and assist countries heavily in debt.

2. **Culture change.**

Inspired by theological, philosophical and anthropological perspectives, we advocate a re-evaluation of debt and the question of debt.

We are concerned here with a cultural change in attitudes to debt and the relationship between creditors and debtors. A debt-free economy is neither conceivable nor desirable, but a society free from the current heavy moral burden of debt should be possible.

3. **A matter of shared and common responsibility.**

Debt is more than a transaction between two parties; it also signifies a relationship between those parties. We propose that debt is not only the responsibility and guilt of the borrower. It is a shared responsibility; the creditor and the debtor enter into a relationship with mutual obligations and responsibilities. And in exceptional cases, it is also a common responsibility.

Debt is the concern of both the creditor and the debtor: they share the responsibility when a debt becomes problematic and impedes responsible actions by either party. That is the shared responsibility.

If externalities that are not the fault of either the creditor or the debtor, such as the corona crisis, are the cause of unproductive debts, the community also shares in the responsibility. In that case, we speak of a common responsibility.

4. **A moral paragraph.**

We propose a moral paragraph in a debt contract to express shared responsibilities. This may specify conditions for cancellation. This paragraph also articulates the responsibility of the community when debt becomes a problem.

Should cancellation be prudent and morally necessary, the question becomes how to identify and express shared and common responsibilities in a concrete distribution of the financial consequences.

The goal is that everyone, including people, companies and countries in debt, can participate fully in society. Cancellation should be the norm when debt stands in the way of full participation in society. Forgiving is part of cancellation. As the prayer Our Father says: "Forgive us our debts as we also have forgiven our debtors."

5. **Regional credit banks.**

An institutional invention that we propose in order to nurture and shape a new culture is the creation of regional (cooperative) credit banks (or a reform of existing credit banks). These banks serve the purpose of having people to participate fully even if they have problematic debts or are financially vulnerable. They do this by taking over problematic debts (after a write-down of the value), agreeing with the debtors on what their responsibilities are. The debtors subsequently deal with a single party (as in the Swedish model). This effectively means the end of debt collection agencies, curators and debt restructuring. Debtors take their responsibility, for example, by deploying Buddy (a digital budgeting system).

The principle of jubilee means that every seven years the regional bank cancels the debts. Debtors have the right to a clean slate.

People in a vulnerable financial position can turn to the credit bank for credit for necessary purchases. This would undermine the business model of companies that profit mainly from consumer loans.

Banks, housing cooperatives, health insurance companies, energy suppliers and local authorities are all parties that can and may want to participate in a regional credit bank, partly in order to achieve their social goals. The cooperative form would therefore be suitable for the organisation of the regional bank.

6. Shared responsibility for problematic debts of countries.

When debtors are countries, the same principles apply. There is a shared responsibility because creditor countries have just as much responsibility when debts become problematic as debtor countries.

The world community shares responsibility when a) extreme circumstances play a role (e.g. corona crisis, corruption) and b) the debt hinders the proper functioning of economies.

The Brady solution to Mexico's problematic debts is a good example of such a shared solution. An international fund is created that takes over problematic debts of countries (after a downgrade) and strives for cancellation. Special drawing rights can be a useful instrument for this purpose.

Elaborations of the institutions we propose

The regional credit banks

Following the Swedish model, each region creates a (cooperative) credit bank with the main social objective of preventing of and dealing with problematic debts. (Sweden has a national institution; with its regional approach to government, a regional organisation in the Netherlands would be more natural, although a national coordinating institution may prove necessary). Insofar as such banks already exist (and they do), they would be transformed as needed.

Financed by public and private funds, these cooperative credit banks lend to people who cannot get loans for necessary expenses from regular banks (which are reluctant to share responsibility) or from retail companies (such as Wehkamp, Dutch online shop).

The cooperative credit bank refinances loans that are problematic. It takes over claims at a discount. The claims are purchased from private parties and possibly also from housing cooperatives, health insurance companies, energy companies, the CJIB (central collection agency for fines) and the tax authorities (all according to the Swedish model). In agreement with the debtors, the regional bank writes off part of the face value of the debts. The creditor can agree voluntarily with the write-down but the credit bank will have enforceable authority to decrease the debt with a reasonable amount in order that the creditor takes his responsibility. From then on a borrower with problematic debts has to deal with only one debtor.

