

Financial services provision and prevention of financial exclusion

United Kingdom stage 2 country report

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Country Report: UK

A Overview of the debate on financial exclusion and inclusion

Financial exclusion has been part of the Labour Government's policy agenda since its election in 1997, and public debate has largely been shaped by the government's priorities in this area. The debate is typified by a wide range of partnerships and widespread involvement of private sector companies (banks, building societies and insurance companies), public bodies (including national, regional and local authorities and public housing bodies) consumer groups, grass roots organisations, including not-for-profit providers of financial and advice services, charitable trusts (who have funded research) and academics (who have undertaken that research).

The first review of the problems of financial exclusion was commissioned by the Government, soon after it was elected. This was part of a wider investigation of social exclusion, which was undertaken by a number of policy action teams, one of which (Policy Action Team 14) considered access to financial services, under the sponsorship of HM Treasury (the Finance Ministry). The report focussed on access to banking, insurance and credit through credit unions and stimulated both debate and development by setting out a series of recommendations to promote financial inclusion (HM Treasury, 1999) (see section B2.1).

Following mixed progress in the areas highlighted by this review, in 2004 the Government published a document called *Promoting Financial Inclusion* which identified three key policy areas where further action was required: (i) access to banking; (ii) the provision of affordable credit; and (iii) the availability of face-to-face debt advice, reflecting the government's increasing concern about over-indebtedness and its links to financial exclusion (HM Treasury, 2004).

Government funding to support work in these areas is provided by a €170 million Financial Inclusion Fund (see section B2.1 below for further details). In 2005, the Government set up an independent Financial Inclusion Taskforce to monitor progress in relation to these key areas and to make recommendations on what more needed to be done. The remit of the Taskforce has recently been expanded to include savings and insurance (again see section B2.1 below). The Taskforce reports annually to ministers and statements on financial inclusion are included in the Chancellor's ¹ reports to Parliament.

In March 2007, the Government published *Financial Inclusion: The Way Forward*, which re-stated the Government's commitment to promoting financial inclusion and set out its plans for the period from 2008 to 2011 (HM Treasury, 2007). This included extending the life of the Taskforce and a commitment to allocate at least as

¹ The UK Finance Minister

much again to the Financial Inclusion Fund to allow it to be extended to 2011². It also announced that a cross-Government ministerial working group would be set up ‘to evaluate the policy options in the light of emerging evidence from new and ongoing initiatives.’ This is chaired by a Treasury minister and includes ministers from the Department for Work and Pensions, Department for Business, Enterprise & Regulatory Reform and the Ministry of Justice.

A.1 Nature of the debate

As banking is seen as the entry point to financial inclusion, it has been central to the debates from the outset. In particular, Government and the banks have a shared goal to halve the number of unbanked people. More recently consideration is being given to ensuring that people new to banking make effective use of their accounts.

But the current debate also encompasses consumer credit, insurance, savings, debt advice and financial capability. In relation to credit, the debate has mainly focused on the role that not-for-profit organisations (such as credit unions) can play in widening access to more affordable credit. The focus of debate on savings is the link between saving and asset-building, and the role of government initiatives such as the Saving Gateway and the Child Trust Fund in encouraging saving among low-income households. In the area of insurance, the main priority since 1998 has been ensuring access to affordable home contents insurance, while the debate on debt advice has centred on making advice more accessible to people who are financially excluded by increasing the availability of free-to-user advice. Finally, the role of financial capability in promoting financial inclusion is becoming an increasingly prominent aspect of the debate, with work in this area led by the financial services regulator, the Financial Services Authority.

It is important to note that the debate in the UK has shifted focus since 1997, from financial exclusion to promoting financial *inclusion*.

² The Chancellor’s annual Pre-Budget Report, published in October 2007, announced a Financial Inclusion Fund of £130 million (€185 million) for the next spending period (2008-11).

B Government response to financial inclusion

B.1 Government commitment to tackle financial exclusion

As we note above, developments in both policy and practice have largely been led by the Government since 1997. This has evolved from an initial investigation into the extent and nature of the problem of financial exclusion, to a long-term strategy for achieving financial inclusion. This has the support of the Prime Minister, is led by HM Treasury (the Finance Ministry) but involves cross-Government working at both Ministerial and official level.

B.2 Political framework and agenda regarding financial inclusion

B.2.1 Policy measures

Almost as soon as it came into office in 1997, the New Labour Government was committed to tackling financial exclusion as a part of its wider policy to tackle social exclusion and inequality. This led to the establishment of a series of independent Policy Action Teams, one of which specifically addressed the issue of access to financial services and was led by HM Treasury. Membership of Policy Action Team (PAT) 14 was broad, encompassing individuals from the commercial financial services sector, local government, consumer groups and academics (all participating as individuals rather than representing their employer) and was chaired by HM Treasury staff. It was informed by existing research on the extent and nature of financial exclusion (Kempson, 1994; Kempson, 1997; Kempson and Whyley 1998; Kempson and Whyley 1999a; Whyley, McCormick and Kempson, 1998). PAT 14 reported in 1999 (HM Treasury, 1999) and, among other things, recommended the introduction of a basic bank account across the banking sector. It provided a blueprint for the basic bank account and was very important in encouraging banks to develop the product. It also made recommendations on the provision of home contents insurance and the development of credit unions.

