

## **Evaluation of Community Banking and Local Provision of Banking and Financial Services**

### ***A Citizens Information Board Submission***

#### **Introduction**

The Citizens Information Board (CIB) very much welcomes the independent evaluation of how community banking and the local provision of banking and financial services can best be achieved. This evaluation is critically important in the context of developing and enhancing community banking to help address issues relating to: (a) financial exclusion and (b) the matter of easy access to credit for small-scale enterprises. CIB is pleased to make a Submission to Indecon on the matter. The 2018 Joint Report on Local Public Banking in Ireland Report/proposal is to be welcomed in its proactive search for banking solutions better tailored to the needs of Irish society.

There are two aspects of the local provision of banking and financial services that are centrally relevant:

- 1) The issue of financial exclusion and the role of community banking in addressing it
- 2) The development at local/regional level of alternative banking models

At the outset, we wish to state that we believe that there is a fundamentally important distinction between the local provision of banking and financial services and community banking. Local banking and financial services deliver the wide range of banking and financial services available from the national pillar banks with a particular emphasis on the provision of finance to support and stimulate SMEs at local and regional levels. Community banking, on the other hand, has broader objectives and includes enhancing financial inclusion to ensure individuals can access banking and financial services as well as supporting rural and regional economic development. Unlike conventional banks or other lending institutions, the funds that community banks lend to borrowers are typically gathered by the local community itself and the community has more control over its operations and lending priorities. Community banks seek to cater for the financial needs of all members of the community.

The 2018 Joint Report noted the many positives in the concept of local public banking in terms of increasing access to finance for SMEs and supporting local communities and regional development. It highlighted the positive contribution by An Post and Credit Unions to the Irish banking sector, particularly in rural areas. However, its primary focus (and the focus of the current evaluation) is on examining the concept of local public banks in order to provide additional competition in the financial services market. This focus, we believe, is too narrow in that it does not include the equally important aspect of community banking as a means of addressing the issue of financial exclusion.

The primary goal of the proposed local public banking model as set out in the Joint Report is to achieve regional development through the support of a banking infrastructure that can support

a vibrant indigenous productive sector. While this is clearly an important consideration, from a CIB perspective, there is another and more fundamental issue which needs to be addressed. Despite the introduction of a Basic Payment Account system in 2016, there is a significant segment of our population who continue to be excluded from financial services and products which means that they cannot play an active and productive role in social and economic life.

The Joint Report concludes that there is no impediment to organisations such as Irish Rural Link engaging with the Central Bank, the credit union sector, An Post or any other private sector body in developing additional financial services without state funding. CIB believes that such an emphasis would not completely address issues of financial exclusion and the underlying objectives of the 2011 Strategy for Financial Inclusion.

### **Focus of Submission**

This Submission is based on previous submissions and reports compiled by Money Advice and Budgeting Services (MABS) and CIB in recent years in which a broad range of issues relating to financial exclusion, access to banking and credit have been identified. Many of these submissions have highlighted concerns about people who cannot gain access to mainstream financial services.

A common feature of the lives of citizens who use CIB supported services - Citizen Information Services (CISs), Citizens Information Phone Service (CIPS) and MABS - is their multi-faceted income support needs.<sup>1</sup> These citizens are typically trying to maximise household income using the optimum combination of income from available work (very often part-time and atypical) and social welfare supports. MABS, in a submission to the Joint Oireachtas Committee<sup>2</sup> considering the Local Banking Report, highlighted that many of their clients who have experienced mortgage or other debt problems had impaired credit ratings and consequently poor relationships with banks and other financial service providers – however they have a continuing need for banking services and access to affordable credit.

CIB support for MABS activity broadly reflects the concept of people being able to ‘belong’ financially and promotes an inclusive approach to people who experience financial exclusion and/or indebtedness or blockages arising from the digitalisation of vital services.

