

10 Review of options

The previous sections outline the needs and demands of those most likely to be financially excluded and explored the extent of current provision. This final section assesses some of the alternatives available, before making a considered recommendation that reflects the findings of the survey and the comments of key stakeholders.

Across the country a number of initiatives have been applied to tackle aspects of financial inclusion and these are discussed generically in Table 9-1. The research has shown that Leeds has an excellent 'live and work' common bond credit union, and such a strong credit union means that a savings and loan scheme (see Table 9-1) is largely superfluous. Furthermore, the PIF will be available shortly to make loans to micro and small enterprises. Leeds also has one of the largest CAB outside of London. Instead any additional provision in Leeds should reflect the gaps highlighted during the report:

1. Loans for those with marginal incomes who are currently using moneylenders. The loans required are normally too high risk for credit unions to make, where the maximum interest rate of 12.68%APR is insufficient to cover possible liability and cost of management. These loans should encompass accessibility and ease of use.
2. Advice aimed at those on low incomes, who may have modest total debt levels, but comparatively high levels when set against their disposable income. Services need to be provided locally by trusted intermediaries, and be available at least five days a week.
3. Similar advice services need to be developed for targeting at potential micro-entrepreneurs. These have to aimed at those who may not previously started a business, while advisors will need to be specifically trained to have an understanding of the requirement for micro-entrepreneurs to juggle household and business income and expenditure.
4. Although microenterprise loans will be available via the internet through PIF, the partners may need to monitor this to ensure it is accessed in disadvantaged communities. The research did not explore the likely usage of an internet based provision, but the general desire for local provision suggests that an alternative more personal service may be required. The partners may need to consider how this could be delivered.
5. The survey indicated that there was moderate appetite for financial literacy courses. However, any long term commitment to financial inclusion must seek to improve general levels of financial capability, while a means needs to be found to deliver services in an informal and engaging way.

Type of Initiative	How it functions	Main plus points	Main Drawbacks	Examples
'Live & work' credit unions	Extends the community common bond of credit unions to include all those who work within the bond area. These credit unions are usually much larger than conventional credit unions, often covering entire cities Levers in public money to focus on serving disadvantaged communities	The scale gives it a greater chance of being sustainable, it also means the organisation has to be more professional. In theory being cross-community should attract wealthier savers thus enable greater lending on disadvantaged areas. Services developed in accordance to need. Concept has had moderate success in the USA	Do not remove the risk element attached to lending in disadvantaged communities. The legal maximum APR that credit unions can offer (12.68%) mean it is difficult to serve the most financially excluded	East Manchester CU, Leeds City CU, Pompey Savers CU.
Community Development Credit Union (CDCU)			Similar challenge over risk and interest rates faced by other credit unions. In addition considerable debate among credit union activists about CDCUs economic viability.	None as yet. Development project being led by NEF.
Savings & Loan Scheme	A partnership between a bank/building society and housing association(s) that offer affordable loans and high interest savings accounts to the housing association tenants Offer affordable loans to entrepreneurs who have been declined by mainstream providers	Targeted at housing association tenants and their households. Links financially excluded to the mainstream providers. Offers both savings and debt products. Lever in public money. They are a long-term investment vehicle in disadvantaged communities. They are highly professional	Too date these schemes have only had moderate success and are unlikely to have impact on addressing financial exclusion	Hew Horizons (Cambridge), Helping Hands (Darlington), & Westerhailes in Edinburgh
Enterprise CDFIs			Don't offer personal loans. They take at least 7 years to reach sustainability. Tendency to drift upmarket to improve sustainability	Aston Reinvestment Trust, Manchester Enterprise, & Bolton Business Venture
Community Reinvestment Trusts (CRTs)	Offer both personal and enterprise affordable lending in disadvantaged communities	All encompassing loan portfolio serve the whole community. Very flexible and can change products to reflect market	Long time to reach sustainability No savings products	East Lancs Moneyline, Portsmouth Area Regeneration Trust (PART), and Salford Moneyline
Financial Literacy courses	Education on understanding money management	Tackles problem of financial exclusion at source. Engenders good financial behaviour	Long-term solution. Client group reluctant to access courses	Saffcash run by Leicester HA, & Cash Crescent by the Basic Skills Agency
Access to bank accounts	Simple bank accounts which allow savings and withdrawals (sometimes direct debit facilities) offered by mainstream providers	Provides access to mainstream services and helps overcome misconception by both clients & banks	No loan service. No links to other services. High costs if go overdrawn	Under agreement with the government every bank must offer a basic bank account service.