Following PAT 14, the Government set out its strategy to tackle financial exclusion in '*Promoting financial inclusion*', published alongside the 2004 Pre-Budget Report (HM Treasury, 2004). The report sets out a range of measures – in three priority areas – access to banking, access to affordable credit, and access to free face-to-face money advice for people who are financially excluded.

A Financial Inclusion Taskforce³ was set up in 2005 as part of this strategy to monitor progress against Government objectives in these areas across Britain. Membership of the Taskforce is broad, including members whose day jobs are in a

³ Note there is no comparable body for either Scotland or Northern Ireland

range of organisations including banks, insurance companies, not-for-profit lenders (eg credit unions), not-for-profit advice agencies that provide debt advice, consumer bodies, grass roots organisations and academic bodies. All members participate in a personal capacity and do not represent their employer. It is serviced by a small team of civil servants in HM Treasury but has an independent chairperson. The Taskforce has three sub-committees, looking at insurance, debt advice and credit through not-for-profit lenders. The Taskforce had an initial two-year budget of £3 million, much of which it has spent on research to improve knowledge of financial exclusion issues, including engagement with banking; problems of access to credit; a baseline survey of debt advice and barriers to the use of financial services. The Taskforce's budget will be increased in line with the life of the Taskforce (see below).

To implement its strategy, the Government also established a Financial Inclusion Fund of £120 million (€170 million) for the 2005-08 spending period to support the two of its priority areas: development of affordable credit and of debt advice for people who are financially excluded (see section B3.1 below). This was later widened, at the request of the Taskforce, to include finance for work to tackle the lack of demand for financial services among the excluded (again see 'Now let's talk money' campaign in section B 3.1 below). It should be noted that this fund covers the three countries in Britain (England, Wales and Northern Ireland) as work in this area is devolved to the administration in Northern Ireland who receive a separate financial allocation for this work

The third priority area, banking, has received no specific funding but is based on a shared goal with the banks to work together to halve the number of people with a bank account.

In March 2007, the Government published *Financial Inclusion: The Way Forward*, in which it re-stated the Government's commitment to promoting financial inclusion and set out its plans for the period from 2008 to 2011, which were confirmed in the 2007 Pre-Budget report (HM Treasury, 2007). This included extending the life of the Taskforce and a commitment to allocate a further £130 million (€180 million) to the Financial Inclusion Fund to allow it to be extended to 2011⁴. It widened the original three priority areas to include savings and insurance and incorporated tackling demand as a core objective. It also widened the remit on banking to include enabling people to make effective use of their bank accounts and ensuring accessibility to banking services. It was announced that a pilot scheme to tackle illegal lending would be rolled out to every region of the country. Finally, it included the announcement that a ministerial working group would be set up to develop a detailed action plan for the period 2008 to 2011.

Subsequently, it was announced that a new credit working group would be established comprising bankers and members of the Financial Inclusion Taskforce to explore ways that banks could provide greater support to stimulate development of third-sector lenders to ensure national coverage in areas of high financial exclusion.. This working party was established in May 2007 and must report to Government in October 2007. In the 2007 Pre-Budget Report the Government also announced that it

⁴ The Chancellor's annual Pre-Budget Report, published in October 2007, announced a Financial Inclusion Fund of £130 million (€185 million) for the next spending period (2008-11).

will be taking forward the pilot Saving Gateway – a matched savings scheme for people on low incomes (see section B3.1 below).

Financial Inclusion Action Plan (Scotland)

Although the Financial Inclusion Taskforce covers Scotland, the Scottish Executive (the devolved government in Scotland) produced their own Financial Inclusion Action Plan in 2005 as part of their approach to tackling poverty. On the whole this mirrors the objectives of the UK financial inclusion strategy. A Scottish Financial Inclusion Forum assists with the delivery of this action plan and meets annually. The Financial Inclusion Fund for Britain covers work in Scotland in all areas except debt advice; finance for this is provided to the Scottish Executive. There is, therefore, a separate financial inclusion fund for Scotland (£10 million - €14 million) (see below under Government as facilitator). Financial inclusion work is undertaken by a small team of civil servants in the Social Inclusion Division of the Scottish Executive.

Treasury Committee

The UK Parliament has select committees of politicians which shadow the work of Government departments. The Treasury Committee has been particularly active in the area of financial inclusion and in 2006 conducted its own inquiry into the subject – including assessing the effectiveness of the Financial Inclusion Taskforce. It has published a series of reports covering: credit, savings, advice and insurance (Treasury Committee 2006a), banking (Treasury Committee 2006b) and financial capability (Treasury Committee 2006c). In 2007 it published a report of a follow-up inquiry into shorter-term savings products (Treasury Committee 2007).

B.3 Government response

To ensure that policy is translated into practice the UK Government has acted as both facilitator and direct service provider, often in partnership with other organisations, including the private sector. It has not, on the whole, intervened with legislation.

