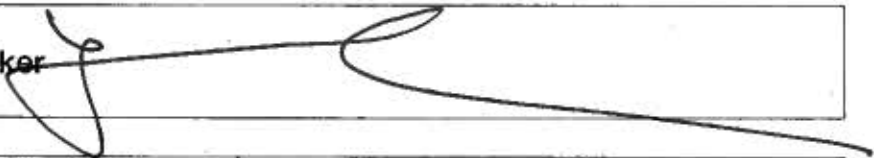




Report for:	Cabinet June 2012	Item Number:	
Title:	Haringey Credit Union		
Report Authorised by:	Lyn Garner, Director Place & Sustainability		
Lead Officer:	Martin Tucker 		
Ward(s) affected: All		Report for Key/Non Key Decisions: Key	

**1. Describe the issue under consideration**

- 1.1 In 2009 Haringey Council agreed to establish a credit union in the borough in response to the economic downturn and recession and the impact this was having on residents disposable income particularly those on low incomes. Credit unions are run as co-operatives with social objectives of contributing to the alleviation of poverty and to economic regeneration. They provide an ethical source of affordable credit for residents and can act as a valuable vehicle to promote and deliver financial and social inclusion. Credit unions also provide an essential alternative to payday loans that generates demonstrable cash savings for residents.
- 1.2 In 2010, after feasibility and then successfully securing £146k over 3 years (£71k Area Based Grant, £75k London Borough of Haringey revenue), Islington and City Credit Union won the tender to deliver a Credit Union project in Haringey.
- 1.3 In March 2011, after receiving the Common Bond<sup>1</sup> agreed by the FSA, Islington and City became Haringey, Islington and City Credit Union (HICCU). In April 2011,

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<sup>1</sup> To join a credit union, a person must come within the 'common bond' of the credit union. The legally defined 'common bond' may cover: Employees of one employer; Members of a particular organisation; People living or working in a particular geographical area



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credit union services become available to residents, workers and students in the borough.

1.4 The initial project had the following objectives to be achieved over 3 years:

- extend services into the borough – marketing and promotion
- develop employer links and payroll savings
- develop outreach provision – commensurate to available resources
- deliver against a set of targets:
  - a. Total number of Haringey residents in membership = 2,000
  - b. Total value of savings held by Haringey residents = £324,000
  - c. Total value of loans issued to Haringey residents = £347,00

1.5 Outreach provision is still being developed. A fixed/regular presence in an established community venue in the east of the borough has been achieved at the Irish Centre (last Thursday of the month, started 27/12/11) but is still being developed in other locations in Tottenham. An action plan on outreach to establish access to provision across the borough including regular surgeries at various locations together with training for frontline staff in customer services, housing, employment advice and other services can be developed with help from council officers.

1.6 Membership savings and loans at 23 May 2012 are:

- a. Total number of Haringey residents in membership = 861
- b. Total value of savings held by Haringey residents = £283,734
- c. Total value of loans issued to Haringey residents = £329, 952

1.7 The number of members taking out loans is outweighing the number of members saving with the Credit Union at a loan to share ration of 117% with the average loan being £989 per family. This situation is most likely caused by the prevailing economic conditions. The result is that the credit union is seeking additional capital to meet the demand for loans from Haringey residents and to ensure sustainable business growth.

1.8 In March 2012, HICCU approached Haringey and Islington for capital of around £250,000 to satisfy demand for loans. Islington have agreed a package of support as follows:

- Translation of a subordinated loan of £250,000 agreed in 2006 and due to run to 2019 into a grant. This effectively suspends repayments that were due to start in 2012, but does not recapitalise the organisation.
- Create a conditional development fund held by the Council for the Credit Union to access that will increase by £25,000 per annum to a maximum of £150,000
- Provide staff support in the form of a secondment for 2 days a week



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- Assist in providing additional premises if required,

1.9 It should be stressed that in return for this Islington are expecting more active involvement in the direction of the Credit Union and targeting of loans.

