

By: Keith Ferrin, Cabinet Member for Environment, Highways, and Waste

Roger Gough, Cabinet Member for Regeneration and Supporting Independence,

Adam Wilkinson, Managing Director of Environment & Regeneration

To: Cabinet - 14 January 2008

Subject: **The Case for establishing a Credit Union for Kent**

Classification: Unrestricted

Summary:

This report outlines an action plan to investigate the potential and develop a proposal to take forward establishment of a Kent credit union, further to an earlier paper that provided some background and research into credit unions both in Kent and elsewhere

For Information

1. What is financial exclusion.

1.1 Financial exclusion represents a significant social challenge: overcoming it is crucial to the County Council's aims, especially those of the Supporting Independence Programme. The financially excluded can be typically shown to share common characteristics such as lack of access to affordable credit, savings, insurance, access to a bank account, assets and access to financial advice.

1.2 There is now a large body of evidence linking financial exclusion to other forms of social exclusion which affect the most deprived neighbourhoods including unemployment, crime and poor levels of education and health.

1.3 Lack of access to even basic financial services can undermine peoples' efforts to take jobs or secure reasonably priced credit. Many people, particularly those living on low incomes, cannot access mainstream financial products such as bank accounts and low cost loans. One in twelve households (or around 2.8m adults - HM Treasury 2004) in the UK lacks access to a bank account. For these households costs of transactions, such as cashing cheques or paying bills are high.

1.4 Families can be locked in a cycle of poverty and exclusion, or turn to high cost credit or even illegal lenders, resulting in greater financial strain and unmanageable debt. There are 3m regular users of the alternative credit market including:

Home Credit or Doorstep lenders *E.g. a loan of £500 repaid at £25 a week over 31 weeks – total amount repaid is £775 at an APR of 365%*
Pawnbrokers - *APRs of around 70% and over*

Telebank - APRs of 40% and over

Buyback Stores - APRs in excess of 1,000%

Weekly Repayment Shops - Often more than double the cash cost

1.5 The impact of financial exclusion is tremendous. Citizens Advice Bureaux consumer credit and debt enquiries increased by 46% over the 5 years up to 2005. They are coping with more than a million cases of serious indebtedness each year – 1 in 45 adults (Guardian November 5 2005).

1.6 The case for creating credit unions is inextricably linked to addressing the problem of financial exclusion. Whilst credit unions are aimed at those on low to middle incomes and not exclusively at the poor, in practice in any given area where they operate they are the major provider to those on low incomes – i.e. a core proportion of their membership are the financially excluded.

2. What are Credit Unions?

2.1 Credit unions are co-operative mutual financial institutions. They are totally owned and controlled by their members through volunteer boards of directors. As such, if organised and managed to appropriate professional standards, credit unions have the potential to offer a much more efficient and cost-effective financial service to middle and low-income groups than either banks or other financial institutions. However it must be noted that the key to achieving a successful Credit Union is ensuring that volunteers and staff have the appropriate knowledge and expertise to effectively manage the complex financial requirements of a Credit Union. Credit Unions can offer the following to combat financial exclusion:

- Practical financial education and advice, particularly to vulnerable adults and children.
- Practical assistance to those on benefits by ensuring that priority payments are paid (e.g. Housing).
- Provide access to affordable credit and encouragement to save and build personal assets.
- Provide a bank account for the financially excluded to have wages paid into so that they don't lose out on job offers because of not having a bank account.

2.2 However, to be strong and thriving organisations credit unions need to offer services and to appeal to a wide range of consumers, not just the poorest in society. They need to be credible and earn their communities' confidence as providers of financial services and they must be run by experienced professional people. In order to ensure sustainability it is important to attract savers as well as borrowers.

2.3 Recent research and learning from successful credit unions overseas suggest the need for and the nature of a new model credit union. New model credit unions are characterised by a focus on financial viability, professional management and competitive financial services. Perhaps most important, new model credit unions have more open definitions of their common bond, making them more accessible to the general public who are interested in the financial services provided but not necessarily in the co-operative social and management aspects of old model credit unions.

