



House of Commons
Scottish Affairs Committee

**Credit Unions in
Scotland**

Second Report of Session 2008–09

*Report, together with formal minutes, oral and
written evidence*

*Ordered by the House of Commons
to be printed 6 May 2009*

The Scottish Affairs Committee

The Scottish Affairs Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Scotland Office (including (i) relations with the Scottish Parliament and (ii) administration and expenditure of the offices of the Advocate General for Scotland (but excluding individual cases and advice given within government by the Advocate General)).

Current membership

Mr Mohammad Sarwar MP (*Labour, Glasgow Central*) (Chairman)
Mr Alistair Carmichael MP (*Liberal Democrat, Orkney and Shetland*)
Ms Katy Clark MP (*Labour, North Ayrshire & Arran*)
Mr Ian Davidson MP (*Labour, Glasgow South West*)
Mr Jim Devine MP (*Labour, Livingston*)
Mr Jim McGovern MP (*Labour, Dundee West*)
David Mundell MP (*Conservative, Dumfriesshire, Clydesdale and Tweeddale*)
Lindsay Roy MP (*Labour, Glenrothes*)
Mr Charles Walker MP (*Conservative, Broxbourne*)
Mr Ben Wallace MP (*Conservative, Lancaster & Wyre*)
Pete Wishart MP (*Scottish National, Perth and North Perthshire*)

The following members were also members of the committee during the Parliament:

Danny Alexander MP (*Liberal Democrat, Inverness, Nairn, Badenoch and Strathspey*)
Gordon Banks MP (*Labour, Ochil and South Perthshire*)
Mr David Hamilton MP (*Labour, Midlothian*)
Mr John MacDougall MP (*Labour, Glenrothes*)
Mr Angus MacNeil MP (*Scottish National, Na h-Eileanan an Iar*)

Powers

The committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No. 152. These are available on the Internet via www.parliament.uk.

Publications

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee are on the Internet at www.parliament.uk/scotaffcom.

Committee staff

The current staff of the Committee are Nerys Welfoot (Clerk), Georgina Holmes-Skelton (Assistant Clerk), James Bowman (Committee Assistant), Becky Crew (Committee Assistant), Karen Watling (Committee Assistant) and Tes Stranger (Committee Support Assistant).

Contacts

All correspondence should be addressed to the Clerk of the Scottish Affairs Committee, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 6123; the Committee's email address is scotaffcom@parliament.uk.

Contents

Report	<i>Page</i>
Summary	3
1 Introduction	5
Background	5
What are credit unions?	5
Funding	6
UK Government funding	6
Scottish Executive funding	7
Local authority funding	9
Recent developments	10
2 The role of credit unions in the current economy	11
Interest rate capping	12
3 Deregulation	15
4 Credit union services	20
Unified services	20
Mergers	20
Access to services	21
Current accounts	22
Wider services	23
5 Government funding	25
6 A central credit union	27
7 Financial education	28
8 Conclusion	29
Conclusions and recommendations	30
Annex: note of visit	33
Formal Minutes	34
Witnesses	35
List of written evidence	35
List of Reports from the Committee during the current Parliament	36

Summary

Credit unions are co-operative organisations which allow members to save and borrow money, described by HM Treasury as “self-help, democratic savings and loans institutions”. They also have a statutory role of providing financial education. Participation in credit unions is higher in Scotland than in the UK as a whole. Central and West Scotland alone contain 35% of credit union members UK-wide. We support the work of credit unions, considering it to be extremely valuable for both communities and individuals.

We are disappointed that ring-fenced funding for credit unions from the Scottish Executive now totals only £250,000, a sharp decrease from over £2.7m before 2008, notwithstanding that the overall pot to which credit unions can now apply to is over £42m.

Provision of low-cost, responsibly-lent finance is crucial to mitigating the debt crisis that causes so much misery in parts of Scotland: encouraging the practice of saving is equally vital to creating a generation of financially responsible people. The “credit crunch” has led to a dearth of widely available credit for those with low-income; there has never been a better time for credit unions to build on their existing success and raise their public profile.

The credit union movement in the UK sees the recruitment of more affluent members to be key to their expansion and security. We agreed with this aim, and recommend that the Government support them in this.

We are glad to see that the legislative reform proposals put forward by HM Treasury in 2008 are in line with the measures for which credit unions have been calling. These include allowing credit unions to pay interest on savings, rather than just dividends, allowing groups to join unions and changing the common bond definition to widen membership. We hope to see publication of draft legislation as soon as possible.

The Government caps the credit union interest rate on loans at 26.8% APR. Over the course of our inquiries into Poverty in Scotland, we have been shocked by the rates of interest charged by other lenders: we urge the Government to introduce a cap on interest rates for the whole financial sector, rather than just credit unions.

We are pleased to hear that the introduction of credit union current accounts has proved a success. There is room for co-ordination between unions and the Post Office to provide current accounts for the 11% of Scottish people who do not have bank accounts. We also ask the Government to provide financial backing to enable more credit unions to provide current accounts.

1 Introduction

Background

1. In December 2007, we published our Report on *Poverty in Scotland*.¹ As part of this Report, we looked at the issue of debt, finding that:

A thriving industry has grown up based upon making money from the poor and those who lack the financial education to fully understand what a particular offer entails. By adding interest and penalty charges to the original loan, lenders lock people into poverty and a never-ending cycle of debt.²

One of our conclusions was that “the impact of high cost credit could be mitigated by greater access to affordable lending. In this context, credit unions play an important role”.³ We felt that this was an area that would benefit from closer scrutiny, and therefore in March 2008, we announced an inquiry into Credit Unions in Scotland, to examine the issues of:

- The future for Credit Unions in Scotland;
- The problem of financial exclusion and financial literacy, and
- Affordable lending, credit and debt.

2. Over the course of this inquiry, we held three evidence sessions, hearing from representatives of credit union operators, debt and consumer experts and the Economic Secretary to HM Treasury. The full list of witnesses is printed at the end of this Report. We also received written evidence. In October 2008, Members travelled to Blantyre for informal meetings with the South Lanarkshire Credit Union Network, a note of which is annexed to this Report. We would like to extend our thanks to all those who contributed to our inquiry.

What are credit unions?

3. Credit unions are co-operative organisations which allow members to save and borrow money, described by HM Treasury as “self-help, democratic savings and loans institutions”.⁴ In the UK their terms of use are set out in the Industrial and Provident Societies Act 1965 and the Credit Unions Act 1979; since 2002 they have been regulated by the Financial Services Authority (FSA). Traditionally, members had to save before they could borrow, and loans were limited to a multiple of their savings. The 1979 Act defined the purpose of credit unions as:

- the promotion of thrift among the members by the accumulation of savings;

1 Scottish Affairs Committee, Second Report of Session 2007–08, *Poverty in Scotland*, HC 128

2 HC (2007–08) 128, para 128

3 HC (2007–08) 128, para 129

4 HM Treasury, *Proposed Amendments to the Credit Unions Act 1979*, October 2001

- the creation of sources of credit for the benefit of the members at a fair and reasonable rate of interest;
- the use and control of the members' savings for their mutual benefit; and
- the training and education of the members in the wise use of money and in the management of their financial affairs.⁵

4. Credit union membership is regulated through a “common bond”, in other words, the members of a union must share a common characteristic. There are four main types of bond: residence in a particular locality; being a member of, or having an association with, an organisation; working for a common employer or in a particular locality; and following a particular occupation. Interest levied on loans cannot be above 2% per month, but many unions do not charge that much; this level was raised from 1% in June 2006 to enable unions to lend more widely. Dividends may be paid on savings after expenses are accounted for; these can be up to 8% a year,⁶ but are normally no more than 5%.

5. The Economic Secretary to HM Treasury informed us that “there are 115 credit unions in Scotland with a combined membership of approximately 250,000. That represents 21% of the total of Great Britain credit unions, and about 40 per cent of British Credit Union membership in Scotland”.⁷ Around 2% of the UK population, excluding Northern Ireland, belongs to a credit union; for Scotland alone, the figure rises to 5%, and central/west Scotland accounts for at least 35% of UK credit union membership. By contrast, the participation rate in Ireland, which introduced credit unions at the same time as the UK, is 70%, and in Northern Ireland the penetration rate is 30%.⁸

Funding

UK Government funding

6. Credit unions are by nature self-funding organisations. However, the Government has a role to play in providing support funding for staff costs, overheads, training and the development of new products such as the Credit Union Current Account. The UK Government funds credit unions through the Growth Fund. The Financial Inclusion Fund (FIF) has received funding of £250 million since 2005 to support financial inclusion activity. From the FIF, £80 million has been allocated to the Growth Fund, over five years, from 2006-11, for credit union and other third sector lenders. This provides capital for small loans (typically under £400) to the financially excluded. The Budget 2009 announced that an additional £18.75m would be committed to the Growth Fund up to 2011 to enable lenders to make additional loans.⁹

5 Credit Unions Act 1979, section 3

6 Financial Service Authority, *Money Made Clear Guide to Credit Unions*, October 2007, www.moneymadeclear.fsa.gov.uk/pdfs/credit_unions.pdf

7 Q 183

8 Ev 35

9 HM Treasury, *Budget 2009*, HC (2008–09) 407, para 5.36

7. Between 2006 and 2009, £4.262m has been allocated through the Barnett Formula from the Growth Fund to Scottish credit unions.¹⁰ Unions must tender for a Growth Fund contract for funding. In the last three years, the Growth Fund has given £3,635,295 to Scottish credit unions, although this represents contracts with only eight credit unions: 1st Alliance Credit Union, Capital Credit Union, Dumbarton Credit Union, Glasgow Credit Union, Glasgow Scotcash (CDFI), North East Scotland Credit Union, Pollock Credit Union and Western Isles Credit Union.¹¹

8. In December 2007, *Financial inclusion: an action plan for 2008–11* was published by HM Treasury, announcing £12 million funding for a financial inclusion champions initiative, which supported local action plans on financial inclusion, including credit unions.

9. The rest of government funding of credit unions comes from the Scottish Executive.

Scottish Executive funding

10. As part of the Scottish Executive “Unlocking the Potential” credit unions action plan launched in 2001, all credit unions in Scotland were offered a one-off non-competitive grant from the Credit Union Kickstart Fund to help them improve and expand their services to the public. In total, 120 credit unions each received £4,000: a total of £480,000.¹²

11. Before 2006, the Scottish Credit Union Capacity Fund offered grants to credit unions of between £10,000 and £60,000. The total fund was for up to £1.1m but grants allocated to credit unions came in over budget at £1,263,192.¹³ From 2006–08, two funds provided ring-fenced funding to Scottish credit unions; the Service of General Economic Interest Scheme Fund (SGEI), and the Scottish Credit Union Assistance Fund, offered one or more awards to unions of up to £10,000.¹⁴ Of the £800,000 available from the SGEI, £663,538 was allocated and £310,352 has been allocated to unions from the Scottish Credit Union Assistance Fund.¹⁵

12. Since 2008, credit unions have been able to apply as social enterprises to the Scottish Investment Fund, a £30m fund, and the Third Sector Enterprise Fund, which is worth £12m,¹⁶ but no ring-fenced funding existed, until the Credit Union Fund was announced in January 2009, which is worth £250,000 over 2008–09 to 2010–2011, to help unions “grow and weather the global downturn”.¹⁷

13. There are differing views on whether credit unions have access to potentially a greater amount of money under the new funds available to Scottish credit unions since 2008.

10 Figure provided by HM Treasury, based on calculation that the Scottish “allocation” under the Barnett Formula is currently 8.7% of the total funding between Scotland, Wales and England.

11 Figure provided by the Department of Work and Pensions.

12 Figures provided by the Scottish Executive.

13 Scottish Executive webpage on the Capacity Fund, www.scotland.gov.uk/Topics/People/Social-Inclusion/17413/SuccesfulCU#top

14 Scottish Executive webpage on “Supporting Credit Unions”, www.scotland.gov.uk/Topics/People/Social-Inclusion/17413/Supporting-Credit-Unions

15 Figures provided by the Scottish Executive.

16 Ev 47

17 “New Credit Union Fund”, Scottish Executive press release, 12 January 2009, www.scotland.gov.uk/News

14. Like credit unions applying for the Enterprise Fund, credit unions who wish to apply to the Credit Union Fund must be established Scottish credit unions and fully comply with all relevant FSA requirements.¹⁸ Organisations applying to both funds must:

- be established third sector organisations with an appropriate legal personality, who reinvest surpluses for a social purpose;
- be located or operating/trading in Scotland—this could however include UK-based organisations working with Scottish beneficiaries, and
- have appropriate management and governance arrangements in place to support the investment.

15. The following are not eligible for the funds:

- organisations that are insolvent or at risk of insolvency;
- unincorporated associations;
- activities that support beneficiaries who live outside Scotland;
- organisations that are in the process of accessing, or have already accessed, the Scottish Investment Fund.

16. The Funds will focus on supporting organisations that want to operate in an enterprising way, therefore proposals for funding should clearly demonstrate “enterprising activity”.

17. With regard to the Scottish Investment Fund, the organisation must show that it is an established third sector organisation located and trading in Scotland with an appropriate legal constitution in place, with social or environmental aims, including related to equality and diversity, and reinvest surpluses for a social purpose.¹⁹

18. It must also have been operating successfully, partly through income generation, for at least three years and have established successful experience in public service delivery or trading in other markets. The organisation must have potential to grow their turnover and/or become financially sustainable, and must be investment-ready in terms of management, governance and financial position or in a position to become investment-ready with business support.

19. The following are not eligible for the fund:

- organisations with no track record of generating income other than grants;
- organisations that are insolvent or at risk of insolvency;
- proposals that seek to replace existing debt finance;

18 Scottish Executive, *Third Sector Enterprise Fund & Third Sector Credit Union Fund: Information and Guidance for Applicants*, January 2009

19 Scottish Executive, *Scottish Investment Fund: Investment Strategy*, June 2008

- third sector support, intermediary or infrastructure functions;
- housing construction and management operations of Registered Social Landlords (RSL) —however in line with the general eligibility criteria RSL owned subsidiary social enterprise trading companies may be eligible and it may be possible for RSLs to be part of joint-ventures;
- proposals that relate to the on-going delivery costs of services or projects;
- proposals that would normally be funded by commercial loan finance or other funding sources, and
- organisations where the beneficiaries live outside Scotland.

20. Applicants must be able to demonstrate how the investment will help to make a transformational step change in their organisation's capacity, capability and/or financial sustainability. They must also provide clear evidence of how they expect the investment to contribute towards improved outcomes.

21. All three funds will consider two main criteria when assessing whether to invest in organisations:

- Criteria 1: the outcomes for Scotland realised by the investment;
- Criteria 2: the organisational potential realised by the investment.

22. In addition, the initial priorities for the investment are:

- employability;
- environmental action;
- the underlying causes of health inequality.

Local authority funding

23. Local authorities are not obliged to give any specific amount to credit unions. From 2005–08, local authorities received funding from the £318m Community Regeneration Fund (the Fund aimed to bring improvements to Scotland's most deprived areas and help individuals and families escape poverty), and from 2006–08 11 local authorities, with the greatest problems of financial exclusion (allocations were based on levels of income deprivation and the proportion of households without bank account or savings), also had funding from the Financial Inclusion Fund, which has £10.8m.²⁰ From 2008–2011, the Fairer Scotland Fund is the main source of funds, and this is worth £435m. Local authorities can allocate funding to local credit unions from these funds in line with their individual strategies.²¹

20 Scottish Executive webpage on the Financial Inclusion Action Plan, www.scotland.gov.uk/Topics/People/Social-Inclusion/17413/22647

21 Scottish Executive webpage on the Fairer Scotland Fund, www.scotland.gov.uk/Topics/Built-Environment/regeneration/fairer-scotland-fund

Recent developments

24. The services offered by credit unions have widened slightly in recent years. Some now offer a basic bank account, which offer a cash withdrawal card and a direct debit facility. Some unions can receive BACS Direct Credit payments, and therefore members can have benefits paid directly into their accounts. Some offer Child Trust Funds, cash ISAs and various insurance products.²²

25. There are proposals to alter the regulations of credit unions in 2009 following consultation by HM Treasury in 2007 and 2008. This will be done by means of a Legislative and Regulatory Reform Order. We cover the proposals in detail in paragraphs 36–41.

2 The role of credit unions in the current economy

26. In the year since we announced this inquiry, the financial services sector in the UK has changed in a dramatic fashion. Banks and buildings societies have been nationalised, interest rates are at their lowest since the Bank of England was established, and lending has become subject to far stricter criteria than has been the case for the last decade or more. As stated in our introduction, the UK Government already recognised the role that credit unions played in providing services for those excluded from banks, to prevent them falling into ruinous patterns of high-cost borrowing. A positive move in the recent past is the introduction of the Saving Gateway Accounts Bill, which at the time this Report was published was still being considered by the House of Lords, which will establish a Government-subsidised savings scheme for people of working age on low incomes and in receipt of specified benefits.²³ These accounts have already been successfully piloted in some parts of the country.

27. Dr Goth of the Scottish League of Credit Unions (SLCU) stated “there is a retrenchment of high street banking. The potential is there to be what credit unions to my mind should be, which is community-owned, financial cooperatives”.²⁴ This was an issue we explored with witnesses in oral evidence. Ms McPhee, of Citizens Advice Scotland, set out for us the pattern that was often seen by her colleagues:

The CAB service would blame mainstream lenders in the main, because that is what we see—which is banks. The problem could be that someone has taken out a personal loan, they struggle to repay it, they get into debt with it, and then all the charges and penalty charges add up and make it worse. The way it is resolved, if you like, is a further loan, a consolidation loan, which means that they are ending up borrowing more than they started over a longer period of time. Even though the initial payments are perhaps smaller than they were paying, it is a load more debt overall and then it goes on and on. Having said that, doorstep lenders at the other end of the scale continue to do that too. It is that layering of loans. You can start off borrowing £200 but you only pay off maybe £100 of it, and then you borrow more and more and you just see it all escalate.²⁵

28. In contrast, borrowing from credit unions requires first that the member saves (in the majority of cases), and secondly that they borrow an amount they can repay. No further credit is extended by the union if the member struggles to repay, avoiding the issue of consolidation lending. In addition, the interest rate of loans is capped at 2% per month, or 26.8% APR. Mr Mark Lyonette, of the Association of British Credit Unions Limited (ABCUL), was able to demonstrate how credit unions approach lending:

23 Saving Gateway Accounts Bill [Bill 3 (2008–09)]

24 Q 89

25 Q 11

We have found, even since last September with Northern Rock, that credit unions are getting many, many more applications for loans. Unfortunately they are having to turn down more of those as a percentage than they might have done in the past. That tells us a lot about how indebted some people are. Unfortunately, we cannot be seen to be irresponsible lenders. There are people who come to you and ask for money to borrow and it is just not a sensible thing. That is where we do believe the credit union emphasis on saving as well is really important.²⁶

We applaud the efforts of credit unions to act as responsible lenders.

Interest rate capping

29. In praising credit unions for their attitude to lending, we must also comment on other lenders and the difference between the two systems. In our *Poverty in Scotland* Report we first raised the issue of the lack of a cap on interest rates levied by financial institutions.²⁷ The UK has no restriction on interest that can be charged, and we are aware of organisations that charge in excess of 100% per annum on loans. Provident Personal Credit, for example, advertises loans at 254.5% APR.²⁸ This is clearly unacceptable behaviour. Dr Goth of SLCU agreed and pointed out that Canada has an interest rate cap of 29% APR.²⁹ Reverend Blount, Secretary of the Scottish Parliament All-Party Group on tackling debt, said that interest rate capping was in force in other European countries and asserted that “it eliminates some of what goes on here but it does not appear across Europe to be creating the credit deserts that are predicted by some of those in the industry”.³⁰

30. We are aware that there are some concerns about the introduction of a rate cap, such as those brought to our attention by Mr Lyonette. Although supportive of a rate cap in principle, he told us “at this point in time, if the Government were to legislate now and put in a cap of any percentage rate for the people who were paying 700%, you would actually put a lot of those people, two or three million people who are using even just home credit for example, in a position where they would not have access to any kind of affordable credit at all. It is more a question of timing”.³¹ The Economic Secretary did not engage with our suggestions of setting a cap, saying “I do not particularly want to be drawn into saying there should be a set limit. We need to consider how we can have lending at fair rates to individuals. Depending on an individual’s circumstances, banks will make different decisions”.³² He also explained how institutions can navigate around regulations:

In Poland where the credit union movement has grown very strong since the Solidarity Movement, the Government legislated to bring in a cap which I think was linked to today’s rate, something like five times base rate, and of course what happened was that lenders who were wanting to charge extortionate rates get very

26 Q 112

27 HC (2007–08) 128, para 128

28 Information taken from Provident Personal Credit website as at May 2009, www.cashloancompany.co.uk

29 Q 144

30 Q 23

31 Q 145

32 Q 196

creative about how they can get round it because [...] you might have people putting on an insurance product, “You won’t get the loan if you don’t take that insurance product”.³³

31. In our Report on *Poverty in Scotland*, we concluded that “there is a case for Courts to be empowered to impose an interest rate cap in order to prevent severe poverty or destitution”.³⁴ In its response to our Report, the Government said that it had reservations about the concept of an interest rate cap because:

- Lenders in countries with rate caps do not provide credit for small loans repayable over a short period, thus excluding some low-income consumers from the market or leading others to take out larger loans than they need;
- The choice of products is reduced, limiting competition;
- Some low-income consumers will take out credit on products that have extra charges which are not included in the interest rate calculation, but which low income consumers are particularly likely to incur, such as late payment charges, and
- The percentage of consumers who admitted to having borrowed from unlicensed or illegal lenders was twice as high in Germany and France as in the UK.³⁵

32. We see great merit in the idea of a cap on interest rates applicable to *all* lenders. The punitive rates of interests charged not only by so-called “doorstep lenders” but other more mainstream lenders are a disgrace. The Government has set out some of the problems that it fears could arise if a cap was implemented; we do not accept they can not be overcome. For example, credit unions exist precisely to provide the sort of small, short-term loans described by the Government. **We recommend that the Government introduce a cap on interest rates for all financial institutions.**

33. We do however recognise that there are issues that would need to be addressed. A sudden change in interest rates could lead to difficulties for existing borrowers, who may find their credit abruptly withdrawn. It is also clear that, as happens with other apparently low-cost options, hidden “extras” could be introduced to offset a rate cap. Illegal lending has in the past been a substantial problem for those on low incomes. **Legislation must be introduced in a way which does not worsen the situation of those dependent on high-rate loans; if necessary, financial assistance should be given to ensure that no borrower is disadvantaged by the regulatory change. Such legislation should seek to ensure that lenders could not introduce extra hidden costs to compensate for lower interest rates.**

34. Credit unions are keen to attract more affluent users, which not only boosts their common fund but encourages participation from people from a variety of backgrounds. As Ms McGillivray told us, “One of the problems in the United Kingdom as a whole is that

33 Q 147

34 HC (2007–08) 128, para 128

35 Scottish Affairs Committee, Second Special Report of Session 2007-08, *Poverty in Scotland and Child Poverty in Scotland: Responses by the Government and the Scottish Executive to the Committee's Second and Third Reports of Session 2007-08*, HC 525

credit unions have been seen as a poor man's bank and I think that has put people off. We have certainly had people come along to South Lanarkshire who have said, 'I can't join you, I'm in work' and that is not the case".³⁶ If people are becoming wary of banks, despite the Government's indemnity of savings up to £50,000, then this is the ideal time for credit unions to step in and promote themselves to wealthier customers likely to have greater savings. As Ms McGillivray made clear, credit unions benefit immensely from the participation of the more affluent:

There was a report published in 2006 from the Joseph Rowntree Foundation [...] that identified that [...] "placing greater emphasis on credit union development based upon a cross-section of the population, including affluent sections of society [...] offers a more viable long-term model than concentrating only on financially excluded people." If we concentrate only on the financially excluded, then the credit union will not be there, because we need the savings from the other people to offer the services.³⁷

35. We questioned the Economic Secretary on how much was spent to promote credit unions. He could not tell us, but responded:

I think you correctly make a point in saying, "Is there a role for government to do more for promoting the concept of credit unions?"—rather than individual credit unions. That is something that we could take away and think about what there is we should do there. I think there is a role for SLCU, the specifically Scottish credit union representative body, to promote credit unions as well. You are right to say that we share an interest here in promoting the fact that credit unions are an important part of our financial system and perhaps we ought to be doing more about it.³⁸

We welcome the Minister's intention to consider what the Government could do to raise the profile of credit unions in the public awareness, and are glad to have brought this issue to his attention. **It is important that credit unions are supported in their endeavours to attract those with higher incomes and savings who might not previously have considered using a union. We recommend that the Government provide funding to promote credit unions across the United Kingdom to a wider public as an integral part of a comprehensive strategy of financial education.**

36 Q 18

37 Q 70

38 Q 206

3 Deregulation

36. In June 2007, the Government issued a *Review of the GB cooperative and credit union legislation: a consultation*, and subsequently published a summary of responses in December 2007.³⁹ In June 2008, HM Treasury announced plans for a Legislative Reform Order, “to enable cooperatives and credit unions to grow in economic terms, and to help increase their efficiency and ability to compete”.⁴⁰ The key measures affecting credit unions specifically will be:

- liberalising membership criteria and radically changing the definition of “common bond”, so that credit unions can provide their services to a wider range of people;
- making it possible for groups, rather than just individuals, to become members;
- allowing credit unions to pay interest on members’ deposits;
- removing the statutory limit on non-qualifying members, which would remove the current limit on deposits from those who do not qualify to become full members, such as those who are too young, and
- allowing credit unions to charge the market rate for services such as chequebooks and money transfers.⁴¹

37. The Economic Secretary told us:

[W]e will shortly be producing our responses to the consultation and also draft legislation which we want to consult on as well. I would like to think we can do that in March [2009]. Obviously there is quite a lot of pressure on the time of Treasury officials at the moment, but I am keen that we can make progress in this and I would like to think we can do it in March.⁴²

38. In evidence, we heard repeated calls for new legislation to enable credit unions to carry out their work more competitively, and with greater regard to the needs of both savers and borrowers. Many of the proposals announced in 2008 are in line with the suggestions of our witnesses. The Minister recognised this himself.⁴³

39. Ms McGillivray, of the South Lanarkshire Credit Union Network, provided an example of the need for regulatory reform:

On average, we hear from one community group per week asking to join the credit union and to put their savings in there rather than go into a bank. Because now there are not as many branches of the banks and things like that, we are more readily

39 www.hm-treasury.gov.uk/consult_creditunions_index.htm

40 “Reforms to provide access to affordable credit”, HM Treasury press notice, 30 June 2008, www.hm-treasury.gov.uk/press_66_08.htm

41 *Ibid.*

42 Q 200

43 Q 201

accessible for them. To have the legislation changed to allow groups to stay with credit unions is essential to these small groups.⁴⁴

Mr Lyonette wanted:

[L]egislation that would allow us to offer the sorts of modern services that other credit union sectors around the world offer. In Canada, they have not grown large by paying a retrospective dividend that you may or may not get six months after you have had your money in there for the year. They have been able to offer an interest rate and say, “I promise you three or 4%.” We need a modern platform for legislation.⁴⁵

ABCUL stated: “Allowing the payment of interest on savings rather than just the annual dividend will allow credit unions to offer attractive rates to compete for the savings of more affluent members of the community who may at present prefer to save with a bank or building society”.⁴⁶

40. A few concerns about some of the proposals had been raised with us during the course of the inquiry. Dr Goth believed the change in interest payments and the loosening of the common bond could lead to some disagreement within the movement.⁴⁷ South Lanarkshire Credit Union Network shared its consultation response with us, setting out its strong opposition to the end of the restriction on withdrawal of shares. On our visit to Lanarkshire, some of those we met suggested that loosening the common bond could damage the community feel of unions. But on the whole, the Government appears to have tailored its proposals to the emerging needs of credit unions. **We welcome the legislative reform proposals addressing the long held concerns of credit unions, specifically those which will enable interest rates to be paid on savings, to encourage more people to save with credit unions, and the introduction of group memberships. It is good to know that the Government is paving the way for a more modern credit union service through changing legislation. However, we should guard against any additional changes which make credit unions one more rootless financial institution. The pegs in the ground should be a clear sense of the group or community to which the union belongs, and the principle of ensuring that the union members invest in the organisation.**

41. On 14 April 2009, HM Treasury published a document summarising the responses to the consultation on proposals for a Legislative Reform Order (LRO) to amend the legislation for Credit Unions and Industrial and Provident Societies (IPS) in Great Britain, and setting out the Government’s implementation proposals.⁴⁸ These are summarised below.

44 Q 71

45 Q 90

46 Ev 44

47 Q 116

48 www.hm-treasury.gov.uk/d/consult_lro_summary.pdf

Proposal B1: Replace the “common bond” requirement for credit unions with a “field of membership” test

42. Respondents generally agreed with the Government’s proposal that the common bond should be replaced with a field of membership test in order to enable credit unions to be open to more people. As a safeguard to ensure that there would be a genuine connection between members of an individual union, the Government thought that a 2 million membership limit should apply to credit unions with geographical common bonds (and not those based on employment or association).

Proposal B2: Reform the requirements relating to membership qualifications and rename them “common bonds”

43. Government stated that it would implement Option B, the preferred option amongst respondents, which would allow a combination of any number of membership qualifications. This would allow for instance a credit union to serve the geographical area along with tenants of two housing associations and employees of two companies.

Proposal B3: Reform restrictions on non-qualifying members of credit unions

44. Currently legislation restricts the number of non-qualifying members (i.e. members who cease to fulfil the qualifications for membership, e.g. they are no longer resident in the area) to 10%. Respondents supported the Government’s view that this restriction be lifted and that credit unions should be allowed to set their own limits on non-qualifying members via their rules.

Proposal B4: Allow credit unions to admit bodies corporate, unincorporated associations or partnerships to membership

45. The Government will allow credit unions to admit corporate members and choose to offer either ordinary shares or deferred shares to corporate members. To safeguard against corporate members crowding out individual member involvement, the proportion of membership that is not individual will be capped at 10% and there will be a limit on the proportion of total assets and lending that may be held by corporate members.