B.3.1 Government intervention as facilitator

Government has acted as a facilitator in three distinct ways: by working with financial service providers to encourage their work on financial inclusion, by changing the way that welfare benefits and pensions are paid and by providing finance to support developments in the not-for-profit sector.

Working with financial services providers.

The main example of work in this area has been the promotion of access to banking through **basic bank accounts** following the report of PAT 14 in 1999. At that time, some, but by no means all, banks had developed basic bank accounts to meet the needs of people on low incomes. As transaction banking is free in Britain as long as an account is in credit, these accounts have been designed to avoid the charges incurred when an account goes into unauthorised overdraft. To stimulate wider availability of these accounts, the Chancellor (the UK's finance minister) issued an ultimatum that all the major banks should have a basic bank account by October 2002. All met the ultimatum. There were no sanctions for failing to comply, although banks

understood clearly that the Government would take further steps if they did not comply voluntarily.

At the same time the **Universal Bank** was established by the joint action of three partners: the Treasury, the Post Office and the banks. The Universal Bank has a number of components. First, all holders of a basic bank account with a major bank can use local post offices (which are often seen as more welcoming than banks by people who are excluded) for routine bank transactions such as withdrawals and cheque cashing, at no cost. Secondly, the Post Office itself developed the Post Office Card Account (POCA) – a stored value card into which welfare benefits and pensions can be paid by the State and withdrawn by beneficiaries, but which offers no other banking functionality. It therefore offers nothing that cannot be obtained by opening a basic bank account – and does little to promote financial inclusion. Banks were required to meet the cost of setting up the POCA. The current POCA contract comes to an end in 2010 and discussions are currently taking place on its successor. The third element of the Universal Bank is the arrangement between a small number of banks and the Post Office that *all* their current account-holders (not just those with basic bank accounts) can use local post offices for transaction banking.

In 2005, Government and banks agreed a **shared goal** of halving the number of people who lack a bank account, with each party agreeing steps it would take⁵. This is being monitored by the Taskforce and the most recent figures show that there has been a substantial fall in the numbers of unbanked (achieving 60 per cent of the goal to halve the numbers) and that the people most likely to have benefited are those who are most financially excluded: low-income households, lone parents, unemployed people and those living in social rented accommodation (Financial Inclusion Taskforce, 2007).

Other areas where the Government has played an active role in encouraging the involvement of the commercial sector, include the recent establishment of the **credit working group** to explore ways that banks could support the development of a national network of not-for-profit lenders and encouragement of insurance companies to develop affordable insurance service through **insure-with-rent schemes**.

Payment of welfare benefits and pensions into bank accounts

An important spur to account ownership amongst the unbanked was the Government's decision to pay all social welfare, benefits and state pensions in Britain direct to beneficiaries' accounts since Spring 2003. A parallel decision was made in Northern Ireland. This always had two motives: achieving financial inclusion and cost-saving for the Government.

Financial support for the not-for-profit sector

The original **Financial Inclusion Fund** of €170 million is supporting support the following initiatives to tackle financial exclusion in Britain:

- £45 million (€63 million) is allocated to support an increase in provision of face-to-face money advice for people who are financially excluded and is being administered by the Department for Business, Enterprise and Regulatory

⁵ It should be noted that this is the only area of work under the auspices of the Taskforce that covers Northern Ireland as well and Britain.

Reform (formerly the Department of Trade and Industry). Funding commenced in April 2006 and more than 500 new money advisers have been recruited and trained and these advisers have assisted more than 44,000 clients. Both monitoring and an evaluation of this scheme is in progress, with the report of the first stage having been published. This aspect of the Fund covers only England and Wales with a separate Fund existing for Scotland.

- £6 million (€8.5 million) was allocated to the Legal Services Commission to pilot mechanisms of money advice outreach aimed at those who do not normally present themselves to debt advisers. Twenty pilots, which employ 47 full-time equivalent advisers have assisted clients with 15,000 debt problems. Again this is being monitored and evaluated and the report of the first stage has been published. This, too, covers only England and Wales.
- £36 million (€50 million) is allocated to a Growth Fund to enhance the coverage, capacity and sustainability of not-for-profit lenders in Britain as a whole. This fund is being administered by the Department of Work and Pensions. Around 100 organisations have received funding through the Growth Fund so far. More than 33,000 loans, totaling £14 million (€20 million) were made in the first year of operation. Again this is being monitored.

Regular up-dates on the monitoring undertaken of the three strands of the Fund are reported by the Financial Inclusion Taskforce (Financial Inclusion Taskforce, 2007)

In addition money from the Fund has also been allocated to:

- capacity building of not-for-profit lenders.
- the ‘Now lets talk money’ campaign – initiated by the Financial Inclusion Taskforce– to promote the use of financial services by people who are excluded altogether or make little use of financial services. It is operated in partnership with intermediary organisations such as social landlords and grass roots organisations that work with people who are likely to be financially excluded with the aim of encouraging the take-up and effective use of bank accounts and increase awareness of sources of affordable credit.
- a scheme to enable third sector lenders to apply for repayment by deduction from welfare benefits where normal repayment arrangements have broken down.

