

# Scottish Citizens Advice Bureaux evidence on the Banking Sector

A response from Citizens Advice Scotland



**Based on the evidence of  
Citizens Advice Bureaux  
clients across Scotland**

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**citizens  
advice  
scotland**

# Citizens Advice Scotland

Scottish Association of Citizens Advice Bureaux



## Scottish Citizens Advice Bureaux evidence on the banking sector

By Keith Dryburgh, Social Policy Officer

Citizens Advice Scotland and its 71 CAB offices form Scotland's largest independent advice network. CAB advice services are delivered through 199 service points throughout Scotland, from the islands to city centres.

The CAB service aims:

to ensure that individuals do not suffer through lack of knowledge of their rights and responsibilities, or of the services available to them, or through an inability to express their need effectively

and equally

to exercise a responsible influence on the development of social policies and services, both locally and nationally.

The CAB service is independent and provides free, confidential and impartial advice to everybody regardless of race, sex, disability or sexuality.

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The Scottish Association of Citizens Advice Bureaux - Citizens Advice Scotland  
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# Introduction

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1. Citizens Advice Scotland (CAS) is the umbrella organisation for Scotland's network of 71 Citizens Advice Bureau (CAB) offices. These bureaux deliver frontline advice services throughout nearly 200 service points across the country, from the city centres of Glasgow and Edinburgh to the Highlands, Islands and rural Borders communities.
2. In 2006/07, 91,475 new debt issues were brought to Scottish bureaux – an increase of 4% on the previous year. This represents more than 250 debt issues brought to Scottish bureaux each day of the year. Consumer debt remains by far the most common single issue that clients bring to bureaux.
3. Many of these debt issues are related to the UK banks, who are one of the main types of creditor used by bureau clients. Banks play an important role for the vast majority of adults in the UK. They are the gateway to mainstream financial services, the provider of current and savings accounts, and the main source of much needed credit. Banks provide mortgages to buy homes, capital for businesses, and are a necessity for anyone who gets wages for employment. Because of this important role that the banks have in UK society, the repercussions of poor policies and practices have a wide and sometimes severe impact on customers.
4. This role has increasingly come into the media spotlight in recent years following the OFT test case in the high court, the much publicised record levels of debt, and the economic downturn and financial crisis following the 'Credit Crunch'. However, what has been missed in all this has been the impact of bank actions on individuals. This briefing looks in detail at this impact, showing the policies and practices that adversely affect clients.
5. The briefing will focus on the problems experienced by Scottish Citizens Advice Bureau clients under the following headlines:
  - Opening and maintaining accounts
  - Bank charges
  - Irresponsible lending
  - Account management
  - Third party dealings

## Opening and maintaining accounts

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6. Personal current accounts act as a gateway for customers to access financial services, and as a basic pre-requisite for operating as a consumer in the economy. It is difficult to sustain employment, receive benefits, and/or secure a tenancy without a bank account.
7. Almost 1 in 10 adults in Scotland do not have a personal current account, rising to 16% of all adults in Glasgow.<sup>1</sup> This group of people either self-exclude themselves from mainstream financial services or experience difficulty in opening an account and holding on to this account when they get it. Consequently, there are many adults who go in and out of mainstream financial services and others who remain excluded on the sidelines.

### Opening accounts

8. The UK Government has a financial inclusion target of ensuring that all adults have access to a bank account. To this end, the UK banks have offered a basic bank account to adults without access to an account. The basic bank account idea has been a relative success: 7.6 million people have signed up for a basic bank account since 2003<sup>2</sup>, granting them access to mainstream financial services.
9. However, clients still experience problems in opening a basic account. The criteria for opening an account can be difficult for a client to meet. For example, clients need to have a form of identity to open a basic account even if they already have an account with the bank, including a passport, driving licence or utility bill as proof of identity. Many clients, especially migrant workers, do not have these forms of identification and cannot open an account.
10. Added to this, the Banking Code that provides guidance on how banks offer basic accounts is voluntary. Bank branches are not obligated to offer a basic account to a customer even if they meet all the criteria. Bureaux have seen clients who have been refused a basic bank account, when specifically asking for it, for a range of reasons, including a previous debt with the bank (even if this has been repaid), or a poor credit history.