Proposal B5: Allow credit unions to offer interest on deposits, provided certain requirements are met

46. The Government decided that credit unions who wish to retain the dividend may do so. Only those credit unions that can show that they have the necessary financial strength and operational ability to offer interest will be able to do so.

Proposal B6: Abolish the 8% per annum limit on dividends

47. The respondents agreed with that the limit ought to be abolished and therefore the Government will go ahead with this proposal.

Proposal B7: Repeal the “attachment” requirement, which restricts withdrawal of shares

48. A number of respondents were against this proposal and so the Government has decided to modify its proposal. Attachment will remain as a tool for the board. Credit unions will be able to offer loans where the shares are either attached or not but the Government wants individual unions to have a transparent policy on this issue.

Proposal B8: Allow credit unions to charge the market rate for providing ancillary services to their members

49. Under current legislation, credit unions may only charge on a cost-recovery basis for services which are ancillary to accept a deposit or making a loan. Respondents agreed with the proposal to lift the restriction and therefore the Government will allow credit unions to charge the market rate for providing services to their members.

50. ABCUL’s response to the implementation proposals was positive:

It’s great news that, following a comprehensive consultation to which we and our members responded, the Government has now finalised proposals for a Legislative Reform Order to update credit union legislation in Britain. This reaffirms the Government’s commitment to updating credit union legislation, which is badly needed by the sector if we are to fulfil our true potential in Britain.

In particular, we are delighted that the Government has listened to our calls to increase the limit for a common bond (which determines who can join a credit union) to two million people for geographical common bonds only and not to impose a numerical limit on common bonds which only cover people with an employment or associational link. This will enable credit unions to meet the needs of many more people.

We are also very happy that the Government has decided to allow credit unions to choose whether to offer ordinary shares or deferred shares to corporate bodies. This means that companies and social enterprises, as well as unincorporated bodies and partnerships, will be able to become full members of credit unions, allowing large numbers of organisations to benefit from credit union services for the first time.⁴⁹

51. The HM Treasury document states that the Government will publish and consult on the draft LRO in the near future.⁵⁰ **We look forward to the publication by the Government of draft legislation on regulatory reform of credit unions as soon as possible.**

52. In addition to the Government proposals for a Legislative Reform Order, the Co-operative and Community Benefit Societies and Credit Unions Bill had its second reading on Friday 24 April 2009. The Private Members’ Bill was introduced by Malcolm Wicks MP, but was drafted by HM Treasury and therefore has government support. One of the

49 “Three cheers for legislation reform proposals”, ABCUL press release, 15 April 2009

50 HM Treasury, *Proposals for a Legislative Reform Order for credit unions and industrial and provident societies in Great Britain: response to consultation*, April 2009, p 6

main objects of the Bill is to give the Treasury powers to make provisions for credit unions corresponding to any provisions applying to building societies.⁵¹ The Explanatory Notes to the Bill state that:

This would allow changes to be made to bring credit union law in line with building society law on specific issues. A number of provisions of the Building Societies Act 1986 deal with issues specific to institutions which accept deposits and could be relevant to credit unions. These include requirements to provide a summary financial statement to members and depositors, audit and accounts requirements, rules on electronic voting, issues relating to directors and governance matters and duty to disclose interests, ownership of subsidiaries and prohibition on floating charges and restrictions on dealing in derivatives and certain other financial instruments.⁵²

51 Co-Operative and Community Benefit Societies and Credit Unions Bill [Bill 14 (2008–09)]

52 Bill 14—EN (2008–09)

4 Credit union services

Unified services

53. Each credit union operates independently and offers services based on its size, income and the needs of its members. This is an entirely understandable state of affairs. It does however lead to confusion among the public about what services, e.g. insurance, cash ISAs, bank accounts, are offered by each union. On a smaller scale, even individual products, such as home insurance policies, will vary from union to union. One effect of this is that those attempting to publicise credit unions cannot give a coherent idea of what they offer. In Ireland, where participation rates in credit unions are so high, most unions offer common products and can therefore create a firmer impression of what they offer in the public consciousness.⁵³ We discussed this on our visit to Lanarkshire, and found that although there was some reservation about how far unions would be able to offer the same products everywhere, the idea of “branded” basic services which were the same in each union had some support.⁵⁴

54. We recognise that it would not be possible for all credit unions to offer the same services, but we believe that some standardisation of basic products, on a regional if not national level, would improve the visibility of unions, reduce advertising costs and allow credit unions to build up a reputation for offering certain services. **We recommend that the Association of British Credit Unions Limited, or individual credit union networks, consider introducing standardised products where possible, to build up public familiarisation with credit union products.**

Mergers

55. ABCUL told us that “alongside the increase in the membership of credit unions, there has been a decrease in the number of credit unions primarily as a result of mergers. It is to be expected that this trend will continue in the coming years”.⁵⁵ The merger of unions will create larger organisations able to provide a wider range of services, but in Lanarkshire we heard reservations expressed about whether mergers could lead to a loss of local services. The Economic Secretary made it clear that mergers are not an issue that will be regulated:

It is up to credit unions themselves to decide if they want to merge and combine, as some have done in the past, or if they want to maintain their own identity but to look to ways to collaborate, to get greater efficiencies. If they are going to appeal more to affluent sections of society, then they need to have the sort of products that those people are interested in. That makes me think that they want to combine in some sort of way and to find out the most appropriate arrangements to do that.⁵⁶

53 For example, as advertised here: www.creditunion.ie/cu_services.

54 See visit note to Lanarkshire, printed as an Annex to this Report.

55 Ev 43

56 Q 193

56. The trend towards mergers is understandable, and in many cases it will benefit users of credit unions, who will have access to more services. However it is important that current members do not feel that they have lost “their” union if a merger occurs in their area. **Mergers are a matter for individual credit unions, but we hope that, when these decisions are made, the importance of retaining access for members to some local services is not forgotten.**

57. Another concern we heard in Lanarkshire involved mergers between different types of credit union. Common bonds can cover community or workplace, and there can be considerable divergence between the services and ethos of the unions. We asked the Economic Secretary if any consideration had been given to establishing different structures for workplace and community unions, in recognition of these differences. He replied:

At the moment we have credit unions with both those sorts of structures. I do not think it will be right for us as a government to dictate to credit unions what sort of structure would be appropriate. With modernising the legislation we want to set out a framework that has less restriction in terms of how credit unions can attract members.⁵⁷

We are concerned at the prospect of mergers between workplace and community unions that could result in disadvantages to members of all unions involved such as loss of targeted services. Furthermore, we feel that, in producing legislation on the regulation of credit unions, it might be useful for the Government to take account of the different structures of various types of credit union. **The Government should ensure that the differences between different types of credit union are recognised in its legislative proposals. Mergers between credit unions with different types of common bond should be considered extremely carefully to ensure that services and membership can be combined without difficulties.**

Access to services

58. An issue crucial to credit unions is the location of their services. Owing to high rents, most are unable to establish offices in prime locations such as high streets and shopping centres, but recognise that this hinders their ability to appeal to a broad section of society. As the Church of Scotland pointed out in its memorandum “too many people in difficulty either don't know of an available credit union or are unable/unwilling to access it”.⁵⁸ We heard in Lanarkshire of a credit union that had been unable to pay rent on a unit in a new shopping development; unfortunately the shop had instead been taken by a pawnbroker.

59. The Government's Planning Policy Statement 3, and the corresponding Planning Policy Statement 3 from the Scottish Executive, set out the obligation on local authorities to produce local development plans which require developers to include an appropriate proportion of affordable housing in their housing projects. This ensures that alongside new housing for the private sector, affordable housing is also built to meet local needs. A similar requirement on those managing existing or new shopping centres to provide a certain

57 Q 193

58 Ev 41

percentage of them at rental suitable for non-profit organisations would enable credit unions and other third sector bodies to achieve a “high street” presence alongside mainstream shops. **We recommend that the Government introduce a requirement on local authorities to ensure that an appropriate percentage of commercial premises in busy locations is let to non-profit organisations at a suitable rate. There should also be an obligation on local authorities to make premises owned by local authorities available to credit unions if they are vacant.**

Current accounts

60. The most significant new service provided by credit unions is the current account. As ABCUL points out:

11% of Scots do not have a bank account. This figure can rise to 18% for those on a low income. That can mean a whole range of difficulties, including the ability to access employment, as many employers now require their employees to have a bank account. Also those without a bank account cannot take advantage of the discounts on basic utility bills without the ability to pay by Direct Debit or Standing Order, and cashing cheques can be extremely costly if you do not have a bank account.⁵⁹

Given this, the development of a credit union bank account was seen as a priority.

61. In 2006, nine credit unions (four of them Scottish) launched the Credit Union Credit Account (CUCA), investing £2.5 million in the scheme. The CUCA has more features than other basic bank accounts, or the Post Office card account, as it offers standing order and direct debit facilities and a debit VISA card. ABCUL told us that the current account has proved successful:

24 credit unions across Britain either offer or are working towards offering the CUCA. There are now over 10,000 CUCA customers across the country, many of whom did not previously have a bank account or access to full banking services. Our latest figures show the take-up rate of the CUCA is increasing rapidly as more credit unions offer it and the year 2 marketing plans of the founder credit unions take effect. In the first week of May 2008 alone, 786 new Credit Union Current Accounts were opened.⁶⁰

62. In oral evidence, ABCUL repeatedly emphasised how important current accounts were to the continued success and expansion of the credit union movement. For example, Mr Lyonette said “We are not going to get big without being able to offer people a current account”⁶¹ and “In time, as in Canada and as in other countries, perhaps more people will use credit unions as their primary financial institution because we will be able to offer them the products”.⁶²

59 Ev 44

60 Ev 45

61 Q 90

62 Q122

63. A barrier which prevents more credit unions setting up current accounts is the financial input required: ABCUL estimated that it costs £120,000 for each credit union to establish current accounts.⁶³ This sum is beyond the reach of many smaller unions. In 2006, the Treasury Select Committee published its Report *“Banking the unbanked”: banking services, the Post Office Card Account, and financial inclusion*, which included the recommendation:

We welcome the development of a credit union-based transactional bank account. We recommend that the Government actively support the development of this account through the Financial Inclusion Fund to enable more credit unions to offer an alternative to basic bank accounts in areas of financial exclusion. We further recommend that the Government give a commitment that it will work constructively with credit unions to maximise their contribution to improving access to banking services for the unbanked.⁶⁴

The Government in response referred to funding of credit unions through the Growth Fund, but no specific assistance for current accounts was promised.⁶⁵

64. Given the large sums involved, it is clear that many smaller unions will be unable to offer bank accounts under the current systems. We are aware that ABCUL is looking at ways of developing CUCAs with this in mind. Mr Lyonette told us “We would like to see [...] a recommendation that we should explore together perhaps in partnership with the whole range of bodies, for example the Post Office. We are working quite closely with the Post Office”.⁶⁶ In February 2009, it emerged that Lord Mandelson, Secretary of State for Business, Enterprise and Regulatory Reform, had asked the Business and Enterprise Select Committee to look into the possibility of creating a “people’s bank” through the Post Office. This idea presents an obvious opportunity for links with credit unions, particularly if the Post Office also becomes a provider of Saving Gateway accounts, and we are glad that discussions between ABCUL and the Post Office are already in train. **We wholeheartedly support the recommendation of the Treasury Select Committee that the Government should provide funding assistance to credit unions specifically to assist in the establishment of current accounts. We encourage credit unions and the Post Office to work together to establish the best way to provide bank account facilities for the financially excluded and welcome the work already done towards meeting this aim.**

Wider services

65. In other countries, for example the US and Canada, credit unions offer products more like those of high street banks, including mortgages. For example, the Cambrian Credit Union, based in Winnipeg, Canada, offers full telephone and on-line banking, mortgages and a credit card. My Lyonette, who has worked in North American credit unions, said:

63 Ev 45

64 Treasury Committee, Thirteenth Report of Session 2005-06, *“Banking the unbanked”: banking services, the Post Office Card Account, and financial inclusion*, HC 1717, para 83

65 Treasury Committee, Fourth Special Report of Session 2006-07, *Financial inclusion: Government and other Responses to the Committee’s Twelfth and Thirteenth Reports of Session 2005–06 and the Committee’s First Report of Session 2006–07*, HC 437

66 Q 157

Even in very low-income communities in the States—never mind just the mainstream credit union sector—and even the very low-income focused credit unions in the States will all offer mortgages. They are very definitely not part of the sub-prime problem in terms of ratcheting up people’s repayments. We need a product range that will match our ambitions to serve a broader part of Scotland.⁶⁷

66. Although a few UK credit unions do offer mortgages, it is not the norm, nor is there any impetus within the movement at this time to move in that direction. Although ABCUL was clear that extending the range of services was key to the future success of credit unions, expansion on this scale is not in the immediate future plans of most of them. In Ireland, where credit unions have begun to offer wider services, there have been complaints from the banking sector that there is now an uneven playing field: Banks in Ireland have become increasingly open in their criticism of credit unions. “Why, they ask, if credit unions are acting more like banks and competing with banks on a broader range of products, can they also be given special business incentives?”⁶⁸ **While we support the principle of credit union expansion, we do not think offering services such as mortgages can or should be a priority for credit unions in the UK in the short-term future.**

67 Q 99

68 *Credit Unions*, Research Paper SN/BT/1034, House of Commons Library

5 Government funding

67. Credit unions themselves are required to generate the necessary funds for loans, and to provide for issues such as bad debt and auditing. However, they frequently require support funding, for example to enable them to run premises, hire staff, improve IT and carry out their statutory education work. Government financial support of credit unions in Scotland is, as mentioned in paragraphs six to nine, mostly through general social funds. This stands in stark contrast to the vast amount of public funding which has been given to banks over the past year. During our visit to Lanarkshire, the issue of available funding was raised. Since ring-fenced funding for credit unions was discontinued in 2008, unions have found themselves competing for funding with a variety of community and third sector initiatives. We heard that the local authority funding for Lanarkshire, which was £170,000 for twelve unions over five years, was less than one London credit union might receive in a year from local authorities and other funds. A common issue for all organisations who face bidding for funding is the staff costs of putting together such bids with no guarantee of success.

68. We asked the Economic Secretary about the apparent disparity in funding for credit unions in Scotland. He broadly agreed that the level of funding for credit unions in Scotland was out of proportion to their numbers and membership compared to England and Wales.⁶⁹ He added “there is some indication that Scottish credit unions have been less on the front foot in terms of applying for money from the Growth Fund and that is obviously something that the Committee will want to consider”.⁷⁰

69. If credit unions are not applying for the funding, they must be encouraged to do so. Mr McKillop, of ABCUL, suggested that this could be changing:

[W]hat we have seen in Scotland from the Scottish Government more and more is the emphasis on credit unions as a social enterprise encouraging credit unions in many ways to tap into funding streams and the resources that have been available for co-ops, community recycling groups and so on as possibly some types of credit unions have not regarded themselves and I think that by various funding streams were not regarded officially either as coming under the social enterprise banner, so we are seeing that more and it is something you get with the investment fund and the third sector enterprise fund.⁷¹

The UK Government should seek to ensure that Scottish credit unions are fully aware of the Growth Fund and how to apply to it.

70. We are disappointed to see that ring-fenced funding for credit unions from the Scottish Executive now totals only £250,000, a sharp decrease from over £2.7m before 2008, notwithstanding that the overall pot to which credit unions can now apply to is over £42m. This has caused difficulties for credit unions, who have not been able to bridge the financial gap adequately through applications to general funds. Credit unions should be supported by all possible financial sources across the UK. Local authorities should have an obligation

69 Q 185

70 Q 186

71 Q 158

to ensure that a suitable proportion of their funding is passed on to credit unions. **Consideration should be given by the Scottish Executive to raising the level of ring-fenced credit union funding to ensure that they are able to provide the services they offer to all those in need of them.**

6 A central credit union

71. During our visit to Lanarkshire, we had a round-table discussion with staff from several credit unions. One idea that arose from this was that of a central credit union, analogous to the Bank of England, which would have credit unions as members rather than the public. This body would co-ordinate the work of credit unions and act as a source of expertise. It would also hold some central investment. This is not an idea that has come up in other evidence to our inquiry, and it would in some ways duplicate the work of ABCUL and the national credit union organisations. It would also have running expenses which would need to be met in some way. However, as the work of credit unions expands, and moves potentially into areas of higher financial risk, some sort of central credit union could be a useful resource. **We recommend that the Government fund a study of the merits of a central credit union service.**

7 Financial education

72. One of the statutory responsibilities of credit unions is “the training and education of the members in the wise use of money and in the management of their financial affairs”. We have received welcome evidence of valuable financial education projects carried out by credit unions in Scotland. Mr Lyonette told us:

There are some really good examples of that in Scotland now, not least because it has become compulsory and schools are therefore really keen for the credit unions to come in and run school savings clubs. That happens in a very different place than anything to do around social enterprise in Scotland or around affordable credit.⁷²

Ms McGillivray described work in schools in South Lanarkshire, including a junior savers’ club, and explained:

It is a practical sense of coming along and starting to save, so that you are giving them the education, you are giving them the practical experience of saving. We see from that, hopefully, that the ripples go out, that the adults then join the credit union, they learn the benefits of the credit union and it would change the debt culture into one of savings.⁷³

73. The ABCUL memorandum explains that education work outside schools can be harder to describe because it is less formal:

Credit unions work on a day to day basis in improving financial literacy through induction of new members, leaflets and newsletters, education of volunteers, training for directors, links with debt counselling agencies, and the like. In many areas New Deal employees and credit unions are finding mutual benefits and opportunities in employment and training within the credit union.⁷⁴

ABCUL also called for closer links with organisations such as Citizens Advice Scotland and the Consumer Credit Counselling Service. **We applaud the financial education work of credit unions, and urge other bodies engaged in similar work to look to credit unions as partners in outreach work. The Government should consider providing funding for credit unions purely for financial education, given the importance of such work during a “credit crunch”. Any formal qualification gained should be duly recognised wherever possible under the Scottish Credit Qualifications Framework.**

72 Q 101

73 Q 35

74 Ev 45

8 Conclusion

74. During the course of our inquiry, we have heard a great deal about the importance of credit unions to the communities they serve and the success of the services they offer. With more Government support, we believe that these benefits could be brought to a wider range of beneficiaries. It would be a great shame if Scotland lost momentum in maintaining a participation rate above that of the UK as a whole because of a lack of support from the Government.

75. The expansion of services, in particular the introduction of the Credit Union Current Account, is a very welcome development. We are not however convinced that they will be able to reach beyond the current range of services until serious efforts can be made to publicise their work beyond the areas in which they have traditionally operated. It is vital that credit unions are able to present a “united front” to the public, to raise awareness of their important work.

76. We remain concerned by the interest rates charged by some financial institutions, which strike a contrast with the responsible lending of credit unions, and we hope this report clearly contributes to the growing dissatisfaction across the UK about the poor financial deal offered to those on low incomes in a time of recession.

Conclusions and recommendations

The role of credit unions in the current economy

1. We applaud the efforts of credit unions to act as responsible lenders. (Paragraph 28)

Interest rate capping

2. We recommend that the Government introduce a cap on interest rates for all financial institutions. (Paragraph 32)
3. Legislation must be introduced in a way which does not worsen the situation of those dependent on high-rate loans; if necessary, financial assistance should be given to ensure that no borrower is disadvantaged by the regulatory change. Such legislation should seek to ensure that lenders could not introduce extra hidden costs to compensate for lower interest rates. (Paragraph 33)
4. It is important that credit unions are supported in their endeavours to attract those with higher incomes and savings who might not previously have considered using a union. We recommend that the Government provide funding to promote credit unions across the United Kingdom to a wider public as an integral part of a comprehensive strategy of financial education. (Paragraph 35)

Deregulation

5. We welcome the legislative reform proposals addressing the long held concerns of credit unions, specifically those which will enable interest rates to be paid on savings, to encourage more people to save with credit unions, and the introduction of group memberships. It is good to know that the Government is paving the way for a more modern credit union service through changing legislation. However, we should guard against any additional changes which make credit unions one more rootless financial institution. The pegs in the ground should be a clear sense of the group or community to which the union belongs, and the principle of ensuring that the union members invest in the organisation. (Paragraph 40)
6. We look forward to the publication by the Government of draft legislation on regulatory reform of credit unions as soon as possible. (Paragraph 51)

Unified Services

7. We recommend that the Association of British Credit Unions Limited, or individual credit union networks, consider introducing standardised products where possible, to build up public familiarisation with credit union products. (Paragraph 54)

Mergers

8. Mergers are a matter for individual credit unions, but we hope that, when these decisions are made, the importance of retaining access for members to some local services is not forgotten. (Paragraph 56)
9. The Government should ensure that the differences between different types of credit union are recognised in its legislative proposals. Mergers between credit unions with different types of common bond should be considered extremely carefully to ensure that services and membership can be combined without difficulties. (Paragraph 57)

Access to services

10. We recommend that the Government introduce a requirement on local authorities to ensure that an appropriate percentage of commercial premises in busy locations is let to non-profit organisations at a suitable rate. There should also be an obligation on local authorities to make premises owned by local authorities available to credit unions if they are vacant. (Paragraph 59)

Current accounts

11. We wholeheartedly support the recommendation of the Treasury Select Committee that the Government should provide funding assistance to credit unions specifically to assist in the establishment of current accounts. We encourage credit unions and the Post Office to work together to establish the best way to provide bank account facilities for the financially excluded and welcome the work already done towards meeting this aim. (Paragraph 64)

Wider services

12. While we support the principle of credit union expansion, we do not think offering services such as mortgages can or should be a priority for credit unions in the UK in the short-term future. (Paragraph 66)

Government funding

13. The UK Government should seek to ensure that Scottish credit unions are fully aware of the Growth Fund and how to apply to it. (Paragraph 69)
14. Consideration should be given by the Scottish Executive to raising the level of ring-fenced credit union funding to ensure that they are able to provide the services they offer to all those in need of them. (Paragraph 70)

A central credit union

15. We recommend that the Government fund a study of the merits of a central credit union service. (Paragraph 71)

Financial education

16. We applaud the financial education work of credit unions, and urge other bodies engaged in similar work to look to credit unions as partners in outreach work. The Government should consider providing funding for credit unions purely for financial education, given the importance of such work during a “credit crunch”. Any formal qualification gained should be duly recognised wherever possible under the Scottish Credit Qualifications Framework. (Paragraph 73)

Conclusion

17. During the course of our inquiry, we have heard a great deal about the importance of credit unions to the communities they serve and the success of the services they offer. With more Government support, we believe that these benefits could be brought to a wider range of beneficiaries. It would be a great shame if Scotland lost momentum in maintaining a participation rate above that of the UK as a whole because of a lack of support from the Government. (Paragraph 74)
18. The expansion of services, in particular the introduction of the Credit Union Current Account, is a very welcome development. We are not however convinced that they will be able to reach beyond the current range of services until serious efforts can be made to publicise their work beyond the areas in which they have traditionally operated. It is vital that credit unions are able to present a “united front” to the public, to raise awareness of their important work. (Paragraph 75)
19. We remain concerned by the interest rates charged by some financial institutions, which strike a contrast with the responsible lending of credit unions, and we hope this report clearly contributes to the growing dissatisfaction across the UK about the poor financial deal offered to those on low incomes in a time of recession. (Paragraph 76)

Annex: note of visit

The Committee visited Lanarkshire on Monday 20 October 2008 in connection with its inquiry into Credit Unions in Scotland. The Committee visited the headquarters of the South Lanarkshire Credit Union Network in Blantyre, the Blantyre Credit Union office, and the ML9 Credit Union office in Larkhall.

The Committee met representatives from the following organisations:

- Blantyre Credit Union
- ML9 Credit Union
- South Lanarkshire Credit Union Network
- Irish League of Credit Unions
- Association of British Credit Unions Limited

Formal Minutes

Wednesday 6 May 2009

Members present:

Mr Ian Davidson, in the Chair

Mr Jim Devine

Mr Jim McGovern

David Mundell

Lindsay Roy

Mr Charles Walker

Mr Ben Wallace

Pete Wishart

Draft Report (*Credit Unions in Scotland*), proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 76 read and agreed to.

Annex agreed to.

Resolved, That the Report be the Second Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report.

[Adjourned till Wednesday 13 May at 2 p.m.]

Witnesses

Tuesday 18 March 2008

Page

Reverend Graham Blount, Secretary of Scottish Parliament Cross-Party Cross-Parliamentary Group on Tackling Debt, **Ms Susan McPhee**, Head of Social Policy and Public Affairs, Citizens Advice Scotland, and **Ms Nancy McGillivray**, South Lanarkshire Credit Union Network

Ev 1

Wednesday 9 July 2008

Mr Mark Lyonette, Chief Executive Officer, Association of British Credit Unions Limited, **Mr Frank McKillop**, Scottish Policy Officer, Association of British Credit Unions Limited and **Dr Peter Goth**, Manager, Scottish league of Credit Unions

Ev 12

Wednesday 28 January 2009

Ian Pearson MP, Economic Secretary, HM Treasury

Ev 26

List of written evidence

1	Scottish League of Credit Unions	Ev 35
2	Scotland Office	Ev 38
3	Rev Ian Galloway, Convener, Church and Society Council, Church of Scotland	Ev 41
4	Association of British Credit Unions Limited	Ev 43
5	Ian Pearson MP, Economic Secretary, HM Treasury	Ev 47
6	Example leaflet used by Scottish credit unions provided to the Committee on its visit to Lanarkshire	Ev 48

List of Reports from the Committee during the current Parliament

The following publications have been produced by the Scottish Affairs Committee since the beginning of the 2005 Parliament:

Session 2008–09

First Report	Work of the Committee in 2007–08	HC 55
--------------	----------------------------------	-------

Session 2007–08

First Report	Effects of tax increases on the oil industry	HC 35
Second Report	Poverty in Scotland	HC 128
Third Report	Child Poverty in Scotland	HC 277
Fourth Report	Work of the Committee in 2007	HC 278
Fifth Report	Experience of the Scottish Elections	HC 78
Sixth Report	Employment and Skills for the Defence Industry in Scotland	HC 305
First Special Report	Effects of tax increases on the oil industry: Government Response to the Committee's First Report of Session 2007–08	HC 376
Second Special Report	Poverty in Scotland and Child Poverty in Scotland: Responses by the Government and the Scottish Executive to the Committee's Second and Third Reports of Session 2007–08	HC 525
Third Special Report	Experience of the Scottish Elections: Government Response to the Committee's Fifth Report of Session 2007-08	HC 1098
Fourth Special Report	Employment and Skills for the Defence Industry in Scotland: Responses by the Government and Scottish Executive to the Committee's Sixth Report of 2007-08	HC 830

Session 2006–07

First Report	Work of the Committee in 2006	HC 308
--------------	-------------------------------	--------

Session 2005–06

First Report	Work of the Committee in 2005	HC 836
Second Report	Meeting Scotland's Future Energy Needs: the Westfield Development Centre	HC 1010
Third Report	<i>Putting Citizens First</i> : the Report from the Commission on Boundary Differences and Voting Systems	HC 924
Fourth Report	The Sewel Convention: the Westminster perspective	HC 983
First Special Report	Meeting Scotland's Future Energy Needs: Government Response to the Committee's Second Report of Session 2005–06	HC 579
Second Special Report	The Sewel Convention: the Westminster perspective: Government Response to the Committee's Fourth Report of Session 2005–06	HC 1634

Oral evidence

Taken before the Scottish Affairs Committee

on Tuesday 18 March 2008

Members present

Mr Mohammad Sarwar, in the Chair

Mr Alistair Carmichael
Mr Jim Devine

Mr Jim McGovern
Mr Charles Walker

Witnesses: **Reverend Graham Blount**, Secretary of Scottish Parliament Cross-Party Cross-Parliamentary Group on Tackling Debt, **Ms Susan McPhee**, Head of Social Policy and Public Affairs, Citizens Advice Scotland, and **Ms Nancy McGillivray**, South Lanarkshire Credit Union Network, gave evidence.

Q1 Chairman: Good morning. Can I welcome you here this morning to our first session of our inquiry into credit unions. Could you please introduce yourselves for the record.

Reverend Blount: I am Graham Blount from the Scottish Churches Parliamentary Office.

Ms McPhee: I am Susan McPhee from Citizens Advice Scotland.

Ms McGillivray: I am Nancy McGillivray from South Lanarkshire Credit Union Network.

Q2 Chairman: Before we start on the detailed questions would you like to make any opening remarks?

Reverend Blount: We are pleased that the Committee is thinking about taking forward some of what was in the report on poverty. Broadly speaking, all three of us are agreed that credit unions have a significant part to play in that, without being the whole answer to the problem of indebtedness in Scotland.

Q3 Chairman: During our inquiry it was obvious that debt is one of the major factors towards poverty in Scotland. How big an issue is debt in Scotland?

Ms McPhee: Last year the CAB service in Scotland dealt with 91,000 new issues relating to debt, which works out to an average of about 250 debt issues brought to the bureau every day. The total debt we dealt with last year was £212 million. Year-on-year it has gone up substantially. In 2002 we dealt with £100 million worth of debt and now we are at £212 million worth of debt. It is fairly significant. We did some research on debt four or five years ago. At that point, we found that Scottish CAB debt clients had average debt levels of about £13,500 and between four to five debts each, but the real issue is that of debt stress levels, which is pound of income per debt, which we found, on average, was £1 to £22. That was pretty significant. That gives you some idea.

Ms McGillivray: I can put it into a local context only in South Lanarkshire. For the people seeking advice either from the local authority or from CAB in the six months April to September last year, there was £14 million worth of new debt, and that was purely in South Lanarkshire.

Q4 Chairman: Why do you think there has been a significant growth in debt over the years? What are the main causes of this debt?

Ms McPhee: We have not published this yet but we are about to. We were looking at older people in debt and so we have done a little bit of research in terms of people aged 60 and over, and most of the debts are on credit cards. The rise in credit cards has certainly a big part to play. In our earlier research across the whole spectrum of debt clients, one in four had a credit card and some had between five to ten credit card debts.

Q5 Chairman: You are right there, the credit card is a problem. My overdraft was going higher and higher and I decided three months ago that I must not use the credit card for at least three months, and it has helped. How can we create an awareness that, if something is on offer, you should have some resistance to use this credit card?