Table 10-1: Generic Financial Inclusion Options

In response to these factors the options for intervention fall into five general areas:

1. Do nothing
2. Create a completely new CDFI
3. Enhance informal coordination and collaboration on jointly developed services
4. Create a back office service delivery agency
5. Community Banking Partnership

10.1 Do nothing

A legitimate approach is to take no further action. This presupposes that either there is insufficient support and/or resources for the key aspects discussed in this report; or that financial inclusion is a lower priority than other issues. We would argue that such an analysis overlooks the impact financial exclusion has on other priorities, in particular economic development. Evidence of the extent of this was apparent in section 9.

So £5,966,593.30 which is not being spent in local shops, supporting local business, who employ Leeds residents. Because financial exclusion has remained hidden and unmeasured it has not made the agenda, but it has a very genuine outcome on the real economy. Consequently we would suggest that doing nothing is only an option if the cost of intervention is greater than £5,966,593.30 every year.

10.2 Create a completely new CDFI

The next option is the development of a new CDFI based on the Community Reinvestment Trust (CRT) model. This approach does fulfil the objective to provide sustainable alternative affordable loans that credit unions are unable to supply. The four CRTs currently trading have lent over £3 million since the launch of the first in July 2000. Clearly, they have shown that there is a market. Research (Dayson 2004, forthcoming) has indicated that CRTs also provide considerable informal advice to both individuals and enterprises. This is done partially because of a lack of capacity among existing advice agencies, plus the CRTs are perceived as more approachable than conventional providers. The research suggested that this experience is replicated among credit unions and it therefore likely to occur in Leeds. Though noteworthy such an arrangement it is ultimately unsatisfactory to both the individual and the CRT/credit union. For the individual wherever possible impartial advice should be divorced from lending, while the service is currently delivered unfunded and therefore it is an insecure basis on which to build a strategy.

However, the crucial element of this option is that the new CDFI option takes no account of existing provision and either sweeps away or ignores these providers. What is suggested is a big bang approach, which will drive a financial inclusion strategy and loan fund without the alleged 'baggage' of existing agencies. This authoritarian approach may ultimately be successful but the process may prove to be politically detrimental. We would recommend a more organic and inclusive approach, which celebrates current achievements while seeking to make them fit for the task of creating financial inclusion.

10.3 Enhance informal coordination and collaboration on jointly developed services

It is apparent from the research that the delivery of services to tackle financial inclusion requires better coordination and Leeds-wide strategy. Therefore a positive first step, or if resources cannot be located, a standalone option is to ensure the delivery of existing organisations is maximised. There are a number of initiatives which can be taken to begin this process:

1. Additional resources for advice agencies and the CAB. It is very clear from the analysis that there is a considerable unmet demand for advice services and that this can only be met with an increase in workforce. However, to ensure support is targeted at the financially excluded, advice services should be encouraged to assist those with modest debts with sub-prime lenders.
2. Credit unions to share development of new products. To be effective throughout Leeds the credit unions require greater resources and investment in product development. One product required is debt consolidation loans and experience elsewhere suggests these could be delivered through a guarantee fund. Guarantee Funds operate where the funder places a pre-agreed sum on deposit, either with the credit union or mainstream financial institution. Credit unions can then offer loans to new members and those unable to save before borrowing. The risk for this lending is offset by the guarantee fund. The most successful guarantee funds have operated where there has been an emphasis on money advice, rather than lending money. Guarantee funds have had a mixed record and unless considerable sums are to be invested it is unlikely they can cover high levels of indebtedness.
3. Recruit members on behalf of the credit unions from the most disadvantaged communities. If this is to be effective a medium term marketing strategy needs to be drafted and resources allocated to help the credit unions cope with the expected increase in demand.
4. Enable credit unions to offer outreach services. Although it was argued earlier that the concept of additional credit union branches was unsustainable (8.3.1), an alternative of providing a dedicated telephone link in the one-stop shops was proposed. This proposal is both practical and financially viable and fits within the broader objectives of the one-stop shops to supply universal services.
5. Promote the PIF enterprise loan funds. As with the credit unions there is probably need for expenditure to be targeted at generic marketing campaign. This proposal benefits both PIF and Leeds. The PIF service needs to make loans and its success should contribute to the development of the Leeds economy.
6. Closer working relationship between Leeds' credit unions and PIF. To maximise the use of resources and reduce overheads the credit unions and PIF should seek to share administration and management functions.
7. A Leeds Financial Inclusion Strategy needs to be drafted which explains the roles of all the partners, the targets, and what resources will be made available. Linked to this delivery agencies need to agree bilateral and multi-lateral working protocols.
8. Improve signposting and networking between agencies. To maximise the capacity to address financial exclusion existing providers need to increase their knowledge of each other and begin to work together. A forum should be established to share good practice and experiences and deliver a Leeds Financial Inclusion strategy.