2.4 Credit unions do NOT fund their loans by borrowing in the money market. Furthermore since 2002 all credit unions have been members of the Financial Services Compensation Scheme; and they have a statutory requirement to be insured against losses due to fraud or dishonest conduct by officers or staff.

2.5 Apart from banks and building societies, credit unions are the only other deposit taking institutions legally able to operate in Britain. They are organisations run not-for-profit, but for service.

2.6 It has always been assumed that Kent is not vulnerable to financial exclusion to the same level as other places. However in certain areas there are significant problems of debt and financial stress. Analysis has revealed a number of hot spots of financial stress in Kent; these are particularly centred around the towns of Ashford, Dover, Ramsgate and Margate. 2 small credit unions exist in Kent covering Canterbury and Thanet.

2.7 In addition the Government's Financial Inclusion Task Force have identified, in a recent report 3 areas of Kent (Dover, Swale and Gravesham) as 'amber' priority areas where financial exclusion must be tackled. Government support on this issue includes a 'Growth Fund' to assist in setting up of Credit Unions.

3. Building a successful credit union

3.1 ABCUL - the Association of British Credit Unions Ltd - takes an active role in supporting the establishment of Credit Unions through advice, regulation and training. ABCUL is the primary trade association for credit unions in Britain representing 85% of the members and assets of the British movement, through a democratic structure owned and controlled by credit unions themselves.

3.2 ABCUL has taken the lead role in setting standards for credit union development and in representing credit unions to Government, the Financial Services Authority and the public. Within the co-operative sector ABCUL represents credit unions on the United Kingdom Co-operative Council (UKCC) and is recognised as the only representative of British credit unions internationally by the World Council of Credit Unions (WOCCU).

3.3 In order to assist credit unions to develop into financial institutions that are able to serve a large membership and to offer a wider range of services, ABCUL has drawn up a set of pre-requisites that any new credit union needs to have in place before it begins operation.

3.4 It is now considered that for any credit union to have a high chance of success, it must have all, or nearly all, the following elements in place: -

- A **common bond** area that is large and diverse, is attractive to savers as well as borrowers
- a solid **business plan**, which targets growth, service to members and success.
- effective **leadership** of a volunteer board and committees, consisting of individuals who are well regarded in the community and have the skills, vision and experience to develop the credit union and make it grow. Learning from case studies has highlighted the importance of having highly skilled, trained and experienced individuals to effectively manage and drive forward the Credit Union.

- **support and sponsorship from respected local institutions**, to promote the credit union and give it credibility. (a key role for KCC)
- **initial funding** or in-kind support to provide the credit union with:
 - attractive premises, conveniently located to people in its community,
 - computerised accounting facilities and
 - trained experienced professional staff to operate the credit union.
- an effective **marketing and promotion programme** capable of attracting between 500 and 1000 members during the first few months of operation

3.5 None of the above elements compromises the basic commitment of credit unions to co-operative, mutual and social goals. However, wherever credit unions have grown significantly, they have all been established as professional financial institutions able to operate effectively within an increasingly competitive financial market place.

4. **Action Plan and timescales**

4.1 As agreed at previous cabinet discussions, a member level Steering Group has been established to be chaired by Roger Gough with the initial meeting in early January. An officer will support the work of the group. This Steering Group will provide the drive and direction to the feasibility and planning.

4.2 The Steering Group will oversee a plan that will consist of the following key steps with a view to launching the credit union in December 08. ABCUL can provide a package of advice and recommendations for groups to use in planning establishing a Credit Union.

4.3 It must be noted that developments will need to include discussions with the existing Credit Unions to ensure that they are involved with new developments.

- **Feasibility Study**

An external expert should be commissioned to carry out research in order to assess whether there is sufficient funding, support and resources to set up a sustainable credit union. In particular to show where the considerable funding needed to underpin the budget for 3-4 years will come from (this can be £300 - £500,000 in total) It will be important to investigate whether there is sufficient demand and potential usage to support a Credit Union and which areas should be considered for initial pilots. The report will also consider how to best to develop further links with Kent's existing credit unions so as to add value and avoid duplication. Initial scoping work and contacts have been made to feed into this stage of the report. Indications have already been received from potential partners interesting in working with KCC on this initiative.