Ms McPhee: It is not just about using it for luxury goods at all. Our research showed there were two streams of client. One stream used credit cards and other things like personal loans from doorstep lenders because their incomes were too low, so used them as a budget management tool: it is not about resisting; they have to use it because they do not have enough income. The second stream was of people whose circumstances had changed: their overtime had been cut or they had lost their job or they were sick or they had to work part-time suddenly—these kinds of things.

Q6 Chairman: You do not think that overspending on the card during Christmas and at other times is a big problem then?

Ms McPhee: Not for CAB clients. Over half had income levels of less than £800 a month and I think for one quarter their income was benefits or pensions. We are dealing very much with the lower end of the scale and we do not tend to see that overspending that we read about in the newspapers.

Q7 Mr Carmichael: Your colleagues in England and Wales were talking this morning on the BBC about a massive increase in the number of people seeking advice with regard to mortgage arrears. Is that something you are seeing north of the border as well?

Ms McPhee: We are beginning to. Certainly with the older people in debt issue, about half of them were homeowners, and, in our previous debt research, about one third were homeowners. We are a bit concerned at that. A lot of people have borrowed on the strength of their home—not necessarily their mortgage but second or third loans—and they have not even realised they are secured. As they struggle to pay these, it is having an impact.

Reverend Blount: For people in poverty, often the total amount of the debt is not going to be as high as the more spectacular cases that make the papers but the margins are much tighter, and, therefore, they are much more vulnerable to a change in their circumstances, to temporary unemployment and things like that, so that a relatively small amount of indebtedness can very quickly become a major problem for somebody with virtually no income.

Q8 Mr Carmichael: It does seem to me that even in the last seven days there has been a big change in the expectations of our economy and individual financial circumstances for the next six months or maybe to a year or so. Are you anticipating an increase in debt problems, say of people not being able to service their level of debt, as part of your forward planning?

Ms McPhee: I think it would be fair to say that is probably likely because year-on-year over the last five years we have seen debt levels constantly increasing and the numbers increasing. Consumer debt has remained the single biggest issue in the Scottish CAB service for the last five years, so I would anticipate that it would continue to be that.

Q9 Mr Carmichael: You have given us some fairly horrific figures this morning, from £100 million to £212 million in a six-year period. What are you anticipating these figures being, say, in 12 months or 24 months?

Ms McPhee: I simply would not like to say. The original research I was quoting before was 2004 and the older people's debt research was last year. The average debt level for them was about £17,500 and that was more or less a 25% increase in debt levels in a four-year period for them, but the debt stress levels were significantly worse—they were something like £1 to £38—because their incomes tended to be much lower and so the level of debt had more of an impact.

Q10 Mr Carmichael: Are we seeing people dying in debt now?

Ms McPhee: Yes. That was the reason for us looking at the over 60s, because, as they end their working life, there is no way of repaying this debt. It is significant for the homeowners because their only asset will be their home. That is the only way they could repay. Although £17,500 was the average, we had some older people owing something like £98,000. Now they are never going to repay that.

Q11 Mr Devine: Whose fault allows somebody to get into that debt? We have heard stories of banks giving loans to 72-year old people. Whose fault is that? Who is causing that?

Ms McPhee: The CAB service would blame mainstream lenders in the main, because that is what we see—which is banks. The problem could be that someone has taken out a personal loan, they struggle to repay it, they get into debt with it, and then all the charges and penalty charges add up and make it worse. The way it is resolved, if you like, is a further loan, a consolidation loan, which means that they are ending up borrowing more than they started over a longer period of time. Even though the initial payments are perhaps smaller than they were paying, it is a load more debt overall and then it goes on and on. Having said that, doorstep lenders at the other end of the scale continue to do that too. It is that layering of loans. You can start off borrowing £200 but you only pay off maybe £100 of it, and then you borrow more and more and you just see it all escalate.

Q12 Mr Devine: That leads us on to the next series of questions. What are the main sources of credit used by people on low incomes? Is it simply the guy who is coming to the door every Friday night or whatever? The banks are not keen to take these people on, are they?

Ms McPhee: It depends on the client and the income levels. The majority of CAB debt clients have personal loans from banks but a significant number have doorstep loans and catalogue company—

Q13 Mr Carmichael: When you say significant, what is significant?

Ms McPhee: In terms of our research, I think it would probably be about half of them.

Q14 Mr Devine: Half the people who come to you with problems are basically as a result of illegal money lenders.

Ms McPhee: It is not illegal, no. Doorstep lenders are like the Provident and Greenwoods, people like that who come to the door, lend money, lend cash loans, as it were, to people. But it is the rolling over of them—that is what makes it unrepayable.

Q15 Mr Devine: One of the things that came up in the Farepak scandal was that companies like the Provident were charging 177% interest rates—and that was the legal money lenders, as such. One of the things we talked about in our paper on poverty was capping interest rates. Do you think that would be a good idea? Are there any arguments against it?

Ms McPhee: The arguments that are put against it are that credit would dry up. However, credit at levels of 185% is ridiculous, unfair and unaffordable, because it is the people on the lowest incomes who are penalised the most. We have lots of examples like that, where the interest levels are very, very high. The reality for the individual is that it often works better for them because they know exactly how much they are paying. That is the advantage, if you like, for them with these loans: if they borrow £200, they

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

know exactly how much they have to pay and if they miss a payment there are no penalties. For someone on a limited budget, that really suits them. With the banks, you can borrow at a preferential rate, a better rate, but as soon as you start to default on something it all gets completely out of hand.

Q16 Mr Devine: What is the most worrying case? For each one of you, what is the case that has come to you with the most outstanding debt? What has been at the top?

Ms McGillivray: To speak for credit unions, we do not see a huge amount because we do not give any money advice or debt advice to people—we would always refer them on to our colleagues at the CAB or at the local authority money advice shops—but we see them coming in with significant debts.

Q17 Mr Devine: What is significant?

Ms McGillivray: I can think of one person I know of, to a doorstep lender, of £8,000—and this was a person on income support.

Reverend Blount: I can recall a case—and I cannot recall the exact figures—where somebody with severe mental health problems walked up the High Street and was actively encouraged to take out store credit cards in more than half a dozen different shops and to make significant purchases on all of them. Clearly this was somebody who was vulnerable, who was being exploited. I do not recall the figures, but I do recall very graphically the case.

Ms McPhee: Offhand, I can think of someone just a couple of weeks ago who was 72 years old and she owed something like £60,000—which, again, was something that would never be repaid. But part of the problem is about small amounts of debt. Perhaps I could read an example out to you of a 19-year-old girl who was living with her parents and working part-time. She had two loans from two different doorstep lenders and she earns £250 a month. Her first loan was for £600 and it had an interest charge on top of that of £372 to be repaid at £18 a week. That loan was paying off a previous loan of £268, so in her hands she only got £232. The second loan she had was for £300 with an interest charge of £165 to be repaid at £15 a week. That loan paid off a previous loan path of £95, so for that loan, she then only got £205. That is how these people get involved: you are paying off previous loans, and they are getting bigger and bigger, but in your hands you are getting quite a small amount of money, and you are on a small amount of money. It is about the percentage of your income that is being repaid.

Q18 Mr Devine: The Committee, as you will have seen from the report, is very supportive of the principle of credit unions. We are going to go and visit Ireland, where credit unions started and are well cemented within the communities. I just wonder why Ireland has been so successful in developing credit unions. The membership is significantly higher per head of population and such like and I wonder what we need to do to improve membership and the profile of credit unions in Scotland.

Ms McGillivray: One of the problems in the United Kingdom as a whole is that credit unions have been seen as a poor man's bank and I think that has put people off. We have certainly had people come along to South Lanarkshire who have said, "I can't join you, I'm in work" and that is not the case. Also, it was the banks in Ireland—the people could not access them as easily as we can do in this country.

Reverend Blount: I think it would also be fair for me to say that the credit union movement in Ireland had very strong support from within the church, and in particular from within the Catholic Church. While both the Catholic Church in Scotland and the Church of Scotland and other churches have been supportive of the credit union movement I do not think that support has been as "hands on" as was the case in the history of the credit union movement in Ireland.

Ms McPhee: I do not know why, but I can say that why I think doorstep lenders are successful is because they are literally there, they are on the doorstep, and they are recruited from within the community. They are there offering you money at a time when you really need it and they are prepared to give you it in cash and then collect it on a weekly basis—so there is not any effort involved, if you see what I mean. I think that is the success of it and credit unions cannot compete with that. Very few could do that kind of doorstep collection.

Ms McGillivray: We certainly saw this in Livingston, when we had some immediate loans that we were able to give out to people through the SGI scheme in Scotland. We found that people could not organise their lives to get to a collection point to pay the credit union loan back, despite us having standing orders and things like that available for them. It was just a chaotic lifestyle really.

Q19 Mr McGovern: I had a case with a constituent in Dundee which it might be helpful to pad out a bit. Jim asked you for the most notable cases you have heard of, and I suppose every MP gets people coming to them as well when they get into difficulties. This case was of a man and a woman, both pensioners, living on the state pension, and the man had a small occupational scheme. He was 69 years and six months old—and the six months is significant. They were offered a loan and they took a loan of £14,000 to buy a caravan. They also took out the insurance on the loan. The man died a year later and the woman obviously thought the insurance would clear the debt. This supposedly reputable company told her that the insurance was only valid up to the age of 70, so they paid this massive premium to get, in effect, six months' insurance for the man. Thankfully, after a lot of badgering and bad publicity, we were able to get the debt cleared. When you speak about doorstep lending, you were saying, Susan, that it is the physical presence on the doorstep, but this couple took this loan as a result of cold calling, just a telephone call. I think everybody gets junk mail through their door every day offering them loans, offering them money. Also, if you are unlucky enough to be in the house during the day watching daytime television, a lot of the adverts in

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

the afternoon, presumably aimed at people on low incomes or unemployed people or pensioners, are offering: "Put all your debts into one pot and come to us" and in some cases it has taken something like 25 years to clear the debt. When you talk about doorstep lending, is it specifically people who knock on your door or is it all these other forms where you can take debt on in your home without leaving your home?

Ms McPhee: There are two different things there. The doorstep lending I am talking about is about people on the doorstep who are lending money to you. They are the people who lend to you, but then there are these other issues about how you manage these debts when you realise that you are in a wee bit over your head. We have lots and lots of case evidence of problems with debt management companies. People have responded to the adverts and gone to them because they are a bit over their head, and they can then find that they are paying quite a hefty fee to these debt management companies and they are taking that off first, before they even start repaying some of these loans, and they are not necessarily repaying all of the loans either. For instance, sometimes they do not pay over your council tax. You think you are paying this lump sum and it is being dealt with and it is not and whoever is not being paid comes back to get you later on. Why do they not go to Citizens Advice Bureaus? We do not have this massive advertising budget that other companies do.

Reverend Blount: Advertising is quite important. We talk a lot about financial education and that is an important part of financial inclusion. The advertising on daytime television offers something that looks hugely attractive: the amount that you are paying a month goes down significantly, you only have one person to worry about, you do not need to worry the next time the door gets chapped about who it might be looking for money from you. You can see the huge attraction in all of that and what you do not see is your indebtedness stretching out for years and years and years into the future, taking a long time. Companies are investing a huge amount and CABs or credit unions are not in any position to compete in terms of the advertising. That is getting to people in their home, as you say, at a vulnerable moment and it sounds attractive. As part of a financial inclusion package, as part of promoting credit unions, I think we do need to look at ways of making people in their own homes aware of that as an option.

Q20 Mr Carmichael: How are all these individual cases aimed? You have this picture you are painting here of debt consolidating into growing debt. Eventually somebody has to pull the rug out from underneath this. Who is doing that? What is happening? Is it insolvency?

Ms McPhee: Nothing has been happening for a lot of people. The charges, *et cetera*, will continue to accumulate and the debt becomes unrepayable. The CAB will try to work out some kind of voluntary repayment, or else, in some cases, some people have been able to go through to the debt arrangement

scheme that is run by the Scottish Government. There have been flaws with that because it does not allow for debt write-off. It has only just started, some time last year, to freeze interest as well, so it is still very new to see how that is working out. For a lot of people who have not been able to access bankruptcy, even if it is the best way for them, what has been happening, in some cases, is that the local authorities are bankrupting them for council tax.

Q21 Mr Carmichael: Is that something that we are seeing again as an increasing phenomenon?

Ms McPhee: It has been very much so in Scotland. In April there are new provisions coming in that will allow people on low incomes with small amounts of assets to access bankruptcy. That may make a difference. That may allow them to write off their debts and start again. Up until now, however, part of the problem has been that creditors do not do what they need to do to allow people to access bankruptcy, so they are just sitting there.

Q22 Chairman: During our inquiry it was clear to us that banks and building societies and financial institutions are charging very high interest rates and penalty charges and particularly to those who are the most vulnerable and needy in our communities. The Committee's view was that the courts should be empowered to impose a cap on the interest rates they charge to their clients. What is your view on this?

Reverend Blount: I certainly would strongly support that. I have been part of the Debt on our Doorstep campaign that has had that as one of its major campaign asks for several years. It should be part of a wider strategy that is also looking at ways of making affordable credit available to the people who are most vulnerable to doorstep lenders at the moment. With banks, it is not so clear cut in terms of being a problem with interest rates, but, as you have said yourself, it is about penalty charges, default payments and all these kinds of things that are in the cost of credit whatever title they are called by. Doorstep lenders are the ones who are charging very high APR interest rates. I think we do need to restrict their activities and their interest rates but that has to go along with the promotion of credit unions. I would also mention maybe a wider use of the Social Fund in terms of making available small amounts of credit, especially for necessary items.

Q23 Chairman: Do you think there should be a cap from the Government imposed? Let us say the base rate is now 5% or 5.25%, that banks and financial institutions should not charge over 20% or 25%. Do you think there is a need for this?

Reverend Blount: Yes, I think so. Many other European countries, for example, seem to operate with such a system. It eliminates some of what goes on here but it does not appear across Europe to be creating the credit deserts that are predicted by some of those in the industry.

Q24 Chairman: When we deal with our constituents, it is not only the doorstep lenders or the illegal lenders who are charging very high interest, the

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

banks and building societies and those institutions have charged high interest rates, high penalty charges and default charges, and in some instances people pay 100% more than that.

Ms McGillivray: If you look at credit unions, they are already capped. It used to be 1% per month and it is now up to 2% per month, which is a maximum of about 26% APR, so there is already capping here in the United Kingdom on credit unions.

Q25 Chairman: No, I am talking about other banks. The point of principle is that if this can be imposed on credit unions, why can it not be imposed on other financial institutions.

Ms McGillivray: Credit unions are not allowed to charge an administration fee or anything like that. That is all within the 1979 Act. It says that the 1% or any other sum thereafter is what is covering all the administration in credit unions, so there is a precedent there within the United Kingdom for capping.

Q26 Chairman: Would you support his campaign, then?

Ms McGillivray: Yes.

Q27 Chairman: I have been personally campaigning for this for the last many years, because I think it is outrageous when the banks can charge up to 100 and 200% and get away with it.

Ms McPhee: What Graham said was correct: it is not just about the interest rates. It would concern me if interest rates were capped and then there were other ways around it in terms of charges and all these things.

Q28 Chairman: It would have to be a complete package.

Ms McPhee: It needs to be taken in the round—all the ways in which creditors can get their money, if you like. One of the other issues for us is the irresponsible lending of creditors. We have seen that over the years. People have been lent money that they could not possibly afford in the first place and then, particularly the banks, when they get into difficulties they are forced to take out another loan because otherwise banking facilities will be withdrawn. So they do not have the choice and yet they are taking on a loan that they know they cannot repay and nothing happens to the banks. There are no penalties for irresponsible lending and yet there are constant, constant things going on for debtors.

Q29 Mr Carmichael: I am going to move the discussion on to financial inclusion and financial literacy, but you have raised an interesting prospect there. Are we talking about some sort of penalties for banks that seem to be acting irresponsibly?

Ms McPhee: I think there should be some kind of penalty for irresponsible lending.

Q30 Mr Carmichael: And can we charge them £20 a letter for telling them that we are imposing it!

Reverend Blount: It is a very tempting thought. One way of dealing with this that has been proposed in the past has been, for instance, that if a bank or anybody else lends to somebody without proper inquiry into their ability to repay that amount of a loan, if they do that, the debt should be unenforceable.

Q31 Chairman: If any financial institution or bank or lender charging high interest rates which are unreasonable and courts are given the powers to make a decision as to what is unreasonable in terms of charges, default charges or in terms of interest, do you not think this will deter people charging high interest rates and high financial charges?

Reverend Blount: I think the experience of the previous legislation, which talks about extortionate interest rates, was that courts were very reluctant indeed to describe something as extortionate. My feeling would be that “unreasonable” would be a much better word to use than extortionate but that there might perhaps be some guidance in subordinate legislation about what was reasonable and unreasonable, with an area of discretion for the court.

Q32 Mr Devine: In the case study you gave us earlier on, Graham, of somebody with a mental health problem, with a lack of income, who goes up the High Street and ends up with half a dozen cards—and these store cards are extortionate, it has to be said—what should be the penalty in that situation? What do you see should be the retribution?

Reverend Blount: That is really what I said to Alistair Carmichael a moment ago. I think that where people are effectively extending credit with no proper inquiry into the ability of the person to repay that credit, the debt should be unenforceable at law.

Q33 Mr Carmichael: It would just be a new species of avoidable contract.

Reverend Blount: Yes.

Q34 Mr Carmichael: Perhaps I could turn to financial inclusion and financial literacy. We have had government priorities, taskforce, every gimmick and piece of jargon known to man and politician. In a nutshell, do you think the Government is doing enough to improve financial inclusion and financial literacy in Scotland?

Ms McPhee: I do not know, as yet. We are hoping to engage with the Thoresen Review that came out in March, which, if it is implemented, should have a significant impact. In terms of preventative measures, it is trying to give money guidance at a much earlier stage and I can see that as being very beneficial. One of the things it is suggesting is to start with a couple of pathfinder projects and we really like to hope that one would start in Scotland. I think if we can see something starting in Scotland before it is rolled out, that could be helpful. That is not necessarily reaching CAB clients; that is reaching people in advance of getting into debt. I think that is very much needed.

Q35 Mr Carmichael: Your ambition surely should be to put yourselves out of business as far as this is concerned.

Ms McPhee: Yes, absolutely.

Ms McGillivray: Perhaps I could talk about one of the schemes that we have going in South Lanarkshire. We are looking at primary four children and talking to them at a very basic level and trying to make it fun. Out of the 22 schools approached, 17 headmistresses immediately said yes they would like this. Linked in with that is a junior savers club, so the children then are encouraged to come along and bring in their money, usually first thing in the morning, in case they lose it, they spend it or whatever happens to it. It is a practical sense of coming along and starting to save, so that you are giving them the education, you are giving them the practical experience of saving. We see from that, hopefully, that the ripples go out, that the adults then join the credit union, they learn the benefits of the credit union and it would change the debt culture into one of savings.

Q36 Mr Carmichael: You have used the word “culture” there which I think comes to the centre of this. I think we have seen a cultural change—probably in my lifetime, somebody in his early 40s—from a culture where my parents’ generation would not borrow—they saw credit as the last resort of the last resorts—to one where there is a much greater acceptance. Do you think we could be doing more about the education, getting a younger age to change the culture, to reinstate this saving effect that we seem to have lost.

Ms McGillivray: Yes. From the experience that I have, both in South Lanarkshire and in Livingston of going into schools, the children then start to save and it becomes almost addictive to see their savings growing. Credit unions also have to do their part in that, in providing little incentives to the kids or in getting them to design posters, so you are continually educating them. I think we have to start as early as primary school. You are talking about your experience and I think a lot of us in the room here could echo that. When we went for our first mortgages we were grilled and no-one offered us loans or anything, and there has been a real change in the culture in the United Kingdom.

Ms McPhee: While I absolutely agree with what Nancy was saying, one of the things that we may not be able to get away from is that people sometimes are just too poor. They are too poor to save money and will always be, and that is why they will always have to be in debt because their incomes are not enough. Our research has shown that for half of them their income levels were just too low and they will always need some kind of eventuality. That is where the Social Fund comes in and other things. If that was working better and giving them access to more money, that would help some of it.

Reverend Blount: That would be why, for instance, for somebody going into a CAB with debt problems, one of the things that would be discussed would be income maximisation; if there are benefits that they may be due that they are not claiming. Again that

was part of your earlier report about minimum income. There is an intractable problem. It is not that poor people are necessarily being seduced, but that making do, living on benefits long-term, is very, very difficult indeed. Coping with the unforeseen, relatively small thing to perhaps all of us sitting here, is a huge bump in somebody’s financial position.

Ms McGillivray: I can certainly agree with Graham in that. For a lot of us, if the washing machine breaks down we can go and buy a new washing machine, and we have people coming into the credit union looking for £50 to repair that, looking for a loan for that. Obviously we can supply that to them.

Ms McPhee: In the next couple of months we will be publishing a suite of briefing sheets on employment issues and the difficulties in trying to get into employment and staying in and what happens after you leave. Certainly one of the biggest problems we have found—even when you are in employment—is getting your pay. A lot of the jobs are very short-term, casual employment, and people are not even receiving pay that they have worked for, so there are lots and lots of problems there.

Q37 Mr McGovern: I have a very brief question to you, Nancy, on what you were saying about visits to schools. I think 17 out of 22 is very, very impressive—and perhaps a slightly sad indictment on the times in which we live—but of the other five, have they just not answered yet or do they have an argument against it? I cannot think of an argument against it but I am wondering if there is one.

Ms McGillivray: This was just a pilot study for my own network. Our network is a charity that seeks out funders and we have not been able to do the 17 schools, we have not been able to give them education there or start up junior savers clubs because we are not funded in that way at the moment, and we are looking for funding for that. Of the other five, off the top of my head three of them approached us within about two months and the other two have not come back to us as yet.

Q38 Mr McGovern: There have been no refusals.

Ms McGillivray: No.

Q39 Mr Carmichael: Is there a role in this for our colleagues in the Scottish Government?

Ms McGillivray: Inevitably.

Reverend Blount: The previous Executive had a financial inclusion action plan that had some successes. Obviously the problem has not gone away and we would hope that the new Scottish Government would look seriously at this.

Q40 Mr Carmichael: To take it away from the realm of government, do the larger lenders, the banks, the credit companies, the store cards and whoever else, have some sort of corporate social responsibility in all this?

Ms McPhee: Very much so. Maybe they could finance some of it.

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

Ms McGillivray: Yes.

Reverend Blount: There are two aspects to that: the CSR bit around the edges, where financing something like Nancy's project would be very welcome, but, also, there needs to be serious conversation with the financial institutions about their practice. Some things can be done by legislation and some things are probably better done in partnership and by talking to them about the impact of some of their policies.

Ms McPhee: One of the things we mentioned before at the last committee meeting was about the community reinvestment that happens in the States, where banks are obliged to publish their information in terms of lending within communities. Then at least you know how much they are paying back into their community but there is also an element of social responsibility, that they have to make a contribution to their community. I think something like that would be very helpful.

Q41 Mr Walker: On the corporate social responsibility of banks, I think the reputation of banks right now is completely shot to pieces. Regardless of whether you are living in total poverty or relative wealth, banks will lend you money with little safeguards put in place and now the chickens are coming home to roost. When you talk about corporate social responsibility, do you think banks have any credibility in this area whatsoever? They talk about it but they do not seem to act it out.

Reverend Blount: I think the scenario you paint is fairly accurate, but if I were—which I am unlikely to be—a senior person in a bank, I would be looking very keenly at ways of recovering some of that credibility.

Q42 Mr Devine: He is a very rich Tory.

Reverend Blount: There are opportunities here for them to... the religious word would be "redeem" themselves.

Mr Walker: I think the financial sector needs to do a lot of redeeming, to be perfectly honest. I personally find it rather offensive that we meet good people, like yourself, who are struggling on behalf of people living in poverty who cannot get access to mainstream banking services, whereas major Scottish banks think nothing of spending tens of millions of pounds sponsoring sporting tournaments. Do you not think there is a slight disconnect here, between what they talk about in the area of social responsibility and what they deliver?

Mr Carmichael: Perhaps I could put it a different way, Graham: before you have redemptions, do you not have to have repentance?

Q43 Mr Walker: I know his parents go to church every week!

Reverend Blount: I am sure that is so, but the offer of forgiveness is perhaps what initiates the process.

Q44 Mr Walker: It is a serious point. When we came up to visit Scotland we visited various parts—we have been to Dundee, Aberdeen, Inverness. There is a shortage of opportunity for people living right at

the bottom of the income scale to access financial services because they are not deemed as being profitable, yet at a time when banks, up until about six months ago, were making vast profits. Why do you think that not even a fraction of this or a measurable fraction of this was ploughed into providing services for the very least well off? How better can you example your commitment to a community than that?

Reverend Blount: I think so. I suspect that, from the bank's point of view, sponsoring rugby tournaments seems more attractive: you get more publicity and you get your logo on the telly for six hours on a Saturday. There is more to be gained.

Q45 Mr Carmichael: You cannot erect a big tent at Murrayfield and give them free drink to see somebody come and get their loan to get a new washing machine, in other words.

Reverend Blount: No.

Ms McPhee: In the last two years running we have asked the Citizen Advice Bureau advisers to tell us who they think is the worst company that they deal with—and this is right across the board. Banks have come top for the last two years running—all the main banks. We are having more problems now in terms of bank accounts. Although they are supposed to have basic bank accounts, people who are becoming bankrupt are not getting bank accounts—they are being shut down. Some banks will shut down a bank account as soon as they know a CAB is involved because then they know this person is possibly in trouble. They shut down the bank account and then there are the difficulties of trying to get another loan there. If we do see more and more people becoming bankrupt—which is what we are expecting—there is going to be a big difficulty in accessing bank accounts and I do not know what will happen. They could do a great deal more. They could do things with overdrafts. In France and Germany I think credit is run for low income people, using just a £200 or £300 overdraft. People could do that if the charges were not so punitive. There are lots of things the banks could do.

Q46 Mr McGovern: It is my understanding that credit unions were originally based on a small business model. The Government are now trying to encourage them to expand and take on more business but the counterargument to that is that too much expansion would mean moving away from their community-based roots and possibly defeat their original objectives. What is your view on that?

Ms McGillivray: I think credit unions are there to serve the community and each and every person in the community. They are a not-for-profit organisation and their members own them, so, therefore, their members control them. I know some of the larger credit unions have expanded and taken over quite a large area. To do that, you really do need to have very good and very strict financial controls on them. Some of the larger credit unions now offer cheque accounts, now offer bank services to their members. Within credit unions, there are two different levels really. We have the community credit

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

unions, such as I am involved with. We cover the unitary area of South Lanarkshire, and the other one which I am involved with covers Livingston. That allows you to grow that business there and to grow that business using sound business practices.

Reverend Blount: The Trustee Savings Bank movement was initiated in Dumfries by a Church of Scotland minister a long time ago for very much the same kind of ethos and reasons that the credit union movement now works to. That Trustee Savings Bank movement grew and developed from the 1960s, from local savings banks that were very much like the credit union movement, by a process of amalgamation and adopting a fairly aggressive business model to Lloyds TSB today—which I would not say is any worse but not substantially different from any of the other major banks. I think the challenge is to find a way of growing the Credit Union Network which does not set in train the dynamic that took us from Trustee Savings Banks to Lloyds TSB; so that there is still part of the ethos of the credit union movement; so that which was lost in the other example can be retained.

Q47 Mr Walker: That is a critical point, because you do not want to diminish the strength of credit unions by turning them into quasi banks or large building societies, and that is going to be a significant challenge for you. I am sorry I was late, but would it be possible for somebody to explain to me briefly, in about two minutes, how credit unions are financially structured. What is their loan book? What interest rates do they charge? Where do they get their revenues from? Can they borrow off mainstream lenders? Do they go to the Bank of England? How do they work?

Ms McGillivray: The credit unions are strictly regulated by the Financial Services Authority. We must have a common bond—which is that people have to either live or work together, or it can be associational; for example taxi drivers or something like that. The credit unions form from that. The board of directors who run the credit union will be volunteers. Many of us now have paid staff. The pot of money that we have to lend out is members' savings.

Q48 Mr Walker: That is all you have, the savings.

Ms McGillivray: That is it. We do have the facility to be able to go to another credit union and borrow if we are exceeding what we have in the savings and that is what we have. Many of us have other projects that are being funded through local authorities, through government or through private charities, financial education and things like that, but, in essence, all the money we have and the way we run credit unions is purely by members' savings and the interest we charge on the loans. That is normally 1% but we can go up to 2% per month; so it is normally 12.68% or it can go up to 26.8% APR

Q49 Mr Walker: What interest rates do you pay savers? Five per cent?

Ms McGillivray: Some of the larger credit unions now can actually offer savings. Many of us, though, cannot say that we will pay you back—because you are investing your money, so you own the company, you get a share of the profits.

Q50 Mr Walker: There could be profit.

Ms McGillivray: If there is any profit.

Q51 Mr Walker: Is there ever any profit?

Ms McGillivray: Normally in community credit unions it is about year eight or nine. However, I will say that the one from Livingstone has paid a dividend since year one and that dividend has range from 1.75% this year up to 3%.

Q52 Chairman: You say share the profit. Obviously credit unions are growing and expanding and you need to have your expansion costs as well.

Ms McGillivray: Yes.

Q53 Chairman: What percentage of the profits goes to the shareholders and what percentage of the profits goes for expansion?

Ms McGillivray: Because credit unions are autonomous, it is really up to their board of directors what they do. We are guided by the FSA on what we should have in reserve. Obviously we have a bad debt reserve as well, because people do not always pay back their credit union loans. For example, if I talk about the Livingston one, we have a development reserve so that we are continually looking to expand and offer new services there. Anything that is left after that is shared out between members. As I say, this year it is 1.75% on our savings and it has been as much as 4.5% in previous years.

Q54 Mr Devine: I obviously have to declare an interest here because I am a member of the Livingston Credit Union. Could you give the figures of turnover, loans and what-have-you?