1.10 Haringey should adopt a response similar to Islington's whereby:

- **The council considers recapitalisation options including a subordinated loan to enable the credit union to meet the demand for loans which is likely to increase considering the impact of the reduction in working tax credits and local housing allowance changes on families in rented private sector accommodation.**
- **A subordinated loan is a key way of ensuring that the Credit Union continues to exceed membership growth targets in the borough. A £250,000 subordinated loan will benefit an additional 562 households over and above the current number of 861 Haringey residents in membership. (see Appendix 1)**
- **assistance with establishing a regular presence in community settings in Tottenham and developing an outreach action plan to raise awareness of the credit union and to establish access to credit union provision across the borough including regular surgeries at a variety of locations**
- **targeting of loan payments to families on low incomes who are turning to pay day loan companies for finance – there are currently at least 10 such companies in Wood Green and Tottenham High Roads alone and these are increasing. Nationally up to 7 million people use sources of high cost credit<sup>2</sup> (almost 18% of the working age population); this would equate to 28,500 people in Haringey using sources of high cost credit. The value of the pay day loan market in Britain is estimated at £2bn with the average loan £500 - £1000 – around 2 million loans or just over 5% of the working age population; this would equate to just under 8,000 people in Haringey taking out *pay day loans at high cost ranging from over 300% to over 4000% interest on a £100 loan. The credit union charge 12.7% interest on the reducing balance of a loan and over time borrowers move to becoming savers.***
- **reconfiguring targets around savings and loans set in 2010 to reflect the new level of investment realising support to 1600 new households including increasing the number of Saver accounts linked to young people supported into work through Jobs for Haringey – 300 into employment resulting in 300 new savings accounts opened**
- **the new investment will result in the credit union delivering annual increases in savings of £324,000 in 2012/13, £501,000 in 2013/14 £1,081,000 in 2014/15 and increases in loans of £332,000 in 2012/13, £622,000 in 2013/14, £1,156,000 in 2014/15 (see Appendix 2)**
- **the council should recognise that increasing the amount of loans via new borrowers will increase the risk of bad debt and will require the credit union to manage that bad debt at a maximum 7% of loans (in line with national figures on bad debt on unsecured loans)**
- **establish monthly monitoring and reporting of key performance indicators to show growth in membership, growth in loans and savings accounts, plus tight**

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<sup>2</sup> DWP –Credit Union Expansion Project – Project Steering Committee Feasibility Study Report (May 2012)



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management of bad debt provision limited to a maximum of 7% (in line with national figures on bad debt on unsecured loans) with a review triggered at 5%

- the council to develop closer working practices with the credit union including identifying a nominee to be co-opted onto the credit union board

### **2. Cabinet Member introduction**

As a council we are determined to do all we can to support our residents through these very challenging economic times. We know that as residents come under financial pressure through unemployment, higher utility bills and steeper fares, the market for payday loans is expanding.

Not only do the incredibly high interest rates on many payday loans make them a threat to our most financially vulnerable residents, but the expanding number of payday loans premises in Haringey undermines our vision for our high streets.

The credit union has proved very popular with Haringey residents, and it is unsurprising that in the current economic climate, there is a greater demand for loans than savings. This means that without a loan from the council, the credit union would be limited in its ability to continue to reach Haringey residents.

We intend to take decisive action to help protect residents and our high streets, by supporting the Haringey, Islington and City Credit Union to further expand the number of residents it can support through a loan. The Credit Union provides affordable credit, but also advice on financial management, debt management and other support vital to residents excluded by mainstream banks.

The paper proposes providing a loan of £250,000, to be supplemented by a further two loan payments of £250,000 if the Credit Union can demonstrate that it is meeting performance targets set out by the council.

### **3. Recommendations**

3.1 To give the Credit Union a subordinated loan of up to £750,000 released in 3 tranches of £250,000 dependent on a satisfactory development plan and performance against set targets; the first tranche of £250,000 released in 2012/13 with the further 2 dependent on business case and performance review

3.2 In return for injecting further financial support the Council will require the Credit Union to better target their loans towards people in the sub prime market - people on low incomes who are turning to pay day loan companies to borrow money

3.3 The Credit Union to set new targets around savings and loans including supporting 1600 new households with regular monthly reporting on key performance indicators on membership, savings, loans including membership amongst residents on low incomes, loans to residents on low incomes

3.4 The Credit Union to limit their bad debt provision to a maximum of 7% of loans with a review triggered at 5%



**4. Other options considered**

**4.1 Do nothing**

Under this option it is likely that the Credit Union would continue to be under-capitalised and Islington members would be effectively cross-subsidising those from Haringey as at present. This is highly unlikely to be sustainable in the medium term and Haringey will come under increasing pressure to contribute if loans are still to be made to Haringey residents

**4.2 Recapitalise up to current borrowing levels**

This option would require around £50,000 of funding being provided either through grant or loan. There is a significant risk that this would just represent a temporary solution and the gap in capital would soon grow again. The Council could seek to mitigate this by promoting saving with the Credit Union and trying to control the level of loans to improve viability, but there is likely to be a resource implication in terms of staff time and/or contracted resource to this, and no certainty that it would change the position.

**4.3 Recapitalise at a level providing a more sustainable future**

The Council could seek to recapitalise up to a value of £250,000. This is likely to give the Credit Union more certainty longer-term and is more likely to prove to be a semi-permanent solution, to be reviewed once demand and take up levels are tracked and monitored. LBH would expect involvement in direction and targeting on par with Islington if this option is approved. However, clearly the degree of risk the Council is taking is much increased with this option.