- **Appointment of Credit Union Development Manager.**

The project will need someone to drive it forward, it is essential that the appointed manager possesses the relevant financial skills and experience to drive the complex financial management needed to ensure that the Credit Union is run efficiently.

Early research has highlighted the importance that trained and experienced individuals are appointed to manage a Credit Union and that the volunteers also have relevant skills base, backed up with relevant training. During this process the Steering Group will work with the manager to fully plan the project as a sustainable not for profit enterprise by identifying funding streams. This phase will produce a detailed business plan based on the results of the feasibility study. At this stage it would be necessary to begin to engage local communities and key local partners as their support will be vital to ensure that the Credit Union can reach its target market.

- **Initial Set Up.**

This phase will put in place key rules and procedures and processes of operation including appropriate governance structures. This will include preparing to meet regulations, which are part of FSA application process. Through this phase Directors of the board and volunteers will be engaged and begin undertaking the appropriate training.

- **The Application Process**

Final details of all aspects of the application pack are agreed before submitting the application to the FSA. There are 2 parts to the application; Part A has forms about the credit union (including registration details, business plan, systems and control policies and procedures) and Form B has forms about the officers and staff who will be running it. A period of up to 6 months can elapse while the FSA examines and decides on the credit union's application. On-going issues and activities for the volunteers and staff must be considered until formal authorisation. This time will be used to continue to raise awareness in the community and to allow volunteers and staff to complete their training and to fully prepare for the launch

- **Initial Operating Phase.**

The first few months after authorisation sees the official launch of the credit union, all the systems and controls being bedded in and the implementation of the plans to achieve agreed targets. Best practice and experience by financial institutions generally shows that Credit Unions should be allowed to grow steadily over time.

4.3 The timescales and milestones are expected to be as follows, however the feasibility study and business planning process is expected to provide updated milestones:

Feasibility study completed	end April 08
Credit Union development manager appointed and full business plan developed	end June 08
FSA Application Pack completed	end June 08
Authorisation (can take up to 6 months)	end Nov 08
Launch credit union (phase 1 area)	December 08

5. Costs

5.1 The costs of starting up a credit union and running a sustainable organisation will be drawn up and presented within the Feasibility Study as a set of 5-year financial projections. The model will include an assessment of the resource needs of a County-wide credit union, eg. Offices, Sub offices, collection points, staff, premises, security, training, volunteers, IT solutions, office set up and other start up costs.

5.2 It is estimated based on initial research and case studies that approximately £500k is required for a 3-4 year operation period.

6. Recommendations

6.1 A feasibility study be commissioned to provide full detail including key elements, based on guidance from ABCUL.

6.2 The key outputs would be:

- ❑ An assessment of the options for COMMON BONDS within Kent with appropriate recommendations.
- ❑ An assessment of the STAFFING AND RESOURCE implications of the proposed options.
- ❑ FINANCIAL PROJECTIONS drawn up, based on the above, that can be used as a basis for aiding the decision-making for credit union development in the area
- ❑ Production of a written REPORT which will assist any subsequent development of a REGULATORY BUSINESS PLAN needed for authorisation by the FSA.

Based on initial discussions the feasibility study could be expected to cost approximately £20K.

6.3 Following the feasibility stage, production of a full regulatory business plan would require appointment of key, experienced staff to drive this process, therefore the appointment of a Credit Union Development Manager could be expected to cost approximately £50K for one year.

6.4 Support staff and operation budget to fund to full business planning completion would be estimated at £30K. This would be expected to include recruitment costs, professional / regulatory fees, advertising and promotion and initial volunteer and staff training costs.

6.5 It should be noted that this level of finance would provide only initial feasibility and business planning and that the full costs to set up a Credit Union for Kent are expected to be in the region of £500K consideration would need to be given as part of feasibility and planning to how these funds will be raised to ensure the Credit Union will have sufficient initial capital to ensure future sustainability.

6.6 It is recommended that cabinet allocate £100K for a full feasibility study to be commissioned, under the guidance of the cabinet members steering group, and to allow development of a complete and full business plan for the establishment of a Credit Union for Kent via the appointment of a Credit Union Development Manager and supporting staff for one year.

Contact Officers
Caroline Toher/Emily Haswell
Tel: 01622 221996/01622 696895