All three of these cover the whole of Britain.

Scotland has its own financial inclusion fund of £10 million (€14 million) which was allocated to support the implementation of the Scottish financial inclusion action plan over the two financial years 2006/7 and 2007/8. This is in addition to existing funding from the Scottish Executive for money advice (£6 million - €8.5 million – per annum) and for credit unions (£1.1 million - €1.5 million). There is no comparable fund in Northern Ireland, although it should be noted that credit unions are far more widely available there.

Unlike England and Wales, all financial exclusion work is fully devolved to the Northern Ireland administration and a financial allocation for this work is made by the

UK Government. There is, however, no separate financial inclusion fund in Northern Ireland.

The other important government funding initiative has been its support for a pilot scheme, operated by local authorities, to identify and prosecute **illegal lenders** in two parts of the UK (Glasgow and Birmingham). An evaluation showed that this was an effective use of resources (Ellison et al, 2007) and it was announced in *Financial Inclusion: the way forward* in May 2007 that funding will be made available to roll the initiative out to all regions of the UK.

B.3.2 Government as direct provider

In addition to facilitating services operated by others, the UK Government has also set up initiatives of its own to tackle financial exclusion - two in the area of saving and one providing interest-free credit.

The **Saving Gateway** is a matched savings scheme targeted at people with low incomes – with the Government matching the savings made by participants. Two pilots have been conducted. In the first pilot accounts were available to adults of working age who received either social assistance or tax credits to supplement low wages. Participants were able to save up to £25 (€35) a month over period of 18 months, up to a maximum of £375 (€525). At the end of the 18 months the Government matched the maximum amount they had had in their account over that time, so participants received 1€ for every 1€ in their account. Money could be withdrawn at any time, but once taken out of the account, could not be paid back in. So if, for example, after 12 months someone had £300 in their account, which they had drawn out but then paid £25 a month for the remaining six months, the maximum they would receive in matched funding would be £300 (the maximum balance in their account over the 18 month period) even if they had paid the £300 they had withdrawn back into the account before the end of the 18 month saving period. This pilot was a great success but a second, larger pilot was mounted to test the effects of different match rates and permitted levels of saving. Accounts for the pilots were managed by a commercial bank – Halifax Bank of Scotland and the scheme promoted by local community organisations, who also offered financial advice on request. Both pilots have been fully evaluated (Kempson et al, 2005; Harvey et al, 2007). The 2007 Pre-Budget Report announced that the government is 'taking forward feasibility work into the system requirements to enable the [national] rollout of the Saving Gateway'. Further announcements will be made in the Chancellor's Budget, subject to the results of the feasibility work (HM Treasury, 2007b).

The second saving initiative, the **Child Trust Fund**, aims to tackle wealth inequality and encourage saving by parents and children. From April 2005, every child born in the UK since 1 September 2002 receives vouchers for £250 (€350) which can only be paid into a special Child Trust Fund. A further £250 will be paid when the child is aged seven. Children in low income families receive double these amounts. Parents and others can add money to their child's account, but no money can be withdrawn until the child is 18. There is no tax on any interest or capital gain.

The initial impact has been evaluated and a baseline survey of saving for and by children undertaken against which the impact of the CTF can be assessed (Kempson et al, 2006).

The **Social Fund** offers interest free loans to people claiming social assistance (Income Support, income-based Jobseekers Allowance or pensioners receiving the minimum income). Although it is seen as an important part of financial inclusion, its existence predates work in this area, having been set up in 1988. It is operated by the Department for Work and Pensions, which administers social assistance payments. There are no restrictions on how the money is spent by individuals, although there are controls on how much money an individual can borrow. Repayments are deducted from benefits before they are paid. Over one million loans are made each year.

The Social Fund has had a controversial history, and the scheme has been revised following criticisms. The effects of the changes have been evaluated and the scheme seems to be working far better. It is highly valued by those eligible for loans but demand far outstrips supply, despite a major injection of funds in 2005 (Collard and Kempson 2005; Kempson, Collard and Taylor, 2002; Whyley, Collard and Kempson, 2000). There are continuing discussions about reforming the Social Fund but no concrete proposals for doing so.

B.3.3 Government intervention as legislator

On the whole, the UK Government has decided to work in partnership with commercial financial service providers rather than legislate to ensure financial inclusion. It has, however, introduced a number of pieces of legislation which have an impact on financial inclusion.

Much of this has related to credit unions. The *Financial Services and Markets Act 2000* brought credit unions under full regulation by the Financial Services Authority (the main regulator) from 2002 and also means that deposits in credit unions are now protected by the Financial Services Compensation Scheme. The key provision (among others) of the *Regulatory Reform (Credit Unions) Order 2003* was to give greater flexibility on common bond requirements. And the *Credit Unions (maximum Interest Rate on Loans) Order 2006* increased the maximum interest that can be charged for a credit union loan from 1% per month to 2% on a reducing balance. Both orders were made under the *Credit Unions Act 1979*. At the time of writing, the Government was consulting on further amendments to credit union legislation.