**4.4 Provide other support either in addition to the options above or instead of.**

Such support could take the form of ongoing revenue funding for staff, direct staff support in terms of a secondment, provision of appropriate premises or more generic marketing and strategic support. This option in isolation would not correct the structural imbalance in the loan book or recapitalise the balance sheet.

**5. Background information**

In 2009 Haringey Council started developing the Credit Union project as a response to the recession – providing services to support residents as austerity measures impacted on disposable income.

Credit Unions operate as co-operatives and are committed to wider social goals rather than simply increasing 'shareholder value' and maximising profits. Whilst they need to trade at a profit to meet running costs, the way they run the business and distribute profits marks them out as ethically different.

The Haringey, Islington and City Credit Union aims and objectives are as follows.

**Objectives**





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The objects of the credit union shall be:

1. the promotion of thrift among its members by the accumulation of their savings;
2. the creation of sources of credit for the benefit of its members at a fair and reasonable rate of interest;
3. the use and control of members' savings for their mutual benefit; and
4. the training and education of members in the wise use of money and in the management of their financial affairs.

Social goals

1. To contribute towards the alleviation of poverty within the community
2. To contribute towards the economic regeneration of the community

The credit union is a democratically owned and controlled co-operative, run by and for its members. Its primary objective is to encourage people to save for the future, as a way of avoiding the risks of excessive borrowing. At times when members need to borrow, or when they are struggling to meet the high cost of existing borrowing, the credit union offers low cost 'Saver Loans' that reduce the cost of borrowing to manageable levels. **The credit union offer 12.7% interest on the reducing balance of a loan so that with each payment the amount owed is less and therefore the charge for that loan.** It also provides guidance and support with budgeting and dealing with debt, and over time members move from being borrowers to being savers.

It was agreed that a Credit Union can play an important role in promoting financial inclusion in the borough as well as responding to the recession. The Association of British Credit Unions Limited (ABCUL) commissioned research that estimated that one and half million households across the UK are without even the most basic financial products, for example current accounts. In March 2007 HM Treasury published a policy on Financial Inclusion that praised the strength of financial services available to British consumer society, but recognised that the market was leaving some people behind – the financially excluded. The policy recognised that this made the cost of living potentially more expensive and made financially excluded individuals and families vulnerable to spiralling debt and poverty. The Financial Inclusion Champions programme, run by the DWP, is a resulting action of this Treasury policy and is working to address institutional and social barriers to financial inclusion.

Key features of a modern day credit union offering include:

- Cheaper loans at an average of 12% APR interest rates compared to upwards of 790% APR offered by mainstream loan providers to individuals not eligible for loans through high street banks.
- Access to banking services for people who have been turned away from high street banks.
- Community based financial advice and debt management integrated into personal finance.
- Debit card facilities and a current account to give customers the benefit of direct debit and standing order services for reduced rates on utility bills etc.



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- Annual dividend payments for members/savers compare favourably with interest rates offered by high street banks whilst interest rates are low during the recession.

***In 2010/11 Haringey Citizens Advice Bureau dealt with 3,372 enquiries regarding debt advice compared to 770 in 2009/10 and 406 enquiries in 2008/09. Local people seeking advice on debt has risen 8 fold in two years.***

There are increases across all categories of advice being sought, particularly around fuel, council tax arrears, overdrafts and unsecured personal loans. The former two can lead to debt situations and latter are debt situations that could be managed better through a Credit Union.

Credit Unions have long been seen as a community led mechanism to reduce the prevalence and impact of loan sharking and other forms of illegal money lending.

However, there has been a recent increasing trend of ultra high interest sub prime lenders that are entirely legal. The figures are stark; customers eligible for a personal loan through a high street bank would expect interest rates of around 10% APR, however those not eligible have only sub-prime lenders, pay-day loans or door-step lending as outlets for borrowing. Example APRs for borrowing £100 are below:

- Cash converters      328% APR
- e-Premier Finance    791.6% APR
- wonga.com            4214% APR

There is growing anecdotal evidence about increasing numbers of people on low incomes turning to pay day loan companies which are in turn increasing the number of their outlets in town centres. There are at least 10 such outlets in Tottenham and Wood Green alone.

The Office of Fair Trading has recently launched a review of the payday loan sector due to the increasing concerns that some are taking advantage of those who cannot afford to pay them back which in turn is increasing the money owed through interest costs.

The four key issues that they will be looking at are:

- Companies giving loans without checking whether the applicant can repay the loan.
- Targeting particular groups of people who have unsuitable or unaffordable credit.
- Continuing loans so that the charges roll over escalating the costs further and making the loans un-affordable
- Treating borrowers who get into financial difficulty un-fairly.