All the above proposals retain the current institutions. Such an approach should help to ensure the continued support and engagement of existing organisations. The weakness of this strategy is that there is no assessment about the relative merits of existing entities, or whether the present institutional segmentation should be continued. The success is also dependent on current providers voluntarily contributing their time towards a partnership based programme.

A focus on enhancement is likely in the short-term to be the most cost effective measure and be the swiftest to implement. This proposal is reliant on building an effective partnership among the different agencies. Without a critical mass of activity or a strong central coordinating point there is a risk that initial enthusiasm will diminish and financial inclusion will slip down the agenda.

10.4 Create a shared administrative function

An alternative strategy for the credit unions could be to promote a secondary delivery organisation. This would not only encourages Credit Union expansion but also develops new services and community partnerships in support of the primary credit union activity. Such a secondary organisation with paid professional officers can supplement and complement credit union activity on the ground. Such an arrangement has been developed successfully in Newcastle on Tyne where Financial Inclusion Newcastle (FIN) in partnership with the local Credit Unions has been able to advance financial inclusion. This has included providing accessible money advice, access to basic bank accounts and insurance, financial literacy and a special loans scheme that covers the rescheduling of loans that would normally fall outside Credit Union criteria. In effect the money advisor helps the client maximise their income, reduce their outstanding debts, and makes a recommendation for a guaranteed loan to the credit union. The credit union assesses the application and the advisor's comments, before issuing the loan. Any default is covered by the guarantee fund. To ensure a separation of responsibilities at no stage does the advisor agree the loan or the credit union offer advice. Lloyds TSB have provided a Guarantee Fund to underwrite this loan activity, agreed local account opening contacts and also have a local business bank manager who will attend meetings to stimulate and develop business activity.