Ms McGillivray: If I talk about Livingston: since we started, which was ten years ago, we have given out over £2 million in loans. At the present moment we are sitting with £600,000 worth of members' savings.

Q55 Chairman: Is there any criteria where you say, if you have £2 million in the pot, that you can give 50% of that or 80% of that?

Ms McGillivray: We would normally give out between 80 and 90% of our members' savings as loans. If we have a pot of money sitting there of £100,000, we are probably lending out £80,000 at that time. We are keeping the 20% to make sure that we have money to pay back share withdrawals and things like that. The children's savings are kept separately from that, so that we can always pay out the children's savings. Obviously under 18 they are not allowed to take loans out.

Q56 Chairman: How long does a member have to be signed up with the credit union before he or she is given a loan?

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

Ms McGillivray: It varies from credit union to credit union. In some we are now starting to do flexible lending, so that someone coming in showing us proof of income may immediately get a loan, but normally we are looking to build up their credit history with us, so you are probably looking at 13 weeks saving with a credit union and going on to a loan and then graduated on to the second loan and the third loan. Again, just quoting Livingston, their third loan is three times their savings. If they have £1,000, they can have up to £3,000.

Q57 Mr Walker: What is the average pot?

Ms McGillivray: The average loan since we started Livingston is about £900 to £1,000.

Q58 Mr Walker: About £300 per saver.

Ms McGillivray: No, that is an average loan.

Q59 Mr Walker: What is the average saving account.

Ms McGillivray: We can only take up to £10,000.

Q60 Mr Walker: That would be the largest, but, in the main, what are people saving?

Ms McGillivray: People are saving about £1,000, £2,000—something as much as that.

Q61 Mr Walker: They have accounts of £1,000 to £2,000.

Ms McGillivray: Many of them under the £1,000, but we have people who have a lot more there because they want to save with the credit union; they want to put something back into the community.

Q62 Mr Walker: Say someone is saving with you on a weekly or monthly basis, is the average deposit £5 or £10 a week or £5 of £10 a month?

Ms McGillivray: Off the top of my head and not being the financial director, probably about £5 a week, something like that.

Q63 Mr Walker: A note, basically—which, if you are on £100, is quite something, to hand over a note.

Ms McGillivray: Yes.

Q64 Chairman: What is the percentage of bad debt?

Ms McGillivray: Traditionally we have been lower than banks. I could not give you the figure off the top of my head. I would have to have the accounts here. We are under 2% for bad debt.

Q65 Mr Carmichael: If you are responsible in your lending, you are not going to see a problem with bad debt. You were speaking there about regulation and the Financial Services Authority and you also have all the money laundering regulations. Are these influences now giving you a pressure within your organisation to be bigger, because, in order to cope with that level of regulation, there is an economy of scale?

Ms McGillivray: I do not think that is what is driving us. I think what is driving us is that we want to provide the services to more people and we want to provide the best service we can to the majority of people in Scotland.

Q66 Mr Carmichael: Do you think the regulation of you as a sector—which has been done by the same people regulating Northern Rock, for example, the big banks, the credit companies—is appropriate?

Ms McGillivray: I have been down and spoken to the FSA on a number of occasions and I have to say that, while they regulate us in the same way, I think they are more lenient with credit unions than they are with the other big lenders. I think the money laundering regulations that have come in may cause a problem but it is not insurmountable.

Q67 Mr Carmichael: What is the nature of the problem from the sharp end?

Ms McGillivray: If you talk of the sharp end, it is purely logistics of managing to get things copied, making sure that everyone knows exactly what it is that the member has to have to join a credit union. It is really the logistics of getting all that copied. I would love to see us being able to have a wireless system, whereby we can stand things in a collection point—because obviously we have our main base and then we have several collection points. To have the new technology to enable us to communicate there would make life a lot simpler.

Q68 Mr Carmichael: You are talking about copying things like driving licences, wage slips or whatever.

Ms McGillivray: Yes.

Q69 Mr Carmichael: If you have a credit union in a village hall or community centre.

Ms McGillivray: The one group we have problems with are the 16-year to 18-year olds who do not have driving licences. Some do not have passports; they do not have utility bills and things like that. That is the group we have problems with, in finding something there.

Q70 Mr McGovern: We heard earlier about the success of the credit unions in Ireland and various views as to what bred that success. Part of it seemed to be that they attracted membership from all sections of the community. Probably the most successful organisation in Scotland that I know of—although that does not mean it is the most successful—is the one the Scottish Affairs Committee visited in Brigdon. You mentioned that credit unions are now employing people full-time and that one certainly does. Do you believe it is crucial for the credit unions in Scotland to attract more affluent members of the community.

Ms McGillivray: It is essential that they attract the more affluent members of the community. There was a report published in 2006 from the Joseph Rowntree Foundation by Peter Goss, Charles Ferguson and Donald McKillip that identified that this was one of the major recommendations. Perhaps I may read this to you: “. . . placing greater emphasis

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

on credit union development based upon a cross-section of the population, including affluent sections of society. This offers a more viable long-term model than concentrating only on financially excluded people.” If we concentrate only on the financially excluded, then the credit union will not be there, because we need the savings from the other people to offer the services. As you may have seen, some credit unions have become insolvent. Many of these were highly dependent on grants purely focused on the financially excluded.

Q71 Mr Devine: Is it right that one of the other things you have lobbied me on is that the legislation needs to change to include groups, like mother-toddler groups and various other community groups, so that they can sign up.

Ms McGillivray: Yes. I have to say within West Lothian we have lobbied Jim about this quite frequently. On average, we hear from one community group per week asking to join the credit union and to put their savings in there rather than go into a bank. Because now there are not as many branches of the banks and things like that, we are more readily accessible for them. To have the legislation changed to allow groups to stay with credit unions is essential to these small groups.

Q72 Mr Devine: Why can you not do it now? Why can you not accept Jim Devine’s Livingston South playgroup?

Ms McGillivray: We are not allowed to do that by law.

Q73 Mr Devine: That is the law.

Ms McGillivray: From Westminster.

Q74 Chairman: What more can the British Government or the Scottish Executive or local government do to promote and expand the credit union movement in Scotland? Graham has mentioned that the church played a major role in promoting credit unions in Ireland. What more can the church do, what more can we do, and what more services can be allowed in the development of credit unions which can help them to expand?

Reverend Blount: Perhaps I could respond to what you say with relation to the church. I was involved with a report within the Church of Scotland which must be nearly ten years ago now where the General Assembly recognised the value of credit unions but one would have to say that very little happened on the ground. One of the factors in that—and it has been alluded to by Nancy in the last conversation—is that it is quite intimidatingly complex for a group of people. However well disposed they are to the idea, it is not something where you can form a wee group of half a dozen people and they will get it running by next week. It is a huge commitment. In one sense it should be, because there is a huge amount of responsibility. You would not want anybody to be able to set up a credit union and take people’s money and disappear. The element of trust is why there is an important strategic role for churches, because I think people do feel that if it is

set up under the aegis of a church then the people to whom you are handing over your money are not about to disappear off to the Caribbean with it next week. That is why there is a contribution to be made. Providing accessible support to groups of people within communities who do want to do this, does not always seem to be a meeting of minds between local authorities—some of whom have had or still have credit union development officers—and groups on the ground that are interested. Somehow connections are not always being made there. I think that is an area we can look to, in supporting people in getting involved in the credit union movement.

Q75 Mr Devine: In a previous life, I was Head of Health in Unison when they set up the Glasgow Health Boards. I started with a man called Robert Ray in Southern General and then we negotiated with the Health Board to deduct at source. It seems such a logical way for the likes of local authorities, health boards and, I am sure, companies. Do you target companies in this sort of area?

Reverend Blount: Many of the most successful credit unions, at least in terms of numbers and the total amount of money that they are dealing with, have been employee-based. There is Capital Credit Union in Edinburgh which was originally Lothian Regional Council’s credit union. It has now expanded its common bond to be a wee bit wider. A lot of the success has been with ones that are workplace-based.

Ms McGillivray: As you say, a lot of the credit unions that were workplace-based have been very successful. We ourselves can offer payroll deduction. As long as we have a live or work common bond within the area, then we can offer pay roll deduction and things like that. Certainly within South Lanarkshire we are looking at perhaps opening up even more access to people and I think that is one of the things that we really do need for credit unions. We have paypoint access, whereby people can go into post offices or stores that accept paypoint and pay into their credit unions. That was very successful. It brought back dormant members, so it showed that they needed the access that we were not able to give them. It also helped with their bad debt problem because people were embarrassed about coming into the credit union and paying again. However, we are looking towards more technology-based stuff as well, to allow for people who are more affluent, who are working, who are lone parents who cannot get out of the house, carers, or the housebound, and to give them access by using interactive websites or SMS texting and various things like that. We want to bring credit unions right into this century. Also, we have set up a group within Scotland where all the trade bodies are involved, as well as National Association of Credit Union Workers and the co-operatives, and we are looking there at trying to get training for credit union officials and also for credit union workers and for the volunteers. We have a big base of volunteers in Scotland and they are superb at giving their time. Many of the credit union volunteers I am involved with in South Lanarkshire are people who perhaps

18 March 2008 Reverend Graham Blount, Ms Susan McPhee and Ms Nancy McGillivray

have mental health problems and this has assisted them back into mainstream. We have had students who have come in and it has assisted them into work. We have had people who are asylum seekers who are giving to the community as well. There are lots of reasons to be a volunteer and the credit union is ideally placed for them there, because we can give them cashier experience, we can give them computer experience, they can come onto the board and they can make strategic decisions and things like that. There is a lot that can be done there with training and with development but that takes money. It takes funding there for the credit unions or the Credit Union Network, whichever way people have set themselves up.

Q76 Chairman: Could you please tell us how small credit unions are competing against High Street banks.

Ms McGillivray: We have a community credit union in my area that has 400 members. They are competing obviously on a different level there. They are competing on the much smaller level and the community level. I do not think any of us could go to a bank and get a £50 loan. They would not give it to us. I can state here that if I cannot get £50 and the minimum is £500, I will find a use for the £450 and I do not think anyone is any different. We are offering that type of loan to people. That is a small community credit union. I think the organic growth of credit unions is great because it starts small. My experience in Livingston is we started small. We started from a church in Livingston and the first collection netted £20. If someone had told me ten years ago that we would have given out £2 million in loans and be sitting in charge of £600,000, I would be frightened, and I think anyone would have been. We have grown with the credit union. We have grown to be able to offer more services to people and we want to be able to offer these services.

Q77 Chairman: Since large banks, in my experience, are not interested in small customers, do you not think there is a huge potential here now for the credit union movement to grow?

Ms McGillivray: I think there is a huge potential. I will give you an instance of somebody who came and spoke to me about a loan. He was a chap who had multiple sclerosis and he wanted to adapt a car and he wanted quite a substantial loan for that. We were able to give him that loan, but, while I was interviewing him, as a responsible person I said to him, "If you go to a bank you will get this at a cheaper rate," and he said to me, "No. You will. I won't." That was the difference. He could not get that. This is also their insurance. Because there is free life insurance with it, many people are using that as the basis for paying for their funerals.

Q78 Chairman: Can I thank you for your attendance today. Before I declare the meeting closed, do you wish to say anything in conclusion, perhaps on areas that have not been covered in our questions?

Ms McPhee: I have just one thing. While absolutely supporting credit unions they will not be the answer to the debt problem. They may be the answer for the future but not for the existing debt problem. Something needs to be done about that.

Q79 Chairman: Are there any pearls of wisdom to come from you?

Reverend Blount: I would agree with what Susan has said. What you mentioned in your earlier report about flexibility and expansion of the Social Fund is part of the same agenda as the promotion of credit unions.

Ms McGillivray: I welcome an inquiry into credit unions for Scotland. I would like to see us leading the way for credit union development there throughout that country so that we are covered completely by credit unions.

Chairman: Thank you for your attendance. I am sure your evidence will be very useful for us when we compile the report.

Wednesday 9 July 2008

Members present

Mr Mohammad Sarwar, in the Chair

Mr Alistair Carmichael
Mr Jim Devine
Mr Jim McGovern

Mr Angus MacNeil
Mr Ben Wallace

Witnesses: **Mr Mark Lyonette**, Chief Executive Officer, Association of British Credit Unions Limited, **Mr Frank McKillop**, Scottish Policy Officer, Association of British Credit Unions Limited, and **Dr Peter Goth**, Manager, Scottish League of Credit Unions, gave evidence.

Q80 Chairman: Good afternoon. I would like to welcome today's witnesses to our session. Can you please introduce yourselves for the record?

Dr Goth: Peter Goth. I am with the Scottish League of Credit Unions.

Mr Lyonette: Mark Lyonette from ABCUL, the Association of British Credit Unions.

Mr McKillop: Frank McKillop the Scottish Policy Officer for ABCUL.

Q81 Chairman: Before we start on detailed questions, do you have any opening remarks you would like to make?

Mr Lyonette: Not particularly, no. We are delighted to be here. It is the first time we have been in front of the Scottish Affairs Committee. We have spoken to the Treasury Select Committee a few times but we are very pleased you are undertaking the inquiry.

Q82 Chairman: Why do you think membership of credit unions in Britain is lower than in other countries such as Ireland and Australia?

Mr Lyonette: Probably the history of credit unions in Britain in many ways is a very different history than Ireland or Australia, the States or Canada. Also, the history of financial services in Britain is quite different. We have had strong mutuals for much of the 20th century. We had building societies, the Trustee Savings Bank, the Airdrie municipal banks. We have had that history. In some ways, the need for credit unions for much of the 20th century was not there in the same way as in Ireland, Australia, Canada or the States. Also, it is not just that history; it is the history of the movement. Credit unions in Britain have often been developed in a way with all the enthusiasm and energy of the volunteers and that is not necessarily going to be a recipe for success. It is almost felt at times that some of that model that was adopted in the eighties and the nineties succeeded in the exception rather than the rule. Many of the credit unions that have been more successful have had to find other ways of operating and being set up. The reality is, even today, many credit unions in Britain only offer basic savings and basic unsecured personal loans. If you look at countries around the world where credit unions have been more successful, by and large, they tend to offer a wider range of products. They tend to have thousands of members, not hundreds. Therefore,

they are more sustainable and they play a much bigger part in mainstream society, not just as a "poor man's bank", if you like.

Q83 Chairman: Since the start of the credit union movement in Britain, do you believe the support extended by the British Government, the Scottish Government and local government matches the support given to the credit union movement for instance in Ireland or Australia?

Mr Lyonette: Interestingly, in many countries around the world, credit unions have not been pumped by the state at all. Certainly at central and perhaps even local level, that has not been the case. Some of what has happened in Britain and Scotland certainly within that has been putting government money into credit unions and local government money as well, on the premise that they can do a job almost solely for poor people, for the most excluded, the most disadvantaged. By definition, that is going to be problematic. While present government investment is welcome both in Scotland and here now in Westminster for the first time, it needs to be used in a way which helps the credit union to grow, not a way that is going to hinder it from growing.

Dr Goth: I agree with what my colleague is saying but I come from a bit of a different angle. The credit union movement in GB—I intentionally exclude Northern Ireland—is certainly quite unique in its development. It is a lot to do with the image that credit unions have developed in GB. When we start looking at countries like Ireland and Canada especially, the US and Australia, credit unions were very much seen as financial cooperatives. That was their function, to act as a financial cooperative to a broad spectrum of the community membership. They tended to have a range of members with different economic circumstances. That has allowed them to financially capitalise because they are bringing quite a bit of money in from their membership. You can see this in Ireland over the years. You have a 70/80% market penetration rate in Ireland which is bringing a wide range of economic realities into it. In Scotland, England and Wales there has been more of a focus on targeted use of credit unions to address perhaps financial disadvantage. The problem with that from a financial point of view is you cannot financially capitalise on that market approach. That in turn has perhaps meant additional reliance on government funding at all levels of government.

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Q84 Mr Devine: The paper was outstanding and was really very helpful. Mackintyre is somebody who was involved in setting up a credit union within the Glasgow Health Board when I was previously the head of health for Unison. The board were very sympathetic and there was a lot of publicity. I had the feeling at times that the credit unions themselves seemed to be fighting like ferrets in a sack. I have local examples of behaviours from one where they have very good local credit unions and yet we have somebody from Edinburgh trying to get into that area. The bond covers the whole of the union but we have other small ones, one of which I am a member of. I get this feeling that there is no control or coordinated strategy from the credit unions and yourselves on how to manage this.

Dr Goth: That is a very valid point. In the environment in Scotland, England and Wales, it is very much an atomised approach to credit unions. Credit unions are very much isolated into autonomous units. You start to look at other systems around Europe especially and in certain parts of Canada and there is a very close network between credit unions. Although they have autonomy, anything can be common between them, whether it is banking or insurance or technology. That is a different approach. There are two types of models. My experience of UK credit unions is very much in the last couple of years. As a movement, I would be the first to say we have a very fractured movement. Maybe that is what you are alluding to. I think it is something internally as a movement that we have to address amongst ourselves.

Mr Lyonette: When I first got involved 10 years ago, there was a lot of talk of different trade bodies and that is really unhelpful. I know that is the history of many democratic movements and parties even, but it is not very helpful. What we have set about doing for the last 10 years is just trying to deliver as much as we can in terms of value for our members and not be interested in trade wars. As a result, the sector has grown quite considerably in the last 10 years. One of the other issues you are perhaps alluding to which is something we recognise and are doing some work on is around corporate governance. Credit unions will have challenges at board level with very small businesses. As they grow, perhaps they need to renew the skills that are involved in the board. Some of our larger credit unions now are bigger than the smaller building societies. The sort of board you need to successfully drive that is obviously quite different than a church based credit union with a couple of hundred people on a Sunday. That is a constantly evolving process. You have grown from here to here; it is not always easy to change the board as you go along and that can be a challenge. One of the things we are launching at the FSA¹ in September is a new corporate governance code for credit unions. Credit unions have had regulation for five or six years now in Britain and that is very good in terms of prudential standards and all of those kinds of issues but it is quite silent on corporate governance. Alongside the existing private sector code and the

existing cooperative code and the building society code, we have now developed a code for credit unions. That will hopefully help drive up some of the standards around the governance side of the industry as well.

Q85 Mr Devine: Who is the referee? Who is the body that says to one credit union, “Leave that part of Livingstone alone. Leave that part of West Lothian alone because it has its own credit unions”?

Mr Lyonette: There is not one, I am afraid, in that sense. That is not a role for the regulator either, the FSA. Our belief is, while it is unhelpful to be fighting for members on the ground, in a different sense if I was living in Livingstone, it might be quite good for me to have a choice of which credit unions I could use. People will often belong to two or three credit unions. Having some choice helps drive up the standards of the credit union, what services are being offered, the fees that are being charged, the interest rates, dividends, etc. Sometimes it can be really helpful. Obviously it should not deteriorate into people spending all their time trying to poach members from one credit union because the reality is, even in Scotland where 4% of the population belong to credit unions, that still means there is 96% of the population to go out and attract to membership. You should not be fighting over the 4%; you should be trying to help the other 96% who might want to use the credit union. I do agree it is not helpful.

Q86 Mr MacNeil: You are saying, rather than fighting each other, fighting banks and other financial institutions for some members should be going on. Why do you think membership is so low in the UK? Is it anything to do with confidence? Is it services that the credit unions provide? Are they just not seen as being bluechip?

Mr Lyonette: It is a number of things. Peter has already put his finger on one of them. Credit unions here by and large did not set out to serve a broad part of society. Often, the people who started them were aiming solely at quite a small segment of society.

Q87 Mr MacNeil: Those excluded by banking?

Mr Lyonette: Not necessarily. In the eighties and nineties, it was probably the working poor rather than the non-working. One of the issues is what is the image of the credit union and that is quite a hard thing to change. Also, you are right. Credit unions that have grown big around the world do not just do £300 loans. We are really pleased that we do a lot of £300 loans but they do much bigger loans. They do mortgages. They offer current accounts. Some of the things that we have done with our members over the last three or four years—we have produced a current account for example. That has been one of the key things around the world that has really helped credit unions grow. It is about access and convenience. The credit unions in the eighties and nineties might be open two or three hours on one or two afternoons a week. For many people, particularly today, that is not a realistic way of servicing them.

¹ Financial Services Authority

Q88 Mr MacNeil: Having been in Canada and seen how credit unions are perceived in Canada, it is very different. The credit union was not a credit union as I might imagine it here. It may have been a credit union that became a bank.

Dr Goth: A lot of it has to do with the whole idea and perception of what credit unions are. It is a very unique perception that seems to be in place in GB from Ireland or Northern Ireland even. The image that has come out of that, for laudable and noble reasons, is that they are a “poor man’s bank”. Because of the government programmes that they implement, they are directed towards disadvantaged individuals in the community. It does not project an image of community, financially owned cooperatives. When we start looking at that in Canada or the United States, it is very much a community. People will criticise and say we have big credit unions in Canada. We do. We have some massive credit unions. Although they have changed that structure, the whole idea is around community. The credit union I am with has day care centres and it has a huge scholarship programme for students. It is that sort of focus that everyone in the community can buy into.

Q89 Mr MacNeil: How does GB go about changing that perception? That seems to be the crux of your problem.

Dr Goth: At government level, what perception do you see for credit unions? When I look at Scotland, I think the potential for credit unions in Scotland is horrendous and unbelievable. Geographically, you have a lot of isolated communities where you are losing services to the central belt. There is a retrenchment of high street banking. The potential there is to be what credit unions to my mind should be which is community owned, financial cooperatives.

Q90 Mr MacNeil: Is not one of the biggest issues social inertia associated with banking? There is a statistic that shows you are more likely to change your wife than your bank account.

Mr Lyonette: Peter and I are absolutely on the same page. We need to project that broader image. The key thing is we need to get there. How do we get there? One of the things we are engaged with the Treasury on at the moment is having legislation that would allow us to offer the sorts of modern services that other credit union sectors around the world offer. In Canada, they have not grown large by paying a retrospective dividend that you may or may not get six months after you have had your money in there for the year. They have been able to offer an interest rate and say, “I promise you three or 4%.” We need a modern platform for legislation. The other part of it is products. We are not going to get big without being able to offer people a current account and a variety of loans. In recent years we have worked with government to introduce child trust funds, cash ISAs,² all of those things that are the sorts of products a wider range of people will use.

We have to not just say we need to change; we have to be able to put things in place. That only comes from scale. Our members have spent £5 million over the last three years on the current account. They would not have been able to do that unless they had got themselves to a point where they could invest in the infrastructure to offer a current account.

Q91 Mr MacNeil: Canada has been mentioned. I am interested in the history of credit unions in Canada. Did credit unions in Canada grow in a vacuum where there was no other financial service? Did they displace banking going back to the inertia of financial products from people? Where do you think credit unions should be pitching themselves? If I am going to be talking to my constituents and saying, “You should be with a credit union” and they say, “Why?” it is a general good thing. People are unlikely to move on the basis of a general good thing when they have just met a fellow in the street saying that.

Dr Goth: The credit union started in Canada in 1901 by a guy called Desjardins. The first one was in North America. It was really to address a social need for cooperative banking. Most of Quebec was rural. It was very difficult to get banking services. Desjardins now have 600 branches. They have 40,000 employees, 150 billion in assets and 4.5 million members. They are a network of credit unions. It is very much this community focus and I think that leads to your second question. How do you sell credit unions? To my mind, it has to be sold on a community basis, to the community, as their financial cooperative like their Coop grocery store. It is that sort of image. How we do that is the big question.

Q92 Mr Carmichael: You have already identified that there is in Scotland at the moment an accelerating process of retrenchment of services from—I hate to use the word—the periphery to the centre. The communities that are at the periphery are the smaller communities, by and large. In your submission you are talking about a process that has seen the number of credit unions shrinking but getting bigger and inevitably that is going to be the case if you are going to be providing the sorts of services and the whole range of things that you are currently providing. In a small community, how do you create that range of services, working with a fairly small pool of what are effectively volunteers?

Dr Goth: What we are trying to do now in the Scottish League is to start networking with credit unions. With a lot of that technology we are looking at a centralised service where even small technologies can link together for their back office. I agree with you. You cannot put a credit union into a small community and say, “Off you go.”

Q93 Mr Carmichael: My mother is involved in the credit union and, when you start talking about doing the sorts of things you are talking about, I can just imagine the blood draining from her face.

² Individual Savings Account

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Mr Lyonette: Peter is right. We need a legislative platform so that we can compete. We have to face it. Competing in Britain in 2008 is quite different from competing in Ireland in the 1950s when banking was not there or indeed in Canada at the turn of the last century. We are in a really competitive financial services market. For us to say we are going to take RBS head on in terms of aiming at their most profitable customers is not going to work. We need to be smart. We need the legislation. We need to get ourselves a broad array of products in a convenient way that people are going to use. For places like the islands, I suspect the reality is that a back office model is going to need to be there. Yes, it is still owned and controlled by the people in that community but, instead of having to all invest in the infrastructure for each individual credit union in Scotland, there can be some common investment so that they can all offer that platform. In the States for example, even though they have lots of billion dollar credit unions, they have an awful lot of still quite small ones. Credit unions with just 1,000 members can offer a full current account—a checking account as they call it—a range of different share deposit accounts and a range of different loans precisely because they have an infrastructure that sits behind it at each individual state level. That is the sort of model that we are beginning to look at now. We have some interest from the UK Government and I believe the Scottish Government in terms of looking at whether that could be achieved. Is there enough scale to get some economies of scale, if you like, by having some common back office services? You have to get over a little bit the fact that each island or community might still want to say, “It is still ours and we still want it to be done in our way.” There is some compromise there but if we are going to thrive and survive we need to be modern and not be afraid of change.

Mr McKillop: It is something special in more rural areas if they had access, for example, to the credit union current account. It would make a real difference there where maybe it does not have the same impact in more urban areas. A lot of the rural credit unions might not have the infrastructure there. That is why we said in our submission it is hand in hand with shared back office services. It is quite important all across Scotland as well because a lot of the community credit unions could really do with a hand if they are going to be able to scale up and offer the sorts of products and services which will increase their membership ultimately.

Q94 Chairman: In recent years the amount of interest credit unions can charge has been increased. In fact it has been doubled from 1% a month to 2% a month. Are you comfortable with this increase?

Mr Lyonette: Yes. The Association thought that was a very good thing. Peter has talked a lot about how the image of credit unions was the “poor man’s bank”. There are still challenges there, clearly. In reality, a number of credit unions were making loans at the previous 1%—about 12.6% APR³—and they

were using state subsidy in order to be able to do that. That seems to me not necessarily a very smart move. In a sense, the state was paying for these principals that will only lend at 1%. Since we have been able to lend at 2%, many more credit unions have used that and they have realised that, by being able to charge just that little bit more—let us be honest, 2% in the way our interest is calculated is such a small amount of money anyway—and if you are competing with people who are paying hundreds of per cent for their credit—and you often are—to be able to offer credit at all to people at 2% has to be a good thing if previously you would have had to turn them down because you would not have been able to take that credit risk.

Q95 Chairman: An increase of 100% you think is a small increase?

Mr Lyonette: It is a small increase. Our interest rates are calculated on a reducing balance. I know this is quite technical but if you borrowed £100 for a year, instead of paying £6, you would pay £12. In the scheme of things, when people are paying hundreds of a per cent for catalogues or through the home credit companies etc., if you can make a loan to people, say, a £500 loan, people will save £250 with the credit union if that is the market you are serving. If that enables credit unions to serve many more people, which indeed I believe it has, and has earned the income to make the credit unions sustainable, pushing them in the right direction, although on the face of it it seems a bad thing to increase the interest rate, it has allowed us to do much more.

Dr Goth: Mark and I disagree on this. I have a concern about going to that type of interest rate for a number of reasons. One, I think it is a high rate. Two per cent a month is a high rate. It does not address some of the problems that we know we have to address. We cannot broaden the scope of our borrowers if we have rates at 2%. If you have variable rates from 5% up to 24%, maybe, but that is a very difficult concept for a lot of credit unions. Some members are paying 24%; some members are paying 5%. If we are trying to look at a community approach to lending, a standardised rate becomes a big issue as well.

Mr Lyonette: Most of our members do not just lend at that maximum interest rate. It is not like they used to lend everything at 1% and they now lend everything at two. It is about having the power to lend at that rate. Many of the strongest credit unions lend at much less than 1%. For example, in the police service in Scotland—I do not just mean officers but families, cleaners, maintenance people, anybody involved in the police service—you would be hard pushed to get a better rate from the high street both on savings and on loans. The reality is credit unions should lend at the best rates and offer their members the best returns that they can. Nobody is suggesting that we should use the 2% if we do not need to.

Q96 Chairman: Committee Members are extremely concerned that financial institutions are exploiting the people who are most vulnerable in communities. They are charging up to 100%. Therefore, I am very

³ Annual Percentage Rate

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

strongly in support of having a cap on the financial institutions and the banking system because it is ridiculous that these banks are charging as much money as loan sharks on the streets to the most vulnerable. I can live with up to 24% which is almost five times more than the base rate but when you said it was a small increase that worried me a bit in case you support further increases of interest rates in the future.

Mr Lyonette: Not at all. A lot of people in the mainstream have store cards which are at more than 24%. If you are competing in that part of the market, as you rightly say, it is not 100% people are paying. It is often 300 or 400%. That is part of what credit unions want to do. We want to make sure that more affordable credit is available to those people. The reality is that, with some of those customers, half the people will not pay half the time so you have to be able to have an interest rate which is fair but which enables you to cover your costs. If you cannot cover your costs, you are not going to be around next year to be able to offer the service to those people. It is about being sustainable and able to compete with those providers. Those providers are rarely the banks at several hundred per cent. It is usually the non-bank lenders, although even the banks tend to have sub-prime subsidiaries that they lend through.

Q97 Mr MacNeil: When you say 1% and 2%, is that 1% and 2% absolutely or 1% and 2% above base rate?

Mr Lyonette: It is 2% on a reducing balance.

Q98 Mr Devine: Per month?

Mr Lyonette: Yes.

Q99 Chairman: That is 24% a year. You mentioned the introduction of ISAs, a credit union current account and a child trust fund. Do you believe that the introduction of these facilities within the credit unions has helped in stimulating growth in credit unions?