### **Government initiatives**

Various measures have been put in place and/or supported by Government over the years to support people on low income and/or experiencing over-indebtedness:

- Provision by all main banks of a basic payment account
- A new Smart Account currently being rolled-out by an Post
- A new regulatory regime for Credit Unions

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<sup>1</sup> In 2018, CISs respectively dealt with 1.017 million queries and 574,096 clients. MABS supported over 40,000 clients via its national Helpline and face to face money advice casework service.

<sup>2</sup> MABS submission to the Joint Oireachtas committee examining the Local Banking Report. [https://www.mabs.ie/downloads/reports\\_submissions/MABS%20opening%20statement%20Government%20report%20on%20Local%20Public%20Banking%2023%20Oct%20....pdf](https://www.mabs.ie/downloads/reports_submissions/MABS%20opening%20statement%20Government%20report%20on%20Local%20Public%20Banking%2023%20Oct%20....pdf)

- Macro-prudential rules on mortgage lending
- The Code of Conduct on Mortgage Arrears and the Mortgage Arrears Resolution Process and personal insolvency provisions
- ABHAILE, and the Dedicated Mortgage Arrears Advisory Service within MABS which provides expert supports for borrowers in late-stage mortgage arrears;
- A new credit register
- The personal micro-credit initiative (implemented by Credit Unions with involvement by many other stakeholders including CIB and An Post)

The latter scheme ('It Makes Sense') which CIB was actively involved in setting up has proven to be very successful. Indeed, CIB regards the personal micro credit loans as the first step of many which could change how credit for low income borrowers is administered in the Irish market. Initiatives such as interest rate adjustments to make micro credit attractive to social-oriented lending institutions, as well as interest rate thresholds to deter high cost moneylenders, could significantly benefit low income households.

Various initiatives have also been put in place to enable access to finance by SMEs. These include the Strategic Banking Corporation of Ireland, the Supporting SMEs Online Tool, the Microenterprise Loan Fund, Local Enterprise Offices, the Credit Review Office and the Credit Guarantee Schemes.

CIB notes that An Post is committed to working with the Government to fulfil the obvious demand for further financial and banking services for retail customers and SMEs nationwide into the future. Both the Irish League of Credit Unions and the Credit Union Development Association (CUDA) have welcomed the 2018 Joint Report on Local Public Banking and see significant potential for credit unions in an expanded financial services sector.<sup>3</sup>

### Financial exclusion

People who live on low incomes are often excluded from mainstream financial services and are therefore frequently forced to make sub-optimal choices when accessing financial services. People in such situations sometimes do not have the time or resources necessary to weigh-up financial decisions due to the financial pressures they face in meeting day-to-day living expenditures. Financial exclusion is complex and multi-faceted and arises because of a number of factors, including:

- Lack of access to day-to-day banking
- The non-availability of accessible, expedient and low-cost payment mechanisms
- Lack of affordable forms of credit

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<sup>3</sup> The Public Banking Forum of Ireland (PBFi) has proposed an alternative banking force comprising a network of new regional public banks in Ireland, along the lines of the German Sparkassen banking model. The proposed new public banks would combine with Credit Unions and Post Offices, using their existing branch infrastructure to avoid duplication. This approach is broadly supported by Irish Rural Link.

<https://www.chg.gov.ie/app/uploads/2017/04/submission-by-pbfi.pdf>

- Inability to access and extract best-value from increasingly complex financial products provided not just by banks, but also through an increasing array of intermediaries.

A recently published International study '*Towards inclusive service delivery through social investment in the EU. The case of financial services*'<sup>4</sup> found that some groups are disproportionately represented in the financially excluded population: lone parents, young people between 18 and 25 years of age, students, unemployed people, single people without children, retired people with low level of education and rural residents. Financial exclusion has been identified in that report as arising because of both supply and demand factors. Supply factors include:

- Risk assessment procedures discriminate against the low-income groups;
- Targeting of richer and educated clients (as in advertisements) could lead to other clients not approaching financial institutions;
- Unclear or restrictive terms and conditions may effectively exclude certain sections of the population;
- Delivery of online financial services, may not be suitable for people on low income for affordability reasons or for those with limited knowledge of and access to digital technology (e.g. older people);
- The financial market does not provide an appropriate service and product to meet the needs of specific groups (e.g., low income households).

