Consultation response:
HM Treasury-British credit unions at 50

Response by the Money Advice Trust
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Introduction

About the Money Advice Trust

The Money Advice Trust is a charity founded in 1991 to help people across the UK tackle their debts and manage their money wisely.

The Trust’s main activities are giving advice, supporting advisers and improving the UK’s money and debt environment.

We give advice to around 140,000 people every year through National Debtline and around 30,000 businesses through Business Debtline.

We support advisers by providing training through Wiseradviser, innovation and infrastructure grants.

We use the intelligence and insight gained from these activities to improve the UK’s money and debt environment by contributing to policy developments and public debate around these issues.

We help approximately one million people per annum through our direct advice services and by supporting advisers through training, tools and information.

Public disclosure

Please note that we consent to the public disclosure of this response.
Introductory comment

Credit unions play an important part in providing access to unsecured and secured credit for people who might otherwise find it difficult, except through high-cost or unregulated sources. In this they help to reduce financial exclusion and develop the creditworthiness of their members in a regulated environment. Credit unions can, for example, be good places to save small sums towards expected large expenses like a holiday, a cooker or a fridge. From a member’s perspective, credit unions are generally a positive experience, enabling them to: save surplus income, obtain small or medium-sized loans and take part in a socially-cohesive scheme.

We need to be clear that it is not always the best option to take out credit even through a credit union. Credit unions are not always the right alternative to a payday loan. Often people should be avoiding further credit altogether (affordable or otherwise) and should instead be turning to debt advice services to get their finances back on track.

As we are not part of the credit union movement, we have made comments in relation to the wider issues of debt and savings. We have left suggestions as to how credit unions could benefit from reform and regulation to those who know the industry best.
Responses to individual questions

Question 1 – Do you agree that the basic structure and objects of a credit union remain appropriate? What changes, if any, are required?

We cannot answer this question in any detail. Clearly there have been substantial recent changes put in place to address this issue. There could be further examination as to how the objectives could be adapted to ensure they are suitable for the promotion of credit union lending to small businesses.

Question 2 – Is the procedure for setting up new credit unions appropriate? What changes, if any, are required?

We cannot answer this question in any detail. Access to support for the new credit union such as being able to use a common IT structure and back-office facilities would clearly be beneficial as there seems little point in starting from scratch. Such support will also assist with costs and the professionalism of the service.

Question 3 – Are the concept of the common bond and the wider rules around membership still relevant and valued by the credit union movement? What changes if any need to be made and what would be the benefits and risks?

Whilst we appreciate the concept of the common bond, this can in some circumstances obstruct efforts for individual employers to join schemes. We would like to see the development of an easily accessible credit union with national coverage, that employers can join to enable their staff to enjoy credit union facilities and includes payroll deductions for their staff, even if in different sites around the country.

Question 4 – Are the various limits imposed by legislation at the right levels to allow credit unions flexibility to serve and attract all kinds of members? What changes, if any, should be made?

We would expect credit unions to be better placed to be able to identify where the rules are not flexible enough for them to expand services for members or to serve new groups such as small businesses.
The Centre for Social Justice, in their recent “Restoring the balance”¹ report, proposed that some credit unions could become “community banks”. They define this as follows.

“A Community Bank would be a type of member-owned credit union that is able to offer ethical affordable financial services – including low cost loans, mortgages and bank accounts – to almost every member of the community, regardless of credit history or income. This is because the ‘one size fits all’ regulations appropriate for smaller credit unions, have limited the growth, sustainability and professionalism of the best and most innovative credit unions in Britain. This status will only be available to a select few credit unions that meet strict requirements to ensure they are well run and have strong stable finances independent of government or charitable subsidy.”

We cannot comment on whether there is an appetite within the credit union movement to relax credit union rules. However, the Centre for Social Justice goes on to argue:

“Some of the most successful and innovative credit unions are severely limited by existing regulation, primarily designed for smaller less professional credit unions, that prevents them from expanding and offering competitive services to people on low incomes. Because they have membership caps, restrictions on investments and have a maximum interest rate they can charge, they are restricted from growing.”