Mr Lyonette: Yes, absolutely. If we want to project an image for a broad part of Scottish society and it is community or employer based or whatever, we need to have products that people want. You are not going to get that sort of penetration into the country if all we have is small loans and simple savings that we cannot promise any interest on. Those credit unions that have introduced a cash ISA for instance with a tax break have found that has really grown the share pot, which is what Peter is talking about. Then of course you can increase the amount that you lend. That brings in more income. That makes the credit union work and thrive moving forward. It has been really important to do some of those things. Not many credit unions can yet offer mortgages. There is a different financial risk in there. If you look around the world, credit unions have not become large by not having that full range of products. Even in very low-income communities in the States—never mind just the mainstream credit union sector—and even the very low-income focused credit unions in the States will all offer mortgages. They are very definitely not part of the sub-prime problem in terms

of ratcheting up people's repayments. We need a product range that will match our ambitions to serve a broader part of Scotland.

Q100 Mr MacNeil: What support does the credit union movement receive from various forms of government in Scotland?

Mr Lyonette: Probably six or seven years ago the Scottish Executive first put some money into credit unions. Going further back, any support tended to be at the local level, at local authority level. Inevitably, if central government starts to fund something, sometimes it has a bit of displacement at local level. I would not want to see support from central government all about money at all, partly because of some of the dangers of becoming grant dependent and those sorts of things. Some of the most important things government can do are to support things like the legislative change, regulatory change that will need to go alongside it, but also to promote credit unions as a viable alternative, so some of the things we have done with the UK Government around the Savings Gateway which is now being launched, around child trust funds, even being able to offer those. The Scottish Government could do similar things, although it is not in control of the regulatory regime or indeed most of our legislation that affects this. Just being able to promote credit unions not just for the most disadvantaged but as a broad alternative for the people of Scotland would be a really positive thing. It is not just about cash.

Q101 Mr MacNeil: How joined up have you found the various levels of government, both the Scottish Government and Westminster?

Mr Lyonette: Not necessarily. We have had a good relationship with the Scottish Government for many years. We have had a good relationship with the UK Government. There is not always necessarily joined-up thinking, even within any two departments within one of those governments. People can sit in the same room apparently day by day and not necessarily join things up. We try hard. There have been some challenges. Some of the things that credit unions do around financial education for example and around schools. There are some really good examples of that in Scotland now, not least because it has become compulsory and schools are therefore really keen for the credit unions to come in and run school savings clubs. That happens in a very different place than anything to do around social enterprise in Scotland or around affordable credit. There is a challenge there and all of us, even the Association, are quite small organisations ourselves so our resources are necessarily limited to be able to try and get civil servants and ministers to work together and to see the common platform, if you like.

Q102 Mr MacNeil: Peter, you are shaking your head.

Dr Goth: There are a couple of new funds that the Scottish Government is coming out with now. One is the Enterprise Fund and the other one is an

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

investment fund. The investment fund would not be applicable so much to credit unions because it is for larger amounts but the Enterprise Fund might be. I have a double edged sword here. If we see credit unions as financial cooperatives, there is a significant role for us to enhance the delivery of credit unions. We can talk about all the products we want, but if we do not have the capacity within the credit unions to manage the credit unions or to deliver those products, it becomes somewhat academic. There is a real shortfall there in managerial skills and business attributes in credit unions. Very few governments give any money to credit unions in any other jurisdiction in the world. The other side of my sword is I do get apprehensive because of “the golden rule”, “the one with the gold makes the rules.” If a local authority is giving money for the credit union, whose agenda is it? If the Scottish or the Westminster Government is giving, what is the agenda behind it? I get a little apprehensive about this whereby we have been steered down the route that we are on now.

Q103 Mr MacNeil: Looking at your knowledge and expertise and looking for a comparable jurisdiction elsewhere in the world, where do you see an example of better governance in the same historical situation for credit unions? Is there anything glaringly obvious where you would say, “Yes, you know what they have done in Belgium? That is what we should have done years ago”?

Dr Goth: If you start looking at other jurisdictions outside North America, Australia and New Zealand, you get into a federated network system where all the credit unions are linked very closely. There are huge credit cooperatives in Germany and France. You go down a different sort of route from that.

Q104 Mr MacNeil: Given the history we have with banks and post offices to a certain extent and credit unions, and that there is social inertia, is there a jurisdiction that has had that similar background where credit unions due to government legislation or whatever have taken quite a different path and been more successful?

Dr Goth: I would say Northern Ireland. No government funding and very, very big growth.

Mr Lyonette: It has had a very different history in terms of banking and lending availability.

Q105 Mr MacNeil: Has that been in both communities or is that an overspill?

Dr Goth: No; you have a big divide in both communities, like everything unfortunately in Northern Ireland. You have two federations, one aligned to the Irish League Credit Unions and the other one to the Ulster League Credit Union.

Q106 Mr MacNeil: The concept of credit unions has got into both communities?

Dr Goth: Yes.

Q107 Mr Devine: This is a point that one of the DUP⁴ members asked about when we visited Northern Ireland. They were saying that within the Loyalist communities credit unions were not successful because they were seen as Republican. I wondered if you could comment on that. When Farepak collapsed, the Scottish Government and Allan Wilson as Enterprise Minister allocated, off the top of my head, about £800,000 that credit unions could tap into. People who were directly affected by Farepak went to the credit unions. Are you saying that was wrong?

Dr Goth: I was not here for Farepak so I could not really answer.

Q108 Mr Devine: Northern Ireland?

Dr Goth: There is a big difference between the two associations. The Ulster Federation has intentionally seen itself as a voluntary organisation. They only have one paid employee in the whole setup. The ones affiliated to the Irish League are very much more community based. They started up as church based but they have tended to become far more community based and of a different size, with a different approach.

Mr Lyonette: One of the problems credit unions have in Northern Ireland though is that they do not have access to the banking system. In many ways they are more disadvantaged than the credit unions of Britain and the Republic because they are literally in between two systems. They are struggling to get access to the Link network and Visa. We are working with the Irish League of Credit Unions and its members to be able to offer them the product we have from the Cooperative Bank because it is the same regulatory framework and the same Link environment. There are one or two problems with Visa there at the moment in terms of how they want to treat credit unions. They are absolutely desperate because they recognise that, although they have half the population approximately in the north using credit unions, they do not have the convenience and the channels that people might possibly want, particularly younger people coming through wanting access to cash with plastic and cash machines and all of those things. The credit unions are really keen but at the moment there are some barriers. That is another thing that government down here might be able to assist us with. We are hoping to ask for support with that as well. Farepak was a real lesson for many people. We work closely here with the Westminster Government. Before that there was not that much awareness amongst civil servants and perhaps even ministers that there were such things, where people were saving but their money was not protected in any way. It is a terrible thing to say that such a tragedy has had some good effects but one of the things it has done which is good is that many more credit unions now offer a competing Christmas savings product. People who want to save start saving in January, do not get the

⁴ Democratic Unionist Party

 9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

money out until November. If you like, you are discouraged from getting the money out for a day out in the summer. That has been really successful. Many credit unions have managed to put out there a useful savings product, something that people are used to, but it has the protection of the compensation scheme and it is regulated by the FSA. There have been some good things out of what was clearly a terrible disaster for many people.

Q109 Mr Carmichael: I wanted to explore with you the part of your submission on the future of credit unions in Scotland, but we have covered a lot of this already. If there is anything else to mop up, I will just give you the opportunity. You made an observation about the number of people in credit unions growing but the number of credit unions themselves declining. What effect do you think that is going to have on the future shape of the credit union movement?

Mr Lyonette: There is a very powerful phrase that small is beautiful. In so far as that can mean local and friendly service, which is really important in financial services along with other things, it is hard to argue that small is not beautiful. What I would argue is that tiny is not beautiful. If we are so tiny that we are not financially viable and we do not have the income coming in from loans and other products, we can think we are as beautiful as we want but we will not be there for the people of Scotland in five or 10 years' time unless we have a business model that makes sense. There are three key things around that. There is the right legislative platform so that we can offer attractive services; there are the right products that flow from that, things that people will want to use and are mainstream. We cannot become more mainstream if we do not have mainstream products. Thirdly, we have to look at things around efficiency really. In many other countries, it is not 500 credit unions, which there are in Britain, working separately. Somewhere behind the scenes there are some economies of scale with the system with a back office network, perhaps several entities that are meaning people can do the same thing more cheaply. Of course that is good for the member as well. The goal is to get things cheaply and a high return for people as well.

Dr Goth: I still come back to networking between the credit unions. I gave you an example of Desjardins, with \$150 billion in assets. Right next to Desjardins, where one of the Desjardins branches is, there is a place called Bay St Lawrence and it is on an island off the east coast of Canada. They have been around since the 1930s. They are all voluntary credit unions. They meet all their requirements. Through the network they can offer every single product that Desjardins does. You can go in there for a marine mortgage for a fishing boat. This little credit union cannot help you but the network can. You do not have to have huge credit unions. You have to have an elaborate network where credit unions can best serve their members. If that is a 1,000 people membership

or a 4.5 million membership, then there is no reason why the people in the smaller credit union cannot get all the services of the bigger credit unions.

Q110 Mr Carmichael: I guess the challenge is how you get this network, this broadening of the range of services and the increase in the size of credit unions while still maintaining the image of what you have, which is essentially good, local and community based. I have an involvement with the RNLI⁵ as a member of their National Council. The RNLI is a very big charity. It runs into hundreds of millions every year. The head of corporate fund raising says that the image most people have of the RNLI is that it is run by two old ladies in a cottage in Cornwall. That is really what we want to keep. How do you strike that balance?

Mr Lyonette: It comes back to some of the things we have said. Behind the scenes we have to be smart and efficient. We have to get the best value for our members that we can and produce sustainable credit unions. What I would really worry about is if, as a result of that drive, credit unions started to only act remotely and make remote loan offers and it was all internet banking. I do not think that is the future for British credit unions at all. There will always be a place for a local, friendly set of financial services that are on your side. That is absolutely key.

Q111 Mr MacNeil: That is a good slogan. You mentioned fishermen on the island off the east coast of Canada going for a mortgage for a boat. Would they be using other financial institutions as well or would their sole financial institution for all their transactions be that credit union, or would it also be the Bank of Nova Scotia, or whatever it is called?

Dr Goth: I will be quite honest with you on this. We did a survey of our credit union. We are not a huge credit union. We have about 16,000 members. We reckon that probably 88% of our members will deal with other financial institutions. People do price shop. In our credit union in North America we have to compete with the banks for rates. We make a good profit. We are regulated to a point where there are a lot of things we cannot do. We cannot lend high-risk money. We have to lend that out of profits.

Q112 Mr MacNeil: At the moment with the global credit crunch and the financial headlines we see in the news and in the newspapers, do you think credit unions will be seeing an opportunity for themselves in this sort of environment? We are in a period of flux and change, when people are forced to change; things are happening out of the norm. Is that an opportunity for you or have you recoiled from the situation?

Dr Goth: I think it would be from an image point of view. Because of the figures you are looking at, I do not know how realistic it would be from a financial point of view. Credit unions are not in a financial position to be an alternate financial intermediary because they do not have the size.

⁵ Royal National Lifeboat Institution

9 July 2008 **Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth**

Mr Lyonette: We have found, even since last September with Northern Rock, that credit unions are getting many, many more applications for loans. Unfortunately they are having to turn down more of those as a percentage than they might have done in the past. That tells us a lot about how indebted some people are. Unfortunately, we cannot be seen to be irresponsible lenders. There are people who come to you and ask for money to borrow and it is just not a sensible thing. That is where we do believe the credit union emphasis on saving as well is really important. We would wholeheartedly support the UK Government's proposition around the Savings Gateway because credit unions' history here tells us that getting people to save is not something that you can easily teach them in a classroom. It is good that there will be personal, financial education. All those things are important but saving is something that you learn by doing. In our experience people only value savings when they have them. The trick is how do you get people to have them rather than saying to them, "You must have savings. They are really good." One of the most powerful tools the credit unions do have here is payroll deduction. We have 20,000 bus drivers across Britain who are not any better at saving than your or me necessarily, but because it is deducted from their wages before they see it that is a really powerful thing. What you have not had you do not miss.

Q113 Mr MacNeil: It is like the granny and her various jars. You said you have had an increase in applications for loans since last September. Is there any corresponding increase in the amount of people coming to you to save since last September?

Mr Lyonette: We only have anecdotal evidence of that, I am afraid. We do not have system wide figures to be able to plot that in the way building societies have done.

Q114 Mr MacNeil: What does the anecdotal evidence say?

Mr Lyonette: Anecdotally, yes, but I could not quantify that for you. The credit unions that have the cash ISA are finding those are really taking off. That unfortunately is not too many of our members at the moment but it is a very successful product. I do not know whether that is people losing confidence in the equity ISA but that seems to be a really big growth area.

Q115 Mr Devine: Recently the government has announced changes to the Treasury, making it easier to join and I am delighted to be able to say that part of that was making groups able to join as well, which I was lobbied very severely with in my locality. Is this going to make a significant difference?

Mr Lyonette: Yes. We have yet to see all the detail as it plays through, obviously, but we were talking yesterday with the Treasury about the sort of reform order that might be needed to make this happen. There are three broad things. One is making the common bond more flexible. At the moment, we are denied in many ways access to many national employers, whether that is across Scotland or the

UK. It will make it much easier for employees of large employers that perhaps go across more than one community to get involved. Also, paying interest on savings. One of the key things we have to do is attract more savers so that we have a bigger pot in order to make more loans. Being able to offer an interest rate and not just a dividend is absolutely key.

Q116 Mr Devine: Peter, obviously the changes that we are proposing are going to make you even more like a bank and therefore any public subsidy, whether it comes from the Scottish Government or local authorities, is going to be more unlikely.

Dr Goth: With those changes, especially the one on interest, we are going down a certain route. On those recent announcements, I think the common bond one and the changes in interest are welcome. I must admit both of them give me a bit of concern because of the internal confrontation within the movement, not necessarily working in harmony. The interest one is good but it changes the relationship with the member because now you are in a contract with the member to pay that. Previously we paid a dividend if we had a surplus. If credit unions are now paying interest, they are contractually bound to pay that interest. Some credit unions are going to be fine with that. There are some provisions in there to say that, to go down this route, they have to have a reserve of a certain amount and I think that is beneficial. What were you saying about government funding?

Q117 Mr Devine: If you are now behaving like a bank, subsidies that may have been available from either the UK Government, the Scottish Government or local authorities may not be.

Dr Goth: I get back to the same thing.

Q118 Mr Devine: I know you want to be away.

Dr Goth: Not necessarily that. It is really an understanding of how Government perceive what credit unions are for. If it is still seen as a sort of delivery system, I must admit that I get concerned with that; I really get concerned with that because that becomes restrictive. If it was for education of volunteers and boards and capacity building within credit unions, I think that would be great. I think it is urgently needed; with the potential opportunity in Scotland, I think that it is necessary. I do still get a little concerned about funding for specific products. If they are conducive to what the credit unions want to do, great; if they are delivery of a local council or a Scottish Government or a Westminster Government's agenda, that gives me a bit of concern.

Mr Lyonette: I think it is hard to find an argument. No credit union system in the world has grown with the legislation we have now. So, yes, it is the interest rate; yes, it is the common bond, but also the organisational membership. It is really important. Credit unions tend to be small groups/small organisations knocking on the door each week saying, "Couldn't we put our funds with you while we run our business?" etc. It could be a grant from the council, it could be small fibre businesses, it could be any number of things. At the moment, we

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

cannot do anything about that. The legislation is absolutely key and, as Peter said, obviously we will look to the FSA to put in place appropriate regulations so that those things are not dangerous. For credit unions that are not used to making a promise on paying interest and just look at what is left over at the end of the year, then obviously that is a big change and we would expect the FSA to put in place appropriate regulation to protect the members' savings so that things were done properly. I think that goes without saying. I should say that I do not expect necessarily all credit unions to very quickly be able to pay interest on members' savings. It may be something that takes some time. Similarly with organisational group deposits or lending. If credit unions go into business lending, that is a very different thing overnight. You would not necessarily feel that people were going to do that without some good preparation and hiring the right expertise. All of these things will need to be with the right protection and the right regulation around that as well.

Mr McKillop: I think the key thing is that it is really the legislation that is giving the opportunity for credit unions to offer these things. It is not so much a case that the Government are saying that they have to do this. It is really just allowing for more products that they will be able to offer and, as Mark said, when the new legislation comes in, we would not imagine that credit unions could immediately take on corporate members. Again, maybe some of the larger ones can immediately offer a competitive interest rate to compete with some of the banks that are doing these things, but again it will not be across the board. It is not something that is being forced on them, but what we certainly very much support is giving these opportunities to our members to be able to offer the sort of products which, as we discussed earlier, may bring more people who currently do not join credit unions and, as I think as you said, just trying to come with an argument as to why they should, the best argument is that we can offer these sorts of products to them. So, certainly we support the legislation for giving us that opportunity.

Q119 Mr Devine: You do not expect an overnight change?

Mr McKillop: No.

Q120 Mr MacNeil: I have been listening to what you are all saying and you seem to be saying that you do not want money for a credit union as such, you want it for training or for working ... I wonder if the context of what you are saying is that basically people just do not get credit unions. I know the Northern Ireland situation (inaudible).

Dr Goth: I would agree with that. I think that the perception of credit unions is misunderstood.

Q121 Mr MacNeil: I have been in the misunderstanding bracket, to be honest with you.

Mr Lyonette: I would disagree to some extent. I am absolutely with you that the image of credit unions in some places in some ways has not been good, but I do not think it is just looking over the water. If you

look at the Glasgow Credit Union which came out of the council, the Glasgow Council Credit Union had at one point, before it opened up to the whole of Glasgow, 61% of all the employees who worked for the council and the various bodies that used to be part of it but are now separate to the council. Any bank in Scotland that had 61% of the employees of a major employer like that would be delighted. None of the banks have that kind of tradition. The point I am making is, if you get the products right and you get it offered to people in a way that they feel comfortable with, then it does work. Even in Scotland and even in England, there are examples like that.

Q122 Mr MacNeil: That 61% go the credit unions as the first stop and then wander off to the next (inaudible).

Mr Lyonette: Until very recently, they had to have a bank account somewhere else because the credit union could not give them a current account and they had to go elsewhere for their mortgage because the credit union could not do any of those things. In time, as in Canada and as in other countries, perhaps more people will use credit unions as their primary financial institution because we will be able to offer them the products. Ten years ago in Glasgow, you had to go to the credit union for saving and for small borrowing; you could not really go for anything else; there was not an option. Credit unions here have managed to do that in examples, so it is about getting it right. It is not just saying that it will never happen in Scotland or it will never happen in Britain.

Q123 Mr MacNeil: I am not saying that, I am just cross-examining my understanding of it.

Dr Goth: On that same theme, one thing I would like to indicate is that what Mark is talking about is employee-based credit unions which originally were employee credit unions which, by the very definition, were not for the most part necessarily addressing a disadvantaged section of society. Basically, all their members were employed.

Q124 Mr MacNeil: Which is what you want.

Dr Goth: Which is obviously what you want, but what I am saying is that, in this case, it has allowed you to financially capitalise to a point where they can grow. They have got to that stage; they can offer those products; they have their core base where you can start offering products. The vast majority of credit unions are not in that position. We have an office in Cranhill in East Glasgow and I do not think anyone in the membership is working. A very high percentage of the members are on benefit. Again, you get back to saying, "We have come out with all these products but are they products that necessarily a credit union is being able to offer?" because they cannot capitalise to do it.

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Q125 Mr Devine: Surely, that is the conundrum.

Dr Goth: That is the conundrum.

Q126 Mr Devine: The changes that we are making will make you more like a bank and the consequence of that is that we are taking you away from the community.

Dr Goth: Exactly.

Q127 Mr MacNeil: Is that right? Is what Jim has said exactly what you think is going to happen?

Dr Goth: Where I am coming from is, if you look at the large credit unions, if you look at the Glasgow, the Scot West and Edinburgh, obviously—

Q128 Mr MacNeil: And Desjardins in Quebec?

Dr Goth: Desjardins does but it cannot through legislation deal with disadvantaged individuals financially. It does but it cannot do it through the legislation. It can do that because it does it out of its profits and they make very good profits; they have by definition because they will need good profits. It is easy in Scotland to say, “Okay, we have this but we need more products, we need more products, we need more products” and there are certain credit unions—I would agree with Mark 100%—that would do fine with that increase in products, very much so, but there are a lot of credit unions that are not at the capacity to do increased products and I think that it is important that we do not and, maybe to answer the question that we would become like banks, I think the worst scenario is that you end up with three or four dominant credit unions that can act as banks because then you have just drawn a division between them.

Q129 Mr Devine: Surely that goes back to what I said at the start about basically fighting like ferrets in a sack. Should we be prescriptive as politicians and be saying, “Here you are”? or draw up a set of guidelines that says that, “If you are based in Edinburgh, you cannot come out to Livingston”. Do we need to do that? You say you cannot do that.

Dr Goth: I think—

Q130 Mr Devine: To take your argument that you want a community base and it obviously worked and not to get it as a big bank, what else are you going to do?

Dr Goth: To make a community base without it becoming a big bank?

Q131 Mr Devine: Yes.

Dr Goth: Why would it necessarily have to become a big bank?

Q132 Mr Devine: I know a lot about them in Ireland; they are on the main streets; they are very well known and very well used. The Irish Allied Bank is there and the Credit Union Bank is there. When you go in, there is no difference in the frontage and there is no difference in any of the service. I was saying to you earlier on about the conundrum which is, can

you say that that is a community-based organisation as a credit union there or is it basically just a bank that competes with other banks in the main street?

Dr Goth: The big difference and if you look at large credit unions is what they do with their profits. At our credit union in Canada, we make good profits—about 1.5% return on assets, which is very good. You can come along and everyone will say, “Well, you’re a bank”. Yes, okay, we are a bank to a certain extent, we compete with banks, but we run day care centres, we have a housing co-op, we have micro-finance lending for businesses. That is how we do our community role.

Q133 Mr Devine: You are not going to be able to do that here with size. Size is important in the issue.

Dr Goth: Yes.

Q134 Mr Devine: If it is big and you are making that sort of profit, you can invest back in. You are not going to be the community bank that you are talking about or, the community service that you are talking about.

Dr Goth: If you take an item like that, like I was saying to you, that credit union, the one next to it is Bay St Lawrence. They are community; they are all volunteers; they have a whole range of products that they can get access to but they are as much a community credit union as any credit union you have in Scotland. It is how they define themselves as to what they want to do. Credit unions do not have to be big, they do not have to be small; it is how they function within the community. I think that it is difficult to standardise all credit unions and say, “This is what they are”.

Q135 Mr Devine: Why would I join that credit union you have just talked about if I can go to the big credit union where I can get all these benefits that the other one does not have?

Dr Goth: It has all the benefits. You can go to Bay St Lawrence and get any product that you can get at Desjardins because they are all networked together.

Mr Lyonette: We are talking on a different scale of the diversity of credit unions in Scotland. The reality is that credit unions with hundreds of members in Scotland at the moment are going to struggle to survive because they do not have the efficiencies to provide that wide range of services. In Britain, one of the problems is around the word “bank”, is it not? I never want to see credit unions being talked about in the way that we talk about banks in the UK, but it is very clear to me that for us to thrive and to grow as in other countries, we have to do banking. So, there is a difference between being a bank and doing banking services. Credit unions in other parts of the world have never ever grown without being able to offer that full range of products. It is just not there.

Q136 Mr MacNeil: It may be that there are too many credit unions because if Edinburgh is competing with Livingston as Jim was mentioning ... Can Desjardins and Bay St Lawrence cope? Do we have too many credit unions being set up with the initial evolution of credit unions?

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Dr Goth: You can look around the world and you can see very clearly a pattern of credit union growth. It is very common and it is consistent with every jurisdiction you look at. To give you an example in Canada, in the 1970s we had 7,000 credit unions in Canada and we are now down to 635.

Q137 Mr MacNeil: Has that been a good thing?

Dr Goth: I would say that it has been a good thing. It has completely changed the way we operate. Although it is down to 635 credit unions, it is still round 2,000 branches or units.

Q138 Mr MacNeil: In essence, the number of credit unions does not matter. It is the size and access to them for financial services.

Dr Goth: To follow on from that pattern, with regard to the financial health and credit unions in these jurisdictions, Canada has the healthiest credit union system in the world; it is very highly regulated but those transitions have made for a very healthy financial movement. I think that we have to go through that stage and I think that it will go through that stage in the UK.

Q139 Mr MacNeil: There are only so many credit unions that a set population is going to hold.

Mr Lyonette: Yes. The credit unions in Britain did peak at 700 a few years ago. I take Jim's point about Livingston and I think that there might be some individual issues there but, by and large, I think that the task is to make sure that a range of quality services are available to the people in Scotland in general. Whether that ends up being 100 credit unions or 50, I am fairly agnostic about that really. I am not too concerned. The real issue is not, as I say, fighting over the 4% of people who already use credit unions in Scotland, it is how can we get that up to 25% or 35% of the population. I am not too concerned about the overall scale; I do not think it is good for people to be competing locally against each other's members because the bigger problem is about offering a wider range of people a good quality set of services.

Dr Goth: I 100% agree with that. The problem is that Mark and I can sit around the table and we can agree with this but it is what that—

Q140 Mr MacNeil: The problem is that you do not fully agree.

Dr Goth: It is, how do you present this overall image of what credit unions are about and I think that we have gone a full circle in this discussion, but I think it comes back to that: what is the perception of credit unions?

Mr Lyonette: I think that Peter and I agree on the vision of credit unions. I would in many ways look to the Canadian system in terms of the way the credit unions work and also I have to say the co-operative movement generally is a very much bigger part of society there than it is still here in some ways, even in Scotland. The reality is, how do we get from where we are now to where we want to be? We agree where we want to be. We cannot just talk about community; we cannot just say that we need to focus

on the wider group of people. We have to have the powers to do that; we have to have the range of products and services that people want; and we have to be big enough and strong enough to still be here in five years' time. I think that probably there is not that much divergence of view on what really needs to happen.

Q141 Mr MacNeil: What is the percentage of use of credit unions in Canada?

Dr Goth: It is about 65% although you have to be very careful with those numbers because, like with all credit union movements, it depends on the sophistication of the credit union movement. We have a central data system—

Q142 Mr MacNeil: In all provinces?

Dr Goth: In all provinces but it is more in the west. Outside of Quebec with Desjardins, British Columbia is probably the next biggest primarily because British Columbia opened up at a time when credit unions were pretty strong in the east anyway, so they moved in there. You have to be careful about those numbers because how many are active members? You can say we have 500,000 members but are they just names in a book or how many of those are actually active members of credit unions?

Q143 Mr MacNeil: Can you answer for me what seems to be a simple question: why are all Canadians not in credit unions?

Dr Goth: Maybe some because of logistics; they cannot get to them because they are all over the place. Some are not for whatever reason you can think of. It is an alternative to a banking system for people.

Mr Lyonette: Some of it is probably a bit like we have as well that, if you have been with RBS and your mum and dad were with the RBS, there is a bit of inertia as you were saying before as well. You may never even in Canada have come across the credit union system in your family and friends.

Q144 Chairman: Credit unions have a cap on maximum interest rate; they charge 2% a month. Do you support this cap on other financial institutions, banks and building societies?

Dr Goth: I do. I am surprised that one is not in place in the UK. We have 29% in Canada, but then you get into the service charges and management fees and that sort of thing which makes it a bit iffy, but I think that a cap is essential.⁶

Q145 Chairman: Mark, you disagree on a few things with Peter.

Mr Lyonette: We do, actually. It is more a question of timing than in absolute because unfortunately, at this point in time, if the Government were to legislate now and put in a cap of any percentage rate for the people who were paying 700%, you would actually put a lot of those people, two or three million people who are using even just home credit for example, in

⁶ *Correction by witness:* The maximum interest rate chargeable in Canada is 60% per annum

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

a position where they would not have access to any kind of affordable credit at all. It is more a question of timing.

Q146 Chairman: But, in principle, you support it?

Mr Lyonette: In principle, we do not want to see anybody paying anything like that for their credit. However, if you were to do it overnight and while the credit union sector has not grown and there were not alternatives for people, we could actually cause more problems than we were initially solving.

Dr Goth: That is a good point.

Mr Lyonette: Of course, we are absolutely horrified by people paying that kind of money.

Mr McKillop: In principle, the idea of people paying 200, 300 or 400% APR in some cases but I think, as Mark says, how you do that has to be timed very carefully because if there was a way of bringing that in that would not have that effect on people ... The argument you always get from Provident, Greenwoods and people like that, is that these sort of people would not get credit anywhere else; they have wriggled out a few times in the past and used that argument. Unless there was a capacity for credit unions to bring in these people as members, financially excluded people who cannot get credit anywhere else, bringing in that sort of legislation would cause more problems.

Q147 Chairman: These financial institutions are in business to give loans to people; that is the only way in which they can make a profit. If a cap is there, they still have to give loans.

Mr Lyonette: There have been examples where this has caused a problem. In Poland where the credit union movement has grown very strong since the solidarity movement, the Government legislated to bring in a cap which I think was linked to today's rate, something like five times base rate, and of course what happened was that lenders who were wanting to charge extortionate rates get very creative about how they can get round it because, as Peter said, you might have people putting on an insurance product, "You won't get the loan if you don't take that insurance product". We have to be very careful that we do not create more problems than we try to solve. One of the key motivations for being involved with credit unions for most of the members in our trade association would be around trying to get people a better deal than people are getting on the doorstep. Remember, the rate in Canada about which Peter was talking about as a cap would rule out most of our High Street store cards. Actually, if you worked out the cost of overdrafts, it would rule out the cost of overdrafts. It is a very low rate if that is the rate. I was not aware that that was the rate in Canada. Lots of mainstream credit in Britain is at that level.

Q148 Mr Devine: I do not see what the difficulty is here. One of the side effects of Fairpak was the National Provi of 188%. If we are saying that, as of 1 January of next year, there is a 29% cap and basically there are no exceptions to it, where is the problem?

Mr Lyonette: Certainly from our sector's point of view, from the credit unions sector, we would not have scaled up significantly enough. We are quite healthy but not enough to capture that two or three million people. Where will those people go for credit on 2 January?