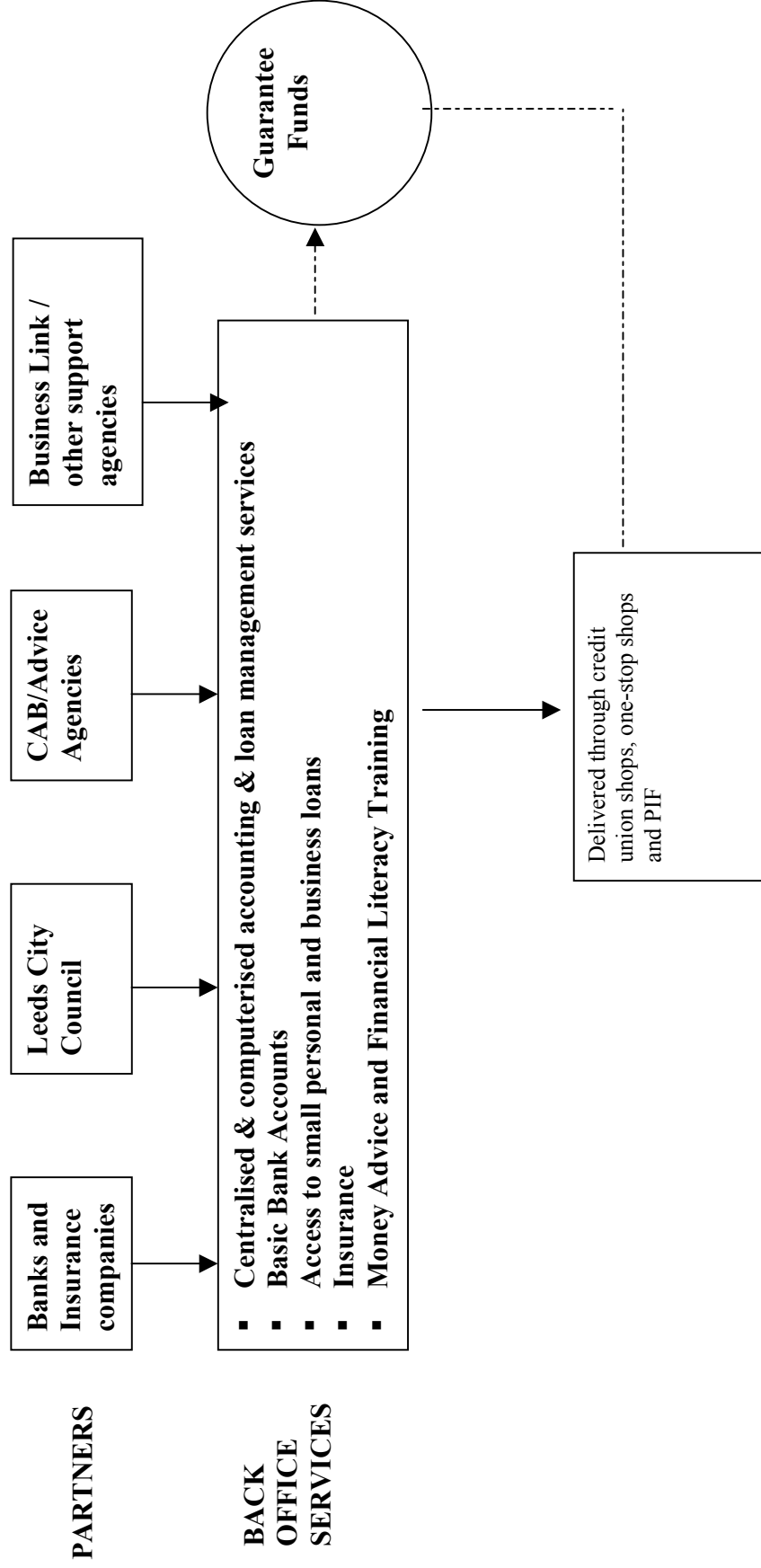
The Shared Administrative Function builds on existing credit unions and loan fund structures. It enables the current credit unions to continue to exist but ensures they work closer together. Moreover it retains the involvement of those engaged in this project, while releasing them to focus on the promotion of their credit union/loan fund rather than getting ensnared in administration. Over time special funds aimed at addressing specific issues may be held centrally, however, there are issues about the accountability of this option. Due to collective development and innovation the service should also help increase the effectiveness of product development. The service would also ensure that advisors are linked with the core objectives and cannot be utilised to support other activities.

There are a number of disadvantages with this strategy, not least issues of accountability. It is important to ensure that the back office has a legal status otherwise disputes over ownership and priorities will arise. Similarly the shared back office will

still need to be embedded within a Leeds strategy, as ultimately it is just an operational centre and unless constituted differently will not have responsibility to deliver a financial inclusion strategy. Being an operational vehicle means the shared administrative function does not reach the financially excluded. Instead it is reliant on the delivery agencies to promote themselves effectively and serve disadvantaged communities. Issues of coverage also need to be resolved as the back office service is a secondary agency and has no contact with residents. Another key weakness with this approach is the asymmetric scale of Leeds' credit unions. In Newcastle the partnership was a means to preserve the autonomy of three small credit unions, while enabling them to develop and expand. In contrast, in Leeds, one credit union dwarfs the others to the extent where the largest credit union already has a professional back office provision. Consequently this proposal could only be justified if the smaller credit unions were excluded or utilised the Leeds City Credit Union's administration centre. Alternatively the full scheme could operate between Bramley and St. Gregory's credit unions, but Leeds City Credit Union would be excluded.

It is difficult to calculate a timescale for the development of a shared administrative function, as it is reliant initially on the development of a partnership and subsequently on building the structure. We would estimate that once the partnership has agreed the legal structure and its terms of reference (which could take anything from four months to a year), the structure would take about four months to establish. There will then need to be a testing period and a gradual roll-out across each credit union and PIF.