The IPPR has issued a report “Jumping the shark”² calling for an Affordable Credit Trust to build both credit unions and to promote the growth of CDFIs. This should be funded by levy on high cost lenders to generate capital. A national network could have the effect of reducing costs, provide a common technical platform and help support innovation.

“A national institution should be established with the remit of mobilising and capitalising a diverse range of local not-for-profit lenders. This institution should initially be capitalised by a one-off levy on the consumer credit market, to provide compensation for the direct financial harm it has caused.”

This idea needs to be explored in more detail as to whether it is a viable solution going forward.

Question 5 – What other help can government give to assist credit unions to attract and retain a wide range of customers and have confidence to serve all customers effectively? What changes can be made to improve this?

We would like to see further funding to be put into place to assist credit unions to attract a wider range of customers.

It is good to see that the funding already committed for the DWP credit union expansion project is already being utilised.

We are also pleased to see the commitment from banks such as Lloyds and Barclays to funding for credit unions. However, we would suggest banks could do more to assist both credit unions and offering short-term lending alternatives to the high-cost short-term credit market.

A truly innovative response from the banking industry would be to look at the example of Australia where the National Australia Bank has partnered with The Good Shepherd Microfinance and the Australian Government to offer a range of shop-front community finance products such as Good Money\(^3\) and the No Interest Loan Scheme\(^4\) which is the Australian equivalent of the social fund budgeting loan scheme. This partnership also offers low-interest loans for low-income households through the StepUP\(^5\) scheme.

Banks could further support the development and reform of credit unions as an alternative source of affordable finance. The recent Centre for Social Justice report states:

“The CSJ is calling for a radical overhaul of credit union regulation to allow high performing credit unions to become ‘Community Banks’ – effectively credit unions unleashed to provide a more comprehensive service to a wider range of people, but also subject to greater supervision to ensure they are well run organisations.”

We welcome innovations such as the London Mutual Credit Union payday loan alternative product. However, for many people, debt advice rather than a further loan may be the answer.

We would also like to see further investment in the development of budgeting or “jam-jar” accounts. This is clearly of particular importance for the DWP in looking at budgeting for those moving from weekly or fortnightly benefit payments to monthly payments under Universal Credit. It is vital that this type of account is offered on a no-cost basis to people who need them. Would credit unions be ideally placed to offer this type of product, given the correct support and funding?

The recent Children’s Society “Debt Trap” report suggested that there should be a trial of savings accounts through credit unions and other providers, including linking this in to financial education in schools, to establish the effectiveness of this approach in promoting savings to young people. The report said that some local authorities are piloting providing school children with “seed money” to open a credit union account through schools.

The BBA in its recent consultation on rebuilding the savings culture has called for the creation of a work-based savings product, which employees could take with them from job-to-job. This sounds like a good scheme, particularly if people were to be incentivised to save by the savings product being available tax-free. However, rather than setting up a new scheme altogether, this scheme could be put in place by building on the work of the credit unions. This could be achieved through a single national credit-union based scheme with common rules by way of workplace deductions from wages. This suggestion is supported by the Centre for Social Justice in their recent report.

“Given that most people want to save regularly but struggle to start, the Treasury should require employers to create a savings scheme for employees with auto-enrolment, ideally through employer-based credit unions (similar to auto-enrolment in pensions).”

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6 http://www.cuok.co.uk/whatiscuok.html
Question 6 – What reasons have prevented some credit unions from offering loans to small businesses, including sole traders, in their communities? What could be done to encourage more activity in this area and allow credit unions a greater role in supporting local small and micro enterprises?

We would suggest that part of the reason credit unions have not been offering small loans to small businesses is the consideration of risk. It is possible that credit unions see a small business as a higher risk than an individual. It would be interesting to have more information about the lending process, for example, whether credit unions consider the business plan, business budget and cash flow forecaster for a small business? It could be that credit unions are not confident in analysing the finances of a small business and therefore do not generally lend.