Q149 Mr Devine: So, that is where you see the difficulty.

Mr Lyonette: Yes.

Q150 Mr Devine: Our assumption was that they would stick with the National Provident because instead of charging 188%, they are now only charging 29%. Are you assuming that there is something ---?

Mr Lyonette: We have just carried out a piece of research with the Joseph Rowntree Foundation, the University of Bristol and the National Consumer Council looking at whether we could introduce a not-for-profit home credit service because we know that the product is valued but it is the cost of it that is exorbitant and one of the things we found in that study is that that industry is actually in many ways withering away. As people have other options, the scale of the home credit industry ... Some of the big players ... People like Cattles and their shopper check brand has been withdrawn and they tried to put forward a direct debit kind of product because it is actually very hard, I would suggest, to try and make that business go particularly because it is all dependent on the agent. Once you lose an agent who has been working in an area and is known by people for 20 years, they have all found it very hard to replace him with somebody new coming along. Obviously, there has been the Competition Commission inquiry into the scale of profits in that industry and they said that they overcharge by 100 million. If you overnight said that the interest rate is here and they are charging up here, I think that a lot of those players would disappear. I do not think that they would continue to think that they could run a successful business at, say, 30%. That would be the danger. That would not be a good place.

Mr McKillop: It is important to note as well that we are talking about some of the extortionate rates that the legal doorstep lenders charge because there is also trouble with illegal lenders, loan sharks. Straightaway, as Mark said, the financial model that the doorstep lenders, the legal ones, use, if there was a cap that they found unviable to their business, they would probably just take the money they have made and close up. Obviously, being illegal, it is difficult to get a figure of how many people across the country are using illegal loan sharks at the present time and there may be a danger of pushing more people towards that if the legal if unethical interest—

Q151 Chairman: That is not justification to allow the banks to stick in whatever they want to.

Mr McKillop: Yes. I am concerned about an overnight change.

Mr Lyonette: I think that we have a duty to try and—

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Q152 Chairman: The loan sharks are committing an illegal act and financial institutions are allowed to charge legally people up to 500%. How can you justify that?

Mr McKillop: Our concern would be the fact that people use loan sharks; they are illegal but there are people using them and you would be pushing more people toward them.

Q153 Mr MacNeil: We have heard about the credit crunch and we know that debt in society is quite substantial. What do you think that credit unions in particular can do for people on low wages? Is there anything specific that jumps out at you?

Mr Lyonette: I think the biggest thing we can do is in many ways what our members have been doing more or less successfully for many years and that is giving one of the most basic messages which is that we all have to live within our means. We cannot spend money that we do not have. One of the things which credit unions have been very good at is encouraging people to get a mixture of savings and borrowing and not just living off endless credit. Having a bit of money put aside, even if it is only a few hundred pounds, can actually make all the difference to people. If you talk to people like Citizens Advice and all the debt advice agencies, they will tell you that having even a small buffer is a way that stops you getting over the precipice.

Q154 Mr MacNeil: They are teaching us some sort of responsibility with money.

Mr Lyonette: Yes. Credit unions have a legal requirement in Britain to help people make the best use of their money and it is a case of using old-fashioned words like “thrift” really. I suspect that the credit crunch is quite a seismic change in terms of the financial markets here and I would not be surprised at all if actually it became wholly different and easier to persuade people to save and not just live off credit. What for the last 20 years has seemed like a right to credit will probably not be there in that way for many people in the future. So, credit will be seen as more precious possibly and therefore we need to all live more sensibly and not be extending ourselves to a place where we cannot afford to repay the credit that we have taken.

Q155 Mr MacNeil: So, after the credit boom we might see the old word like “prudence” coming back into fashion.

Mr Lyonette: With all of these things, you have to look for the good things, do you not? You have to look for the things that might help people make the most of their money. Potentially, whilst the credit crunch is clearly leaving some people in difficulties with renewing mortgages and things like that, over a period of time, we might learn some lessons from it I suppose is what I am saying.

Q156 Mr Devine: May I ask one question just to wind up. We obviously at the end of this make recommendations. What would be your two recommendations here?

Dr Goth: For the credit unions?

Q157 Mr Devine: Yes.

Dr Goth: I think that it is promoting the image of credit unions and increasing the capacity of credit unions, not just product-wise but education-wise within the credit union with training. That would be my favoured approach.

Mr Lyonette: It is probably some of the things that we have said several times. I would like to think that, as it passes through hopefully Parliament in the next year, it would be good to have support for the legislative change. We cannot have too many politicians supporting that, I do not think. We would like to see perhaps a recommendation that the credit union current account or some kind of banking service is important in terms of credit union growth but also a recommendation that we should explore together perhaps in partnership with the whole range of bodies, for example the Post Office. We are working quite closely with the Post Office which might be part of the challenge for the rural issues that we were talking about before to encourage the credit union sector to work both on its own and in partnership with others to see whether there cannot be models of a back office/models of partnership that would allow us to serve many more people across Scotland.

Mr MacNeil: Should it not be credit saving unions?

Q158 Chairman: I am surprised that these words of wisdom have not come in over the last 90 years!

Mr McKillop: I think it is again encouraging a savings culture and, as Mark has said, certainly new legislation would give support for that and the opportunities that will allow the opportunities to introduce the credit union current accounts more. Another thing I would emphasise is what we have seen in Scotland from the Scottish Government more and more is the emphasis on credit unions as a social enterprise encouraging credit unions in many ways to tap into funding streams and the resources that have been available for co-ops, community recycling groups and so on as possibly some types of credit unions have not regarded themselves and I think that by various funding streams were not regarded officially either as coming under the social enterprise banner, so we are seeing that more and it is something you get with the investment fund and the third sector enterprise fund. That will bring more opportunity, so that would help credit unions perhaps to think of themselves more as a thriving local community co-operative and an ethical alternative to banks for people to turn to in their communities.

Dr Goth: With that percentage rate that I mentioned to you, perhaps I could track down the legislation behind that because I do not know if it was in the Bank Act or within the loan sharking control, but I will certainly get something to the Committee to confirm that rate.⁷

⁷ *Correction by witness:* The maximum interest rate chargeable in Canada is 60% per annum

9 July 2008 Mr Mark Lyonette, Mr Frank McKillop and Dr Peter Goth

Q159 Chairman: If there is anything that you want to send to us later in writing, please, do so before we compile this report.

Dr Goth: It will confirm that percentage rate.

Q160 Chairman: I would like to thank the witnesses for their attendance. Before I declare the meeting closed, would you like to say anything in conclusion perhaps on anything which we have not covered in our questions?

Mr Lyonette: We have talked a lot about some of the negative things and some of the challenges which the credit union sector has faced over the last 20 or 30 years, but I think that we should also take stock of how much has changed and how much has grown.

Ten years ago, you used to have to save with the credit union before you could borrow. Now we are much more flexible about those things. We still encourage saving. We are now at nearly 700,000 people across Britain. We are all so much more visible and I do not think that it is always around the financial inclusion agenda and the disadvantaged agenda, although it is important that we continue to serve those people. I think that we should not be pessimistic. I am quite optimistic that if we put in place all of the things that we are talking about and which we are in the process of doing, actually, I do not see any reason why, in five to ten years' time, we do not see a much bigger credit union movement in Scotland. I think that is quite likely.

Chairman: Thank you.

Wednesday 28 January 2009

Members present

Mr Mohammad Sarwar, in the Chair

Mr Ian Davidson
Mr Jim Devine
Mr Jim McGovern

Mr Charles Walker
Pete Wishart

Witness: Ian Pearson MP, Economic Secretary, HM Treasury, gave evidence.

Q161 Chairman: Good afternoon. I would like to welcome you to our session. Before we start on the detailed questions, would you like to make any opening remarks?

Ian Pearson: Thank you very much, Chairman. To emphasise the importance that the Government attaches to credit unions throughout the United Kingdom, we want to see a well-resourced credit union sector with a modern legislative framework, providing high quality services. We welcome the contribution that credit unions make, together with our mutual societies, in providing choice and diversity in the financial services sector overall. We particularly support the work they do in terms of financial inclusion and capability, and I am sure we will discuss that in detail in due course. We welcome the very positive attitude that the credit union movement right across the UK has taken to supporting government initiatives, the Child Trust Funds in particular. I suppose the last thing I want to say is that the credit union movement is extremely strong in Scotland. It is very strong in Northern Ireland, but it is very strong in Scotland as well. No doubt we will come on to that as well.

Q161 Chairman: In this current banking crisis and economic climate, when people are feeling real difficulty in going to their banks for loans, especially people who do not have that much money and depend on the banking system, do you think the role of the credit unions will change?

Ian Pearson: As you know, we have taken action, through recapitalising the banks and other measures that were announced last week, to ensure stability in the financial system. One of the things that we clearly specified when we did the bank recapitalisation was that we wanted to make sure that the banks continued to make available lending at acceptable rates, at 2007 levels, and, as you will be aware, we have set up a lending panel and we are lending to businesses and individuals on a regular basis. But there clearly is a global credit crunch. It has affected the United Kingdom. People are finding it difficult accessing credit when they need it. I would like to think that there has always been a strong role for credit unions in the United Kingdom, but particularly during times of economic difficulty. I think it reinforces the message that a credit union has, with its very strong community or work-based ethos. I want to say very strongly that we are committed to credit unions. We definitely believe that they have a role in helping people during these difficult financial times that we are all facing.

Q162 Chairman: What practical measures are you prepared to take to encourage people to use credit unions, especially the people who are very often in mainstream financial institutions?

Ian Pearson: One of the things that we have done recently, as you know, is to establish the Growth Fund. The Growth Fund, in the work that it has done, has been trying to encourage particular disadvantaged groups to access funding through credit unions. I think that has been very successful in Scotland and more widely as well. We see credit unions as being an important part of our financial inclusion agenda generally. The other point I want to make here is that during times when people find it is difficult to make ends meet, those who have previously been in credit unions have a savings habit, and perhaps for the first time they need to take out loans from credit unions and they are in a situation that maybe makes them better placed than others. I think that once we get through this economic crisis we will continue to see the development of credit unions as part of the fabric of our financial services system and a key part of that fabric.

Q163 Chairman: When we conducted an inquiry into poverty in Scotland, it was visible that banks and financial institutions are exploiting those who are the most vulnerable in our communities. The people who take small loans, for instance £500 or £1,000, are being charged 100%, 200%, and even 300%. In those circumstances, do you not think that the credit union is the answer to the problems of the people who are underprivileged?

Ian Pearson: It certainly is not the high street banks and the main lenders that are charging those sorts of rates.

Mr Devine: They are.

Q164 Chairman: They are.

Ian Pearson: The banks are regulated by the Financial Services Authority and I would be very surprised if there were specific examples of mainstream banks that are charging the extremely high interest rates that you suggest. Certainly if you wanted to make any information that you have available to Treasury officials, that is something that I think we would want to investigate. There has been a clear problem with doorstep lending, with loan sharks, with the non-mainstream financial community, where—

28 January 2009 Ian Pearson MP

Q165 Chairman: I can assure you, Minister, that is the view I had before we conducted this inquiry, that it was just the loan sharks who were charging people these kinds of interest rates, but we were astonished when we were provided with the evidence. People who have got a loan of £500 are paying almost £20 a month and their loan is increasing rather than decreasing. There are problems and unless somebody acknowledges this we cannot find a solution.

Ian Pearson: I would be interested to see the evidence. When you suggest a £500 loan paying off at £20 a month, that seems quite a reasonable thing to do.

Q166 Chairman: The loan is increasing.

Ian Pearson: We know what APRs are like on credit cards, which tend to be higher than on normal loans that individuals can take. I would be very interested in the evidence that the Committee has. Certainly it would be a valuable inquiry for us to consider your findings.

Q167 Mr Devine: I raised a ten minute rule bill in December on capping interest rates on store cards and on legalised lending. The example used was comparing one of the large credit unions which loaned somebody £500 with the National Provident. The National Provident charged an interest rate of 183%.

Ian Pearson: That is a staggering figure, is it not.

Q168 Mr Devine: Exposed in the *News of the World* after I did the debate was that there was another company charging 432%. I do not know if you have them on your streets but they are certainly there in my constituency, this “cash a cheque before your pay day.” Some of that can be up to 700 or 800%. Are you saying that you are unaware of this?

Ian Pearson: No, I am not saying that I am unaware of that, and certainly some of the door-step lending and—

Q169 Mr Devine: We are talking about legalised.

Ian Pearson: The issue of “pay day loans” is an important one. You are right to say that some of these are charging extortionately high rates. One of the things we are very keen to do as a government is to encourage institutions like credit unions to provide viable alternatives to some of those extremely high rates that there are.

Mr Devine: One other figure from the debate was that if you had a £1,000 balance on a Debenhams store card and you paid the minimum payment, it would take you 15 years to pay it off.

Q170 Chairman: The base rate is now 1.5%. What percentage do you think it would be reasonable to charge people?

Ian Pearson: I do not think it is a simple straightforward answer to say there is one figure. It depends on how much you want to borrow over what time scale, and these are matters that are regulated by the Financial Services Authority. I do

not know whether you are intending to invite them to the Committee but that might be something that you want to consider doing.

Q171 Chairman: Do you think 50% or 100% is reasonable?

Ian Pearson: Personally I do not think that is reasonable. I think that some store cards have very high APRs and people should think carefully whether that is what they want to take out when they are making their individual financial decisions. As a government we have to set a policy framework. We have a system of independent financial regulation through the Financial Services Authority and the Financial Services Authority has certain statutory responsibilities to ensure fair practices. You may want to decide as a Committee whether you want to ask the Financial Services Authority for further information in these sorts of areas. I am sorry, I should be clear: credit cards and personal loans are not FSA regulated. They fall under the Consumer Credit Act and they are regulated by the Office of Fair Trading. It depends on which area you are talking about as to who has responsibility.

Q172 Mr McGovern: Could I ask the Minister if he, like me, has constituents coming to his surgery complaining not only about interest rates but bank charges, where people, if they default on one payment, have then found themselves in a multiplier situation where because they have missed one payment within a period of six to eight weeks they find themselves possibly £200 or £300 in debt and they are never going to be able to get out of that because it is just a downward spiral. Also, I would like to ask the Minister if he has a view on fee-paying ATMs operated by some banks and financial organisations.

Ian Pearson: First, I do have constituents coming to me about bank charges as well. If those bank charges are unfair, then there is a complaints procedure that can be gone through. You will be aware how that operates. With regards to ATMs, one of the things we have tried to do to help promote financial inclusion is to encourage the installation of more free ATMs, particularly in rural areas where there have been difficulties with people having to travel many miles to access a bank or an ATM outlet. That has been an area where we have been working with the industry to try to make some progress to enable greater financial inclusion. Particularly on the point that you make about ATMs that charge, again I think this is a matter for people to decide whether they want to accept that fee or not. I do not think as a matter of public policy we are thinking of banning fee-charging ATMs but we want to ensure that there is a proper supply of ATMs out there, with a good geographical coverage, that do not charge.

Q173 Mr McGovern: First, the Minister mentions that bank charges are unfair. I would like him, if possible, to define for me what is an unfair bank charge and what is a fair bank charge. Certainly my impression is that the charge should reflect the cost of administering the default payment. When that is

28 January 2009 Ian Pearson MP

£35, I do not think that is a particularly fair reflection of the costs involved. Second, on the subject of fee-paying ATMs, the minister says it is a matter of choice for the consumer but I do not think it always is a matter of choice. They sometimes feel they have no choice.

Ian Pearson: I know that this is an inquiry into credit unions rather than into the banks, but if you want to decide to extend your inquiry and talk to the banks, that is something that as a Committee you might decide would be a valuable thing to do. You will be aware that there is an OFT investigation into bank charges at the moment and there is a test case. I do not think it would be appropriate for me to comment further on that but I am quite happy to talk about credit unions in Scotland.

Mr McGovern: On the second matter of ATMs, you feel it is a matter of choice, that if somebody does not want to use a fee-paying ATM they do not have to use it, but they might live in a small village that does not have a free ATM.

Q174 Chairman: I appreciate this is an inquiry about credit unions, but obviously it is a matter of great concern to me. If the Minister thinks it is a matter only of choice, there are people who are in terrible conditions—

Ian Pearson: I did not quite say that. It is currently a matter of choice and I am not aware of any government plans to outlaw fee-paying ATMs. As I have said, we do want to ensure there is a healthy supply of free ATMs right across the UK so that people can have access to their money when they need it and do not have to pay a charge for that.

Q175 Chairman: Do you not accept, when taxpayers are paying £27 billion and billions of pounds in terms of guarantees, that the Government has a legitimate right to ensure that banks are giving a fair treatment to their customers and to the people in this country?

Ian Pearson: We always want banks to treat their customers fairly. That is why we have a system of banking regulation. That is why we have the Consumer Credit Act. That is why we have the Office of Fair Trading. What we sensibly do as a government is set up a framework of legislation. There are remedies there for individuals who believe that the banks are not treating them fairly. I would encourage people who think that they have not been treated fairly to use the complaints procedures that are there at the moment.

Q176 Mr Davidson: A number of the points that you make about the behaviour of the banks are fair enough. However, given that the Government has now such a substantial stake in the banks, do you not think that it is no longer just a commercial decision of the banks to take and that the Government really ought to be intervening much more directly to stop banks ripping people off in terms of inappropriate charges and the other measures they are taking which are essentially gouging the consumer?

Ian Pearson: We have said that the banks in which we have financial stakes as part of the bank recapitalisation scheme will be run on an arm's length basis. We have a set up UKFI as a body that will represent the UK's interests. Banks have to be run as banks. We expect banks to treat their customers fairly, whether they are individuals or businesses. As I said at the outset, we are monitoring their availability—

Q177 Mr Davidson: Is that not just washing your hands of the issue, to say that you are going to conduct it on an arm's length basis? That essentially allows the banks, in dealing with ordinary people, as it were, rather than those with big mega-dosh, to continue to gouge them unmercifully in the way they have been up until now? Surely a Labour Government ought to be doing a bit more to curb some of the excesses of the banks?

Ian Pearson: One of the great strengths of the Labour Government has been its focus on the individual and standing up for the individual against vested interests. We have a framework of legislation that I think is important in ensuring that we have consumer rights.

Q178 Mr Davidson: Just to clarify, are these matters under review then? Particularly in the banks like RBS, where we have an overwhelming public share, is the question of the outrageous charges being levelled by the banks being reviewed?

Ian Pearson: You are making allegations which you will need to substantiate. The situation is as I explained. The stakes that we have in RBS, TSB, Halifax, Bank of Scotland, are run on an arm's length basis through UKFI. As I have explained to you, it is not the case that the Government can involve itself in the millions of individual transactions that take place during the banks on a regular basis.

Chairman: After talking to my constituents who come from a business background and the people who have loaned money from the banks, I can say on the record that banks are charging excessive rates of interest. They are charging astonishing service charges and penalty charges and they are looking for any excuse. For an overdraft that is just £5 up, they are charging £25.

Mr McGovern: £35.

Q179 Chairman: £35 now. Certainly when we are subsidising these banks, saving them from going bankrupt, we expect them to behave in a way which is at least fair to their customers.

Ian Pearson: I expect them to act fairly as well, Chairman. I am sure the banks will hear what you have said today. Perhaps we can discuss credit unions in Scotland.

Q180 Mr McGovern: Minister, you mentioned unfair bank charges and I asked if you could define what an unfair bank charge is. You have not answered that yet.

28 January 2009 Ian Pearson MP

Ian Pearson: I am not going to either. This will all depend on the individual circumstances so I do not think it is possible to give you a particular definition.

Chairman: The last question on this and then we will move on.

Q181 Mr Walker: You are currently pioneering a bill through the House of Commons, the Saving Gateway Bill, which I am sure will apply to Scotland. That is right, is it not?

Ian Pearson: Yes.

Q182 Mr Walker: Do you think the additional moneys to support savings will be of benefit to credit unions? I think you started off by saying that credit unions are fairly well established in Scotland and we are looking at renewed impetus or additional impetus to encourage the savings habit and also to help support their loans. Do you feel that the Saving Gateway and what comes out of that is a positive step in the right direction for encouraging the credit union to flourish?

Ian Pearson: Yes. I strongly believe that the Saving Gateway is an important way in which we can engage people on relatively low incomes to save. I think that is a good thing to do. I am very pleased at the positive response we have had from credit unions about getting involved with the Saving Gateway. As I have said, they have been involved with the Child Trust Funds already and I think the Saving Gateway could potentially open up new savings opportunities for millions of people which will be incredibly important for the long term.

Q183 Mr Walker: How far do you think the credit union movement can go? Are we at the very early stages of the journey or the middle of the journey? I do not imagine we are near the end of the journey. How big could this movement be if we get it right?

Ian Pearson: We are on a journey and I think it is difficult to say exactly how far along any particular path we are. In preparation for the Committee I asked my officials to produce some figures on Scottish credit unions and how they compared with credit unions in the rest of Great Britain. It might be helpful just to give some of figures. According to the information I have, there are 115 credit unions in Scotland with a combined membership of approximately 250,000. That represents 21% of the total of Great Britain credit unions, and about 40% of British Credit Union membership in Scotland. Scotland is a lot more active in terms of the number of people who are participating in credit unions than in the rest of Great Britain. The figures also suggest that there is round about £200 million in savings in credit unions in Scotland and about £150 million in loans, with a heavy concentration in the West of Scotland, as the Committee will be aware. There is a good track record of credit unions in Scotland. Right across Great Britain you might want to describe the credit union movement as being patchy. It is not represented in all communities and one of the agendas for us as a government is to see how we can

encourage credit unions to promote financial inclusion, because we do believe that they have an important role to play in that area.

Q184 Mr Davidson: If we have to go further down the road in developing credit unions, more government money will be necessary, will it not, to support them? Why do you think it is that there is more government money going to support the development of credit unions in England and Wales than is the case in Scotland at the moment? The budget there seems to have been cut. Is that your fault?

Ian Pearson: My understanding on funding is that at a UK level we have the Growth Fund and through that we have provided £80 million over two spending periods to increase the supply of affordable credit through credit unions and community development finance institutions. Scotland has other mechanisms as well, through the Scottish Investment Fund and the Third Sector Enterprise Fund. They are obviously not the responsibility of the UK Government, so I cannot comment on those.

Q185 Mr Davidson: There is a big pocket of money in England and Wales, £80 million or so which is spent on development of the credit unions. Under the Barnett equivalent of that, we would be expecting to see £10 million spent in the development of credit unions in Scotland. That is not the level that is being spent. Does that mean that the money is being siphoned away to something else?

Ian Pearson: The figure that I have today is that approximately 6% of Growth Fund loans, both by number and value, have been made in Scotland. You are right to say that is probably less than the share that would be expected either under Barnett consequentials, if something was devolved, or given the strength of the credit union movement in Scotland. The advice I get is that the process that takes place for Growth Fund money is that credit unions and CDFIs bid for Growth Fund money, and it is allocated on a contractual basis according to the capacity of institutions to deliver against value and performance targets which are set by the Government to ensure that it is money that is being lent to the genuinely financially excluded and that it supports sustainable growth for the sector. Of course the sector is already quite strong.

Q186 Chairman: Can we move on.

Ian Pearson: Could I just say in response that I think it is a point that it is legitimate to make, because there is some indication that Scottish credit unions have been less on the front foot in terms of applying for money from the Growth Fund and that is obviously something that the Committee will want to consider.

Q187 Mr Devine: I am a big supporter of credit unions. I am not convinced that we as a government are doing enough to promote them. We only have 1% of the population across the UK, slightly higher in Scotland and certainly higher in some parts of it. When I was a union official we tried to get, for

example, the Glasgow Health Board and all the health boards to write out to everybody and say, "You've worked in the Health Service. Here's a credit union. Would you like to join it?" I have not seen any examples of that from the Government. Is there any strategy like that, of writing to local authority workers, health workers and such like? The Association of British Credit Unions when they came to see us were a bit critical about the lack of support that they were getting. Out of interest, are you a member of a credit union?

Ian Pearson: I used to be but I am not now. My wife used to be involved in running one in the past. I am very familiar with the importance of credit unions to individual workplaces and also the need to look to modernise the legislation.

Q188 Mr Devine: Have you said to local authorities, have you said to health boards, have you said to companies, "Come in and meet with us"? The problem that you keep referring to about the economically excluded, at the end of the day credit unions become poor people's bank and they need to get away from that as an image.

Ian Pearson: I am certainly aware that through the work of the Financial Inclusion Taskforce work has been going on to encourage the development of credit unions, and obviously credit unions look to market themselves. If there is more information I can provide, perhaps I could write to the Committee and explain some more of the detail that is going on.¹

Q189 Mr Devine: That would be helpful. The Association of British Credit Unions told us in July that they were engaged in discussions with you over legislation to allow credit unions to offer more modern services: bank books, cheque books, and that sort of thing. Would you tell us how this is going?

Ian Pearson: We have been having a review of credit union legislation and we have had a number of regular meetings between ABCUL and others and officials. We had a consultation on proposals for legislative reform and that closed in the middle of October. The key things we are trying to do through reforming the legislation is to replace the common bond requirement for credit unions with a wider field of interest, a field of membership test, because we have had representation to us that the common bond is sometimes too restrictive. We also talked about reforming the requirements relating to membership qualifications and renaming common bonds, allowing credit unions to admit bodies corporate, unincorporated associations, or partnerships to membership, and we have had representations to do that and on allowing credit unions to offer interest on deposits as well, providing certain requirements are met. We have had a very positive response to the consultation. We intend to produce a summary of the responses shortly, and then I think we need to move on, in looking at the legislative reform and making sure that is drafted appropriately. I am very keen that we work closely with the credit union

movement to make sure that we get the Legislative Reform Order right and we will endeavour to do that.

Q190 Mr Devine: Is there any indication that there is an increasing use of credit unions? A group can join. In the past it used to be individuals. When you look, for example, at penetration levels in Ireland, they are at 7 or 8%, and we are sitting here at 1 or 2%. Are there any indications of growth?

Ian Pearson: Certainly allowing groups to join—that is why I talked about corporate bodies and unincorporated associations. That will cover the fact that groups might want to join credit unions en bloc. That is something that would be not permissible at the moment under the legislation, which is one of the reasons why we think it needs to be modernised. Of course one of the intentions behind getting a more modern framework is that we can potentially expand the number of individuals that have access to credit unions in the future, which is what we would like to see.

Q191 Mr McGovern: Minister, as I am sure you are aware, the membership of credit unions has increased significantly over the past six or seven years. Paradoxically, as the membership has increased, the number of credit unions has decreased, mainly due to mergers. Does the Government support the trend towards fewer credit unions but with larger memberships?

Ian Pearson: I think we want to see what is appropriate depending on local circumstances. In Scotland we do have some very big credit unions. The Glasgow Credit Union has a membership of 21,500, as I understand it. The Scot-West Credit Union has 21,000 members. In many cases bigger credit unions can offer a greater range of services to their members. There are also some economies of scale in terms of processing transactions, but it does not always have to be done by saying it has to be one big credit union. Certainly we have seen trends in the credit union movement for sharing back office functions, so you can still have small credit unions focused on a particular geographical area or a particular workplace but they might share some of the back office processing functions in order to operate efficiently—and of course credit unions want to operate efficiently just as other financial institutions do as well.

Q192 Mr McGovern: In my view, credit unions are usually started off by community groups and they then devolve from there. My colleague mentioned credit unions in some places being considered as poor people's banks. If the Government does have policies vis-à-vis credit unions, could you tell me how those policies would try to attract more affluent people into membership of credit unions?

Ian Pearson: I think you have mentioned a good point here. We see credit unions as important to our financial inclusion agenda. Through the Growth Fund, in particular, we have been seeking to bring new individuals into credit unions and to provide them with loans. I think it is right to say that from

¹ See Ev 47

28 January 2009 Ian Pearson MP

the long-term sustainability of the credit union movement we want to see them able to attract membership from a wider client base, including more affluent sections of society. That is why I think removing some of the restrictions on the common bond and modernising of the legislation is important, because it will allow credit unions to appeal to a broader membership base. I think that is an important thing for the future.

Q193 Mr Devine: There are four credit unions that cover my constituency. There is one that has a common bond for the whole of Lothian, one that has one for Blackburn and Livingstone, and Blackburn and Seafeld, and one that has a local government bond. Sometimes it is like ferrets fighting in a sack, quite frankly, when you have a conference with them. Has any thought been given to either a work-based or community-based structure?

Ian Pearson: Both options are clearly possible. At the moment we have credit unions with both those sorts of structures. I do not think it will be right for us as a government to dictate to credit unions what sort of structure would be appropriate. With modernising the legislation we want to set out a framework that has less restriction in terms of how credit unions can attract members. It is up to credit unions themselves to decide if they want to merge and combine, as some have done in the past, or if they want to maintain their own identity but to look to ways to collaborate, to get greater efficiencies. If they are going to appeal more to affluent sections of society, then they need to have the sort of products that those people are interested in. That makes me think that they want to combine in some sort of way and to find out the most appropriate arrangements to do that.

Q194 Chairman: If it is possible to cap the rate of interest charged by the credit unions, could a similar cap not be introduced across the finance market as a whole?

Ian Pearson: You have two “ifs” there. First, in terms of credit union interest rates my understanding is that the legislation we are considering will allow credit unions to offer a rate of interest. Currently they are not able to do so. I am not aware that we are planning to impose a cap on that.

Q195 Chairman: Credit unions are not allowed to charge more than 2% per month under the present legislation.

Ian Pearson: I am sorry, yes.

Q196 Chairman: Do you think that a similar cap can be introduced? The reason I am saying this is that banks and financial institutions are the major contributor towards poverty. Where people are caught up in the vicious circle of poverty, the banks are playing a role in this. Do you not think that a cap on the interest rates could be helpful?

Ian Pearson: I think we were talking at cross purposes. I was talking about the interest rate that could be given to savers and you were talking about the interest rate that would be charged on borrowers.

