

Financial exclusion

Financial Services Consumer Panel response to: HM Treasury's Financial Services Policy Action Team consultation on financial exclusion

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Introduction

1. This document forms the response of the Financial Services (FS) Consumer Panel ("the Panel") to HM Treasury Financial Services Policy Action Team consultation on financial exclusion. It was prepared by a sub-group of the Panel with direct experience of working with low income groups.
2. The FSA established the Panel to advise the FSA Board on the interests and concerns of consumers and to report on the FSA's performance in meeting its statutory obligations. There are eleven panel members,

representing a broad range of consumer interests. The Panel is independent of the FSA – it can: raise its own concerns, initiate research and publish reports.

The complexity of financial exclusion

3. Financial exclusion is a complex issue with a number of dimensions including the access to products and services; the level of awareness of what is available; and the suitability of products/services for low income groups.

'Poor' individuals and 'poor' communities

4. Individuals may exclude themselves from financial services. Products/services are available but 'exclusion' may be due to a lack of awareness or a choice not to use 'services' which incur costs. Additionally, for many it is not the low income *per se* but the regularity and volatility of their income that makes the current design of financial products unsuitable.
5. A distinction needs to be made between individuals and communities. Individuals are excluded but area effects can also occur. For example it is conceivable that within largely affluent areas there will be a significant number of individuals whose circumstances will cause them to be excluded from using financial services and products. This is likely to apply to both urban and rural areas. In rural areas the issue will be the availability of facilities within reasonable distance of the rural poor for whom transportation (cost and access) is a barrier.
6. Higher rates or charges may also apply in certain geographical areas. The poor pay a higher proportion of their income and a higher price for financial services/products. See the section on House content insurance.

Provider barriers or self-exclusion

7. It is not clear to what extent the assessment criteria employed by financial providers exclude individuals compared with self-exclusion through ignorance of products or eligibility.
8. There is emerging evidence that a significant number of low-income consumers are self-excluding themselves from basic financial services through a belief that they would not be eligible. In some instances where people need basic paying in and cheque accounts they are not aware of their availability or that they would be eligible for such accounts.
9. The Panel also acknowledged that there are or will continue to be a proportion of people who will never use financial services or products for structural or demographic reasons. There are some whose income may be so low or sporadic that they will never consider certain financial products as something that they can afford or make use of - household insurance is an example. For others, particularly the very elderly, for whom lifetime financial transactions have been purely cash based, their conversion to the usage of more than the very basic financial services may be a lost cause. Demographic changes will reduce the size of the latter group. The former group may require more specific social policy measures rather than through action by the financial service sector.

Access

10. It is unclear to what extent the physical presence of a facility is required to allow access to services. The employment of new technology may provide one possible means of allowing greater access to financial services for example, through the telephone and computer. However, these electronic means of access are disproportionately concentrated among high compared with low-income groups. Thus, low cost electronic provision may not be the solution for increasing access in the short to medium term.

Promotion of Good Practice

Social and economic policy

11. There may be some argument for legislative requirement or encouragement for financial service providers to either locate in certain areas or to provide certain types of product or service. Where this compulsion is felt necessary it will be as much a decision based on social policy as on economic policy. That will require legislation from Central Government.

The Cruickshank Review of UK banking services

12. The scope of the Cruickshank review should be extended to look at incentives for socially responsible lending. This issue should not be excluded from such a review of banking services.

The cost of regulation and its affect on service provision

13. The cost of regulation to small or low cost providers needs consideration (e.g. what scope exists for low cost providers or those with products/services aimed at low income groups to 'pay' less for regulation). Credit Unions are likely to come within the FSA's future scope and it will be incumbent on the FSA to consider what type of regulation is appropriate and cost effective. We would hope to be involved in discussion with the FSA as this policy evolves.

Debt counselling, money advice

14. The voluntary sector, is the main provider of debt counselling and money advice. In many areas they are unable to meet the level of demand being made upon them.

15. Greater funding and support need to be provided through a partnership of government (local and central), the private sector, and regulators.

Good practice

Access

16. In areas where individual banks and building societies may not consider the establishment of an outlet to be viable access may be improved through a number of conduits.

Social Fund

17. **The Social Fund** is already an established means of access to 'loans' for low-income groups. Given the established network ways should be found to extend the Social Fund so as to negate the use of unlicensed money lenders.