Figure 10-1: Leeds shared administrative function – activities



10.5 Community Banking Partnership⁸

At the recent Credit Hearing held in Leeds and organised by Church Action on Poverty, possibly the most important message of the event was the absolute necessity to combat the issue of extortionate credit on two points; firstly the capping of interest rates and tighter regulation on moneylenders and secondly the availability of affordable credit. The Shared Administrative Function (see 9.4) proposal through its guarantee fund offered a means to partially address this challenge. Additionally its other services began to develop a holistic financial inclusion project. The challenge though is to establish a more sustainable and integrated approach.

As discussed earlier there are a number of credit unions and loan funds across Leeds and most find it challenging to penetrate disadvantaged neighbourhoods. The challenge with a multi-agency approach is that it is unlikely that all of the credit unions or loan funds could become sustainable, with the result that they will be perpetually at the mercy of funders and changes in policy direction. Leeds City Credit Union resolves this through cross-subsidising, but as they acknowledged, without external support this policy has its limits.

Credit unions are also constrained by legislation that fixes their maximum interest rate on loans at 12.68% APR. This restricts their capacity to offer loans to high-risk clients, such as those with multiple indebtedness or for those unable to save. In theory they could serve these markets but the probable loss rates would have a detrimental impact on their balance sheet. In the USA credit unions resolve this by charging higher interest rates, sometimes in excess of 20%, well in excess of the British legal maximum. An alternative strategy would be to create a loan guarantee fund, such as that incorporated in FIN, but as Jones (2003) has stated these have had a mixed record to date and are unable to offer higher risk consolidation loans in sufficient quantity.

The obvious solution is to create a CRT, however, as discussed above this would prove too disruptive in Leeds, where existing organisations are successfully established. Instead a holistic approach is recommended in which Community Banking Partnership (CBP) is established within which a CRT is located. The CBP would work alongside Leeds City Credit Union in a purely supplementary and complementary role and could be accessed by Bramley and St. Gregory's. It would seek to serve customers that the credit unions could not serve, while simultaneously building a partnership to deliver to non-credit elements of a financial inclusion strategy. In its simplest form the CBP would perform two interrelated functions. Firstly, it would supply affordable loans as an alternative to moneylenders. Secondly, it would build a coalition, through its a

⁸ The proposed Community Banking Partnership (CBP) approach is being developed by Community Finance Solutions (CFS) in partnership with the National Association of Credit Union Workers (NACUW) and the New Economics Foundation (nef). Copyright 2004 All Rights Reserved

stakeholder based ownership structure, to ensure the delivery of the advice, financial literacy and capability, elements of an agreed financial inclusion strategy.

The new institution would be an ideal vehicle to be the driving force, and main owner, of any financial inclusion strategy. If designed effectively the CRT should act as a link between advice and finance, working with advice services to ensure the client receives the most appropriate assistance. For example it could target its funds at high-risk clients who, once their initial problem is resolved, could move to a credit union. Furthermore, it would work in partnership credit unions to deliver a seamless service to customers and offer graduated interest rates linked to risk. This is both good business sense and fair on existing credit union members, ensuring the most prudent savers and borrowers receive the best interest rate without excessively 'punishing' those trying to improve their situation. Furthermore, new customers could also begin saving with the credit union while they repaid a loan to the CRT. Equally, it would bridge the gap between personal and enterprise finance by lending to enterprises in situations which are currently outside of credit unions legal boundaries.

The main advantage of the CBP is that it offers a pan-Leeds approach, while building upon the excellent work put into existing credit unions and agencies. It also overcomes parochialism by providing a joint venture entity in which all financial inclusion partners have a stake. The new entity would need an inclusive name, which can then be marketed as a new universal and generic service. Also its loan fund structure will enable local authorities and regeneration projects to invest on a hypothecated basis. The CBP will extend the level of support new and existing enterprises, while seeking its own sustainability. It will create a critical mass to initially building capacity to fill gaps and offers the benefit of complete coverage without destroying existing schemes. Furthermore it will supplement and complement the credit unions as it cannot offer a savings facility or undercut the interest rates offered on credit union loans. Another advantage is that new situations often present themselves and this approach will enable flexible, strategic, and rapid responses to new policy and funding opportunities.

