From:	Paul Carter, Leader of the Council David Cockburn, Corporate Director of Business Strategy & Support
To:	Policy & Resources Cabinet Committee - 6 December 2013
Decision No:	Not applicable
Subject:	High-cost short-term credit providers
Classification:	Unrestricted

Summary: This report sets out for Members the current position around high-cost short-term credit providers, the proposed national changes in regulation, and action already underway in Kent, and outlines some possible areas for action that the County Council may want to explore further.

Recommendation

The Cabinet Committee is asked to advise on whether further work should be undertaken in the light of the issues set out in this paper

1. Introduction

1.1 "Payday lending" continues to be an issue that has had a high media profile for some time; recently even the Archbishop of Canterbury added his voice to those advocating the need to curb the more irresponsible practices and find lower cost alternatives for people who are struggling to make ends meet. There has been widespread publicity around action taken by a number of councils including restricting access to the websites of such companies, preventing advertising, and preventing them opening new shops on the high street. At the September County Council, Mrs Dean asked a question suggesting that Policy & Resources Cabinet Committee should explore whether there is action that Kent County Council should take to "limit the activities of so-called payday loan companies".

1.2 Elsewhere on the Committee's agenda today is a report providing an update on the impact of welfare reforms in Kent which provides some evidence that poverty and financial exclusion is still growing, although there are also now signs that the economy is picking up and unemployment is falling in Kent. The Kent Child Poverty Strategy highlighted that costs were rising faster than wages; over half of children in poverty have at least one parent in work; and that debt management (or avoidance) was a key issue for low income families. In this context, there is sometimes a need for people to borrow relatively small amounts of money (under £1,000) for a short period in order to cope with a particular event or crisis. The expression "payday loan" is commonly used, but this refers to a specific practice of paying back when a borrower is next paid (or receives their benefits). In this report the term "high-cost short-term credit" is used as this is the preferred nomenclature of the Financial Conduct Authority because in practice borrowers are able to borrow for shorter or longer periods. Also, lenders are increasingly developing more longer-term high-cost products that are repaid over several months.

2. Background and National Policy Context

2.1 High-cost short-term credit providers provide short-term loans to people who need instant-access funds. According to work done by Europe Economics, the sector was worth an estimated £2.0 to £2.2 billion in 2011/2012, up from an estimated £900m in 2008-9, so has grown very substantially in a short time. Nationally, there are many licensed payday lenders but the largest three companies represent around 70% of the market (by turnover). The average amount borrowed is £265-270 over a 30 day period. These loans are usually accompanied by high interest rates and the opportunity for borrowers to extend their loan beyond the initially agreed period. There is currently no restriction on the Annual Percentage Rate charged by the loan companies; companies just have to clearly state what they charge. Equally, there is no cap on the total cost of credit charged.

2.2 It has been clear for some time, however, that the market is not working well for many people, and that the guidance and voluntary agreements that the Government and the Office of Fair Trading (OFT) tried to put in place are not being fully implemented by the sector. The OFT conducted a compliance review of payday lending and published a report in March 2013 that showed:

- Around a third of loans are repaid late or not repaid at all
- 28% of loans are rolled over or re-financed at least once, providing 50% of lenders' revenues
- 19% of revenue comes from the 5% of loans which are rolled over or re-financed four or more times
- Debt advisers reported that borrowers seeking help with payday lending debts had on average rolled over at least four times and had six separate payday loans
- 30 of the 50 websites the OFT looked at emphasised speed and simplicity over cost – in some cases making claims that, if true, would amount to irresponsible lending
- 38 of 50 lenders OFT inspected failed to comply with at least one of the complaint handling rules of the Financial Ombudsman Service

2.3 The OFT found evidence of poor compliance with the law and guidance across the market and throughout the lifecycle of payday loans from advertising of loans to debt collection. They found:

- Lenders competed by emphasising speed and easy access to loans, but borrowers were not getting a balanced picture of the costs and risks of taking out a payday loan;
- The majority of lenders were not conducting adequate affordability assessments, and their revenue streams relied heavily on rolling over or re-financing loans;
- Many lenders were not treating borrowers in financial difficulties with understanding and forbearance. Many were promoting rollovers when borrowers would be better served by a repayment plan, and a number were using aggressive debt collection practices;
- Continuous payment authorities (where borrowers give lenders permission to take repayments directly from their credit or debit accounts) were poorly explained to consumers, and as result some people were ending up with insufficient funds to live on.

