CONSULTATION QUESTIONNAIRE (Page One)
Credit Union Debts in Protected Trust Deeds

The deadline for responses is **25 June 2007**

Your details

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For the purpose of analysing responses, it would be helpful if you would also indicate the capacity in which you are completing this questionnaire, please tick as appropriate.

Advice Sector	☐	Legal Body	☐
Business	☑	Professional Body	☐
Individual	☐	Statutory Body	☐
Insolvency Practitioner	☐	Other (Please Specify) _____	☐

Questions for Consultation

1a. Do you think that cancelling debt in a Protected Trust Deed has a particularly harsh impact on Credit Unions?

Yes ☑ No ☐

1b If yes, what evidence do you have to support your comments?

PLEASE SEE ATTACHED RESPONSE

1c Do you think that Protected Trust Deeds should give special protection to Credit Unions?

Yes ☑ No ☐

CONSULTATION QUESTIONNAIRE (Page Two)
Credit Union Debts in Protected Trust Deeds

2a Do you think that cancelling debt in a Protected Trust Deed has a particularly harsh impact on any other creditor?

Yes ☐ No ☐

2b If yes, what other creditors are affected?

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2c Do you think that Protected Trust Deeds should give special protection to any other type of creditor and which ones?

SEE ATTACHED RESPONSE

3a Do you think that introducing special protection for credit unions (or another type of creditor) would unduly harm the interests of the rest of the creditors?

Yes ☐ No ☑

3b If yes, what evidence do you have to support your comments?

SEE ATTACHED RESPONSE

4a Which of the following options do you think would be the most appropriate?

☐ Option 1 (Do Nothing) –The intended reform of Protected Trust Deeds will be sufficient to protect the interests of all creditors, including Credit Unions.

☑ Option 2 (Debts not Cancelled) - Debts due to Credit Unions should not be cancelled by Protected Trust Deeds.

4b Why do you think this option is most appropriate?

SEE ATTACHED RESPONSE

4c Do you have any other comments on these options that we should consider?

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Capital
CREDIT UNION

Credit Union Current Account

30th May 2007

Accountant in Bankruptcy
1 Pennyburn Road
Kilwinning
KA13 6SA

- 4 JUN 2007

RESPONSE TO CONSULTATION ON CREDIT UNION DEBTS IN PROTECTED TRUST DEEDS

Dear Sir/Madam,

Thank you for inviting us to tender our responses to the Consultation Paper on Credit Union Debts in Protected Trust Deeds. Our consultation questionnaire is enclosed with this letter. Our further detailed responses to the questions raised in the consultation are listed below along with the relevant question number where appropriate.

1b. What evidence do you have that cancelling debt in a Protected Trust Deed has a particularly harsh impact on Credit Unions?

It was extremely heartening to note that the Consulation Paper recognised the crucial and ground-breaking work which is being done by Credit Unions throughout Scotland in combating Financial Exclusion. It is important that the crucial differences between Credit Unions and other lenders is recognised at this stage in the consultation. Principally credit unions are **member driven** organisations which exist to serve the needs of their members within their common bond rather than the needs of a potentially much more diverse group of shareholders or even the financial markets who are ultimately most interested in bottom line return. We feel that that the fact that the raison d'etre of credit unions is to serve their membership rather than provide shareholder returns and profits is one of the key, and perhaps the most critical differential, that separates us from other lenders and enables us to pursue our financial exclusion agenda in the way that we do.

In practice this means that credit unions do not make loan decisions based around the perceived profitability of loans and do not price their various products in such as way as to compensate them for the cost of bad debt in the way that other lenders might choose to. Instead, in making a loan decision the critical factor within Capital Credit Union and other Credit Unions in Scotland is the ability of the member to repay the loan they have asked for. If a member is unable to meet loan repayments then it is of no benefit to either party (the member or the credit union) for the loan to be granted. The majority of Protected Trust Deed costs suffered by Capital Credit Union arise

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either because the debtor has taken out new debt with other lenders subsequent to borrowing from Capital or because they have maliciously topped up their borrowing shortly before signing a Trust Deed. We rarely if ever find that a credit union has chosen to lend to a member causing them to be over-committed and subsequently have to sign a Trust Deed.

Over the last two years the average balances owed to Capital Credit Union by members signing Protected Trust Deeds were £2,225. In only a single instance was the debt owed to the credit union greater than ten thousand pounds. This clearly indicates that it is not debt to credit unions which is pushing individuals into Trust Deeds, but rather irresponsible lending by other financial institutions. The impact of Trust Deeds on credit unions is significant not because of the individual value of each loan which is fairly low, but rather because of the increasing number of them being signed which aggregates up to create a substantial problem for the future viability of credit unions.

Other than assessing their ability to pay, Capital Credit Union do not otherwise rate or credit score our members. We do not cherry-pick and aim to treat all of our members equally irrespective of their own personal circumstances. We believe that we offer individuals in the community an opportunity to borrow and to rebuild their credit rating after they have been rejected by other mainstream lenders. This inevitably creates a level of risk for the credit union because many of these individuals do come with historic credit problems, but we feel that if we are to service the needs of our members that fall into this category then it is important that we assess all individuals based on their ability to pay their loan and not other factors. We are also limited in the range of interest rates we are permitted to charge unlike the majority of other lenders. Likewise we do not charge fees, either for setting up loans or for any other aspect of our business unlike many mainstream lenders who are able to rely on such fees as a significant source of income. If however the cost of Trust Deeds continues to rise in the way it has been then there may come a time when credit unions, including Capital, may be forced to cherry-pick the best loans and turn away some of the more risky applications we receive. The only alternative then for these individuals would be to turn to door-step lenders which is exactly what both the credit unions and the Scottish Executive are seeking to avoid.