The disadvantages are linked to how existing entities will respond to the proposal. It is entirely understandable that current boards of management may be hesitant. However, an inclusive approach, which seeks to capture existing good practice and place it within a more sustainable framework, may offset some of the concerns. Resistance may also be found among the credit union activists who may perceive the initiative as a threat. Again this can only be addressed through an inclusive approach, supplemented by clear demarcation lines agreed in a working protocol.

10.5.1 Community Banking Partnership approach

The core mission of the CBP approach is a customer focussed 'one stop shop' delivery service that incorporates existing community finance provision by credit unions, money advice and financial literacy agencies, and mainstream financial institutions but also develops new services to deliver affordable banking to the poorest people in the community. To deliver in this 'one stop shop' way, it is proposed to create a specially

designed group structure that will bring together proven British best practice by credit unions that are already in operation in Britain (particularly in Leeds), Ireland and the USA, with the good practice in high risk personal credit delivery emerging from the CRTs (see Figures 10-2 and 10-3).

Customers will access the services of a CBP either through credit union shop front premises or through other outlets including credit union collection points in neighbourhood locations, advice agencies outreach surgeries in the community, and via housing associations, bank and local post office partners. In the USA, the credit union shops provide the brand for Community Development Credit Union (CDCU) 'community banking services'. In Birmingham where the first 'community banking partnership' model is under development, (see Case Study 10-1) a system of 'dual branding' is emerging. One brand promotes the local community credit union and its name (e.g. South East Birmingham Community Credit Union) and the other brand promotes the 'Birmingham Credit Unions' citywide logo and brand. In theory a similar strategy could be used in Leeds.

The CBP Staff Team will provide a 'holistic' approach whereby a wide range of community banking services is available to customers. This will result in either the CBP meeting the need directly through the provision of Leeds Financial Inclusion Strategy products or through partnering arrangements referring the customer on to:

- PIF and other enterprise/business lenders.
- Mainstream banks for Basic Bank Accounts and other financial services;
- CAB, Advice UK and other debt advice agencies in respect to in-depth money and debt advice case work where litigation and time consuming court work is involved.

Case Study 10-1: Birmingham Community Banking Partnership – First Prototype Project

Birmingham with 31 credit unions, over 20,000 members and almost £19 million in assets represents the largest concentration of credit union activity in England and Wales. Birmingham's Ladywood Credit Union collaborated with Riverside Credit Union in Liverpool and Portsmouth Area Regeneration Trust to develop a British model with New Economics Foundation for testing the successful Money Advice and Budgeting Service (MABS) in the UK. This Factor Four service provides low-income households with four integrated services:

- (i) Money and Debt Advice;
- (ii) Energy Advice and assistance to claim Warm Front and energy efficiency grants;
- (iii) Bill payment and debt repayment services via a Credit Union or a CRT;
- (iv) Access to affordable credit from a Credit Union or a CRT.

Birmingham has been funded as the first Factor Four pilot by npower, Severn Trent Trust Fund and Barclays Bank. Participating credit unions include Ladywood Credit Union and South East Birmingham Community Credit Union (SEBCCU). In addition SEBCCU has been awarded the first CDCU funding nationally from the Adventure Capital Fund, Barclays Bank and RBS NatWest. The setting up work in

Birmingham has brought both Factor Four services and the CDCU pilot services together as the first Community Banking Partnership.

A comprehensive five year business plan sets out a clear strategy for a full scale roll out of a mass membership drive. This will be implemented from April 2005 through the proposed development of a shop front network of four CDCUs in Birmingham. To enable higher cost loans and micro-enterprise loans to be made, the business plan calls for Birmingham Credit Union Development Agency (BCUDA) to become a CDFI with a Community Reinvestment Trust group structure. The CDFI will also facilitate cost saving economies for the delivery of home improvement loans in partnership with ART Homes and for the longer term funding of the Birmingham Factor Four service. With support from the City Council and local Trading Standards officers, BCUDA and Birmingham Credit Unions are developing a product brand for Birmingham Community Banking Partnership services

To fulfil the objective of financial inclusion it is essential that existing mainstream banks and building societies be incorporated into the CBP. Their contribution will be dependent on the actual requirements of an individual user, but the following will be the key areas of focus: provision of transactional services through a basic bank account for personal customers; creation of a 'shared' customer/banking relationship; and a referral mechanism. It will however, be important that client choice prevails and that introductions can be made both ways.