2.4 The OFT concluded that irresponsible lending was not a problem confined to a few rogue traders, but had its roots in the way that competition works in this market. Many consumers are in a weak bargaining position and firms compete on speed of approval rather than on price. (Annex 1 provides some typical case studies that illustrate the sorts of problems people are facing.) OFT immediately began considerable enforcement activity, including formal investigations against a number of payday firms. It also referred the payday lending market to the Competition Commission. The Commission is currently taking evidence and intending to produce its final report by the end of 2014.

2.5 Another significant change nationally is that the Government has tasked the Financial Conduct Authority (FCA) to assume responsibility for consumer credit regulation in April 2014 in order to be more stringent about how firms are supervised. From April, each high-cost short-term credit company will need to apply to the FCA for its licence to operate. In preparation for this, a consultation paper into detailed proposals for the FCA regime for consumer credit was launched in October. This report built on the OFT findings, and the research from Europe Economics.

2.6 The consultation paper recognises that there is a place for high-cost short-term credit, but that too many consumers are currently getting loans that they can never afford to repay. The FCA has developed (and is consulting on) a set of interventions aimed at ensuring lenders pay more attention to responsible lending. There are two key aims:

- To ensure that firms only lend to borrowers that can afford it, and
- To increase borrowers' awareness of the costs and risks of unaffordable borrowing, and ways to get help if they have financial difficulties

2.7 The specific proposals are:

- The FCA should enforce implementation of the OFT affordability guidance (the guidance is good, but too few firms currently implement it)
- Cap the number of times loans can be rolled over to two
- Introduce a limit of two unsuccessful attempts on the use of 'continuous payment authorities' (ie permission to take money directly from a person's credit or debit account) to pay off a loan, and a ban on part payments
- Apply a risk warning (like a health warning) for high-cost short-term credit financial promotions
- Require high-cost short-term credit providers to give an information sheet, including information on free debt advice, before a loan is rolled over

Most of these proposals will come into effect from July 2014, but the enforcement of the OFT affordability guidance, and the risk warning (on on-line adverts) will take place from April.

2.8 So, in summary, national action is already underway that should have significant impact on irresponsible high-cost short-term lending. Unless the FCA's consultation results in some unanticipated changes to the proposals, by July the consumer credit industry will be more tightly regulated, operating under significantly different rules as set out in 2.7 above. Then by the end of 2014 the Competition Commission will have published its final report into how the market operates, which should produce recommendations that will reduce the costs of short-term credit for small sums of money.

3. Action by Other Authorities

3.1. A number of authorities have taken specific action in relation to the 'payday loans' market, usually as part of a wider exercise to promote financial inclusion or prevent financial exclusion. Examples include:

- **Medway Council:** Produced a comprehensive well-received report "Fair access to credit" last year, and as a result payday lending websites have been banned on all public access computers owned by Medway Council, and there is no advertising of payday lenders on Medway-owned property, hoardings and bus shelters.
- **North Tyneside Council:** Along with banning access to payday lending websites on public computers, the council has also pledged to prevent payday loan firms from setting up business in commercial property owned by the council.
- **Stockport Council:** In the build up to banning access to payday lending sites on public access computers Stockport council campaigned to help residents with financial advice. They also ensured that library staff could help advise those needing financial advice surrounding payday loans.

- **Plymouth Council:** Plymouth banned access to payday lending sites on public access computers and banned advertising from payday lenders on bus shelters and billboards.
- **Southwark Council:** The council changed the rights surrounding development of buildings in their locality. The change prevents payday loan companies, pawnbrokers and betting companies from using existing high street properties to set up business.

3.2 The ability of local authorities to influence issues around advertising on and access to high-cost short-term credit is limited. Whilst there does seem to be a trend towards banning advertising on publicly-owned property and hoardings, the most significant advertising is on the television (a number of people, including Ed Miliband, have recently proposed banning such adverts during children's programmes) and the internet.

3.3 When it comes to banning access to payday lending sites on public access computers, there is not yet any consensus about whether this is worth doing. Informal contact with councils in the south east suggests that whilst a small minority have indeed taken action on this, there are more who have considered and rejected action on this front. In order to block access to websites on public access computers, the exact address for each website must be known and specifically targeted. As such, larger companies can be targeted, but it is easy for smaller companies to be missed. Any new sites created would subsequently need to be blocked, so ongoing monitoring of the situation would be required. Consideration would also need to be made for those people who already have high cost short-term loans and are using public access computers to manage the repayments. For some, removing this service could leave them in a difficult position and potentially could push such people further into debt.