Generally, where Business Debtline have small business clients who need a small loan (i.e. under £10,000) and have a poor credit history, they would normally refer to the Community Development Finance Organization at http://www.cdfa.org.uk/.

Question 7 – Is there anything that government can do to improve, simplify or clarify the legislation to make rules changes and the Boards power to act easier to navigate and meet the needs of their members?

This is a question that credit unions would be best placed to answer. They will have the practical everyday experience of how the legislation and rules affect their operations and affects their members.

Question 8 – What else can the government do to encourage wider knowledge and understanding of credit unions?

It is impossible for credit unions to individually match the advertising spend of payday lenders. This was estimated in a 2013 article 9 to be:

“The sum spent on advertising by the big five payday brands is comparable with that spent by one of Britain’s leading high street banks. NatWest, Santander, HSBC and Lloyds TSB spend between £25million and £39million each, according to advertising industry sources. Only Barclays spends significantly more – £77million.”

The Government could fund awareness campaigns about the benefits of credit unions. Could the Money Advice Service promote alternatives to payday lending such as credit unions though a national advertising campaign?

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In some ways, making credit union membership “the norm” in society and to facilitate the growth of credit unions by making them easily accessible through employers, clubs and associations, unions and religious organisations will be effective. However, we appreciate that this degree of recognition and usage takes a long time to build up and become embedded across society.

**Question 9 – What can the government do to bring about further efficiencies and stability to the credit union movement?**

We would hope to see further developments through the work of the Credit Union Expansion Project to achieve economies of scale by way of collaboration and pooling certain functions. Government should consider further funding of this project if necessary to develop these aims further.

We would suggest that the Canada model as outlined in the consultation document where each credit union participates in a liquidity pool by depositing a certain percentage of its assets with a central institution is certainly worth exploring.

**Question 10 – Should the government do more to ensure that credit unions have the flexibility to run their business but protect members by ensuring sound financial management?**

It is important that credit unions can function as sustainable entities. However, given the disparate nature of credit unions from the small and localised credit union to the large, expanding credit union, it is reasonable to suggest that Government and other funding is needed to continue to support development in the sector.

**Question 11 – What can the government do to help credit unions grow while continuing to uphold strong governance and lend responsibly?**

It is of course important that credit unions lend responsibly. However, it is also important that a loan is not always seen as the answer.

The paper states:

“Some credit unions have raised concerns that increasing numbers of people are turning to them as a last resort, expecting the credit union to be able to ‘bail out’ members who have got into difficulties with high cost credit providers. Often these situations may have gone too far for credit unions to be able to help, as the customer no longer represents a reasonable risk for lending.”

We would suggest that there should be greater links forged with debt advice agencies and stronger referral arrangements put in place. We have found that, in many cases, people turn to payday loans in an attempt to solve their financial problems and to cover household bills. In our experience taking out more credit can often make a situation spiral rapidly, generate a demand for more loans in a vain attempt to keep afloat, and put off the day when people have to seek help to deal with their debts. Rather than take out more credit or turn to loan sharks to help pay their household bills, we would urge people to seek free debt advice.
sooner rather than later. We suggest that more needs to be done to ensure that lenders including credit unions refer potential borrowers to sources of free debt advice.

It is possible to argue that people are caught in a vicious circle. They do not belong to a credit union and so have not built up any emergency savings funds. They may then need to access credit for unexpected household spending and turn to payday lenders which FCA research\(^\text{10}\) shows can exacerbate the problem rather than solve it. By the time they ask the credit union for a loan, they are in such a difficult financial position that they need debt advice, and not further borrowing.

It is also important to look more widely at how people on low incomes can access alternative sources of financial help for unexpected household expenses. The localised welfare assistance scheme is not being funded by central Government from April 2015. Following the abolishment of the centrally run social fund scheme, local authorities may offer their own versions of the scheme or choose to offer no assistance at all. Perhaps Government could address this gap in provision by exploring whether funding a central scheme through the credit union movement could help.