The other key area of legislation with a bearing on financial inclusion is the *Consumer Credit Act 2005*, which is the first major revision to consumer credit legislation since 1974. The two key provisions from a financial inclusion perspective are:

- the widening of the definition of ‘extortionate credit’ to include terms and conditions not just price.
- bringing credit transactions under the remit of the Financial Ombudsman Service, rather than relying only on the courts to consider unfair agreements.

C Market responses to financial inclusion

Trade bodies and most financial service providers support the Government initiative to promote financial inclusion. This spans the commercial sector, including banks, building societies and insurance companies, many of whom have specialist staff with a responsibility for financial inclusion. It also includes many providers in the not-for-profit sector.

C.1 Banking industry

Banking industry commitment has, primarily, related to the provision of **transaction banking**. As we note above, some banks had already begun to offer basic bank accounts that could not be overdrawn prior to Government intervention. Since October 2002, 16 major banks have offered a basic bank account, with arrangements for post offices to undertake basic transactions on these accounts (withdrawals, deposits).

Few of these accounts, however, offer the ideal package of features: accounts that cannot be overdrawn, offer a debit card where transactions are checked before they are processed and where there is a small 'buffer zone' (about €15) that allows someone to withdraw money from an ATM without incurring a charge if the minimum amount that can be withdrawn is greater than the amount they have in their account.

Most basic bank accounts offer direct debits, but none currently offers a bill-payment facility that is more appropriate for people on low incomes (direct debits can result in default charges if there is insufficient money in the account). Two banks (Bank of Scotland and Woolwich) experimented with such bill-payment services and both involved regular weekly payments into a linked bill-payment account, from which bills were managed by the bank. A small fee was charged but this was much less than the cash savings for paying bills by direct debit. Neither scheme still exists.

As we have noted above, banks have agreed a shared goal with Government of halving the number of people without a bank account. When basic bank accounts were first introduced, there was widespread criticism of the extent to which banks promoted them or made them available when asked to do so by their customers. To tackle this problem, a commitment was given in the *Banking Code*⁶. The *Banking Code* is a voluntary code of practice that covers current accounts, personal loans, savings and credit cards and covers most of the prime lenders. It sets out standards of good practice, which are to be followed as a minimum by banks, building societies and other financial services providers that subscribe to it. It contains sections on responsible lending and dealing with people in financial difficulties. Compliance with

⁶ It should be noted that banking conduct of business is regulated by the Financial Services Authority but is derogated to the Banking Code.

the code is monitored continuously by the independent Banking Code Standards Board. The two main commitments in the 2005 edition of the Code are:

Paragraph 3.1. *“We will assess whether your needs are suited to a basic bank account (if we offer one) and if they are we will offer you this product”*; also, *“We will offer you a basic bank account if you specifically ask, and meet the qualifying conditions for one”*.

Paragraph, 3.2. *“Where we offer basic bank accounts, we will tell you if they can be used at the post office”*.

Furthermore, a clear definition of a basic bank account is provided in the Glossary: *“A basic bank account will normally have the following features:*

- *Employers can pay income directly into the account.*
- *The Government can pay pensions, tax credits and benefits directly into the account.*
- *Cheques and cash can be paid into the account.*
- *Bills can be paid by direct debit, by transferring money to another account or by payment to a linked account.*
- *Cash can be withdrawn at cash machines.*
- *There is no overdraft facility.*
- *The last penny in the account can be withdrawn”*.

Compliance with the Code is monitored by an independent body – the Banking Code Standards Board (BCSB). The BCSB has carried out four mystery shopping exercises to assess the extent to which banks are complying with the commitment in the Code. These have shown a steady improvement, with all banks now having adequate systems in place. Any failures of compliance are attributed to individuals in branches not to systemic failures.

Nevertheless, the current provisions are likely to be tightened further still in the 2008 edition of the Code, following the independent review of the Banking Code that is currently underway. This is likely to focus on the availability of basic bank accounts for people facing financial difficulty

Although most attention has been paid to transaction banking there are two initiatives in other areas of financial inclusion, both of which have already been discussed:

- the **Saving Gateway**, which was operated on a pro bono basis by Halifax Bank of Scotland, and
- the direct involvement of banks in the Credit Working Group set up by ministers through the Financial Inclusion Taskforce, to explore ways that banks can support not-for profit lenders. (This and current support for not-for-profit lenders is described in greater detail in section C4).

C.2 Insurance industry

For some years, UK insurance companies have had arrangements with local social housing providers to provide low-cost home contents insurance to tenants. These are

run as a partnership, with the housing provider effectively acting as a broker selling policies to their tenants and collecting repayments with rent. The commission they receive is either used directly to reduce premiums or to improve security of homes so that the insurance company reduces the premium in future years. This is a rare example of an initiative where everyone wins: insurance companies receive more business; tenants gain access to cheaper insurance that can be paid for weekly rather than in an annual premium, and local housing providers avoid empty properties resulting from tenants having to give up their homes following a burglary, or rent arrears as people struggle to replace stolen items (see Whyley, McCormick and Kempson, 1998).