You are right to talk about the 2% per month figure. We think that is the right sort of range of figure that we should be talking about for credit unions. I think there is a live debate that we can have about borrowing rates which we started to get into at the start of this evidence session. I do not particularly want to be drawn into saying there should be a set limit. We need to consider how we can have lending at fair rates to individuals. Depending on an individual's circumstances, banks will make different decisions. I am not really here to talk about the situation with regard to bank lending but I am very happy to talk about credit unions.

Q197 Chairman: Could I have your personal view, then? An interest rate of 24% when the base rate is 1.5%, any bank and financial institution charging people more than 24% is unreasonable.

Ian Pearson: Obviously during these difficult economic times, but in any event, that is something the Government wants to look at closely and see what is fair on the part of consumers and what reflects the risk profiles that borrowers have. We will always keep these matters under review.

Mr Walker: For the record could I point out that if a bank is borrowing money at 2% and lending it out at 24%, its margin is 1,200%. It is making a 1,200% gross profit on the cost of its borrowing, so the figures are far worse than you are indicating.

Chairman: Thank you.

Q198 Mr McGovern: The Minister seems very reluctant to speak about banks. I do not know if the Minister has seen this, but the terms of reference of this inquiry are to examine the future of credit unions in Scotland, the problem of financial exclusion and financial literacy, and the issues of affordable lending of credit and debt, so why should we exclude banks from that when we are asking you questions?

Ian Pearson: It is up to the Committee themselves to decide their terms of reference.

Q199 Mr McGovern: They are the terms of reference that we have.

Ian Pearson: My reading of the terms of reference was that it is a new inquiry into the credit unions in Scotland and in the inquiry into credit unions in Scotland they would cover those areas, including affordable lending of credit unions and credit and debt. If you are saying that the Committee's inquiry is broader than that, okay, that is a matter for the Committee.

Mr McGovern: The Chairman has not ruled anybody out of order for asking you about banks.

Q200 Chairman: When will you be introducing the regulatory reform order on affordable credit?

Ian Pearson: As I indicated, we will shortly be producing our responses to the consultation and also draft legislation which we want to consult on as well. I would like to think we can do that in March. Obviously there is quite a lot of pressure on the time

28 January 2009 Ian Pearson MP

of Treasury officials at the moment, but I am keen that we can make progress in this and I would like to think we can do it in March.

Q201 Chairman: Will these measures mean that credit unions will operate more like banks, which might make it hard to justify the privileged access to public funding streams?

Ian Pearson: I do not see it making credit unions more like banks. I see that the Legislative Reform Order is making some welcome changes that the majority of credit unions have been asking us to do—as I suggested, to move to the field of interest rather than the way the common bond currently operates and to make some of the other changes I have mentioned that will help modernise the credit union legislation that we have at the moment. I think, overall, the credit union movement has welcomed what we are trying to do. The stage we have reached now is to say, “We understand what you are telling us you want to see happening, let’s put together a reform order that we think achieves what you want, let’s hear your final views about whether you think it does do that and let’s implement it.”

Q202 Mr Walker: Minister, can we quickly look at the lending profile of credit unions for a moment because I think this is quite interesting, to ascertain exactly what lending niche they will serve. At the end of the day, they are serving communities that are less prosperous than other communities traditionally served by banks. When it comes to lending money, how much would you see credit unions lending? Up to what sort of level? Money to buy a property? Money perhaps to take a loan out for a car? Are we talking tens of thousands, hundreds of thousands, maybe thousands, or below a thousand as the normal upper limit?

Ian Pearson: At the moment I think the average credit union loan is something in the region of about £500. That reflects the client group of your average credit union. If we are saying in the future that for the sustainability of the credit union movement we might want to attract more affluent individuals, the credit union movement might want to offer a broader range of services, and then you might expect that that figure would increase over a period of time. I do not think we are talking about dramatic change here but, again, I would want to see credit unions continue to be involved in projects like the Child Trust Fund that I have mentioned but in the Saving Gateway as well. With Saving Gateway people who fully invest in them over a period of time produce savings significantly in advance of the loan figure that I mentioned.

Q203 Mr Walker: I have a lot of sympathy with your view, because I think that one of the strengths of the credit union movement is that they are not going to be banks. I think the building societies have done well that have resisted the temptation to become

banks, although there have been some upsets there. What would you say would be the different mission of a credit union from that of a bank—the corporate mission? What would you say would be the difference in mission between the two?

Ian Pearson: I think credit unions are distinctive. They do play an important role in terms of the financial inclusion in many instances. There are credit unions that we all know of that have been set up on a workplace basis. A number of local authorities have credit unions, the Scottish Police Force has a big credit union because it has had that common bond tradition. They have distinct identities in a way that our big banks do not in that sort of sense of the word. I am sure they would argue that they have their own distinctive features. As such, credit unions do have a valuable role to play within the overall financial system.

Q204 Mr Walker: One of the attractions is that they serve local communities. They are owned by the local community, there is a sense of ownership. Will that place a limit, in a sense, upon how large a credit union should become or can become? In a sense, they start losing that distinctiveness if they get too big. If they are serving Jim’s constituency, that is great, but when does Jim start to get worried potentially? Is that when they are serving the whole of a county or the whole of Scotland? Do you see a natural limit in the size of credit unions?

Ian Pearson: I do not think it is right to talk about natural limits. I do think that you see some very, very different credit unions at the moment and they do come in some very different shapes and sizes. As a government I think we would like to see a vibrant credit union movement that is offering a range of services to its members that has a flexibility that has not been there in the past. Of course, credit unions are distinctive in the sense that unlike banks they are essential not-for-profit organisations and have a different ethos.

Q205 Mr Devine: To go back to a point I was making earlier on, I have never seen a television advert or a newspaper campaign or leaflets saying to people, “Go and join a credit union.” What do we spend on publicising the benefits of credit unions?

Ian Pearson: I do not have a figure of what the Government spends on that. I am not sure that it is the role of government to market individual credit unions.

Q206 Mr Devine: No, I am not talking about individual credit unions. I am talking about, “Here is the benefit of credit unions.”

Ian Pearson: I think you correctly make a point in saying, “Is there a role for government to do more for promoting the concept of credit unions?”—rather than individual credit unions. That is something that we could take away and think about what there is we should do there. I think there is a role for SLCU, the specifically Scottish credit union

28 January 2009 Ian Pearson MP

representative body, to promote credit unions as well. You are right to say that we share an interest here in promoting the fact that credit unions are an important part of our financial system and perhaps we ought to be doing more about it.

Q207 Mr Devine: I would suspect that a lot of people do not even know what a credit union is.

Ian Pearson: I am not aware of what polling has been done on that. There might well have been market research that has been done on the awareness of credit unions. I think you are right to highlight it as an issue.

Q208 Mr McGovern: Jim is referring specifically to advertising. You are saying that as far as you are aware we do not provide any support for advertising.

Ian Pearson: We do not see our role to market individual credit unions.

Q209 Mr McGovern: Obviously I listened to your answer, but do we provide any sort of financial support whatsoever to credit unions throughout the UK?

Ian Pearson: Certainly we have funded the development of credit unions. I mentioned the Growth Fund. In the way the Growth Fund operates, that is money going into credit unions and then they lend out to individuals, but that helps to support credit unions as well as achieving our public policy objectives. It has been the policy of this Government to support credit unions ever since we came to power, as you are aware. There is always a debate about whether we should do more, just as there is in lots of other areas as well.

Q210 Mr McGovern: Are you in a position to put your finger on what the financial support is at the moment?

Ian Pearson: I am not sure I have the numbers to hand. If the officials behind me cannot dig them out, then I will drop a note to you.²

Mr McGovern: Okay.

Q211 Mr Davidson: Minister, I was particularly glad that when you spoke recently you indicated that over the coming year one of your key priorities is going to be visiting the joint credit union and post office that is opening in Silverburn in my constituency. In addition to that visit, what do you think you could work for in terms of increasing the co-operation between the post office and the credit union? Both of them are very much community routed and oriented in a way that the evil and malignant banks are not always.

Ian Pearson: I would be very happy to pay a visit to a credit union in your constituency as part of a programme of visits. The Post Office are interested in Saving Gateway and being involved in offering Saving Gateway accounts, and we have been having

a number of discussions with them. I know that the Post Office have also been talking to credit unions. You are right to say that there are some similarities and there are some big differences as well, but there is scope to explore greater co-operation between the Post Office and credit unions.

Q212 Mr Davidson: This particular location in my constituency is the first example of a credit union taking over a sub post office and running it. If you do not have any more information today, maybe you would be able to let the Committee have a note of the ways in which the Department is seeking to build that link between the Post Office and the credit unions in order that it can be widely disseminated.³ Also in the context of your world tour to Silverburn and my constituency, one of the things your Department has been involved with is the Illegal Money Lending Project which is based in Glasgow. I wondered whether or not you would also be visiting that and whether or not you would be able, either now or in a note, to give us some information about the recent successes that the Department and that unit has had in putting illegal money lenders into gaol or having other actions taken against them.

Ian Pearson: You are right to say that one of the things we have been very keen on doing as a government is clamping down on illegal money lending. We have run pilots in Scotland, as you are aware, and also in Birmingham on this. There have been successes in terms of prosecutions. I am not sure whether I have the detailed information.

Q213 Mr Davidson: If your officials have failed to brief you properly for this eventuality, then possibly you could give us a note.

Ian Pearson: I did read it but I cannot find it.

Q214 Mr Davidson: All right. Maybe you could give us a note because I think the publicity is a considerable deterrent.

Ian Pearson: I can give some information that there have been 30 prosecutions in Glasgow and £200,000 in illegal debts written off. I am sure that is something that will be welcomed.

Q215 Mr Davidson: It would be helpful if we could get some further details about that. Also, I am not conscious of that having been adequately publicised and maybe you could let us know what actions have been taken to publicise the actions that have been taken against illegal money lenders.

Ian Pearson: I would be very happy to do that.⁴ I think the more that we can publicise the fact that these sorts of activities are not acceptable and that we are taking action, the better it is for the people who can find themselves in the unfortunate position of being preyed on by the those loan sharks.

² See Ev 47

³ See Ev 48

⁴ See Ev 48

28 January 2009 Ian Pearson MP

Mr Davidson: Some of these loan sharks are even worse than the banks which we now own!

Mr McGovern: Not many of them.

Q216 Chairman: Minister, could I thank you for your attendance this afternoon. Before I declare the meeting closed, would you like to say anything in conclusion, perhaps on an area which we have not covered during our questions?

Ian Pearson: There were a number of issues where I have indicated that I will write to the Committee with further information. We welcome the inquiry. At the outset you mentioned some very high interest rates being charged on loans. If this is information the Committee can make available as a result of its inquiry, we obviously will want to consider it.

Chairman: I will ask the Clerk of the Committee to send you the information which we have. Thank you very much.

Written evidence

Memorandum from the Scottish League of Credit Unions

INTRODUCTION

1. I would like to thank the Committee for allowing me this opportunity to present my views, thoughts, and considerations regarding the development of the credit union movement in Scotland. The content of this document reflects my thoughts as a 40 year plus advocate, practitioner and academic researcher of credit union governance in UK, Ireland, Canada, United States, and Eastern Europe and not solely as an Executive of the Scottish League of Credit Unions (SLCU). Throughout this document I draw on my experiences, my research material and that of collaborative work with my colleagues Professor Donal McKillop and Charles Ferguson (Goth, McKillop, & Ferguson. *Building better credit unions*¹ published in association with Joseph Rowntree Foundation by the Policy Press, 2006. McKillop, Hyndman & Goth *The Structure, Performance and Governance of Irish Credit Unions*, The Institute of Chartered Accountants Ireland, Dublin, 2007).

EXECUTIVE SUMMARY

2. From the outset it is necessary to clearly understand what is the function and nature of the credit union philosophy and ethos. The credit union is simply a financial cooperative that has historically developed to provide its owner-members with access to basic financial services in a manner that retains any surplus or profit for the benefit of its members and the community which it serves; credit unions are basically just an alternative form of corporate structure.

3. It would be fair to say that the viewing of credit unions as principally an instrument for addressing financial exclusion is unique to the GB. This very limited interpretation of their functions has severely restricted their natural development and inhibited them from becoming community-wide providers of basic financial services and significant contributors to social enterprise and community economic development; roles that credit unions throughout the world have very successfully undertaken.

4. Throughout Great Britain (Northern Ireland intentionally omitted) the majority of credit unions have neither the organizational structure nor the financial and non-financial capacities and resources to undertake their “perceived” function as providers of credit to primarily low income individuals. The financial and business risks are too high, severely jeopardizing the viability of the majority of credit unions.

5. Additionally, it would also be fair to say that outside of industrial credit unions, the public perception of this “close association” of credit unions with financial exclusion has resulted in their stigmatization and them being considered a “poor man’s bank”. This perception has been extremely detrimental to both the image of the credit union movement and its ability to financially capitalize and develop itself to a stage of self-sufficiency. This is a reality that becomes strikingly evident when GB credit unions are compared to their counterparts in other credit union jurisdictions; the credit union movement in Ireland for example started at the same time as in GB with the former presently achieving a 70% market penetration rate while in the latter the figure is closer to 2% with Scotland being approximately 5%. (Central/west Scotland represent 35%+ of GB membership). Challenges are often presented to say that the comparison of growth/penetration between GB and Ireland is not valid given a suggested difference in the availability of consumer credit between the two countries; however, Northern Ireland with a current 30% market penetration rate and a growth rate greater than that of the remainder of the UK may be more indicative.

6. Northern Ireland is a credit union environment that operates successfully with significantly reduced levels of government support but in contrast to the remainder of the UK its development and growth has been based on its appeal to a community-wide cross-section of the population, including affluent sections of society.

7. It is axiomatic to say that any micro financial intermediary can not lend money [loans] unless it can raise money [deposits] and the economically “financially excluded” generally do not have sufficient surplus funds to deposit thus severely restricting a credit union’s ability to adequately financially capitalize. Without adequate capitalization the credit union will not develop and will have an increased likelihood that it will eventually fail. Research has consistently shown that a community-wide focused credit union structure offers a significantly more viable long-term model.

8. Additionally it can be shown that the needs of the socially and financially excluded are best served not by credit unions concentrating exclusively on low-income communities—that simply circulates money among the poor and creates financial exclusion ghettos—but by mobilizing the monies of the “rich as well as the poor”.

¹ May be downloaded from the Joseph Rowntree Foundation Website
<http://www.jrf.org.uk/bookshop/eBooks/9781861348302.pdf>

9. The proposal to this committee is not to suggest a reduction or an increase in the Government's financial involvement with the Scottish credit union movement but rather a re-defining of its involvement and a re-allocation of its contributed resources based upon an alternative consideration of the primary and historic roles and purpose of the credit union concept, its financial and non-financial capabilities and capacities, its potential as a provider of basic financial services and, perhaps most importantly, its significant role as a participant in Scotland's social enterprise and both its urban and rural community economic development.

10. In concluding this executive summary I think that there are four pertinent considerations that are particularly germane to this committee's discussions:

- a. Credit union development that concentrates solely on serving the needs of the financially excluded is inherently weak. Development based on a cross-section of the population, including affluent sections of society, offers a more viable long-term model. Greater emphasis should be given to this by credit unions, trade associations and the government.
- b. Given the critical role of volunteer credit union boards, more investment must be made in training and professional development of the volunteers who serve on them.
- c. Government financial support, channeled through the trade associations, could be profitability utilized both to extend the range of training on offer and to subsidize its cost to the credit union.
- d. I would like to particularly draw the committee's attention to section 19 below regarding an analysis of Scottish credit unions that is currently underway by the Scottish credit union trade associations, Cooperative Development Scotland, and Communities Scotland.

BACKGROUND

11. In order to comply with the Committee's established word limits I have attached extracts from the UK credit union research . . . Goth, McKillop, & Ferguson, *Building better credit unions*, published in association with Joseph Rowntree Foundation by the Policy Press, 2006.

Community-wide focused credit unions

1. . . . *The success of the credit unions in NI is in part due to their being organizations inspired by the community for the community, and also recognizing from the outset that their long-term viability requires that they attract a cross-section of people from local communities, and not just those who are socially or financially excluded.*
2. *In GB, certain credit unions have fallen into the trap of over-focusing on low-income communities, thus creating the perception of credit unions as the poor man's bank and, in so doing, hindering the development of these credit unions, and, indeed, the movement as a whole in GB."*

Training and professional development

3. *The research highlighted that credit unions with an appropriately skilled and motivated manager/management team, and an appropriately skilled and motivated board of directors, significantly outperformed counterparty credit unions. It was evident from the research that many credit unions did not meet the World Council of Credit Unions (WOCCU) identified "job prerequisites". Areas of failure for both weak and strong credit unions were knowledge of risk management and effective management, familiarity with asset liability management and familiarity with marketing concepts. However, more worryingly, the research identified that many boards have a considerable numbers of directors with no "ability to read and interpret financial statements".*
4. . . . *If a credit union is located in a deprived area, stewardship may be provided by persons that do not have the required level of competence or experience. This may make it unattractive to potential members who have higher incomes, thereby restricting the credit union's potential for growth among the poorer sections of the community.*

Other considerations:

5. . . . *Another stumbling block may be the perception held by many that credit unions are "poor people's banks" (Jones 1999). This view may restrict the monies that circulate within them to the persons on low income.*
6. *Reifner (1997) argues that the circulation of money among the poor alone is not enough, as circulating the money of the poor within the poor community creates exclusion ghettos. Therefore, to be successful, credit unions need to mobilize the money of the rich as well. In fact, Reifner takes this view further by suggesting that financial cooperatives need to be integrated with larger financial networks to provide the best and reliable service.*

7. *Consistent with these views, Ryder (2002) argues that the long-term success of credit unions requires that they attract a wider cross-section of people from local communities, not just those who are socially or financially excluded.*

CAWT: COOPERATION AND WORKING TOGETHER

12. A group consisting of the various trade bodies representing Scotland Credit Unions.- ACE, NACUW, SLCU, UKCU, and ABCUL (ABCUL subsequently decided to withdraw from the group)

13. It was readily acknowledged by all the participants of the CAWT group that a full review of the current credit union movement in Scotland is urgently needed. In conjunction with Communities Scotland and Cooperative Development Scotland the following brief was drafted and has been submitted to Cooperative Development Scotland for funding:

14. The Brief: At the January 25th 2008 meeting of the CAWT group addressing the future development of the Scottish credit union movement the following three (3) strategic areas were identified as warranting clarity, structure, and definition:

- What is the long term strategic focus/objective/purpose of the Scottish credit union movement?
- The need for the Scottish credit union movement to “speak” with one voice
- The necessity for the development of enhanced operational and structural capacities of Scottish credit unions and the Scottish credit union movement (financial and business sustainability, and professional development—financial capitalization, education, training, etc.)

15. The CAWT recognizes the potential that a financially strong Scottish credit union movement can play in the areas of consumer finance and social and community development throughout Scotland. This claim is supported by the traditional influence that credit unions have repeatedly established, and are currently establishing, throughout the world, although at the present juncture in Scotland, and to a greater extent in Great Britain, growth, financial strength, and market penetration rates have dramatically lagged behind those experienced in other credit union jurisdictions. This latter reality might well be considered as being the underlying premise for this assessment initiative with its primary objective being the foundation of an appropriate process through which the traditional credit union attributes and qualities may be maximized throughout Scotland.

MANDATE

16. The independent consultant’s mandate is:

- a. To ascertain the interpretation, considerations and expectations of the various Scottish credit union trade associations (ACE, UKCU, NACUW, ABCUL, and SLCU), the appropriate departments and agencies of the Scottish Government through its Social Enterprise Team and Cooperative Development Scotland, and any other relevant Scottish credit union organization/group/body relating to the three (3) aforementioned strategic issues.
- b. To clearly identify areas of commonality and areas of variance within the Scottish credit union movement towards the development and implementation of the credit union ideals and philosophy in Scotland.
- c. To recommend/suggest how the Scottish credit union movement might maximize the benefits of the identified areas of commonality and agreement.
- d. To recommend/suggest how the Scottish credit union movement might harmonize identified areas of variance.
- e. To present a workshop of the assessment composite finding to the CAWT group.
- f. To prepare a written final report of the assessment findings along with recommendations and suggestions for presentation to the CAWT and the project sponsors.

REFERENCES

Jones, P. *Towards sustainable credit union development*, Research Paper, ABCUL 1999

Reifner, U. *New financial products for inclusive banking*, in J Rossiter, *Financial exclusion: Can mutuality fill the gap?* London: New Policy Institute and the UK Social Investment Forum pp16-21 (1997)

Ryder, N. *Credit Unions and financial exclusion: the odd couple*. Journal of Social Welfare and Family Law. Vol. 24 no4 pp 423-34 (2002)

May 2008

Memorandum from the Scotland Office

1. The Government welcomes the Scottish Affairs Committee's inquiry into credit unions, following on from their recent investigation into poverty in Scotland. We are pleased to have the opportunity to highlight work to support credit unions, and also our broader agenda in relation to financial inclusion and capability.

BACKGROUND ON CREDIT UNIONS

2. Credit Unions are mutual financial organisations providing savings, loans and other financial products to members. They are legally obliged to define a group of people who share a "common bond" from whom they can recruit their membership, and to whom they can provide services. This is often the workplace and/or the local community. Currently membership is only open to individuals, although this issue is being considered under the current review cooperative and credit union legislation, discussed below. Since 2002 Credit Unions in Great Britain have been registered and regulated by the Financial Services Authority.

3. The Government recognises that Credit Unions can provide a vital alternative to expensive forms of credit often used by people on low incomes, such as home credit, pawnbrokers, or far worse, illegal loan sharks.

4. As well as support for low-income families, the Government and credit unions realise the importance of attracting more affluent members of the community. Larger credit unions are offering an increasingly diverse product range, for example:

- 11 credit unions now offer transactional bank accounts, with more expected to follow in 2008. These accounts allow their members to access ATMs worldwide, and to make payments by direct debit and standing order. There is a small monthly charge for these accounts, but no penalty charges.
- Credit unions with the necessary IT to receive BACS payments are able to have DWP benefits, tax credits and child benefit paid into accounts.
- Credit unions are able to offer Child Trust Funds and Cash ISAs.
- A number of credit unions offer a range of insurance products through an arrangement with CUNA Mutual Group.

SCOTTISH CREDIT UNIONS

5. Out of the 355 credit unions registered under the Association of British Credit Unions Limited (ABCUL) there are 73 Scottish credit unions. Scotwest Credit Union Ltd and Glasgow Credit Union Ltd are the two largest credit unions registered with ABCUL, with Capital Credit Union Ltd coming 6th on the list.

Scotwest Credit Union Ltd—Members: 19,700:

Open to anyone who lives or works in the West of Scotland. Offers a range of financial services including savings accounts, personal loans, mortgages, HomeSecure loans and current accounts.

Glasgow Credit Union Ltd—Members: 18,302:

Established in 1989, open to anyone who lives or works within Glasgow or the 'G' postcode area. Offers savings, loans, mortgages, current accounts, insurance and much more.

Capital Credit Union Ltd—Members: 11,967:

Established in 1989, Capital now has a live or work Common Bond for Edinburgh, the Lothians and Scottish Borders. Capital offers excellent service in a friendly, member driven environment.

GROWTH FUND FOR CREDIT UNIONS

6. The Government has committed a total of £80 million over five years (2006-11) to a Growth Fund for credit unions and other third sector lenders. The Growth Fund provides credit unions with:

- Capital for making small-sum affordable loans (typically £400 or less) to financially excluded people
- Revenue support to meet the staff costs and overheads associated with this additional lending activity; and
- Further support for training and development.

7. In Scotland, the Growth Fund has provided support to five credit unions—1st Alliance (Ayrshire), Capital (Edinburgh), Dumbarton, Glasgow, and Western Isles—and one Community Development Finance Institution (Scotcash, Glasgow). Up to December 2007, 3,284 affordable loans, totaling almost £1.5 million, had been made to financially excluded people in Scotland through Growth Fund support.

8. To support the Growth Fund, in 2006 the Government increased the maximum interest rate that credit unions are permitted to charge, from 1% a month to 2% a month. This change has been vital to the success of the Fund, allowing new lending to low-income and higher-risk consumers, without requiring a minimum savings balance.

REVIEW OF COOPERATIVE AND CREDIT UNION LEGISLATION

9. The Treasury published Review of the GB cooperative and credit union legislation: a consultation in June 2007 to identify the need for updating what is essentially a consolidation of 19th Century legislation. The long-term aim of the review is to provide cooperatives and credit unions with an effective legal framework to enable them to continue their valuable social role.

10. Responses were received from over 200 individuals and organisations, and a summary was published in December 2007. Treasury are now working with key stakeholders, including trade bodies that represent credit unions in England, Wales and Scotland, to consider the key issues in more detail.

11. Some of the key issues for credit unions highlighted through the consultation were: Common Bond definition; restrictions on non-qualifying members; prohibition of corporate membership; ability to pay interest on savings; and electronic communications. It is thought that resolving these issues could help to attract more affluent members of communities, as well as enabling the use of credit unions by small community groups. This would be achieved by relaxing the common bond restrictions to allow more people and groups to join credit unions, and by allowing increased flexibility to offer a wider range of savings products that might appeal to more affluent members of the community.

FINANCIAL INCLUSION

12. In December 2007, the Government published *Financial inclusion: an action plan for 2008-11*², setting out how the Government will support financial inclusion activity over the next three years. Since 2005, the Government has invested £250 million through a Financial Inclusion Fund, including:

- Over £120 million to recruit, train, and support more than 450 new debt advisers, collectively advising more than 90,000 financially excluded and low-income customers;
- £80 million to establish a Growth Fund for third sector, “not-for-profit” lenders, as highlighted above.

13. The action plan announced a new £12 million financial inclusion Champions initiative, which will support dedicated financial inclusion teams in key local areas across Great Britain. Champions teams will be responsible for developing local action plans on financial inclusion, increasing access to and take-up of appropriate home contents insurance schemes for social housing tenants, and establishing new affordable credit provision through credit unions and other third sector lenders in priority areas.

14. The action plan also included an agreement from the chief executives of the major banks to support third sector credit, including establishing new third sector lending provision in 25 high priority areas identified by a Financial Inclusion Taskforce Working Group. 3 of these high priority areas are in Scotland—North Ayrshire, Dundee City and Inverclyde.

15. The action plan builds on the Government’s March 2007 document *Financial inclusion: the way forward*, setting out the Government’s strategy to ensure that everyone has access to appropriate financial services, enabling them to:

manage their money on a day-to-day basis, effectively, securely and confidently;

- plan for the future and cope with financial pressure, by managing their family finances to protect against short-term variations in income and expenditure, and to take advantage of longer-term opportunities; and
- deal effectively with financial distress, should unexpected events lead to serious financial difficulty.

16. In February 2005, the Government established a Financial Inclusion Taskforce comprising senior figures from the financial services industry, academia, the third sector, and consumer groups. The Taskforce, which has been extended to 2011, monitors and evaluates the Government’s financial inclusion initiatives. The Taskforce has a specific remit to monitor a goal, shared by Government and the banks, to halve the number of adults without access to a bank account, from a baseline of 2.8 million in 2002-03, and will make a final evaluation later this year.

² HM Treasury, December 2007

FINANCIAL CAPABILITY

17. The Government has an active role to play in meeting the financial capability challenge. The aim is to raise consumers' financial capability—the knowledge, skills and motivation to manage their finances—in order to achieve lasting long-term benefits for individuals, the financial services industry and the wider UK economy. The Government recognises that education is key to improving levels of financial capability, and there is an associated need to engage with young people.

18. In January 2007, the Government published its long term approach to financial capability, which set out aspirations for the next 10 to 20 years. These are:

- all adults have access to high quality generic financial advice;
- a planned programme of personal finance education; and
- a range of Government programmes focused on improving financial capability, particularly on the most vulnerable.

19. The Government will set out how it intends to deliver these aspirations in the Financial Capability Action Plan, to be published shortly. The Plan will include information on access to high-quality financial advice across the UK—impartial information and guidance on a range of money matters, which is personalised but does not recommend or sell products.

20. Otto Thoresen, CEO of Aegon UK, was commissioned by the Government to conduct a feasibility study into a national approach to generic financial advice. His report was published on 3 March 2008. The Government has already announced that it will take forward his central recommendation of a £12 million two year Pathfinder (large scale pilot) for a “Money Guidance” service. The Pathfinder will be delivered by the FSA, and jointly funded by the FSA and Government. The Financial Capability Action Plan will set out the steps for taking this forward, including a target date for the launch.

21. The forthcoming Action Plan will also provide information on boosting financial literacy in schools. It will explain how a £11.5 million package of support for personal finance education in English schools will be spent. Given education is devolved in Scotland, the Scottish Executive received an associated allocation of funds through the Barnett formula—it is for them to decide how these funds are spent. The Action Plan will provide information on how Scotland, Wales and Northern Ireland are taking forward financial literacy in schools. Scotland does not have a statutory curriculum, but financial education will be included as a cross-cutting theme in the Curriculum for Excellence, which will be implemented from 2008/09.

CONSUMER PROTECTION

22. The Government recently undertook a three-year review of consumer credit law, culminating in the Consumer Credit Act 2006. The Act introduces a stronger, more effective consumer credit licensing regime, and gives the Office of Fair Trading (OFT) increased powers to take action against unscrupulous lenders and unacceptable practices. Many key provisions have come into force, and the Act is due to be fully implemented by October 2008.

23. From 6 April 2008, OFT are now able to assess a company's ability to run its business in a fit manner in the future, as well as assessing past conduct, and to monitor the conduct of a licence holder on an ongoing basis. OFT will be targeting businesses that work in areas where there is high consumer detriment, such as the home credit market, subjecting these businesses to more in depth scrutiny.

TACKLING ILLEGAL LENDING

24. The Department of Business Enterprise and Regulatory Reform (BERR) are funding a project to tackle illegal lending and provide support to victims in every region of England, Scotland and Wales. The Scottish team based in Glasgow has been funded since 2004, and all projects will be funded by BERR until 2011.

25. The Illegal Money Lending Project includes additional financial inclusion objectives:

- to develop formal relationships and processes for referring victims/enquiries to local debt advisers, sources of legal affordable credit or other sources of support, and to record these referrals; and
- to develop an understanding of the victims' needs in the medium to long term and the interventions required for a sustained move away from illegal lending.