## **6. Comments of the Chief Finance Officer and financial implications**

Haringey Council has so far provided £121,000 in support to the Credit Union. This



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has taken the form of £71,000 of funding around initial set up costs and £25,000 for staff costs in both 2010-11 and 2011-12. A further £25,000 for staff costs is budgeted for in 2012-13 but no further commitment or funding exists beyond this point.

The funding already supplied should be considered in any comparison with the funding recently agreed by Islington Council.

The proposed additional funding will be provided in the form of a *subordinated loan* rather than a grant. Subordinated loans are those that are paid back after other, higher priority obligations are met and, as such, are higher risk loans. It is important that the Council manages this risk and will, therefore, provide a high level of bad debt provision to mitigate against the possibility of non repayment should the Credit Union encounter financial difficulties. This is the prudent approach the Council should take in supporting this proposal.

### **7. Head of Legal Services and legal implications**

The Council has power to pursue any of the options identified in the report pursuant to Section 1 Localism Act 2011 (the general power of competence) which came into force on 18th February 2012.

Consideration has been given as to whether assistance in the forms identified in the options would contravene European state aid provisions. This stems from the original EC Treaty which provided that 'Any aid granted by a member state or through state resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall insofar as it affects trade between member states, be incompatible with the common market'

Over time, the test for whether or not an undertaking amounts to state aid has been distilled into a number of criteria, all of which must be met for state aid to be present. These proposals have been considered against the criteria, and only one and arguably two of the five are met. Accordingly the Council can proceed confident that there is no breach of European law in these proposals.

It should be noted that if the option in paragraph 4.3 is to be pursued, then written assurance should be obtained from the other members of the HICCU evidencing their agreement to the expected "involvement in direction and targeting" before any commitment is given to make the recapitalisation funding available.

There are no other immediate legal implications arising from this report.

### **8. Equalities and Community Cohesion Comments**

8.1 Credit Unions promote financial inclusion and tackle poverty, and therefore seek to be inclusive to all members of the community.

### **9. Policy Implication**

### **10. Use of Appendices**

**Appendix 1 £250,000 Subordinated Loan Projections**





**Haringey Council**

## **11. Local Government (Access to Information) Act 1985**



## Appendix 1 £250,000 Subordinated Loan Projections

£989 Average Loan Value at April 2012

253 No. of Loans From Sub-Loan

21 Loans per month per annum

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Loans issued	21	21	21	21	21	21	21	21	21	21	21	21
Cumulative	21	42	63	84	105	126	147	168	189	210	231	252
Cumulative Value	£20,769	£41,538	£62,307	£83,076	£103,845	£124,614	£145,383	£166,152	£186,921	£207,690	£228,459	£249,228
Added Savings £26pcm	£546	£1,092	£1,638	£2,184	£2,730	£3,276	£3,822	£4,368	£4,914	£5,460	£6,006	£6,552
Annual savings												£78,624
Added loans from extra savings												79
Loan repayments	£0	£1,731	£3,462	£5,192	£6,923	£8,654	£10,385	£12,115	£13,846	£15,577	£17,308	£19,038
Annual repayments												£228,459
Added loans from repayments												231
Total Number of Households												562

### Notes:

The calculations are based on a sum of £250,000 which would be issued as loans to Haringey residents over a 12 month period. Given the current average loan value of £989 it is envisaged 253 household could benefit directly from this investment of loan capital.

Because all of the new borrowers will also start saving, this will increase the amount of money available to lend. This is an indirect benefit of the subordinated loan and this additional shares/savings will fund an additional 79 loans to Haringey residents during the year.

The average loan is repaid over a 12 month period. The spreadsheet calculates the amount of money repaid over the year. This money is then available to lend to Haringey residents and will fund a further 231 loans.

From this analysis it can be forecast that a £250,000 loan will reach an additional 562 households each year. Any larger subordinated loan would increase the number of people to move from borrowing to saving.



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**Appendix 2**

Assuming the full £750,000 subordinated loan is drawn down within a maximum 3 year period the Credit Union envisage annual increases in savings and loans balances held by Haringey residents being as follows:

	Shares/savings	Loan balances
Year one (C U financial year 2012-13)	£324,000	£332,000
Year two (C U financial year 2013-14)	£501,000	£622,000
Year three (C U financial year 2014-15)	£1,081, 000	£1,156,000

**Notes:**

1. These are annual increases, not cumulative figures.
2. Each year, the increase in savings and loans is in excess of the value of the subordinated loan.
3. Cumulative increases in savings & loans generates the additional loan interest income to repay the subordinated loan when due.
4. The Credit Union's financial year runs from 1 October to 30 September.