These schemes were investigated by PAT 14 and, as a consequence, guidelines were issued to local authorities and other social landlords to encourage them to establish one if they had not already done so. The most recent figures show that around half did offer an insure-with-rent scheme (Kempson, 1999).

The Association of British Insurers (the trade body for insurers) has played an active role in promoting these schemes and has also undertaken research into unmet needs for research. It has played an active role in relation to the Financial Inclusion Taskforce, since the remit of the Taskforce was extended to cover insurance.

C.3 Other commercial providers

A range of other commercial providers have set up services to meet the needs of people on low incomes. All are run on a commercial basis and some are more benevolent than others.

Bill-payment

PayPoint is a national network of 16,000 payment collection terminals based in convenience stores, supermarkets, garages and newsagents where a range of household bills can be paid in cash, usually without charge (Collard, Kempson and Dominy 2003). People on low incomes often pay for fuel using pre-payment meters. They can make these pre-payments at either a post office or a PayPoint outlet.

Cheque cashing

There are an estimated 2,000 commercial cheque cashing outlets in Britain, operated by around 350 companies including specialist cheque cashers, pawnbrokers and home credit companies (Dominy and Kempson, 2003). Charges are typically around 7 per cent of the cheques value, plus a handling charge of £2, although this varies company to company.

Remittance services

Remittance services are available through a wide range of commercial providers in the UK, typically money transfer organisations such as Western Union or Travelex. Western Union typically charges about £14 for every £100 remitted, although charges vary in proportion to the amount remitted (the larger the sum, the lower the proportionate charge). There are also informal remittance services that are unregulated and therefore more risky. These include local foreign exchange agents

and finding someone who is prepared to travel with the cash and deliver it personally (Atkinson 2006).

Consumer credit

People who have low or insecure incomes, poor credit records or a history of bad debt find it difficult to access credit in the mainstream or prime credit market, mainly due to the credit scoring techniques used by mainstream lenders (Collard and Kempson, 2005).

There is a well-developed sub-prime credit market in the UK. At the upper end this comprises commercial companies that offer secured and unsecured loans to people with a history of bad debts or poor credit records. These companies largely resemble lenders in the prime credit market except that their charges are significantly higher to reflect the higher-risk borrowers they serve. Their terms and conditions may also be more punitive than lenders in the prime market (Kempson and Whyley, 1999b). Mintel (2002) estimate that the overall number of sub-prime consumers in the UK in 2001 was 3.2 million, and forecast this figure to increase to 3.65 million by 2005. This includes sub-prime mortgage lending as well as unsecured lending.

At the lower end of the sub-prime market there are commercial home credit companies (also known as licensed money lenders, doorstep lenders or weekly collected credit companies) that are largely used by people on low or insecure incomes to access unsecured cash loans. The UK home credit market is dominated by four companies, of which Provident Financial is the largest (Datamonitor 2004). Loans are typically for £500 or less, repayable over six to 12 months. Compared to the prime market costs are high, with APRs ranging from 100 to 400 per cent or more. There are, however, no extra charges if a borrower misses a payment or needs the loan rescheduled (Collard and Kempson, 2005; Jones, 2002; Rowlingson 1994). Despite the high cost, many people on low incomes prefer to borrow in this way because of the flexibility of repayments and the lack of default charges. It is estimated that between 2 and 2.5 million people borrow in this way. (Collard and Kempson, 2005; Whyley and Brooker 2004).

Pawnbrokers also operate at the lower end of the sub-prime market. They offer small cash loans secured on property or jewellery. There are two national companies in the UK with about 50 stores each, as well as many small local companies. The APR on a £100 loan works out between 70 to 200 per cent APR (Collard and Kempson 2003). A recent survey estimated that around 0.1 per cent of the population use pawnbrokers (Kempson 2002), but this is likely to be an underestimate. Extrapolating from information from the main UK trade association and research in the US produces an estimate of around three quarters of a million users in the UK (Collard and Kempson 2003).

Companies such as Cash Converters and Cash Generator offer 'sale and buy back'. Although not strictly a credit product, sale and buy back involves customers selling goods to the store for cash. The customer retains the right to buy the goods back within an agreed amount of time. As sale and buy back is not covered by the consumer credit legislation, companies do not have to advertise their APRs and there are large differences between the amounts paid by companies to purchase goods (Collard and Kempson 2005).

There are a growing number of companies that offer pay day loans, including specialist pay day lenders as well as pawnbrokers and cheque cashers, with an estimated 1,500 outlets. Customers write a cheque that is not cashed for up to 30 days, for which they receive the cash (less the fee). Charging structures vary widely across the industry – some charge only a percentage fee (typically between six and 12 per cent per £100), others combine percentage charges and fixed fees (typically between six and 12 per cent, with a fixed charge ranging from £1 to £2.50 per £100 cheque) (Dominy and Kempson, 2003).

As well as cash loans, there are commercial companies that offer credit tied to the purchase of goods. An estimated 14 million people in the UK use agency mail order catalogues (Competition Commission, 2004), but numbers have declined sharply over recent years. The market is dominated by a small number of large firms. The price of goods is significantly higher than on the high street. While goods are technically interest-free, if payments extend over 40 weeks or more, the APR is usually 28.8 per cent or more (Jones 2002). There are also rental purchase companies such as Brighthouse, which provide household goods and furniture on credit without the need for credit checks. The goods are relatively costly and, while the average APR is around 29 per cent, additional costs such as insurance and default charges may increase the overall cost considerably (Jones 2002).