In respect to the money advice and financial literacy aspects of the Community Banking Partnership, the Birmingham prototype service includes 'Factor Four', which delivers to all financially excluded households budgeting help, money advice up to 3.5 hours for each customer, and access to a bill payment and debt repayment service. In Leeds it is expected that similar service should be developed in partnership with Education Leeds.

The CBP Group Structure links sovereign organisations, such as Leeds City Credit Union, to a joint venture CRT and a charity. It is proposed that the CRT's shareholders are the financial inclusion stakeholders but that Leeds City Credit Union performs its management functions. The service would be open to all residents of Leeds, while the most effective means to maintain its complementary and supplementary role is to have it operated by Leeds City Credit Union. As a joint venture the CRT could also be accessed by other Leeds credit unions, whom could develop integrated products with the CRT, though the CRT element would be contracted through Leeds City Credit Union. The CRT would deliver the loan fund element of the financial inclusion strategy. Meanwhile, the charity, which again will be a joint venture, would be responsible for ensuring the delivery of the advice and financial literacy/capability parts of the strategy.

The roles and attitudes of the members drawn from the savers and general public will be crucial in cementing the processes and practices of the CBP in its day-to-day operations. For regulatory accountability, the credit union will retain its distinct identity though it would have a close working partnership with the CRT and the charity. The charitable company (or in future potentially a 'community interest company') in the 'group' will enhance both the ability of the credit unions and the CRT to meet their target markets

through attracting additional charitable funds and grant aid. This proposal is deliberately vague about staffing, but theoretically the CBP should not preclude any individual simultaneously holding posts within the loan fund, a credit union, and the CBP. In fact a combination of these would possibly be the most efficient and desirable outcome.

With regards to funding, since the beginning of this research the Treasury have announced a Financial Inclusion Fund and a Financial Inclusion Taskforce. Further details of these initiatives will be released in the autumn, but it is speculated that the Financial Inclusion Fund may be operated similarly to the SBS Phoenix Fund, which funded enterprise loan funds. This was a competitive fund that supported projects most likely to be successful, those with strong business plans, those targeting hard to reach groups, and those employing imaginative, innovative, and partnership based solutions. The CBP proposal presents Leeds with an opportunity to fulfil these objectives, placing partners in a healthy position to bid for funding.