We would like to see the credit union movement work more closely with the free debt and money advice sector. Concerns have arisen about the practice and policy of the credit union community in the recovery and enforcement of their loans. There is a balance to be struck between the understandable aims of an individual credit union to ensure its loans are repaid, and the needs of the credit union member who finds themselves in financial difficulties. If a client is unable to repay their loan to a credit union, the credit union may eventually cancel the client’s membership and set off any savings against the debt.

Although the credit union has a duty to the other members to safeguard its operation, the exclusion from membership of the credit union is an unhelpful action against the client. It goes against the ethos of credit unions, which generally seeks to promote financial inclusion.

We would like to see a re-evaluation of whether it is reasonable to use the High Court as part of credit union debt collection strategy. We would also like to explore how credit unions could exercise the forbearance strategies used by other lenders under FCA rules. There is an ongoing debate about the use of savings to offset debts owed to the credit union.

We would like to see the credit union movement recognise the Common Financial Statement (CFS) which is a standard budgeting format with agreed upper limits for spending, which the Money Advice Trust provides on behalf of the sector. The CFS is widely used and recognised within the advice sector, credit industry, regulators and public bodies\(^\text{11}\) as the industry standard tool for working out an affordable budget and offers of payment. The Trust is currently working with the Money Advice Service, Citizens Advice and StepChange Debt Charity to create an updated version of the CFS which will aim at universal recognition. Savings will be integrated into this revised CFS and accompanying guidance as a named item of spending.

**Question 12 – What experience and support can wider society most usefully share with credit unions? What can government do to support and facilitate this?**

We would like to see the credit union movement work more closely with the free debt and money advice sector as indicated above. The Government could support and facilitate this

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\(^\text{10}\) [http://www.fca.org.uk/your-fca/documents/research/consumer-research-into-the-hcstc-market](http://www.fca.org.uk/your-fca/documents/research/consumer-research-into-the-hcstc-market)

\(^\text{11}\) Full information on recognition of the Common Financial Statement can be found at [www.cfs.moneyadvicetrust.org](http://www.cfs.moneyadvicetrust.org)
agenda. There could be recognition of the importance of savings for people in debt through a credit union by way of the new savings element within the CFS. Credit unions could work with the debt advice sector to develop a support package for debt advice clients that include a budgeting account and a savings facility to help with financial recovery once debts are cleared. Would a small revolving credit facility help to smooth financial emergencies and avoid debt clients getting further into debt with high cost short term lenders?

**Question 13 – What can the government do to help credit unions achieve more positive outcomes if they get into financial difficulty?**

We would support both the suggestions outlined in the paper. It seems to make sense to strengthen the powers of the Prudential Regulation Authority to be able to intervene when a credit union is struggling.

The creation of a stabilisation fund along the lines of the fund successfully operating in Ireland would appear to be a very good idea. If small struggling credit unions can be rescued through a stabilisation fund, or at least the credit union membership be transferred to another credit union with less disruption for members, and protection for the credit union that is taking over, then this should be put into effect as soon as possible.

**Question 14 – Should the government be doing more to assist healthy credit unions to come together to benefit from the potential economies of scale which may come from the larger resulting credit union?**

This sounds like a sensible suggestion, but we will leave it to the credit union movement to suggest how this support could best be put in place to work for the benefit of those credit unions.

**Question 15 – In which other areas is government action required to deliver its aspirations for the credit union movement?**

Could the Government consider adding a small deposit as a nest egg to those who open credit union accounts to help to encourage savings? There could also be consideration given to incentives such as matched funding schemes. This approach could develop the concept whereby people on low incomes can qualify for a bonus after making regular savings for a set period. We appreciate that this is a costly option.

We would encourage the Government to develop credit union savings schemes in schools with auto-enrolment and consider assisting with the seed money to incentivise children to use their accounts.

We would also suggest Government discuss with banking trade bodies, the possibilities of developing credit unions, savings and loan products along the lines of the National Australia Bank initiatives.

The Government should explore the idea of addressing the gap in local welfare assistance provision from 2015 by setting up a centralised single scheme through credit unions.
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