

**The Highland Council**  
**Finance, Housing and Resources Committee**  
**27 November 2013**

Agenda Item	<b>23</b>
Report No	<b>FHR/ 167/13</b>

**High Cost Short Term Credit**  
**Report by Assistant Chief Executive and Director of Finance**

**Summary**

This report advises Members of the forms of high cost short term credit available and the work being undertaken both locally and nationally to monitor the activity of this sector, including future regulation.

**1. Background**

At the August meeting of the Finance, Housing and Resources Committee it was agreed that a report would be brought to a future meeting by the Assistant Chief Executive and Director of Finance on the issue of payday/doorstep lending in the Highlands. This report offers Members further information on the areas of activity, such as payday lending, which are considered as high cost short term credit.

**2. High cost Short Term Credit**

Generally there are three forms of activity which are considered to be high cost short term credit: payday loans; home credit or doorstep lending; and pawn broking.

**2.1 Payday loans**

Payday loans are short-term cash advances. The borrowers present either a post-dated cheque (incorporating the appropriate fees and interest) or provide the lender access to their current account, often by means of a Continuous Payment Authority (CPA). The loan amount is redeemed after 30 days or on the borrower's payday. The size of loans advanced to first time borrowers is usually restricted to between £200 and £300. The maximum sums lent are between £750 and £1,000. Interest of approximately £25 for every £100 borrowed is charged. This can generate Annual Percentage Rates (APRs) of between 1000% and 2000%, given the short term nature of the loans.

Payday loans are a form of short term lending aimed at individuals who need cash or choose to borrow in advance of their normal payday. Payday loans are a fairly new product having originated in the USA in 1994 and taken root in the UK from 1997.

Available evidence suggests that payday loans appear to be gaining in popularity and, subject to funds being available, would appear to provide an alternative source of credit. The Personal Finance Research Centre has noted that payday loans are an easy way to access small sums of money, the

process does not feel intrusive or drawn out, and they do not, in general, involve a credit check and put credit records at immediate risk.

There remain concerns about how effective the affordability checks undertaken by payday lenders are, given research that indicates some borrowers have to 'roll over' loans, i.e. the borrower takes out a new loan each month because of their inability to repay the original loan. This can lead to the borrower being totally unable to extricate themselves from payday debt.

Payday loans repayments are now most commonly made via a continuous payment authority which gives the lender direct access to the borrower's bank account and can be re-presented many times if funds are not available initially.

## 2.2 Home Credit or Doorstep Lending

Home credit involves the provision of small, unsecured loans which are repaid in instalments to a collection agent who calls at a customer's home on a weekly basis. Typically home credit loans are for sums not in excess of £1000. For short and medium term loans (up to 55 weeks) the total charge for credit is generally between £40 and £80 for a £100 loan and the APR varies from around 150% to nearly 500%.

A number of home credit lenders also sell shopping vouchers or hampers on credit and this can act as an 'introduction' to cash loans. Unsolicited door-to-door selling of loans is an offence.

## 2.3 Pawn Broking

Pawn broking is the provision of small monetary loans secured on items of value (typically jewellery) which the pawnbroker accepts from the borrower and holds as collateral for a minimum redemption period. At any point during this period, the borrower is entitled to buy back the item by repaying the amount of the original loan with additional interest.

Typically loans are in the order of £100 to £150 although some pawnbrokers specialise in high-value lending. The average monthly interest rate charged is 7%, which equates to an APR of approximately 100%. A common feature of all the forms of high cost short term credit discussed above, is that they provide an opportunity for individuals to borrow small sums of money, often for short periods, which the majority of High Street banks do not.

## 3. Current Activity

There is significant work being undertaken by Council officers, from both Trading Standards and the Finance Service's Money Advice Team, to monitor this area of financial activity. The two teams have effective lines of communication which allow them to share information and identify matters of concern. The Council's teams work in partnership with the network of CABx in Highland. The CABx and their parent organisation Citizens Advice Scotland have also been monitoring the effects of payday and doorstep lenders on their

client base. The recently established Highland Consumer Partnership will assist in taking this work forward.