An East of Scotland CAB reports of a client who had difficulty opening any type of account due to a poor credit rating. The client had started new employment and required a bank account for his wages to be paid into. However, he was told that he couldn't open an account with one bank as he held a debt with them. Another bank told him that they would require a photographic ID to open an account which he does not have.

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<sup>1</sup> Scottish Household Survey Annual Report 2007

<sup>2</sup> British Banker's Association - <http://www.bba.org.uk/bba/jsp/polopoly.jsp?d=1569&a=15130>

A West of Scotland CAB reports of a client who was refused a bank account due to a previous debt that had been repaid to the bank. The client was in debt to her current bank and was advised to open a basic account with another bank to have her benefits paid into. The client spoke to the branch manager about opening a basic account, with no overdraft or cheque book facility, which the client was assured was available to all customers. Three weeks after opening the account, the client was told that the account was now being closed as the client had had a previous debt with the bank – even though this had been repaid some years ago - and that the client should not have been offered the account in the first place.

## Maintaining accounts

11. The current policy of the majority of UK banks towards customers who have been made bankrupt is to close their account – which in turn can deny customers access to any funds in their account including state benefits - and to refuse to open accounts for undischarged bankrupts. The result of this policy is that clients who become bankrupt are often marginalised and excluded from mainstream financial services, risking their employment, benefit payments, and housing tenure.
12. This situation has moved up in the agenda in Scotland since 2008, with the advent of the Low Income Low Assets (LILA) route to bankruptcy in April. LILA allows debtors with a low income and high debts to make themselves bankrupt in order to release them from their cycle of debt. The LILA scheme has resulted in a jump in the number of personal sequestrations in Scotland, which is expected to be prolonged with a backlog of debtors accessing LILA coupled with the expected economic downturn.
13. There were 4,514 bankruptcies in the first four months of the LILA scheme from April 2008.<sup>3</sup> Assuming that the number of people accessing LILA remains constant in the short-term, this figure can be extrapolated to above 13,000 this financial year. This is around 1 in 300 of the adult population in Scotland who will lose their bank account this year and experience difficulties in opening another.

A South of Scotland CAB reports of a client who was awarded sequestration, but came back to the bureau in distress as her bank had frozen her account. The client's account only held her Pension Credit which she could not access. The bureau spoke to the bank, who said that a bankrupt person could not hold an account with them. The bureau managed to get the client access to her money, which she put into a Post Office Card Account.

<sup>3</sup> Accountant in Bankruptcy October 2008 –  
<http://www.aib.gov.uk/News/releases/2008/10/16122123>

A West of Scotland CAB reports of a client who had successfully applied for sequestration through LILA. She had her current account frozen by her bank without warning, leaving her without access to benefit payments. It took three weeks to resolve the issue and only a letter from the Accountant in Bankruptcy's office proved effective. In the mean time, the client was forced to borrow money to feed her family.

## Switching

14. The problems involved in opening and maintaining accounts affect clients in other ways. Those with accounts tend to stick with them, often through a misplaced sense of loyalty to their bank, which can have negative effects for the customer, including lost interest and the loss of benefit payments needed to repay overdrafts.
15. Past and current problems with switching has lowered client confidence in switching their own account, with the OFT market study into Personal Current Accounts<sup>4</sup> finding that almost half of consumers (45%) wouldn't be confident that the switching process would be smooth. These fears are borne out by the finding that over a quarter of clients who had switched their account had experienced problems.

A West of Scotland CAB reports of a client who experienced problems in switching her bank account. The client cleared her overdraft with her bank before changing to a different bank. Her new bank told the client that they would take care of transferring the direct debits to the new current account. However, a few months later the client received a letter from her original bank stating that she had gone over her overdraft limit of £1000. It transpires that the bank account was not closed and that direct debits have been going out of both accounts. The two banks are blaming each other for the mistake, while the client's original bank is threatening legal action to reclaim the overdraft debt. The bureau contacted both banks and has not received a response from either.

16. Many clients are disinclined to switch their account due to a negative past experience. However, a number of clients who have not switched their account have never even considered doing so. This is because they do not understand the costs of their existing account - which they perceive to be free of charge - and therefore have little understanding of the benefits of switching. Customers also display a misplaced loyalty to banks which they have been with for years, when they could be much better off with a different account. Bureaux have seen clients who have experienced significant financial difficulties through the retention of their existing account.