Recent years have seen substantial increases in the number of Capital Credit Union members signing Trust deeds with 25 Trust deeds to a value of £65k being signed in 2005/6. Six Trust deeds were signed in the first four months of 2006/7, but following the recent change in legislation with the introduction of the Bankruptcy and Diligence (Scotland) Act 2007 a further 11 Trust Deeds were signed in the space of 3 months.

It was noted above that Credit Unions are not set up with a profit objective in mind, however it is necessary for Credit Unions to generate some level of return in order to compensate those members who choose to save with the credit union. Generating an adequate return to members to encourage them to continue to save with the credit

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procedures will occur with an increased emphasis on cherry-picking the best loans and avoiding those which are considered too much of a risk. In practice this would probably mean that individuals with security such as home owners would be preferred for loans whilst those with less assets and in most need could be turned away. This is certainly not a route which Capital, and presumably most other credit unions would want to go down, but if Trust Deeds continue to have the high profile impact they are having then they might not have any other option. Ultimately this leads to a loss in the potential of Credit Unions to combat Financial Exclusion and to further poverty amongst those most in need. The only winners are those individuals who chose to over commit themselves on consumer debt, enjoy a short period when then spend as they choose and then take the easy option, signing all of this spending away over the space of a couple of years and leaving themselves debt free.

A final difference between credit unions and other lenders is in our approach to the recovery of arrears amounts and potential bad debts. Capital, in line with many other credit unions, will only contact outside agencies for debt collection after all other avenues have been exhausted. If at all possible we will attempt to accommodate the needs to the member, where appropriate rescheduling loans, reducing loan repayments, cancelling interest and offering support and advice for members in arrears. We are always prepared to go the extra mile for members to help to keep them out of financial difficulties.

For all of the reasons above we believe that Credit Unions, including Capital, are particularly harshly affected by Trust Deeds.

1.c Do you think that Protected Trust Deed should give special protection to Credit Unions?

In addition to the comments above we believe that Credit Unions are so fundamentally different from other lenders that they deserve to be treated differently where Protected Trust Deeds are considered. We believe that all of the reasons listed above which differentiate us from other lenders provide justification for a different treatment under the terms of a Protected Trust Deed.

We feel that it would be perfectly fair for all lenders if debts due to credit unions were not cancelled at the end of the Trust Deed period. We do not feel that this would adversely prejudice other lenders who would be entitled to receive the same dividend from the Trust Deed that they would be entitled to without the non-cancellation of credit union debt.

Further we believe that because individuals would not have received loans from credit unions in excess of their ability to pay them back then we do not believe that any outstanding loan balance at the end of the Protected Trust Deed period would prove overly onerous on any individual. This is illustrated by the fact that the average amount owed by individuals signing Trust deeds to Capital was £2,225. In the event

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that an individual's circumstances had changed between taking out the loan and signing the Trust Deed, whether through the loss of employment, the break-up of a relationship or for any other reason, the credit union would of course take its normal sympathetic approach to the recovery of the debt and would not force through unfair claims against any debtor who was genuinely unable to meet the repayments.

2c. Do you think that Protected Trust Deeds should give special protection to any other type of creditor and which ones?

We believe that the proposal to protect amounts provided for student loans is also fair based on the criteria provided in the document. Any other claims from other creditors would have to be assessed on their own merits.

3a. Do you think that introducing special protection for credit unions (or another type of creditor) would unduly harm the interests of the rest of the creditors?

We do not feel that treating credit unions as protected creditors would unduly harm the interest of any other creditors. This is because all creditors would be able to make their normal claims and would receive the same dividend irrespective of whether Credit Unions were treated as Protected creditors or not in a Trust Deed. At the end of the Trust deed period, all other non-protected debts would be cancelled and therefore the fact that Credit Unions were able to continue to pursue the debts owed to them would not in any way impact on other creditors.

The only organisations which would be affected adversely by such a proposal would be other organisations which had also been offered protected creditor status who could find that the ability of a debtor to make payments to their remaining debt was prejudiced by payments to a credit union as a protected creditor. In these circumstances we would anticipate that this would result in the debtor making payments to both creditors over a slightly longer period until both debts were serviced.

4b. Why do you think the option to offer credit unions Protected Trust Deed Status is the most appropriate?

We believe that we have argued convincingly above that it is fair and correct for credit unions to be treated as a special class of creditor in the event of a Protected Trust Deed being signed. This is in part due to our ethos and in part due to the legislative and social environments in which we operate which not only expose us to a higher degree of risk than other lenders, but which also encourage us to serve those who have been abandoned or let down by the conventional banking system. We are committed to the rejuvenation of communities and need to ensure that we can fairly

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service the needs of all of our members. We want to ensure that there is fairness in the system and that decisions made by other lenders to overly burden individuals with debt do not adversely impact on innocent parties.

I hope that you will give due consideration to our response to the consultation paper. If you have any questions with regard to any of our answers please feel free to contact me directly.

Yours sincerely

Marlene Shiels

Marlene Shiels
Chief Executive Officer