### 3.1 Trading Standards

The Trading Standards Annual Performance Report 2012/13 ([http://www.highland.gov.uk/NR/rdonlyres/792CD17A-BAD0-42FA-B9C8-AFC0FD5E172E/0/TradingStandards2012\\_2013PerformanceReview.pdf#page=91](http://www.highland.gov.uk/NR/rdonlyres/792CD17A-BAD0-42FA-B9C8-AFC0FD5E172E/0/TradingStandards2012_2013PerformanceReview.pdf#page=91)) sets out details of a project undertaken to establish the level of activity in Highland. The project identified ten premises that offered high cost credit in Inverness which were operated by seven different lenders. All of the premises were visited and officers have expressed reasonable confidence that the businesses were operating in line with consumer credit legislation. There was no evidence that the home collected credit operators in Highland were failing to comply with consumer credit legislation.

The project concluded that the service would monitor complaints and referrals to detect possible areas of concern. The focus of monitoring would be upon how such loans are advertised and general compliance with consumer credit legislation.

### 3.2 The Highland Council's Money Advice Team

As noted above, the Money Advice Team has well established links with Trading Standards.

The experience of the service is that many people access payday borrowing via their phone. People also have the option of visiting the premises found in Inverness.

Doorstep lending in this area is offered by two particular companies. The companies are strictly regulated and both appear to be very compliant. Their Head Offices are described as being easy to deal with and they act responsibly when notified of genuine cases of hardship. Doorstep lending is often accessed by whole families on a generational basis and in some families it is the norm to have an ongoing loan.

### 3.3 Highland Citizen Advice Bureaux

The experience of CAB clients in relation to payday and doorstep lending varies across the Highland area. Bureaux from the north report a limited number of clients presenting with issues relating to payday lending, however bureaux from the south report that this is a growing problem. Where clients are presenting with issues, these tend to relate to refinanced loans, pressure to refinance loans and the penalties incurred if payments are late.

At a Scotland level, evidence from research undertaken by CAS suggests that 62% of loans come without proper checks to establish whether the borrower is able to repay the loan and 7 in 10 borrowers find themselves under pressure to rollover loans.

Due to the growing concern of the impact of payday loans, Nairn CAB are currently working on a campaign to raise awareness of how clients can take control of the payday loan debt which includes a video and a promotional campaign at the local football ground and in football programmes.

#### **4. Future Monitoring and Regulation**

##### **4.1 Local Monitoring and Regulation**

Discussion is currently underway in Highland among the respective interests to seek to agree an action plan. This area has been highlighted as a growing issue and therefore it is important to monitor action going forward. For example, the Money Advice Team will seek to gather intelligence on payday/doorstep lending from clients by asking them to complete a short questionnaire. It will also survey clients on how often they rollover payday loans and the purposes for which such loans were sought, an issue highlighted as a presenting problem. The questionnaire will also be shared with local CABx to allow use by their money advisers. This joint working will allow Trading Standards to target their investigation and enforcement action.

Further liaison will be undertaken with the British Bankers' Association to identify best practice in relation to how banks can assist customers who would experience genuine hardship if the continuous payment authority held by the payday lender was actioned. In practice, currently, the level of assistance can vary from bank to bank.

Members and officers recently participated in a Roundtable Session with the Accountant in Bankruptcy and Fergus Ewing MSP. Issues discussed included:

- The speed with which the loans are granted
- The possibility of inserting a 'health warning' into any loan application
- The challenges faced by credit unions as their application process takes longer
- The prevalence of payday outlets in Inverness

##### **4.2 National Monitoring and Regulation**

The COSLA Executive Group has discussed high cost credit, in particular payday lenders, and has expressed concern that the most vulnerable members of society may be resorting to punitive methods of borrowing.

In addition, COSLA's Community and Well-being Committee have been asked to look at a number of alternatives to payday lenders, including credit unions, and Community Development Finance Initiatives. The Committee will report to COSLA's Executive Committee in November.

The Office of Fair Trading (OFT) recently gave fifty leading payday lenders, accounting for 90 per cent of the market, twelve weeks to prove they had addressed areas of non-compliance. Nineteen of the lenders have informed

the OFT that they are leaving the payday market. Four of these have surrendered their licences and will not be required to provide an audit report. The remaining fifteen continue to trade in other areas of business that require a credit licence and have been required to provide an audit report to the OFT. The OFT has received audit reports from forty-six lenders, including all those who retain a licence. Since the OFT published the final payday review report in March 2013, three firms engaged in payday lending have had their licences revoked and a further three lenders have surrendered their licences. None of the payday lenders identified for enforcement action by the OFT currently have physical locations in the Highlands.