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<sup>4</sup> Personal Current Accounts in the UK July 2008 - <http://www.of.gov.uk/news/press/2008/84-08>

An East of Scotland CAB reports of a client who experienced significant financial and housing difficulties when his benefit payments were swallowed by bank charges. The client lost his job and was unable to continue his contractual obligations while on Job Seekers Allowance (JSA) and went into overdraft. The client's housing benefit and JSA were paid directly into his account, but all monies were swallowed up by bank charges for unauthorised overdraft, failed direct debits and default letters issued to the client. The client went into rent arrears and was evicted by the landlord. He is currently homeless and staying with a friend. The bureau arranged for the client's housing benefit to be paid directly to a landlord and another account opened for his JSA to be paid into.

17. Low levels of switching are a distinctive feature of the personal current account market, especially when compared to other markets in the UK. The OFT market study on Personal Current Accounts<sup>5</sup> found that the personal current account market has a very low level of switching, with only 13% of consumers having switched their account in the last five years. This compares poorly with the electricity (54%), gas (54%), and car insurance (61%) markets, as well as with other financial products, such as credit cards (31%) and savings accounts (20%).
18. The knock-on effect of low levels of switching is a lack of competition in the market, and clients are therefore unable to make the threat of switching to banks that provide a poor service. A lack of competition then manifests itself in poorer terms and conditions, as the main banks are not incentivised to offer better deals to win more customers.
19. Despite the lack of switching, it is clear that clients can benefit from moving to another bank. The OFT market study found that yearly savings from switching would range from £7.50 to £110, mostly through switching to an account offering a higher interest rate. Clients who persistently incur insufficient funds charges have potentially the most to benefit from switching their accounts.

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<sup>5</sup> Personal Current Accounts in the UK July 2008 - <http://www.of.gov.uk/news/press/2008/84-08>

# Bank charges

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20. Overdraft charges, or insufficient funds charges, has been a hugely significant issue for Scottish Bureau clients in the last five years. They are a contributory factor to the increase in the number of bureau clients seeking advice on debt, while bureau have been active in helping clients to reclaim unfair and disproportionate bank charges.
21. Our evidence shows that customers have little understanding of the level and likelihood of incurring overdraft charges. The system of overdraft charges is unclear and confusing for bureau clients who do not understand the charges until they start to incur them – and once charges are levied, they can be so high that they do not offer clients much of a chance to learn from their mistake.
22. Despite the outcome of the High Court case between the OFT and the UK banks in 2008, bureau clients continue to experience problems with their overdrafts and subsequent charges. This response will look at the problems under the following headings:
  - Disproportionate charging
  - Direct debits/standing orders
  - Item charges
  - Multiple insufficient funds charges
  - Unclear terms
  - Responses to client requests

## **Disproportionate Charging**

23. Scottish bureaux have seen a number of clients who have built up substantial charges for a very small overdraft. These clients often go into their overdraft without realising that they have done so, and find that they have incurred high overdraft charges at the end of the month.
24. These overdraft charges are often highly disproportionate to the level of overdraft infringement. This system inherently discriminates against low income customers, where the level of charges is insensitive to the level of infringement.

An East of Scotland CAB reports of a client with severe mental health problems who quickly built up substantial bank charges for an overdraft of £1.92. The client used her debit card for a purchase of £4.25, not realising that there was only £2.33 in her account. Over the next two months her overdraft of £1.92 grew to more than £180, solely as a result of interest and charges imposed by the bank. The client was very worried as to how she could possibly pay this from an income of £79 per week.

An East of Scotland CAB reports of a client who received excessive bank charges for a small overdraft. The client is a mature student who works part-time. The client went 60 pence into his overdraft and was charged £28 and a subsequent charge of £38. Since then, the client has been unable to clear his overdraft. The client only earns £50 per week, and finds himself in an impossible situation.

A West of Scotland CAB reports of a disabled, lone parent who was given an overdraft charge after exceeding her overdraft limit for one day. The client stated that she regularly checks the status of her account using the telephone services and was at no time made aware of a problem with her account. The client exceeded the overdraft limit on her account for only one day and feels that the £28 charge is excessive and unfair.

An East of Scotland CAB reports of a pensioner who received excessive charges for exceeding her overdraft limit. The client recently exceeded her overdraft limit by £46.74, with her bank statement showing charges of £170 for exceeding the limit. The client lodged a complaint about the excessive charge, but despite being a pensioner found that the local manager was unsympathetic to her situation.

25. Overdraft charges can have a significant impact on clients whose only source of income is benefit payments. These clients can budget in pennies, then find that a slight overspend can mean that they owe up to £100 in charges. A standard overdraft charge of £25 can be a daunting prospect for those living on benefit payments.
26. The consequence of this policy is that low income customers can very quickly be in a lot of debt to a bank due to a small overdraft. The customer's low income would then preclude any chance of getting out of the overdraft, thereby trapping the client in a cycle of debt.
27. The consequence of this cycle of debt is that clients begin to have their benefits – which are necessities for living - swallowed up by charges. Under the present system, benefits lose their identity when they reach the client's account, and are used by the banks for paying bank charges. This can leave clients with very little to live on.

An East of Scotland CAB reports of a client who has bank charges taken from her account each month even though her income consists entirely of benefits. The client gets about £40 per week, but this month's bank charge was £120, leaving the client with £10 a week to live on. The client is stuck in a cycle of bank charges that her limited income will not allow her to escape from.

An East of Scotland CAB reports of a client who experienced significant financial and housing difficulties when his benefit payments were swallowed by bank charges. The client lost his job and was unable to continue his contractual obligations while on Job Seekers Allowance (JSA) and went into his overdraft. The client's housing benefit and JSA were paid directly into his account, but all monies going into the account were swallowed up by bank charges for unauthorised overdraft, failed direct debits and letters to the client. The client went into rent arrears and was evicted by the landlord. He is currently homeless and staying with a friend. The bureau arranged for the client's housing benefit to be paid directly to a landlord and another account opened for his JSA to be paid into.

28. The system of overdraft charges impacts most severely on clients with low incomes. The charges do not discriminate between small and large overdraft infringements, or between high earners and low earners. The result is that low income clients are left with unaffordable charges that do not reflect their level of infringement or personal circumstances.

## **Unpaid item charges**

29. A common problem for bureau clients is high charges for unpaid items. This is particularly the case for missed direct debits and standing orders. These charges are for a high amount (commonly £35) and can be charged a number of times in the same month for a client with multiple direct debits. The impact of this is that a client who is not in their overdraft can be dragged over their overdraft limit by one missed payment and consequently incur a number of charges.
30. For example, a client who has £34 in their account and has a £35 direct debit to be paid from the account on that day will be likely to incur a £35 missed payment charge and then a £25 charge for going over the overdraft limit. This would leave the client with a £26 overdraft and liable to receive future charges – including the missed direct debit.
31. A client may have set up multiple direct debits for the same day. If the anticipated balance is not available to meet these costs, this can result in multiple charges for the client with disastrous consequences.

An East of Scotland CAB reports of a client who went into his overdraft and consequently was charged for missing nine direct debits. The client does not have guaranteed hours of work and already owed more than £15,000. The client's debt problems were aggravated by receiving £351 of bank charges for missed direct debits in a two week period. The charges are approximately the same as his monthly wage.

A West of Scotland CAB reports of a client who was charged twice for the non payment of a standing order. The client had insufficient funds for a standing order of £17 and received a charge of £38 for the 'unpaid item'. He put money into the account to cover both costs, but then received a letter from the bank advising him of an additional charge of £28 for an unauthorised overdraft relating to the same standing order. The customer feels that these charges are excessive and is being charged for the same thing twice.

A West of Scotland CAB reports of a client who returned from holiday to find that she had been charged for a missed direct debit as she was 2 pence short. The bank charged the client £35 for the missed direct debit. The client was extremely unhappy with the charge as she has been a customer with the bank for over 20 years.

32. Clients may be also charged for the number of items that they purchase while in their overdraft. These charges can be significantly and disproportionately high for a client who does not realise that they are already in their overdraft. The charges are very difficult to predict, as it is difficult for a client to know at what point they will start to incur the charges. The charges are also insensitive to level of the purchase, often charging the same set fee for a £2.50 food item as luxury goods costing £1000.

33. For example, a client that enters into their overdraft while on a shopping trip could incur charges for every item paid for over the limit. A client who buys three items over the limit could expect a £25 overdraft charge and three charges of up to £30 for each item – a total of £115 worth of charges.

A North of Scotland CAB reports of a client who has received excessive charges on items paid for when in his unauthorised overdraft. The client has an authorised overdraft of £2,000, but has occasionally been over this limit in the last year. His bank charges £30 for every item paid for over the limit, with a maximum of three such charges per day. The client has paid a total of £1,135 in overdraft charges in five months, mainly due to the item fees.

## Multiple Insufficient Funds Charges

34. The variety of different types of overdraft and similar charges – insufficient fund charges, missed payment charges, and item charges, among others - mean that clients can receive levels of charges that are massively disproportionate to the level of infringement. It is not inconceivable that a client could slip into their overdraft unknowingly by a few pounds, miss two direct debits, and buy three items while over the limit. Using the cases in the briefing so far, this could mean charges of nearly £200 for a small overdraft.
35. This is an example of a 'snowball' effect, in which a client enters their overdraft on one occasion and incurs multiple charges. This effect can cause severe detriment to clients and condemn them to an endless cycle of charges. Alternatively, clients may go in and out of their overdraft in the same month and incur a charge for each separate occasion.
36. Analysis by MoneyExpert.com found that the average total charges are £44.98 for an overdraft infringement and fees for an unauthorised overdraft can go much higher. Around 30 per cent of all current accounts charge a combined fee of £60 or more for straying beyond the borrowing limit.<sup>6</sup> By contrast, fees for defaulting on a credit card are a standard £12 after being effectively capped by a recent investigation by the Office of Fair Trading.
37. The upshot of the variety of charges that clients can incur has resulted in a substantial cross subsidisation from those who incur charges and those who do not. According to the OFT market study, and supported by our evidence, this cross subsidisation is from low income, low saving clients, to high income, higher saving consumers. Indeed, the revenue made from the customers who incur charges is actually keeping the cost of an account low for other higher income customers.

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<sup>6</sup> <http://www.moneyexpert.com/ContentArticle/None/Overdraft-mistake-costs-nearly-fourty-five-pounds-on-average/Article.aspx?articleID=237&productTypeID=0>

## Transparency and client awareness

38. A significant finding from the OFT market study is that consumers have a poor understanding of the consequences of going over their overdraft limit. Consumers often underestimate the likelihood of incurring fees and the cost of doing so. Nearly four fifths of consumers in the market study who had been charged in the previous twelve months had never heard of such charges, while only 7% of consumers knowingly went into overdraft.<sup>7</sup>
39. Evidence from Scottish bureaux suggests that clients can have little idea of the likelihood and the cost of incurring overdraft charges. Unfortunately, this is a mistake that can have long-term negative effects for a client.

A South of Scotland CAB reports of a client who incurred bank charges after assuming that his card would be frozen after he ran out of funds. The client did not know about bank charges, thinking that he would be told when he had no money. The bureau asked for a refund of charges, but found it very difficult to find somebody who would talk about the client's situation.

40. Clients need to take responsibility for knowing how their current account works and the charges for its misuse. However, banks have a responsibility for ensuring that the terms and conditions of use for current accounts are clear and understandable. This is not always the case. The OFT market study raised concerns over a 'lack of transparency' over 'less visible' terms and conditions in current accounts. This is borne out in Scottish bureaux evidence.

An East of Scotland CAB reports of a client who opened a student account upon starting her studies, and built up substantial charges without ever using the account. At some point, the client's account changed to a 'royalties account' which meant a charge of £6 per month for use of the account. Because there was a zero balance the £6 charge put the account into the red and a £28 per month bank charge plus interest began to be applied. By the time the client realised what had happened, she had a debt of over £300 and rising. The client maintains that she was not told that the unused account was going to be upgraded to the new fee-charging account nearly two years after she had initially opened the account.

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<sup>7</sup> Personal Current Accounts in the UK July 2008 - <http://www.of.gov.uk/news/press/2008/84-08>

## Responses to client requests

41. A significant problem for bureau clients is the attitude and actions that banks take when clients question or ask for reprieve from charges. The responses from banks to customer queries are unpredictable and erratic, and can adversely affect the customer.
42. Scottish bureaux have found that attempts to negotiate with banks over overdraft fees are often met with unhelpful attitudes.

An East of Scotland CAB reports of a client who had her agreed bank overdraft removed after sending the bank a letter requesting repayment of bank charges she felt were unfair. Upon receiving the letter, the bank removed her agreed overdraft, leaving her liable to charges once again, and gave the client a week to repay the overdraft (£600). The bureau feels that the bank's actions were retaliatory, and advised the client to report the matter to the Financial Ombudsman.

An East of Scotland CAB reports of a client whose account was frozen after he sought advice on clearing his overdraft. The client had financial problems that had pushed his account over his authorised overdraft limit. At this point, the client sought advice from the bureau to help him stay out of his overdraft and avoid charges. The bureau wrote to the bank asking them to consider reimbursing some of the charges to help stabilise his position while he worked out repayments to the bank and his creditors. The bank responded by freezing the client's account, leaving the client with no access to funds, even though he was within his authorised overdraft at that time. The bureau requested an explanation and was told that the account had been frozen as the accounts were "at risk". The client feels he is being punished for trying to be responsible with his money and repay his debts.

A South of Scotland CAB reports of a client whose bank refused to agree to an arranged overdraft limit leaving the client in financial difficulty. The client, who was retired, was keeping up with his finances, but found that he was slightly in debt at the end of each month, which meant that he was incurring significant bank charges. The client asked repeatedly for an overdraft facility of £100 on his account, which would have allowed the client to easily get out of the cycle of overdraft charges. However, the bank refused as the client already had a loan with them.

43. Another common response from banks is to pressure clients to take out new products while they are stuck in their overdraft. This can include consolidation loans, re-financing loans, and other products. Clients feel under pressure to agree to these requests as overdraft charges mount up. It is also common for banks to ask for high rates of repayment of overdraft arrears and to be unresponsive to other offers of repayment.

An East of Scotland CAB reports of a client who has an overdraft with a bank who is pressuring her to take out other products as part of a repayment agreement. The client is trying to repay an overdraft she incurred while at university. The client has since changed her account for financial reasons. The bank has sent correspondence stating that the client must re-open an account with them, take out a credit card, and are asking for £260 per month. The client cannot afford to pay this amount, and has tried repeatedly to contact her branch to negotiate. Meanwhile, her account continues to incur overdraft charges.

An East of Scotland CAB reports of clients who were offered a consolidation loan after advising their bank that they were experiencing difficulties repaying their overdraft. The clients had an overdraft of £3,546 which they felt unable to repay. At the time, both clients were under considerable stress and did not fully understand the nature of the agreement. The loan included insurance cover of £1,281 which was not required as neither of the clients are able to work, a fact the branch manager was aware of. The clients now have a debt of £8,600, an increase of £5,000 on the original debt.

A South of Scotland CAB reports of a client who was pressurised to take a consolidation loan to repay his overdraft. The client is currently unemployed and living on Job Seekers Allowance. The client noticed that the interest on the consolidation loan was greater than he was currently paying on his overdraft. His income is only £42.70 per week and he is not in a position to take on a loan.

## Irresponsible Lending

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44. A hugely significant problem for Scottish bureau clients in recent years has been the inappropriate lending of credit to borrowers. The era of easy credit that has taken place over the last decade or so has led to substantial lending to clients who haven't been in the position to repay their debt. Bureau have seen numerous examples of clients being given substantial and expensive credit when they are unemployed, on a low income, suffer from mental illness, or are likely to be too old to repay the debt.
45. Scottish bureau debt clients are less likely to be in full-time employment, significantly more likely to be unemployed, and more likely to live in local authority housing, than the Scottish population in general. Bureau clients are therefore predominantly low income clients – and yet bureaux see cases every day of clients struggling with significant credit commitments.<sup>8</sup>
46. There are few adults in the UK who don't currently have or have held credit. Many low income consumers supplement their income with credit just to get by, or need credit to replace essential items, such as cookers, that they cannot afford on their income.