Demand factors (self-exclusion factors) identified include:

- Perception that bank accounts and formal financial services are not for 'poor' people
- Lack of information about costs and perception of cost of financial services to be unaffordable
- Lack of trust in the viability of financial institutions and fear of loss of control over non-cash financial resources
- Negative previous experiences such as being refused a financial service
- Fear of seizure of assets or income in case of default

CIB strongly agrees with the conclusion of the 2018 European report referenced above that it is *not* the lack of competitiveness and inefficiency of the financial sector, as argued by the EU that lies behind financial exclusion...*"the fundamental cause of financial exclusion is low and*

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<sup>4</sup>Messkoub, M. (2018). Rotterdam/Leuven: Erasmus University, IISS/HIVA-KU Leuven. This study explores the link between the EU Social Investment Package and availability, access and use of financial services. Ireland is deemed to be in the medium – high group of financial exclusion (12 – 28%) along with Italy, , Portugal, Greece, Estonia, Czech Republic, Cyprus, Malta, Slovakia. <http://www.re-invest.eu/>

*precarious income that cannot meet current household needs and their unexpected expenditure.*<sup>5</sup>

It is widely recognised that access to financial services is a key component in social inclusion<sup>6</sup> and that some people, e.g., welfare dependent families and indebted households, may experience difficulties in securing access to financial services, including basic banking services. People who find themselves excluded from the range of financial services and products generally available to the public are likely to be further marginalised.

Additional challenges have emerged in recent years as a result of disappearing bank branches, a move to transact business online and limited transaction services available in remaining branches. Use of financial services can also become more difficult as a result of physical/sensory disabilities. For people who are affected by mobility issues, travelling to bank branches or ATMs can pose a challenge. The lack of financial services infrastructure, especially in rural areas, is a particular barrier to financial inclusion for this group. Complex sets of rules and procedures associated with financial products can leave the individual consumer in a weak and vulnerable position *vis a vis* the provider.

Those who do not have a bank account can find money management and bill payment more time-consuming and costly and they can face difficulties accessing affordable credit and accumulating assets (e.g. savings, insurance). Financially excluded individuals are also at risk of over indebtedness.

- People excluded from services, products and cheaper offers as they could not pay by way of direct debit. Higher charges are thus being imposed on the poorest to simply pay their regular household bills;
- Mental health issues arising from over-indebtedness and money management difficulties are obviously compounded by financial exclusion

Having a current bank account is a crucially important consideration for daily living in that it allows people to access a range of services, including access to cash, bill payment facilities and money transfers. It also acts as a gateway to a range of other financial products such as credit and insurance. However, it is estimated that about 1 in 5 of the Irish adult population live without access to a bank account. The reasons for this in Ireland are varied and include account closure due to arrears, bad credit rating, inability to afford bank charges and low income exclusions. A 2016 study<sup>7</sup> undertaken with a sample of MABS users living without current bank accounts, reported that they experienced not only these consequences but other exclusions

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<sup>5</sup> *Ibid.* p.4

<sup>6</sup> Financial Exclusion and Over-indebtedness in Irish Households, ESRI  
<https://www.esri.ie/publications/financial-exclusion-and-over-indebtedness-in-irish-households>

<sup>7</sup>Harris, G, (2016), 'A study of the causes and effects of living without a current account in Ireland 2016 as experienced by a sample of clients of the Money Advice and Budgeting Service', Masters in Social Research Skills, School of Criminology, Politics and Social Policy, Ulster University.

which resulted in self-exclusion. Managing limited household resources, limited income and bill payments outside the banking system are more costly and time-consuming. The research concluded that public policies in place are not sufficiently protecting MABS clients from being unbanked and financially excluded.

A Basic Bank Account (available in Ireland since 2016) clearly can help to bridge the exclusion gap for people living on low incomes, social welfare supports or looking to return to work. However, while the basic account provides transaction banking, it does not provide for any access to credit facilities on the account.

SILC 2017 data shows that 15.7% of the population live in relative poverty with 6.7% in consistent poverty. Hidden behind these percentages are people who struggle with an additional layer of disadvantage because they are 'unbanked'.<sup>8</sup> These people are financially excluded because they have problems accessing mainstream affordable financial products such as current and savings accounts, credit, savings and insurance.

### **Financial exclusion and access to credit**

Access to credit is an issue for citizens in vulnerable situations and high-cost credit is a significant issue which can intensify the problems of those who are already in financial difficulty. Without access to manageable credit, people's options are greatly limited. It is very likely that lending decisions are frequently overly influenced by past credit history rather than rigorous assessment of current and future affordability. This is particularly important in the context of the many borrowers who were adversely affected by loss of income during the recession and the absence of affordable credit creates an ongoing vulnerability for this group.

In June 2018, CIB in conjunction with MABS prepared a submission in response to the Central Bank review of the Consumer Protection Code for licensed moneylenders. The submission stated that any review of the Code must be considered in the broader context of the alternatives available to low-income borrowers – noting that many MABS clients have few choices when considering credit options and are, thus, reliant on the moneylending sector.

### **The crucial role of Credit Unions**

CIB recognises the important role that the Credit Union sector plays and can continue to play in driving and promoting social finance and financial inclusion. Credit unions have traditionally played a central role in providing access to small emergency and budgeting loans to their members in Ireland. They are well positioned to play a key role in dealing with the overall problem of financial exclusion as was noted in the 2011 Strategy for Financial Inclusion.

The Credit Union movement was instrumental in the inception of MABS and informing its ethos and there remains strong links between the two organisations to this day. CIB believes that, irrespective of what local public banking model is put in place, the future of the Credit Union sector must be secured, not least, because the importance of their social ethos and the vital role they play within communities and society. Indeed, the 2017 Joint Committee on Finance,

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<sup>8</sup> Irish data on financial exclusion is out of date. For example, there is no current data on unsecured debt.

Public Expenditure and Reform, and Taoiseach Report on the Review of the Credit Union Sector recommended that greater emphasis should be placed on the issue of financial inclusion and noted the absence of a body in Ireland to examine/research responsible credit.

The Committee concluded that the credit union movement has the capacity to survive and flourish into the future and recommended the establishment of an independent body to examine and report to Government on an ongoing basis in regard to credit within the Irish financial services sector.

As Credit Unions extend their role and become more into line with mainstream banks through public banking initiatives, care must be taken that they retain a focus on lower income groups.

### **Developing a public banking system at local level: Key considerations**

Notwithstanding our concerns about the absence of focus on financial exclusion, CIB believes that many parts of rural and regional Ireland would clearly benefit from a public banking service and a model should be rolled out as quickly as possible. Any such model will need to address a number of diverse issues<sup>9</sup>:

- The broad issue of financial exclusion and related matters which tend to be strongly reflected in MABS casework
- The closure of bank branches and consequent impact on communities
- A perceived market failure in the provision of credit (to SME's in particular)
- The lack of competition in Irish banking and consequent cost of mortgage credit and cost of funds
- Providing a potential economic safeguard against a future banking collapse
- Enabling Credit Unions and Post Offices to more fully develop their potential

While understandably, the Government would wish to focus on combining public banking with a functioning and competitive private market and is fully supportive of increased competition in the banking sector, this focus is too narrow. The issue of financial exclusion needs to be fully acknowledged by Government and the deliberations around establishing a local public banking model provide an ideal opportunity to address this matter. It is not only a social inclusion matter but also a matter of enabling more people to participate in the productive economy. Put simply, people continue to need access to affordable, simple, and reliable banking and financial services and proper local public (community) banking can be a potential partial solution to the financial inclusion of those currently excluded. However, this clearly requires any public banking system to avoid the 'one size fits all' model of provision as offered by the main banks.

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<sup>9</sup>See Opening statement to the Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach's roundtable discussion on 'the recent Government report on Local Public Banking in Ireland, financial inclusion and related matters', Tuesday, 23rd October, 2018

[https://www.mabs.ie/downloads/reports\\_submissions/MABS%20opening%20statement%20Government%20report%20on%20Local%20Public%20Banking%2023%20Oct%20....pdf](https://www.mabs.ie/downloads/reports_submissions/MABS%20opening%20statement%20Government%20report%20on%20Local%20Public%20Banking%2023%20Oct%20....pdf)



Ireland can learn from the practice in other jurisdictions. For example, in a US model, banks are required to meet the credit needs of low income groups. One of the recommendation included in the European report referenced above is '*adoption of a US style affirmative regulatory system of Community Reinvestment Act (CRA) whereby financial institutions offering banking services are encouraged to meet the credit needs of the communities they operate in, especially in the moderate to low income areas.*<sup>10</sup>

### Financial education

As a general point, CIB notes the challenge faced by the majority of citizens/consumers in understanding the complex set of legislative and regulatory provisions and related protections relating to financial services and products. For some, the lack of an adequate income is at the root of their financial problems but for many this can be exacerbated by a low level of financial literacy. Many people are at a clear disadvantage *vis a vis* financial institutions and may have difficulty in applying the *caveat emptor* condition.

CIB believes that education and advice has an important role to play in addressing financial exclusion. Independent generic information on the financial products most suited to the target groups will need to be an integral part of the public banking system. More importantly, education in money management, to include knowledge, skill and attitudes, will be fundamental to the success and acceptance of any public or community banking initiative. Developing a more integrated approach to money management and debt prevention in society is necessary in order to help to address the significant underlying structural aspects of financial exclusion. Here, it is noted that one of the core objectives of MABS is to facilitate people experiencing debt to develop the knowledge and skills required to avoid getting into debt or to deal effectively with debt situations that arise.

### Concluding Points

- 1) There is a need to place much greater emphasis on the issue of financial inclusion in line with the Strategy for Financial Inclusion;
- 2) There is a need for a more focused discussion on how both the existing and alternative banking systems can address the issue of financial exclusion in a practical and sustainable way – this is missing from the current Joint Report;
- 3) Policy responses to a wide range of potential causes of financial exclusion call for an equally wide-ranging approach to tackling it;
- 4) The short-term and long-term credit, savings and investments consumption needs of people irrespective of where they are on the income and assets scale all need to be provided for;

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<sup>10</sup> Messkoub, M. (2018). Towards inclusive service delivery through social investment in the EU. The case of financial services (Delivery 6.3). Rotterdam/Leuven: Erasmus University, IISS/HIVA-KU Leuven, p.24



5) Any new public banking model must:

- Recognise low income consumers as having real potential as customers;
- Provide low cost overdraft facilities and low cost credit for low income groups along the lines of personal microcredit scheme – the reality is that some people require low value banking;
- Ensure that there is an appropriate balance between different banking objectives – the prudential side and consumer choice and protection;
- Achieve an appropriate balance between universal non-discriminatory banking and safe and sound banking;
- Address the banking needs of ethnic and transient populations – migrants , homeless people, Travellers (those who have difficulty with verification/addresses);
- Shift the onus from individual customer responsibility to banks' responsibility to engage with local communities and to identify local needs in banking provision and how these can be best delivered;
- Look at access to credit in the context of poverty and deprivation and the intrinsic link between over-indebtedness and financial exclusion.

Finally, CIB believes that a culture change is required in our approach to banking in which citizen welfare is taken into account as well as government spending priorities. We need to move away from a competitive approach to one that is based on collaboration in the context of enhancing social and financial inclusion and acknowledging that the banking needs of all citizens must be catered for. This needs to be addressed at both provision and regulatory levels. To this end, the scope of the current evaluation of public banking provision models needs to be broadened significantly. The establishment of the Irish Banking Culture Board will provide welcome opportunities to address the societal, and not just the economic, environment in which banks need to operate in the communities they serve.