The Financial Conduct Authority will assume overall responsibility for the regulation of consumer credit from April 2014. Last month FCA published a consultation document which proposes new rules for high cost short term lenders which it believes will help to improve outcomes for consumers and address the issues being caused by harmful business practices.

The proposals have two main aims:

- a. To ensure that firms only lend to borrowers who can afford to repay the sums borrowed – the proposal is to limit the number of times a high cost short term credit loan can be rolled over to two, and to limit to two the number of unsuccessful attempts to use a CPA.
- b. To increase borrowers' awareness of the costs and risks of borrowing beyond their means and ways to get help if they have financial difficulties.

## **5. Further Steps – What Highland Council can do?**

There are two areas in which the Council can take a further role in relation to payday/doorstep lending – awareness raising; and monitoring and restricting access. These are discussed in more detail below.

### **5.1 Awareness Raising/Monitoring**

It is important for the Council and its partners to monitor and assess the potential impact of high cost credit, given the increase in this area of business and the impacts of welfare reform on a sizeable proportion of our community. As outlined in sections 2 and 3, the Council's in-house teams and CAB partners are monitoring the challenges affecting individuals accessing these forms of credit and equally promoting sources of help in dealing with these.

A further area for work is to raise the profile of alternative sources of credit. As part of this, Highland Council has long been a supporter of local credit unions and since [2010](#) has been working in partnership with and promoting the availability of Hi-Scot Credit Union as an alternative source of credit for individuals living throughout the Highlands and Islands. This approach keeps money within the local economy through a third sector, non-profit making provider. The credit union can provide access to low value loans (i.e. less than £1000), which cannot be accessed through High Street banks, but the repayment rates associated with this form of credit are considerably less than

the examples of high cost short term credit identified. The rates offered are not representative rates, which means that customers know that the rate advertised is the rate that they will be offered. Credit unions carry out financial assessments of any potential borrowers. Whilst this does increase the time taken to access loans, it helps to ensure that those borrowing can afford to repay the loans accessed, protecting the interests of credit union members assets.

Awareness raising of Hi-Scot and its services continues to be important going forward. Members of the public can access membership forms at Council Service Points and also have their ID checked and verified there in order to expedite the application process. Wherever appropriate, information on this service is included in Council newsletters and publications, e.g. tenants' newsletters, staff payslips.

A number of local authorities across the United Kingdom have sought to restrict or block access to websites operated by payday lenders on computers managed by the authority, either for staff or for public use, e.g. in libraries.

5.2 Currently the Council does not restrict access by Corporate PCs used by staff and Members to websites operated by payday lenders. These sites, along with many other banking sites, are categorised by filtering software as being 'Financial Data & Services'. If a block were placed on such sites, this would create issues in the legitimate access to other sites falling within this broad category. The alternative approach would be to identify all of the payday loan sites and put a restriction in place. As noted above, experience within Highland has found that most transactions with payday lenders are conducted by phone rather than by internet. This would suggest that any move to restrict access via Corporate PCs may have limited effect.

5.3 Public access computers are predominantly found in libraries operated by HighLife Highland (HLH). HLH have advised that their aim in offering public access computers is to offer 'as near home computing experience as possible' subject to clear restrictions on illegal and offensive websites. There are no restrictions in place on accessing payday lenders' websites currently and no plans to introduce such restrictions. HLH have indicated that they would be keen to publicise local credit unions and to hold information on websites offering details of sources of affordable loans.

## **6. Implications**

6.1 There are no legal, climate change/carbon clever or risk implications arising from this report

6.2 Resources

Work to monitor the potential impacts of high cost short term credit will be met from within existing budgets. Opportunities to promote awareness and facilities of Hi-Scot Credit Union will be incorporated into ongoing Council business where appropriate.

### 6.3 Equalities

The potential impact of these services on vulnerable groups, likely to include individuals with protected characteristics, will be monitored going forward.

## **7. Recommendation**

Members are asked to:

- i. note the current activity being undertaken to monitor the impact of the availability of high cost short term credit and to offer information and advice to users
- ii. continue to support and raise the profile of Hi-Scot Credit Union as a viable alternative form of affordable credit to consumers across Highland, and invite a representative to make a presentation to a future meeting

Designation: Michelle Morris, Assistant Chief Executive

Date: 15 November 2013

Author: Stewart Fraser, Head of Legal and Democratic Services

Background Papers: