REPORT TO: POLICY AND RESOURCES COMMITTEE – 26 NOVEMBER 2012

REPORT ON: HIGH INTEREST RATE LENDERS

REPORT BY: CHIEF EXECUTIVE

REPORT NO: 436-2012

1. PURPOSE OF REPORT

This report is for the purpose of informing members about the effects of easy access to high interest rate loans and credit, and to greater regulation of that industry.

2. RECOMMENDATIONS

It is recommended that Committee instructs the Chief Executive to:

a) write to the UK Government recommending that it introduces regulations to cap the interest rates charged to borrowed by high interest lenders

b) write to the Scottish Government requesting that it investigates whether there is any action it can take within its existing powers to assist people in debt due to the policies of high interest lenders

c) write to both Governments encouraging them to maximise support and investment in the expansion of the credit union movement

3. FINANCIAL IMPLICATIONS

There are no financial implications.

4. BACKGROUND

4.1 Credit and lending has long been an established element of the fabric of society and how it functions. It has put homes, holidays, university education and so on within the reach of people who would otherwise not have had the capital to pay for them. It has enabled people to achieve better standards of living and can contribute to economic growth. Responsible lending can serve the common good.

4.2 Money advice agencies in Dundee are reporting escalating levels of personal debt experienced by their clients, and in particular the impact of easily accessed loans at high interest rates. See Appendix 1.

4.3 High interest rate lending falls into two main categories - Doorstep lending, where payments tend to be via collectors calling at borrowers' homes, and un-secured short term loans, commonly called 'Payday' loans.

a) <u>Doorstep Lending</u>

Loan amounts are typically small, £100-£500, and are usually paid in cash with loan repayments also in cash over a period of around a year or less. Interest rates typically exceed 250% APR. One well-known company's website currently shows that a £200 loan repaid over 32 weeks would cost £320 (399.75% APR)

b) Payday Loans

These lenders advance short-term loans to be repaid on the borrower's next pay day by means of a post-dated cheque or authorisations for a direct debit on the borrower's bank account. Charges tend to be typically anything from £15-£30 per hundred borrowed.

Some payday loan companies, many of whom are currently investing in high profile advertising campaigns, can charge interest at over 4000% APR.

One leading Pay Day Loan company's website includes a loan calculator which shows that a £400 loan, the maximum allowed for a first time borrower, to be repaid in 30 days, will cost £525.48 if paid back on time – an APR of 4,214%. However, elsewhere on the website borrowers are advised that if the pay back date is missed, interest will be added at 1% per day for up to 60 days, adding an extra £315 in interest plus a £20 penalty – a total owed at the end of 3 months of £860.48. It is estimated that as many as 16% of their customers miss pay back dates.

Debt advice agencies have expressed concern that not only are these cost implications not made clear, but the speed of processing these loans and depositing them in customers' accounts is such that they have doubts about whether adequate checks are carried out on customers' income and ability to repay. In January 2012 Citizens Advice Scotland and Shelter jointly issued a statement expressing concern about the huge number of people taking out payday loans and other credit to pay rent or mortgages.

4.4 Addressing these practices would require action at a UK and Scottish Government level. This would require the UK Government to introduce greater regulation of the high interest rate lending and credit industry. In addition, the Scottish Government may be able to make a positive contribution by investigating whether it can take action within its existing powers to create mechanisms to support people facing the result of rapidly increasing costs associated with an inability to repay loans within the required period.

4.5 Dundee City Council, through its Financial Inclusion policies and strategy, has encouraged the development and expansion of the credit union movement in the city, and with support credit unions could achieve the scale of penetration into the savings and loans market that can make them self-sustaining and a long term source of affordable credit for people who might otherwise be excluded from the benefits of modern financial products. Further encouragement and support from UK and Scottish Governments could accelerate the success and expansion of the credit union movement.

5. POLICY IMPLICATIONS

This report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality and Impact Assessment and Risk Management. The recommendations in this report aim to secure legislative protection for financially excluded people and will therefore support the Council's anti-poverty objectives.

6. CONSULTATIONS

The Director of Corporate Services and the Head of Democratic and Legal Services have been consulted in the preparation of this report.

7. BACKGROUND PAPERS

None.

David K Dorward
Chief Executive ………………………………… 19/11/2012

Appendix 1

A recent Dundee Citizens Advice Bureau Case Study

The past 12 Months have seen a noticeable increase in debt clients needing help with payday loans. The following case highlights one example:

Joe (not client's real name) found himself struggling with his credit card payments. His credit rating became impaired due to missed payments; default notices and his debts were increasing with ongoing interest.

He then found out about payday loans, after applying for one he was instantly approved and the money was granted almost straight away. He then faced the problem of paying back the loan. Each payday the loan was rolled over leaving him with even less money every month due to the charges applied - £425 to payback £300. Joe became reliant on payday credit but he soon found he was facing debt repayment at the month end which exceeded his net wages.

Joe then became ill and was off work sick (with depression and anxiety). He advised that when he could not sleep he used to go online and open his online bank account up, open gambling websites up and he would open 2 or 3 payday loan websites up also.

He would apply for the payday loans, then check that they had been put into his bank account and then he would use the money on the gambling websites, (this goes to show how accessible and readily available these loans are)

In desperation Joe applied for a loan through a broker who took an upfront payment of £80 and assured him that they would find him a loan suited towards his circumstances. After two weeks of silence the broker rang to say his application had been declined and that the administration charge was non-refundable, it was then that Joe realised the difference between loan brokers and actual loan companies.

Joe contacted the Citizens Advice Bureau to speak with a money adviser, and completed income expenditure calculations before discussing different debt options. It became apparent during the interview that 8 out of his 10 creditors were in fact payday loan companies. Joe favoured a pro rata debt management plan and this was put into action. Initial holding letters were sent out introducing us and advising his creditors that we would be managing his accounts for the foreseeable future.

The majority were more than happy to supply all the relevant information so that a pro rata repayment plan could be put together, however 3 of the payday loans were very uncooperative.

One payday loan company refused to deal with us directly and instead opted to call the client 6 or 7 times daily threatening him and demanding payments they also advised the clients that they do not discuss or negotiate with any debt management companies and they also threatened to send Sheriff Officers to Joe's address.

The payday loan company was called advising that their phone calls breached Clause 1.20 of the Office of Fair Trading guidelines on debt management, which quotes:

"Where payments are tendered, not by the debtor personally, but by someone acting on his behalf, it is a principle of law that creditors cannot refuse to accept those payments. The practice of creditors returning payments, or not crediting payments to consumers' accounts, purely because they are received through a DMC, therefore, is not acceptable and is a matter which the OFT regards as seriously detrimental to the fitness of the creditor. This is so even in circumstances where a creditor has indicated that it will not negotiate with a DMC acting as a representative of the debtor".

The payday loan company was also reminded that the threat to send representatives to his address was a breach of clause 2.12 of the OFT guidelines on debt collection.

Joe is now making inroads into his debts and hopefully it won't be long before he has cleared all of his debts. He is now back at work and his wages have increased and he has regained some quality of life. He has also been advised that Discovery Credit Union as a good source of saving and low interest borrowing.

It is the experience of the debt adviser that when dealing with payday loan companies negotiations to get interest and charges frozen are more difficult. When telephoning a payday loan company, , the call is dealt with in either South Africa or Illinois in the USA. It is often easier and more effective to communicate with payday day loan companies via email and cc the client into emails (and vice versa) It is not uncommon for clients calling into the CAB with debt problems to have payday loans included in their debts.