4. The current position in Kent and possible areas for KCC action

4.1 There is a wealth of work already underway which contributes in general terms towards reducing poverty and financial exclusion which need to be taken into consideration when exploring action that KCC might want to take in response to the issues caused by the high-cost short-term credit market. There are three broad areas where KCC might consider taking action:

1. **Restrict access to and awareness of high-cost short-term credit options**

   Such actions could include banning advertising of products and access to websites on publicly owned computers.

2. **Increase availability of and awareness of lower-cost alternatives**

Actions here would aim to divert people who need to borrow small sums of money away from the "payday lenders" and towards more responsible and lower-cost lenders. Whilst high-cost short-term credit providers are providing a legal service, and are a better option than illegal loan sharks, there are sometimes better options if people only knew where to look and understood how much cheaper the alternatives could be.

Also, it is important to appreciate that high-cost short-term lending is only one potential source of debt problems. Statistics gathered by the Consumer Credit Counselling Service show that at the end of 2011 the average UK family was paying almost £200 a month in interest – we live in a culture where people utilise credit extensively. Also, according to the South East consumer empowerment partnership, more people get into debt as a result of unauthorised overdrafts than as a result of using 'payday lenders'. The broader objective, therefore, is to support people who need to borrow money quickly in finding the cheapest and most suitable product for them.

3. **Preventative action to improve people's money management**

   This is a much longer-term aspiration, which may go beyond the scope of this paper, but the best way to reduce inappropriate use of high-cost short-term credit would be to prevent the need for such services arising in the first place. Having said that, it must be recognised that some people fall into budgetary difficulties, despite managing their resources very carefully, because of circumstances beyond their control.

4.2 Below, some potential areas for action are set out which cross the spectrum of areas highlighted in 1-3 above, taking account of action already underway in the county.

Banning all advertising for high-cost short-term credit from KCC-owned property

4.3 Currently there is no such advertising in place. There is no advertising (for anything) on any KCC-owned or controlled property, although there has been in the past. No advertising (for anything) is allowed on street lighting columns. Commercial Services have confirmed that they would not allow any companies promoting products that the Council would not want to be associated with, including high-cost short-term credit providers, to advertise on roundabouts. So, although KCC does not have a formal policy prohibiting advertising of these products, there is a de facto ban in place.

Banning access to high-cost short-term credit providers from KCC computers

4.4 As set out in section 3, a number of authorities have banned such access from public computers, and there is also the option of banning access from staff computers as well. Paragraph 3.3 sets out some of the practical difficulties of taking this action. Also, whilst banning access to such websites would carry a clear message that KCC does not support such businesses, it could cause problems for those who already have such loans whilst not preventing others from accessing such loans via other means. If KCC were indeed to go down this route, it would need to be carefully planned so as to ensure that those currently using public computers to access high-cost short-term credit providers are supported to manage their loans by alternative means. Another variant of this option is to explore whether other information, signposting alternative sources of advice and lending, could be targeted at those who access high-cost short-term credit providers on public computers. Initial inquiries suggest this would be difficult, but it may be that there is potential learning from other authorities.

Promoting Credit Unions as an alternative source of short-term credit

4.5 Credit Unions are nationally recognised as an alternative to high-street high-cost short-term credit providers, intended to provide loans to individuals who cannot access mainstream banking products, and to encourage saving. Typically they have a much lower APR, membership is required and, importantly, they are non-profit organisations. However, it does take time for credit unions to process applications, so they are not able to provide the almost instant access to cash that some high-cost short-term credit providers currently do.

4.6 HM Treasury has recently approved the increase of interest rates on credit union loans from 2% to 3% per calendar month. Credit Unions argued this increase will help them to become self-sufficient as businesses. This increase would allow Credit Unions to offer more short-term loans. In conjunction with the forthcoming new regulations requiring high-cost short-term credit providers to act more responsibly, there is a real opportunity for the credit union market to expand and compete more effectively.

4.7 Kent's Credit Union, Kent Savers, was set up with financial support from KCC in 2009. It is a successful but small operation with only 3-4 employees. It has no high-street presence, and most work is currently done through postal applications for loans with a high proportion of applications being turned down as Kent Savers can only issue loans where there is a very strong likelihood of repayment.

4.8 Contrastingly, Wantsum Savers is another small credit union which functions from a small high-street store in Margate and only serves those who live and work locally.

4.9 Kent Savers must expand if it is to provide more loans to people who need this service in Kent. The Church is being supportive, with projects being rolled out in the Dioceses of both Canterbury and Rochester which use church volunteers to help people open Kent Savers accounts. Barclays Bank has also agreed to refer customers that they cannot help to Kent Savers. Most significantly, an on-line membership application service is being developed (see the next paragraph) which provides much greater scope for expansion.