Post Office

18. **The Post Office** has an extensive network of branches, many run as agencies. One suggestion is for banks and building societies to link into this network for the provision of basic banking services. This idea could be extended to making use of other existing facilities through which physical access may be provided to basic services e.g. public houses, shops, news agents etc etc which form a focal point for local communities.

'PayPoint'

19. **The 'PayPoint'** system currently used for paying utility bills and local authority community charges and rent should be investigated for the provision of basic banking services – paying-in and cheque accounts.

Local shops

20. **Local shops** could provide a means of operating small value and flexible savings accounts.

Products

House content insurance

21. Low income groups often consider themselves unable to afford household insurance. The poorest individuals often live in high crime areas that incur a loading on premiums. However, even in some affluent areas there are pockets of deprivation with significant numbers of residents with low income. Such areas are often highly rated in terms of insurance premiums. This can be seen in Inner City areas such as the London boroughs of Islington and Wandsworth. While the higher income groups in such areas can afford the loaded premium those on low incomes do not consider household content cover to be of sufficiently high priority to allocate expenditure within their more limited budgets.
22. It is suggested that security could be improved in the homes of such groups. In part this would require social policy action through the local authority, or even central government grants, for improved house security as a preventative measure against burglary.
23. A further suggestion is for some form of low-cost area insurance scheme administered by the local authority or housing associations. Such schemes could be administered alongside implementing physical prevention measures to secure reductions in premiums.
24. The redesign of products is a further suggestion. The provision of indemnity insurance schemes is suggested as a way of providing less expensive products to low income and vulnerable groups. The new for old policies offered by many providers may not be necessary for low-income groups.

Life Insurance (including pensions)

25. Life insurance, pensions and similar long-term savings are low on the list of priorities of many low income individuals. Immediate expenditure needs are met first.
26. Two issues arise for this product area: What is needed? Cost and flexibility of products
27. The industry does not often promote the low cost or basic products that would meet the need of low-income consumers.
28. There is a need for basic level products to meet more tangible financial costs on the horizon, for example funeral plans and low cost term insurance.
29. Government proposals to introduce stakeholder pensions (SHP) are intended to increase the range of suitable pensions for those on lower incomes, but suitability will remain an issue. A wider look is needed at the taxation system in general and how it impacts on those who do not have the resources to make arrangements to minimise the tax impact on their financial planning.

Savings and borrowings

30. The emerging research is suggesting that the need among vulnerable and low income groups is for saving and borrowing facilities that operate with small values. The uneconomic cost of servicing such small sums is one of the arguments put forward by financial institutions for not providing such facilities.
31. Low income groups seem in need of funds to replace household items or meet emergency demands. Investigation should be made of how existing mechanisms can be extended for operating small saving and borrowing accounts.

32. It has already been suggested above that the Social Fund could be extended to meet this need, and 'shops' could be licensed to operate small savings accounts. Credit Unions are put forward as one means of meeting this need and is discussed next.

Credit Unions

33. The work of existing credit unions is applauded. However, some doubt is expressed as to how much they form a solution to financial exclusion. Not enough is known about credit unions and whom they serve – do they mainly serve those who have access to other sources of finance or those who would necessarily be classified as low income.

34. It would appear that those currently excluded from financial services and products want to deal with mainstream providers not the alternatives. Mainstream providers give the less sophisticated financial consumer a greater sense of security about their money. To this end it is felt that some encouragement to develop credit unions which have links to mainstream financial providers may be a way forward.

35. The Kempson (Savings and low income and ethnic minority households, PIA, 1998) report on informal saving clubs among black and minority ethnic groups identified a source of savings and 'loans' for low income or excluded groups. It is not felt that formalising or greater regulation of this sector would be advantageous. Much of its strength depends on its informality and trust between group members.

36. Some examination is needed of the impact of regulation on credit unions and other small value service providers. And, we would expect the FSA to take account of this in developing the regulatory framework.

37. More detailed examination is required of the experience of credit unions in countries where they are more successful, for example the Netherlands and Ireland.

Examples of good practice

38. Examples not detailed above.

- Home Improvement Trust, Nottingham – equity release scheme linking those who need services with providers.
- Hackney local business link (HLBL) – HLBL is a local authority funded unit that provides support to local small businesses. It helps small businesses to secure funding for start up or expansion plans by assisting them to put together business plans and providing a guarantor for loans.
- Bank of Scotland. Basic financial product developed for low income consumers using cash-card and ATMs.