Figure 10-2: Community Banking Partnership - possible structure

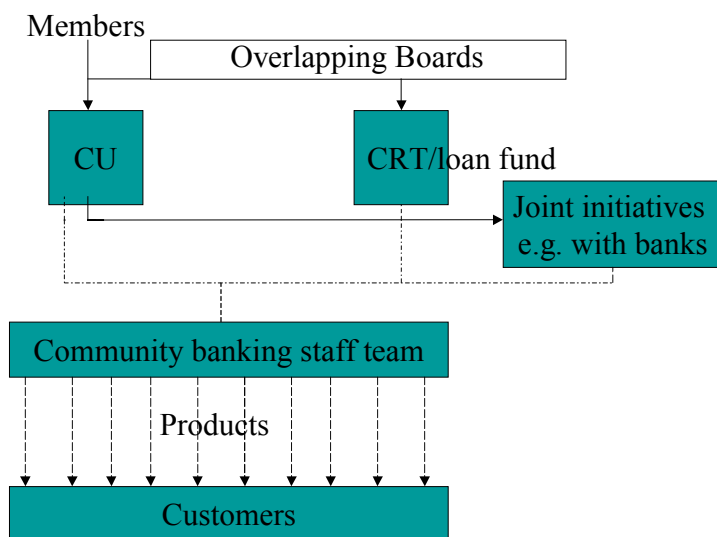
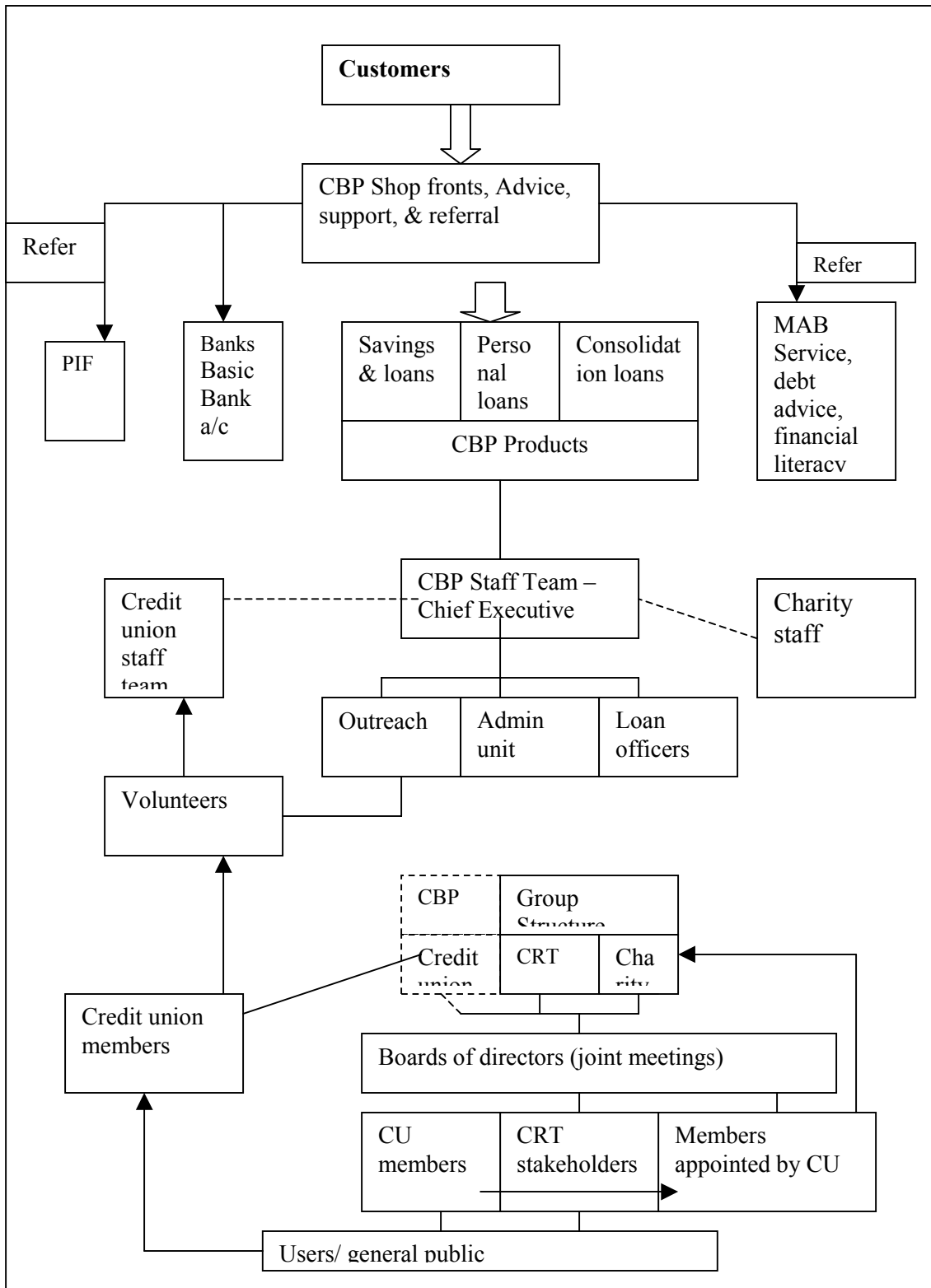


Figure 10-3: Community Banking Partnership - possible structure (detailed)



This report has demonstrated that there is considerable demand for greater investment in advice services and that many residents and enterprises are not accessing services. It went on to discuss the current provision and highlight potential gaps. The most notable of these was the absence of an over-arching strategy. In the final section a number of modes of delivery for elements of a strategy were considered. The CBP is by far the most complex and challenging of the options discussed but it offers a genuine opportunity to develop a sustainable and holistic solution to financial exclusion. Furthermore it is a partnership based approach that offers ‘additionality’ to existing providers, while maximising the opportunity presented by the proposed Financial Inclusion Fund. The other alternative options all have the merits but are reliant on the goodwill of existing agencies. If financial inclusion is to become a strategic priority it would be incongruous to base it on informal connections. It is on this basis that CBP is the recommended option, though this should occur in tandem with enhancing existing providers as discussed in 10.3.