Shared responsibility is an explicit part of the agreement. The common responsibility is also made explicit. In that case the community (represented by the local government), takes responsibility in resolving the debt (as is happening in Corona time).

The debtor party agrees to the use of the Buddy approach or any other method to take personal responsibility.

The principle is that after so many years, say after seven years, in the system of the credit bank, the debts are cancelled. That is the jubilee.

Participation in this credit bank by private parties, such as banks and local enterprises, contributes to the realisation of their social "purpose" or "corporate social responsibility". Banks, in particular, have a social benefit from participation.

The credit bank eliminates the growing debt recovery sector. It makes debt collection agencies, curators and armies of municipal officials who are now engaged in debt obsolete. A company such as Wehkamp will have to change its business model; an era when retailers profit from people not being able to pay their debt is over.

This proposed credit bank corresponds with the National Guarantee Fund proposed by the SchuldenLab (Debt Laboratory) led by Mr. Gerrit Zalm. This fund would buy irrecoverable debts. Zalm receives support from the same parties involved in the credit bank in our proposal. The SchuldenLab also proposes to cancel debt and to reduce debt restructuring to one year.

Our proposal goes a few steps further. The credit bank is regional because it needs to provide more than debt restructuring; employees of the credit bank enter into a relationship with the debtors, seek solutions, and call upon creditors to assume their responsibility. Inhumane debt restricting programs are over: the goal is full participation of the debtor in society. Another difference is the involvement of all parties in a cooperative organisation. The regional credit bank is a public-private partnership.

A moral clause in a loan agreement

With the existence of a credit bank and its intermediary role, we propose the addition of a moral clause to loan agreements as follows. This makes explicit the shared and common responsibilities.

The creditor and the debtor have a shared responsibility for this agreement. They enter into a relationship based on mutual trust and in which each party assumes his or her responsibility.

The creditor takes responsibility for complying with standards as laid down by law and by supervisors, and acknowledges a duty of care should the debtor unexpectedly be unable to pay the agreed principal repayment and interest. Should the loan be transferred to a credit bank for that reason, the creditor will assume his or her responsibility by agreeing to a fair and reasonable write-down of the debt amount, to be determined by mutual agreement.

In this agreement, the debtor agrees with the creditor the term at which the debt will be cancelled and under what conditions. The guideline is seven years. This is based on the borrower assuming his or her responsibility.

In the case of a mortgage, the amount of this agreement is the outstanding amount of the loan that is not covered by the market value of the collateral.

The debtor assumes responsibility to comply with the terms of the debt agreement. In the unlikely event of failure to do so, the debtor assumes responsibility for making reasonable and fair arrangements with the creditor, and if, for example, the existence of multiple debts makes it impossible to do so, to transfer the debts to a credit bank and to make clear arrangements with that bank for resolution.

The responsibility of the debtor consists of taking measures such as calling in assistance (buddies/helpers), a budget coach (digital or personal) and other interventions that are necessary in consultation with the other party (the credit bank) in order to continue to participate fully in society. In the event of further problems, the debtor takes responsibility for requesting advice and the necessary help.

The baseline is that a debt that becomes problematic because the borrower cannot pay off the debt has a limited duration; seven years after the problems have been acknowledged by both parties, the debt will be cancelled, provided that both parties assume their specified responsibilities. (In the case of a mortgage, for the unsecured amount).

Should the problems of the creditor and/or debtor arise due to matters beyond their control, for example economic adversity, social developments, natural disaster, virus outbreak, the community in the form of the (local) government has a responsibility to take over (part of) the debt.

The community also takes this responsibility should both parties fail to reach an agreement, with or without the mediation of the designated credit bank, and the debtor finds himself in a situation that is unworthy and unnecessarily impedes proper functioning in society.

The position paper is largely based on contributions from experts with different disciplinary backgrounds during a workshop held on March 12th and 13th in Utrecht in the last minutes before the lock down. In addition, we also consulted various experts.

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June 2020