26. The Illegal Money Lending teams identify loan sharks and remove them from the community, but without access to affordable and legal alternative sources of credit it is hard for their victims to make a permanent transition towards financial inclusion. The credit union movement, supported by the Growth Fund, is striving to fill this gap by increasing its outreach to the most financially excluded.

27. BERR and DWP are collaborating on a number of mini pilots between the established loan shark teams and Growth Fund supported credit unions. The aim is to identify cost effective and easily replicable actions which can be taken up more widely by the credit union movement, and others active in frontline financial inclusion.

28. In Scotland, the Glasgow illegal money lending team and Scotcash are working in partnership with Growth Fund contractors in their area to trial intensive support and advice for illegal money lending victims, with a view to improving these borrowers' capacity to access and successfully manage affordable third sector loans.

May 2008

Memorandum from Rev Ian Galloway, Convener, Church & Society Council, Church of Scotland

(A) Executive Summary

The Church of Scotland's long-standing concern with the spiral of poverty and debt led to support for credit unions as part of a strategy to break the spiral. Joined-up policies from Governments are needed, looking at credit union development alongside regulation of credit (including an interest rate cap), financial education, advice provision and reform of the Social Fund. So, too are partnerships with existing credit unions, faith communities and others, to take the growth of credit unions to a "tipping point", and provide a real alternative to predatory lending.

(B) The Church's experience and View

1. Since 1996, the Church of Scotland's General Assembly has received a series of reports on the ways in which debt and poverty reinforce each other. In many cases, these reports have been sparked by the pastoral experience of ministers and elders, especially in Scotland's poorest parishes.

"Credit can function as a desperately needed sticking plaster over inadequate income, to cover major unexpected items. But it can also deepen the spiral of debt. The proliferation of adverts for "buy-out loans" (offering relief from creditors' pressures along with some cash in hand) shows the level of need, while the high costs and risk to home-owners in such tempting offers represent huge long-term problems." (General Assembly Report 2005)

2. These ongoing concerns led the Church to be part of the "Debt on our Doorstep" (DooD) campaign, whose main thrust is to call for concerted, "joined-up" action to tackle the vicious spiral of debt and poverty. The key campaign objectives are (a) to develop policy proposals and initiatives to help reduce and eradicate irresponsible and extortionate lending; (b) to campaign for reform and/or replacement of the Social Fund to ensure adequate access to grants and loans; (c) to promote credit unions and other community finance initiatives; (d) to promote socially responsible service provision by high street banks; and (e) to campaign for methods of debt recovery to become more equitable, just and effective by ensuring that adequate protection is available to people unable to repay their debts.

3. In Scotland, where the Church has co-ordinated the DooD campaign, it has been particularly important to emphasise, post-devolution, the need for joined-up action when the policy tools are spread across different administrations.

4. It is in this context that we welcome the Committee's inquiry into credit unions in Scotland, especially when that is viewed in the setting of concerns about affordable lending, credit and debt, and the problems of financial exclusion and financial literacy.

5. We have welcomed the substantial efforts by the previous Scottish Executive to promote credit unions. While this achieved, by 2006, a quadrupling of the number of people using credit unions, they remain a relatively small part of the credit market. For those who are members, they clearly provide a real alternative to the usury of exchange rates which continues to characterise the home credit market. However, too many people in difficulty either don't know of an available credit union or are unable/unwilling to access it; and some would argue that tighter regulation has made it even harder to establish small, local credit unions.

6. In 2005, a General Assembly report asked

"What is it that has inhibited their growth here, in contrast to Ireland (where the Catholic Church has had a significant role in their development)? Perhaps it is here—in stimulating and supporting credit unions—that the church can have a real impact, building on the concerns that led a minister in Dumfries many years ago to play a key role in the formation of the Savings Bank."

7. However, while the General Assembly has encouraged congregations to take the initiative in working with other groups to form local credit unions, especially in light of the Irish experience, the Church has not yet been able to devote the resources needed to work with local congregations on what can seem a daunting project to take on.

8. The 2005 report also urged the (then) Scottish Executive—not least in the interest of ensuring value for the money they put into credit union development—to make further investigation of this a priority, including consideration of other community-based solutions such as financial inclusion partnerships and community banking partnerships (building on successful initiatives such as that in Wester Hailes).

9. Last year, at a major conference on responsible credit held in Edinburgh, the Minister for Communities in the newly-formed Government said “The Scottish Government is determined to tackle the problems of debt which affect communities by continuing with effective established approaches such as money advice as well as developing new solutions”.

10. We would therefore hope that there is sufficient common ground to ensure that UK and Scottish Governments can work effectively together on this in the future. The effectiveness of that working will also depend on imaginative and bold thinking to put the credit union on the map for those who are most at risk from predatory lending.

11. The need for partnership working goes beyond Governments. Partnerships with financial institutions, existing credit unions, and with other interested voluntary sector bodies (including faith communities), are also needed. We would particularly emphasise here, as on the development of financial education packages, the crucial role of people with direct experience of the interwoven problems of poverty and debt, in ensuring that solutions are effectively tailored to their experience.

12. “Financial education” is rightly seen as a key way forward. Credit card terms and conditions are complex, often with subtle differences between apparently identical cards, yet straightforward information on them can be hard to come by; marginally different ways of calculating APR can make crucial differences to repayment costs. While economists broadly agree that APR is overall the best way of comparing different credit options, research shows very low levels of understanding of what APR means; the NCC found that almost 80% of home credit customers did not know what interest rate they were paying. Partly, this reflects the fact that it is the weekly repayment which crucially determines whether the credit can be afforded, not the interest rate (though obviously the two are interwoven).

13. It is a reminder that effective financial education cannot be about the financially literate telling those in poverty how to live on benefit. However, programmes developed by Learning Teaching Scotland through the Scottish Centre for Financial Education and others aim much more at building “financial capability”, ie the ability to make informed choices. Education is not a panacea for debt problems, especially where choices are restricted and people are powerless to change the terms they are offered; however, backed up by good, accessible money advice, and personal support, it could play a significant part.

14. It is from the experience of people living in poverty that we learn that flexibility (of access and repayment) is a key attraction of doorstep lenders. Finding ways of enabling credit unions (and the Social Fund) to offer that kind of flexibility without the pitfalls of crippling interest rates would help offer people attractive alternatives.

15. While the prospect of setting up a credit union remains a daunting one, there are also huge benefits to be gained in empowering people within their own communities. As Nancy McGillivray told the Committee in the preliminary evidence session of this inquiry earlier this year,

“I think the organic growth of credit unions is great because it starts small. My experience in Livingston is we started small. We started from a church in Livingston and the first collection netted £20. If someone had told me ten years ago that we would have given out £2 million in loans and be sitting in charge of £600,000, I would be frightened, and I think anyone would have been. We have grown with the credit union. We have grown to be able to offer more services to people and we want to be able to offer these services.”

16. We would also underline the point made in that session that credit unions are (already for some, and potentially for many more) part of the solution, but not the panacea for Scotland’s debt problems. A strategy for empowering people will also include development of financial education/literacy, and other ways of tackling irresponsible lending (including the Committee’s support for powers for the courts to re-open unfair credit agreements where interest rates are above a ceiling).

17. Following the responsible credit conference in Edinburgh last year (organised by Citizens Advice Scotland, DooD, and others), a call was issued by participants that

- “mainstream financial services must re-engage with low income households;
- irresponsible lending must be prevented;
- default charges must be fair and transparent;
- greater efforts must be made to stop illegal lending;
- the cost of credit must be transparent and fair, and harmful lending stopped;
- a comprehensive national debt advice service is required;
- regulation must be improved and enforcement strengthened;
- Government needs to join up its response.”

18. Those who are sometimes described as “casualties” of the expansion of credit are not people hit by an unpredictable freak of nature; their debt problems are in fact predictable—not on a personal basis but statistically, in a market where exceptionally low default rates are more likely to be taken as evidence of unduly cautious lending practice failing to exploit the market to the full.

19. This is not a matter of making an easy target of, for example, banking profits, but of genuine accountability for those whose success is built on the problems of others. Some of the major financial institutions have been taking very welcome steps to express their corporate responsibility in various projects, from financial education materials to community banking schemes. More of this needs to be done, especially in developing simple and straightforward credit products to meet the needs of low-income customers.

20. While the impact of the “credit crunch” is much discussed, in ways that challenge quite fundamentally the credit-based consumer growth of recent years, it remains those who are poorest who most need small sums of credit, who pay—by a long way—the most for it, and who feel the crunch hardest.

May 2008

Memorandum from the Association of British Credit Unions Limited

EXECUTIVE SUMMARY

1.1 The Association of British Credit Unions Ltd (ABCUL) welcomes the opportunity to make a submission to the Scottish Affairs Committee’s inquiry into Credit Unions in Scotland. ABCUL is the main trade association for credit unions in England, Scotland and Wales. ABCUL represents around 70% of the 513 credit unions throughout mainland Britain and ABCUL members serve approximately 85% of credit union members.

1.2 ABCUL is also the main trade association for credit unions in Scotland. Approximately two thirds of Scottish credit unions are members of ABCUL, and our members serve around 80% of Scottish credit union members.

1.3 The credit union movement is proportionately stronger in Scotland, with 22.6% of British credit unions based in Scotland. In 2005, there were 213,000 credit union members in Scotland, saving over £174 million and borrowing over £140 million.³

1.4 ABCUL, like its member credit unions, is an Industrial and Provident Society. It is a co-operative owned and controlled by its members. ABCUL is the only British or Scottish member of the World Council of Credit Unions, the worldwide apex body whose members represent 172,000,000 members of 46,000 Credit Unions in 97 countries.

1.5 Over the last decade, ABCUL has played a leading role in reforming and modernising the credit union movement in Scotland. As a result the credit union movement is now adopting models of development and offering a range of products which has dramatically improved the scale of many credit unions. Credit unions aim to provide inclusive financial services in the communities and/or workplaces they serve. As a result they offer much more affordable, short term credit and small scale savings products than many other financial services providers and do not aim to serve only the more profitable end of the market. As not-for-profit organisations they invest any surplus in reserves to strengthen the business, in developing services for members, or to pay a dividend on members’ savings.

1.6 Credit union membership has almost doubled since 2002 and British credit unions now serve over 600,000 adult members and 80,000 junior members.

1.7 ABCUL believes there is great potential for the continued growth of credit unions in Scotland. We believe credit unions can not only help engender a savings culture and provide affordable credit for the financially excluded, but that as thriving social enterprises offering a wide range of products and services, Scottish credit unions can offer a viable ethical option in the provision of financial services.

1.8 We would be very pleased to provide further information or clarification of any part of this submission and would welcome the opportunity to contribute oral evidence to this inquiry.

THE FUTURE FOR CREDIT UNIONS IN SCOTLAND

2.1 As at the end of 2007, there were 121 credit unions in Scotland. These range from the largest such as Capital, Glasgow and Scotwest (which began as local authority employee credit unions) to smaller community and volunteer based credit unions. Alongside the increase in the membership of credit unions, there has been a decrease in the number of credit unions primarily as a result of mergers. It is to be expected that this trend will continue in the coming years.

2.2 The previous Scottish Executive made £800,000 available from April 2006 to March 2008 in the Scottish Credit Union SGEI (Service of General Economic Interest) Fund. Credit unions could apply to this fund to help them develop and offer one or more of a suite of financial inclusion products, namely Flexible Credit based on ability to repay, Credit Union Savings Accounts, Credit Union Budgeting Accounts, and insurance. A total of 53 awards were made and this fund has now closed.⁴

³ Financial Services Authority 2006 Credit Union Statistics

⁴ <http://www.communitiesscotland.gov.uk/stellent/groups/public/documents/webpages/cs—015416.hcsp>

2.3 In their Budget of November 2007, the Scottish Government announced a Scottish Investment Fund of £30 million over three years “which will support enterprise in the third sector by investing in assets, business development and the skills of people working in the sector”.⁵ Details of the funding streams available through this fund are expected to be published in June 2008, and it is hoped that credit unions will be able to apply for support for their development as businesses. ABCUL feels that offering new products such as the Credit Union Current Account (CUCA) is a major step in the development of credit unions as viable, sustainable and thriving social enterprises, and we hope the Scottish Investment Fund will support this.

2.4 ABCUL is investigating the possibility of shared back office facilities for credit unions to help produce economies of scale, and we would welcome support for efforts to make this viable.

2.5 For the sector to continue to grow, it is important that Scottish credit unions attract members from across the social spectrum. While the provision of affordable credit and savings for the financially excluded remains a key part of the credit union ethos, we should seek to move away from the image of a “poor person’s bank”. Updated legislation and new competitive products and services will allow Scottish credit unions to grow, to better serve their members, and to be better placed to help tackle financial exclusion.

2.6 In December 2007, the UK Government published its proposals for a review of credit union and co-operative legislation following a major consultation process.⁶ ABCUL welcomes the Government’s acceptance of calls to liberalise the common bond to allow wider and more flexible membership for credit unions. We are also enthusiastic about the Government’s proposals to allow credit unions to admit corporate bodies to their membership and to pay interest on members’ deposits. We look forward to the Government legislating to implement these proposals at the earliest opportunity to put in place a legislative framework for the credit union sector which is fit for the 21st century.

2.7 When enacted, these legislative changes will create new opportunities for credit unions in Scotland. More flexible common bonds will better allow credit unions to attract and retain members, and corporate membership will allow credit unions the chance to provide financial services for community organisations, housing associations, local co-operatives, social enterprises and the like. Allowing the payment of interest on savings rather than just the annual dividend will allow credit unions to offer attractive rates to compete for the savings of more affluent members of the community who may at present prefer to save with a bank or building society. Expanding the membership to more affluent savers will not only grow the sector but will also better equip credit unions to serve the financially excluded.

2.8 ABCUL has this year launched Project DELTA, a Department for Work and Pensions (DWP) funded project to support Growth Fund credit unions to deliver the maximum benefit to people who are financially excluded. Many of these credit unions are new to capacity based lending, had little experience of targeting users of doorstep credit and will need help in changing. Our experience of introducing PEARLS into Britain suggests that many of these credit unions are capable of reform but may need help in identifying and implementing change. This project provides PEARLS as a tool to all growth fund credit unions to help direct and support their financial analysis. Project DELTA will link training to a process of organisational change and not simply a menu of training offered to growth fund credit unions.

2.9 ABCUL believes the legacy from Project DELTA will be one of higher standards and measures across the whole British and Scottish credit union movement. It is a further recognition by the Government that credit unions have now come of age and are a vital part of financial choice on our high streets. Project DELTA will bring a welcome cash injection into vital training development within the movement, improve the ability to measure success across peer groups of credit unions, embed a fresh approach to capacity based lending within credit unions and allow for specific support for the Growth Fund credit unions in terms of mentoring, measurement and training. Many of the resources ABCUL is developing for this project will be available to all credit unions, not just Growth Fund recipients.

2.10 Around the world, it is recognised that credit unions have made significant strides forward when they have been able to provide a fuller range of services, including banking services to their members. Some ABCUL credit unions now offer a wide range of products and services comparable with those offered by high street banks and building societies, such as ISAs, Child Trust Funds, mortgages and now the Credit Union Current Account (CUCA). ABCUL believes that extending the range of services available is

⁵ Scottish Budget Spending Review 2007, p100

⁶ HM Treasury, Review of the co-operative and credit union legislation in Great Britain: summary of responses to consultation, December 2007

a vital part of scaling up the sector and welcomes Government support for credit unions to develop and offer these services.

TACKLING FINANCIAL EXCLUSION—THE CREDIT UNION CURRENT ACCOUNT

3.1 One of the priorities for Government around financial inclusion is to reduce the number of people that are unbanked. 11% of Scots do not have a bank account. This figure can rise to 18% for those on a low income.⁷ That can mean a whole range of difficulties, including the ability to access employment, as many employers now require their employees to have a bank account. Also those without a bank account cannot take advantage of the discounts on basic utility bills without the ability to pay by Direct Debit or Standing Order, and cashing cheques can be extremely costly if you do not have a bank account. Therefore this creates a situation where the poor pay more.

3.2 In recent years, ABCUL and its members have invested over £2.5 million in the development of banking services for our credit unions. In November 2006, the Credit Union Current Account (CUCA) was launched. Nine ABCUL credit unions were involved in the development and launch of the CUCA. Four of these were in Scotland.

3.3 ABCUL believes the launch of the CUCA is a particularly important development for the credit union sector in Britain and Scotland because this product serves both as a means to bring banking services to financially excluded people and as a product which can help develop and grow credit unions as strong, viable, successful businesses.

3.4 The CUCA enables people to withdraw cash at any ATM machine in the LINK network, use direct debits and standing orders to pay regular household bills (thereby saving money) and use a VISA debit card to pay for goods in millions of retail outlets around the world. These features set the CUCA apart from other products aimed at the financially excluded, such as basic bank accounts or the Post Office Card Account.

3.5 Eighteen months on, 24 credit unions across Britain either offer or are working towards offering the CUCA. There are now over 10,000 CUCA customers across the country, many of whom did not previously have a bank account or access to full banking services. Our latest figures show the take-up rate of the CUCA is increasing rapidly as more credit unions offer it and the year 2 marketing plans of the founder credit unions take effect. In the first week of May 2008 alone, 786 new Credit Union Current Accounts were opened.

3.6 ABCUL would like to see the availability of the CUCA extended across the country. At present, half the population of Scotland is within the common bond of a credit union which offers the CUCA. We would like to see every person in Scotland with access to the CUCA. ABCUL recognises that in some areas such as Grampian and the Highlands and Islands, there are particular geographical obstacles to people accessing regular banking services. ABCUL believes the CUCA could help tackle this geographical financial exclusion.

3.7 The main barrier for credit unions who might wish to offer the CUCA is the high level of investment required at the start. As mentioned above, ABCUL and its members have invested over £2.5 million to launch this product. For a credit union to start offering the CUCA, they must spend (or raise from other sources) approximately £85,000 in entry costs, plus allow for a first year deficit of up to £35,000. In other words, it costs a credit union approximately £120,000 to start offering the CUCA.

3.8 Needless to say, it is projected within the business model that the CUCA will become a sustainable and profitable product for the credit union, but this up-front cost is understandably prohibitive for some.

3.9 ABCUL welcomed the recommendation of the Treasury Select Committee in 2006 that Government funding should be available for credit unions that wished to offer the CUCA. The Department for Work and Pensions has offered funding for this purpose to some credit unions through the Growth Fund. ABCUL would welcome the availability of further such funding to help cover the set-up costs of the CUCA whether from UK Government or other sources.

FINANCIAL LITERACY

4.1 Section 3(d) of the Credit Unions Act 1979 stipulates that one of the objects of a credit union is: “the training and education of the members in the wise use of money and in the management of their financial affairs.” Credit Unions are actively involved on a day to day basis in improving the financial literacy of their members even though in the majority of cases there is not a formal financial literacy policy, structured programme or specific responsible member of staff.

4.2 A lot of the work is on an informal basis and as such is not well documented.

Credit unions work on a day-to-day basis in improving financial literacy through induction of new members, leaflets and newsletters, education of volunteers, training for directors, links with debt counselling agencies, and the like. In many areas New Deal employees and credit unions are finding mutual benefits and opportunities in employment and training within the credit union.

⁷ Scottish Executive, Financial Inclusion Action Plan, 2005

4.3 ABCUL has produced member education leaflets which can be distributed by credit unions to their members, and around 1.5 million have already been distributed. However, ABCUL believes closer links with the likes of Citizens Advice Scotland and the Consumer Credit Counselling Service would further help credit unions to raise the levels of financial literacy among their members and would welcome this.

AFFORDABLE LENDING, CREDIT AND DEBT

5.1 In Scotland 37% of people have no savings and for many, credit is the only way they can budget for larger purchases.

5.2 Credit unions currently provide affordable credit to over 200,000 adults in Scotland, lending over £140 million in 2005.⁸ The demand for credit union loans generally peaks around Christmas. Research carried out by the Scottish Executive revealed that in Scottish credit unions, 58% of loans are for less than £1000.⁹

5.3 As of June 2006, the credit union statutory maximum interest rate is 2% per month on a reducing balance which works out at 26.8% APR. However, a high proportion of Scottish credit unions continue to lend at the previous limit of 1% per month on a reducing balance, or 12.7% APR.

5.4 As the Scottish Affairs Committee noted in its report on Poverty in Scotland, many doorstep lenders charge extremely high rates of interest and many of their customers are financially excluded. For example, a loan of £500 from Provident Personal Credit would be paid back at £15 per week for 56 weeks, making a total repayment of £840 (183.2% APR).¹⁰ A £500 loan from a credit union at 1% per month paid over 52 weeks would mean a total repayment of £531.07,¹¹ a massive saving of £308.93.

5.5 The first Community Development Finance Institution (CDFI) in Scotland, Scotcash, opened in Glasgow in January 2007. Setting up this CDFI required significant investment from Glasgow City Council, the Scottish Government and the DWP Growth Fund. Scotcash is intended as an alternative to doorstep lenders for those who wish to borrow relatively small amounts or who do not have access to mainstream lenders. The typical APR charged by Scotcash is 47.92%.¹² In their first 13 months of operation, 98 Scotcash customers have opened savings accounts with Glasgow Credit Union. Customers who do not have a bank account are encouraged to open a basic bank account with Royal Bank of Scotland.

5.6 In recent years, CDFIs have been supported by some on the back of criticisms of the failure of credit unions to achieve coverage and scale. ABCUL shared many of those frustrations with the prevalent approaches to credit union development in the 80's and 90's. However, it was ABCUL's view that the most effective way forward was to reform the credit union movement. We believe that the comparative progress over the last decade has shown that this strategy was a sound one.

5.7 ABCUL does not believe establishing CDFIs is the best or most cost-effective way to make affordable lending and credit available to the financially excluded. ABCUL believes a more "joined up" solution which includes the opportunity to save with the institution is key, as is regulation by the Financial Services Authority. Therefore, ABCUL believes that support for the existing credit union sector to offer loans to financially excluded members, such as through the Growth Fund, and for the development and provision of new products and services such as the Credit Union Current Account is the better approach.

5.8 ABCUL recognises that there is a need for some reforms in the credit union sector in terms of lending practice, including the use of credit reference agencies to ensure responsible lending.

5.9 ABCUL understands fully that the availability of affordable credit is not in itself the long term answer to financial inclusion. It is the ability to build small sum savings which provides the safety net which helps prevent people from falling into debt or poverty and the vehicle through which people lift themselves out of poverty.

5.10 In the last few years the move to direct payments of benefits has greatly increased the number people having their benefits paid into a credit union. There have been some interesting consequences, particularly around the level of benefit that credit unions have retained in savings. The credit unions that administer benefit payments on behalf of their members are reporting between 5% and 10% retention of benefits in savings.

5.11 ABCUL welcomes the UK Government's decision to move forward with the roll out of the Saving Gateway. This is a valuable initiative which will help to encourage low-income savers and we look forward to working with the Government to ensure that the scheme is a success. Credit unions, along with Citizens Advice Bureaux and social housing providers, have indicated that they would be willing to work with the Government to deliver information on the Saving Gateway scheme, including support with account opening.

⁸ Financial Services Authority 2006 Credit Union Statistics

⁹ Hayton K, Gray L and Stirling K (2005), Scottish Credit Unions, Meeting Member Demands and Needs, GEN Consulting, Scottish Executive Social Research, Edinburgh

¹⁰ <http://www.providentpersonalcredit.com/products/LoanCalculator.aspx>

¹¹ <http://www.abc.ul.coop/page/calculate.cfm#repayment>

¹² <http://www.scotcash.net/AffordableLoans/>

5.12 To help people become more confident in managing their finances and to reduce reliance on credit, it is vital that those on low incomes are able to save and build up their personal assets. The Saving Gateway aims to encourage savings among low-income households and to promote engagement with mainstream financial services. Credit unions are already trusted savings institutions in many low-income communities, so are ideally placed to play a significant role in promoting and providing Saving Gateway accounts.

CONCLUSION

6.1 ABCUL regards the future prospects of credit unions in Scotland with great optimism. The sector continues to grow rapidly with great opportunities for further growth. The imminent legislative reform will free up credit unions to target new memberships, and the provision of new services such as the CUCA are key to scaling up the credit union sector. ABCUL welcomes the support the Government has given to the development of the CUCA and would welcome further support to help more credit unions to offer the current account to more of the Scottish population.

6.2 ABCUL's vision is for Scottish credit unions to be successful and self-sustaining. Credit unions should therefore be seeking development capital rather than working capital. Funding to provide services like the CUCA allows a credit union not only to offer banking services to the financially excluded, but helps the credit union to grow and succeed as a thriving local social enterprise.

6.3 ABCUL would be happy to provide further information on any of the points in this submission which the committee may require.

May 2008

Memorandum from Ian Pearson MP, Economic Secretary, HM Treasury

Thank you for inviting me to give evidence to the Scottish Affairs Select Committee on 28 January. As I hope I made clear, the Government is keen to see a greater role for credit unions in serving both a wider range of members and specifically financially excluded customers. A number of initiatives are underway to help secure a vibrant and diverse future for the Credit Union sector.

When I gave evidence to the Committee I said that I would write to you to respond to some of the questions raised that I was not able to answer immediately. I apologise for the delay in supplying this information, but my officials have been in contact with a number of third parties to ensure that we have dealt with each point appropriately.

(i) Government investment in credit unions

The Government has in recent years provided credit unions with the following:

The Scottish Investment Fund (SIF)	£30 million
Third Sector Enterprise Fund	£12 million
Third Sector Credit Union Fund	£250,000

Total £42.25 million

The Growth Fund has provided £42 million (in Great Britain) for 2006–08 and a further £38 million is committed for 2008–11.

(ii) Credit union marketing

Individual credit unions generally have their own marketing budgets, which given the scale of the organisations is often very small. This Budget (and how) it is used is a matter for the Credit Union's management.

No specific Government funding is offered for publicity or promotional work.

The Government's recent "Now Lets Talk Money" financial awareness campaign did refer callers to credit unions where appropriate, but the Government has not funded any initiatives to promote credit unions as a concept to the general public.

It is worth noting that market research conducted in the sector shows that average awareness of credit unions in Scotland is greater than in other Growth Fund Regions.

(iii) *ATM access in Scotland*

HM Treasury issued a press notice (<http://hm-treasury.gov.uk/press—139—08.htm>) on 18 December 2008 which stated that in response to the ATM Working Group's recommendations to place around 600 free to use ATMs in low-income areas 72 new free ATMs were placed in Scotland, with a further 20 to be supplied within 6 months. These new ATMs are part of the nationwide "LINK" ATM network and are operated by banks, building societies and independent operators.

Banks and building societies currently pay a fee when machines operated by other companies are used to access their accounts. As part of the initiative to encourage the placement of free ATMs in low-income or rural areas a per transaction financial inclusion premium is paid to cash machine operators—offsetting increased average costs per transaction that may occur in low-use areas.

More broadly, there are currently about 38,000 free ATMs across the UK (11% of these in Scotland—versus approximately 8% of the UK population living in Scotland), which currently account for 96% of cash withdrawals. The remaining 4% of UK withdrawals are made at the 27,000 ATMs that levy a charge on users.

(iv) *Lending by high street banks*

We have no evidence to suggest that "High Street" banks charge interest rates (ie APRs) in excess of 100 per cent on personal unsecured loans.

However, if members of the Committee have evidence of such practices by banks, I would suggest that it is submitted to the consumer credit forum at BERR. Alternatively my office will be glad to pass on any information that the Committee wishes to share.

(v) *Credit unions and the Post Office*

There is currently no central agreement between credit unions and Post Office Limited to enable access to credit union accounts at the Post Office.

However, as some credit unions have an agreement with the Co-Operative Bank, in practice a significant number of credit union members can access their accounts at the Post Office. Additionally, the Association of British Credit Unions Limited (ABCUL) is in discussion with Post Office Limited on this subject. The Government is keen to see such co-operation furthered, but any decision must be taken by the respective parties on commercial grounds.

(vi) *Tackling illegal money lenders*

The press have been notified of work conducted in Scotland targeting illegal money lenders, and there have been a number of mentions in the Glasgow-area local press.

As recently as 25 January this year The Observer published an article about the work of the Scottish Illegal Money Lending Unit and noted how since Christmas it has received numerous referrals from the public across the country and particularly in the poorest areas of Glasgow.

(vii) *Credit union representation*

ABCUL have raised the point with my officials that references to the Scottish League of Credit Unions (the SLCU) as the 'specifically Scottish credit union body' by one of the committee members were misleading. The SLCU actually represents around 9% of the credit union movement in Scotland while ABCUL represents 85%.

I trust that this letter provides the information and clarification that the Committee expected. I will look forward to discussing this important topic with you and your colleagues again in the future.

February 2009

Example leaflet used by Scottish credit unions provided to the Committee on its visit to Lanarkshire

Mrs Rush

Dear Diary

I need to borrow £300 to pay for a new washing machine.

I've seen an advert for easy loans in the paper.

Week 1

I've borrowed £300 from Provident Personal Finance.¹³ The lady was very nice and I can repay it at £9 per week over 56 weeks.

Mrs Wise

Dear Diary

I need to borrow £300 to pay for a new carpet.

I've seen an advert for my local Credit Union.

Week 1

I've borrowed £300 from my local Credit Union. The lady was very nice and I want to repay it at £9 per week.

¹³ Info taken from Provident Personal Finance website 22/02/08

Week 10

I am not really missing the £9 per week I think I'll repay it alright.

Week 28

I'm just half way to paying it off.

Week 36

Another 20 weeks to go! I'm still able to cope with the repayments but it's dragging on too long. I wish it was paid off!

Week 56

Debt free at last.

The £9 was just about manageable but now I think I need to borrow more money for a carpet.

That cost me £204 in interest.

No wonder it took so long to repay.

Week 10

I am not really missing the £9 per week I think I'll repay it alright.

Week 28

I asked in the Credit Union and they tell me I've only got seven weeks left until I have paid it off!

Week 36

The loan was paid off last week. I've decided to keep paying £9 per week in the credit union to build up my savings.

Week 56

I've got more than £180 in my account!

I need a new washing machine. I may take out another loan with them.

That only cost me £12.50 in interest.

No wonder I paid it off so quickly.