### Low income clients

47. Low income clients who need credit are often able to access it, but not at affordable levels. It is a feature of the financial services market that the cost of a small loan is disproportionately bigger than that of a large loan. The cost of credit is therefore greatest for those who need to borrow the least. It also creates a perverse incentive for banks to lend more money to customers than they need to in order to maximise income. The result is that low income clients often have access only to unaffordable credit, and, rather than dissuading clients from taking credit that they cannot afford, banks and others are encouraging these agreements. This can often lead to intractable debt problems for clients.
48. Low income consumers need sustainable levels of credit, but the odds are stacked against them. Armed with statistics stating that low income customers are a bigger default risk, creditors place terms on customers that make credit too expensive and make these customers more likely to default.
49. Scottish bureaux have reported cases in which clients have been given credit that is highly disproportionate to their low level of income. In such cases, it is very difficult for clients to make repayments on a loan and consequently take out further credit to meet payments. This is an unsustainable situation for a client and leads to a cycle of debt that is difficult to escape.

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<sup>8</sup> On the Cards: The Debt Crisis facing CAB clients, Citizens Advice Scotland 2004

A West of Scotland CAB reports of a retired client who was given a loan of £30,000 by his bank. The client is a council tenant who lives on a pension of £900 per month. The client made repayments using five credit cards, but has now reached the limit on all of them. The client's total debt is now £47,000.

A North of Scotland CAB reports of a disabled client who has been unable to work for over a decade yet was given a £10,000 loan from his bank. The client's income consists of Incapacity Benefit, Disability Living Allowance, and war pension, amounting to £160 a week. The client tried to negotiate lower payments but the bank refused and would only accept the agreement amount. The client has now fallen behind on his payments, which is causing the client considerable stress.

A West of Scotland CAB reports of a client whose bank has lent him substantial sums of money despite his only income being Income Support and Disability Living Allowance. The client has now received over £10,000 of loans from his bank. The bureau wrote to the bank querying why a client whose sole income was benefit payments was given such substantial credit, but did not receive a reply. The client came back to the bureau to say that he has now been given an agreed overdraft limit of £2,000. The client has used this overdraft to live on while his benefit payments have gone towards his debts.

50. The argument behind lending to low income clients is the provision of a service to customers who otherwise would not be able to obtain credit. However, for many of these clients, high cost credit does not answer the problems of low income, and merely exacerbates their problems to the extent that their low wages or benefits are completely swallowed up by their ever increasing debt.

## **Clients with poor credit histories**

51. Scottish Citizen Advice Bureaux have a number of clients who have been given credit despite already having considerable debt. While this type of practice helps the client in the short-term, in the long term it adds substantially to the client's overall indebtedness.
52. The problem appears to lie in a 'don't ask, don't tell' attitude from banks that have not checked whether clients already have credit and debts from other creditors. In some cases, clients have been given credit despite already having multiple debts with the same bank.

A West of Scotland CAB reports of a client who was given a loan for £3,000 despite already having over £30,000 worth of debt. Already owing some of this money to his bank, he was given the loan without any problems or questions about his other debt. The client now has over £33,000 worth of debt and is unable to repay this amount.

An East of Scotland CAB reports of a client on income support who was given a loan of £10,000 from her bank. The client had approached the bank for a loan advising them that her income consisted of income support and occasionally £40 cash in hand weekly employment. The bank did not ask for proof of the client's income. The client already had debts of over £14,000 prior to asking for the loan. The client used the loan to supplement her income, and could only make the first few repayments. The client is a homeowner and is now forced into selling her home to repay this debt.

## **Pressure on clients to take credit**

53. Scottish bureaux have seen many cases in which clients have been offered credit when they originally had no intention of asking for a loan and were unlikely to be able to afford credit. This type of selling can be harmful for clients who are tempted by the offer of large amounts of money and who do not have time to think through the cost or implications of their decision.

An East of Scotland CAB reports of a client who was offered a loan by her bank as she withdrew money from her account, despite having no disposable income and relying solely on benefits. The client went into her local branch to withdraw the last £6 from her account, and was offered a loan and a credit card by the bank teller. The client agreed, and received a £2000 loan and a credit card with a limit of £1500. However, the client only has a little over £4 a week in disposable income, and could never have been able to afford the offered loan. The client now has debts amounting to £4,785 with her bank.