4.10 DWP has a Credit Union Expansion Project which started in May. This aims to develop credit union products/services ranging from a budget account to a common debt recovery service for all credit unions. The intention is also to make available extensive market research on barriers to credit union growth and production of marketing materials. An automated loan assessment tool will enable credit unions to process more loans without increasing staffing and improve risk assessment. Kent Savers is about to go live with this tool.

4.11 Discussions are also underway between KCC (Business Intelligence), Districts and Boroughs and Kent Savers around improving targeting of credit union services to people who are financially excluded.

4.12 Is there more KCC could and should be doing to publicise and expand Kent Savers? It has a very low profile amongst staff, many of whom run small Christmas clubs and other such saving schemes that could be channelled through Kent Savers. Are there ways in which its service could be promoted to specific, possibly vulnerable, groups? Could CAB and other organisations that advise on debt management do more to promote Kent Savers? Other possible avenues for exploration include having a higher profile on Kent.gov.uk, leaflets or notices in libraries, or a Kent Savers screen on public computers.

Provide Information, Advice and Guidance on money management

4.13 KCC's child poverty strategy and subsequent work on welfare reform has resulted in a more co-ordinated approach to on-line information and advice on financial planning and management. Kent.gov.uk now contains a range of money management advice, with links to other useful websites including the Money Advice Service online, CAB, Kent Savers, and the "entitled to" and "better off in work" calculators to enable people to check that they are receiving benefits to which they are entitled and work out how much better off they would be if they took paid employment (see kent.gov.uk/community and living/money matters).

4.14 Community Learning & Skills provide some money management 'training' via family learning programmes targeted on primary schools in deprived areas and the 'Response' provision in Kent's poorest communities. CLS is also providing workshops with a number of social housing providers and other agencies to promote understanding for residents of the impact of Universal Credit along with developing appropriate budgeting and computing skills. There are examples of Children's Centres or Gateways holding sessions for local people on money management, but such activity is locally determined and organised.

4.15 As far as influencing the financial management skills of future generations is concerned, financial management is a core part of the PHSE curriculum.

Raising awareness, and taking action over, illegal activity

4.16 High-cost short-term credit providers are legal, licensed, organisations that can provide a useful and needed service. However, as the OFT and FCA reports show, many such providers are lending inappropriately in the way in which they operate. Even when the new regulatory framework comes into effect in April, it will still be important to ensure that providers actually follow the regulations in practice. KCC Trading Standards has a role to play here, and will support the FCA in its enforcement responsibilities.

4.17 Loan sharks, on the other hand, are illegal. KCC Trading Standards has, for a number of years, worked in partnership with Birmingham City Council who have Government funding for the national Loan Sharks project. So far in Kent this has resulted in two prosecutions and one formal warning with a further six cases on-going. The Loan Shark Team employ an officer whose works across the South East to inform, educate and gain intelligence for the enforcement teams locally. Examples of recent work include:

- A large campaign in Margate in May. A 'week of action' took place and it is estimated that 700 people were engaged directly and 1,000 indirectly just in this area alone. During the week there was training, meetings with key agencies including the Police, display stands in high-foot fall areas where the Community Wardens helped speak to people and give out and gather information. This resulted in a contact list of around 100 people and 70 different organisations in the Margate area.
- Various Registered Social Landlords (RSL) and Private Tenant Forums have been trained or received presentations and key and intelligence has come from a couple of RSLs this year.
- There is scope to explore further work with Kent Savers and Wantsum Savers.
- The team is planning a campaign in schools at the end of this year, with free lesson plans being advertised to all schools across Kent.
- KCC Trading Standards successfully bid for some money seized as proceeds of crime from loan sharks. This was used to run a short education programme in secondary schools.
- Work was carried out at the time of the closure of Sheerness Steel to prevent former workers falling victim to loan sharks. This included placing food items wrapped in packaging carrying the anti-loan shark message into food parcels and also contact numbers.

4.18 KCC could write to local organisations, including voluntary, community and church groups, asking them to notify Trading Standards and the financial Ombudsman Service of any instances that come to their attention of firms acting inappropriately or illegally. This would ensure that such firms can be investigated in an appropriate and timely fashion, and illegal activity quashed quickly. Trading

Standards already have “you can help” submission pages on the kent.gov website which could be expanded, as well as providing telephone and written access.