Christmas savings (hamper) clubs

A number of companies offer Christmas savings clubs, collecting weekly payments from their customers throughout the year. Just before Christmas, customers receive either shopping vouchers or a hamper (basket) of food (Pomeroy, 2007).

No interest is paid on money ‘saved’. And until May 2007 there was no protection of the money deposited. The largest company went bankrupt just before Christmas 2006 and customers lost all their money. This resulted in a Government inquiry and an agreement that all deposits would be held in a separate, ring-fenced account (Pomeroy, 2007). In addition, some building societies (mutual savings and home loans banks) and credit unions now offer savings clubs that work in the same way as the hamper clubs except that people get interest on their savings and get the money in cash just before Christmas.

C.4 Not-for-profit sector

Two main networks of not-for-profit organisations are active in the area of financial inclusion: credit unions and community development finance institutions. They are seen as the main plank of Government policy for making affordable credit available to people on low incomes.

There are currently around 560 registered **credit unions** in Britain, with half a million members. Not all members are on low incomes. All credit unions offer savings and credit services, with borrowing facilities traditionally being linked to the regularity of saving and amounts saved. Members receive an annual dividend on their savings, the level of which is set annually by individual credit unions. Interest rates on loans are capped at two per cent a month on a reducing balance (equivalent to 25.4 per cent

APR). The average loan size in 2002 was £470 (Collard and Kempson 2005). The credit unions who have received financial support from the Financial Inclusion Growth Fund are using that finance to target people who are financially excluded and are making lending decisions based on people's ability to repay rather than on the amount they have saved

Some credit unions now offer transactional bank accounts, through a pilot initiative between ABCUL (the main credit union trade body) and the Co-operative Bank. The account offers an ATM card for cash withdrawals, a debit card and access to direct debits and standing orders to make payments. For the most part, these are credit unions that have also received support from the Financial Inclusion Growth Fund.

A small number of credit unions also offer other services, including instant access and debt buy-out loans, bill-payment services, insurance and Christmas savings clubs. For the most part, these are credit unions that have adopted (with support from Barclays Bank) the PEARLS system of financial management, with a view to attaining financial sustainability.

Like credit unions, **not-for-profit community development finance institutions** or CDFIs offer low-cost loans to people who find it difficult to access the prime credit market. Unlike credit unions, they do not link loans to savings – indeed most are not deposit takers.

Both networks have benefited from a major injection of Government funding, largely through the Financial Inclusion Fund. This finance has included loan capital to enable an expansion of lending to people on low incomes and investment in capacity building of organisations funded in this way. After many years of grant aid to this sector, there is now an emphasis on building organisations that are financially sustainable, covering their running costs from the services they offer.

As we note above, a Credit Working Group has been set up by the Government, as an off-shoot from the Financial Inclusion Taskforce, to look at ways of scaling this sector up so that every community with high levels of financial exclusion has access to a financially sustainable not-for-profit lender. The working group has commissioned a major piece of work to assess the abilities of existing credit unions and CDFIs to serve people who are financially excluded and to map this against areas of high financial exclusion. From this it is intended to identify areas that lack access to not-for-profit credit; areas where there is inadequate provision by a lender that lacks financial sustainability or the capacity to meet the needs of financially excluded people, and those where there are financially sustainable lenders already serving people who are financially excluded. When this is complete, meetings are planned with bankers to discuss how they can support future development of these lenders both in cash and in kind.

C.5 Commitment of other organisations

In addition to the organisations just described, the Post Office and social landlords have also played a role in tackling financial exclusion – in both cases in partnership with others.

Post Office

There are currently 14,300 post office branches around the UK, around 8,000 in rural and 6,500 in urban areas. The post office branch network has declined significantly over time, and this trend will continue with a reduction of 1,800 outlets planned for 2008. Even so, it will retain a much larger network of branches than the banks and will continue as the only provider of financial services in many excluded areas. Since 2003, all basic bank accounts can be used without charge through the Post Office network in the UK. Moreover, in response to the Treasury Committee inquiry into fee-charging ATMs, many post offices in remote rural and financially excluded areas now have an ATM offering free transactions. Many household bills can be paid at a local post office (although some creditors levy a charge for this) and it is also possible to buy savings stamps for some household bills such as TV licences and utility bills.

In 2003, the Post Office Card Account was set up to enable the electronic payment of welfare benefits and pensions to people who do not have or do not want to use a current account or a basic bank account. Welfare payments are credited to the POCA, and the claimant can then withdraw some or all of the money at a post office counter using a plastic card, without charge. Over 4 million POCAs have been opened – although a number of these people were previously financially excluded, they include a high proportion of pensioners who already had a bank account. The POCA contract with the Post Office will, however, be terminated from 2010 and it is almost certain that a new product or products will replace it. Experience with the POCA shows that there is a need for a card with more banking functions, including being able to pay other money into the account and also for a card-based savings account (as many people let child benefits, in particular, build up in their POCA account).

Social landlords

The insure-with-rent schemes run by social landlords have already been discussed (see section C2). In addition a small number of housing associations (not-for-profit providers of rented housing for people on low incomes) have experimented with savings and loans schemes. Typically an arrangement is made between the housing association and a building society with the housing association putting a large sum of money on deposit. Tenants' savings are then treated as if they are added to this sum – so they get a higher rate of interest. The money on deposit also acts as a guarantee for very low-cost loans (one schemes offers them at Bank of England base rate plus 1%). Such schemes are undertaken as part of corporate social responsibility and are not sustainable financially. Take-up has, however, been surprisingly low.

C.6 Partnerships

Partnerships run throughout most of the developments described above. Indeed they are seen as the best way of achieving financial inclusion as, in most instances, a commercial solution is not possible and needs outstrip Government subsidy.

At the strategic level, Government, commercial providers and the not-for-profit sector work together and all three sectors are represented on the Financial Inclusion

Taskforce. The ‘Now let’s talk money’ initiative, to tackle the low level of demand for financial services, is based on a partnership approach, as are the plans for increasing access to affordable credit.

There are also many examples of practical initiatives involving partnerships as described in the sections above. For example, banks have worked with government and the Post Office to reduce banking inclusion. Halifax Bank of Scotland acted as provider of the Saving Gateway. In addition banks often work in partnership with, or provide finance to, local not-for-profit bodies to enable them to tackle financial exclusion. Good examples would be the Bank of Scotland Wester Hailes Community Banking Partnership and the Community Banking Partnership pilots being set up in England.

Some banks have given considerable financial support to credit unions and CDFIs to allow them to extend their services. Barclays Bank has sponsored the introduction of PEARLS into credit unions to enable them to move towards financial sustainability, and has provided considerable financial support to individual CDFIs. The Co-operative Bank has supported the introduction and operation of basic banking services through credit unions.

Insurance companies have worked with local authorities and social landlords to provide affordable insure-with-rent schemes. While building societies have set up partnerships with housing associations to enable them to offer savings and loans clubs.

In addition, there are many local initiatives to tackle financial exclusion run by not-for-profit organizations (often with financial support from or in partnership with commercial banks). These are too numerous to list, but a good example would be SAFE (Services Against Financial Exclusion) run by Toynbee Hall in London. In addition, many local governments are involved in local initiative. Financial Inclusion Newcastle Ltd - run by the City Council is a good example.

D Evaluation of impact

Many of the initiatives described above have been evaluated and, where appropriate, this has been indicated in the text. It is, however, only possible to summarise some of the more successful initiatives. The Financial Inclusion Taskforce, in particular, plays an important role in monitoring and commissioning evaluations of key initiatives. Reports are made annually to Ministers summarising this work (see for example Financial Inclusion Taskforce, 2007) and reports of individual evaluations can be downloaded from the Taskforce website (www.financialinclusion-taskforce.org.uk).

It is clear that steps taken to halve the number of people without a bank account are bearing fruit. Between 2002/3 and 2005/6 (the latest figures available) there was a drop of 800,000 people living in 500,000 households who were completely unbanked – over 60 per cent of the target to halve the number of people without an account. Over the same time period, 1.6 million people gained access to a transaction bank account, with basic bank accounts playing a major role (Financial Inclusion Taskforce, 2007). The provision of basic banks alone would not have achieved this outcome. The inclusion of a commitment in the Banking Code to promote them and the extensive monitoring by the independent Banking Code Standards Board played a very important part. So, too, did the Government decision to pay all state benefits and pensions into bank accounts. The introduction of the Post Office Card Account (POCA), however, has almost certainly reduced the numbers of people brought into banking as some people chose to open a POCA rather than a bank account to receive their state benefit or pension payments.

Support for not-for-profit lenders from the Financial Inclusion Fund has greatly expanded the number of financially excluded people able to access affordable credit. Before this funding the numbers served were considerably lower (Financial Inclusion Taskforce, 2007). There is, however, some evidence that serving the needs of this new group of borrowers is challenging for these lenders.

The illegal lending pilots have, likewise, been shown to be highly effective at removing illegal lenders from financially excluded neighbourhoods. The evaluation does, however, conclude that more needs to be done to provide affordable credit in areas where illegal lending has been closed down. Knowledge of credit unions and CDFIs in these areas was poor and these not-for-profit lenders did not always have the capacity to provide credit to former customers of illegal lenders. Without this provision, there is a danger that the void will be filled by other illegal lenders. (Ellison, Collard and Forster, 2007)

The Saving Gateway has been shown to assist people on low incomes to save, with higher levels and greater regularity of saving compared with a control group. Moreover, participants retained the saving habit after the pilot had finished. Almost all of this was new saving (Kempson, McKay and Collard, 2005).

Finally, an evaluation of insure-with-rent schemes has demonstrated that they offer benefits to all three groups of participants: tenants, insurance companies and social landlords (Whyley, McCormick and Kempson, 1998).

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