Encourage banks to promote easy access to Basic Bank Accounts

4.19 KCC could write to the main banks operating in Kent, encouraging them to promote easy access to Basic Bank Accounts as a means of encouraging people without bank accounts to set them up, and also emphasising the importance of providing affordable alternatives for people needing short-term loans (to avoid unauthorised overdrafts), with transparent fee structure and fair charges.

Work with partners to promote financial inclusion

4.20 Many of the underlying issues in this report around financial inclusion can best be addressed if the work different partners are doing is co-ordinated to get the benefits of synergy. There may be more work that could be done to share intelligence and make connections that enable better targeting of activity.

4.21 Kent Council Leaders (which comprises the Leaders from all the local authorities in Kent and Medway) has recently agreed to establish a “Tackling Disadvantage Commission” to identify the most effective interventions which could reduce disadvantage in Kent. The scope of the commission is still being defined, but addressing issues of financial exclusion, and by extension seeking to reduce the number of people applying to high-cost short-term credit providers for money to cover essential expenditure, may well be incorporated within the terms of reference.

4.22 There is also a Welfare Reform Task & Finish Group, chaired by William Benson, the Chief Executive of Tunbridge Wells, which brings together local authorities, Job Centre Plus, and the CAB to have a co-ordinated and planned approach to the reforms and keep a watching brief on their impact. The group is planning to discuss the issues in this report, including whether District and Borough Councils in Kent are already banning, or planning to ban, advertising for high-cost short-term credit providers.

5. Conclusions

5.1 This report has set out the context in which high-cost short-term credit providers operate, explained that they are legitimate businesses that are providing a service that some people need, although there is plenty of evidence that the market is not working for a lot of people. There are big changes ahead as the Financial Conduct Authority takes over the regulation of the market in April, and further changes could be put in place once the Competition Commission has reported at the end of 2014. But is there more that KCC could or should be doing to divert people from inappropriate use of such products or to prevent them from needing to take out loans in the first place? **Members are asked for their views on whether any of the**

potential areas of subsequent work set out in this report should be explored further, such as:

- **Banning advertising for such products from KCC-owned property**
- **Banning access to such providers from KCC computers**
- **Promoting Credit Unions as an alternative source of short-term credit**
- **Provide more information, advice and guidance on money management**
- **Raising awareness and taking action over illegal activity**
- **Encourage banks to promote easy access to Basic Bank Accounts**
- **Work with partners to promote financial inclusion**

Background Papers: None

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ANNEX 1

CASE STUDIES

These examples, from the Financial Conduct Authority's October 2013 consultation paper, demonstrate how people can get into debt as a result of using high-cost short-term credit lenders.

A Citizen's Advice bureau in the Midlands reported the case of a young woman who was unemployed and received jobseeker's allowance (JSA) at the lower rate due to her age. She had been unable to find full-time work and had accumulated debts of approximately £1,700 that she could not afford to repay on her low income. She contacted a payday lender to ask for a payday loan and told them that her only income was JSA of around £200 per month. The company gave her a loan of £200, which she then struggled to repay.

StepChange, a charity that supports people who get into debt, gave an example of a client with severe mental and physical health problems. Despite the client's only income coming from employment and support allowance and disability living allowance, he was able to take out eight loans with five separate companies. These loans have been rolled over multiple times, adding significantly to the debt. For example, one company has rolled over the debt each fortnight for a year, at a cost of £10 per rollover. This has had a severe impact on his stress levels.

StepChange advised a woman who had a debt management plan (DMP) with a for-profit debt management company. While on the DMP her income fell sharply after she left work on maternity leave. She attempted to maintain payments by taking out payday loans with multiple lenders, who allowed her to borrow money despite the fact they knew she was on a DMP and was on maternity leave. Where she was not able to repay the loan on time, lenders rolled over the debt several times, which resulted in a total debt of £6,000.

An individual who got into difficulties with a continuous payment authority (CPA) arrangement told his story:

"I lost my job, and had to cancel my CPA with [the lender] and [the bank]. [The lender] then decided to steal money from my bank account, without my authorisation, stating they have card details and can do as they wish, and that they do not enter into repayment plans. They kept taking money until the loan was repaid, constantly taking it until repaid, even though I had made agreements they carried on taking them anyway. They tell you to wait until your due date and default, which means you have the stress of either arranging for wages to be paid into a different account if it's not too late or cancel the CPA and hope for the best, and you still have the worry that they will still somehow find a way to clear your account before a repayment plan is agreed. Which is, I might add, what happened to me just last week."