An East of Scotland CAB reports of a client who took out a loan with his bank after receiving loan offer literature with his bank statement. The loan was for £8,856 repayable over five years. The client was 81 years old, and died two years later. His wife has now taken over the repayment of the loan as the bank had insisted that the loan was taken jointly due to her husband's age. She has very little means of affording the repayments and has fallen into arrears.

54. Similarly, banks put pressure on clients to take out further credit on top of their initial loan, rather than take actions to help the client repay their original commitments. The additional loan is often euphemistically referred to as a 'top up' on the loan, when in fact the top up is actually a new loan with the client paying the interest on the new loan on top of that of the old loan.

A North of Scotland CAB reports of a client who was given a 'top up' on her existing loan having gone into her bank branch asking for an increase in the overdraft limit on her bank account. The client was kept in the branch for over three hours, during which time the client was seen by an assistant, the manager, and an insurance representative, none of whom mentioned interest rates. The £1,500 loan was used to repay mortgage arrears. The client then received a confirming letter showing that the whole loan was to be repaid at 14% interest, compared to the original loan rate of 7.4%, and the repayment schedule had been extended. The letter stated that the client had 14 days in which to change her mind. The client phoned the contact number given, and was told to communicate by letter.

A West of Scotland CAB reports of a retired client who received calls at regular intervals by her bank offering to "top up" her loan. The client has a number of debts which she believes amount to around £20,000. The client was contacted by the bank suggesting that she "top up" her loan, which she agreed to do, and now has a repayment of £243 per month. The client was unaware that the "top up" was in fact a new loan altogether and as a result she is paying interest on interest. The bureau feels that the bank should be taking the client's multiple debt situation into account each time they offer a new loan.

# Account management

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55. When clients get into arrears with repayment of credit, banks have varying policies in response. Some of these policies can help debtors while others only hinder, making an affordable loan difficult to repay. This section looks at the policies and practices of banks when clients get into arrears.

## Interest and charges

56. A bank's policy on interest and charges on arrears can have a significant impact on the debtor's ability to repay their debt. A common policy operated by banks is the decision to allow debtors only one short period in which interest and charges can be frozen, before they are restarted and the debt is sold to a debt collection firm. This policy gives the debtor little chance to repay their debts and can have the effect of increasing the value of a debt before it is passed to a debt collector.

A West of Scotland CAB reports of a client who had interest applied to his debt due to a new bank policy. The client has been regularly making repayments of £80 a month towards his debt for around a year. After a review of the repayment schedule, the bank requested an additional £92 a month payment for interest charges. The bank had a new policy of suspending interest for a fixed period of around six months, after which interest and charges are reapplied to the account. The bureau was informed that the account would be passed to a debt collector whether or not the client continued to make payments. The client decided not to make payments until the account reached the debt collector as they will not apply interest. The client then began to receive phone calls late at night from the bank regarding the debt.

A West of Scotland CAB reports of a client whose bank began to add on interest to a debt without warning after a period of freezing interest on the account. The client had been making the agreed £4 repayments to the bank, but was sent a letter stating that the client was now in arrears of £20.73. The bureau called the bank who explained that their policy is to freeze interest for a "once in a lifetime period" of one year. After that interest gets added for 4-5 months, at which point the account will be passed to a collector. The bureau pointed out that the client had adhered to the payment plan and that the interest charges far outweigh what she can afford and she will never make inroads into the debt.

## Policies on arrears

57. Banks can also be unhelpful or unsympathetic when a client reports financial difficulties. Common responses include increasing agreed overdraft limits, decreasing credit limits, offering consolidation loans, and in some cases closing the client's bank account.

A North of Scotland CAB reports of a client who had her account closed by her bank after offering a reduced repayment for her debts. The client is a pensioner whose main source of income is her state pension. The client was having difficulty meeting the repayments on the loan and the bureau made a reduced offer of repayment to the bank and sent the bank a copy of her financial statement. The bank immediately closed her bank account with the result that her state pension which was due on that day seems to be lost. The bank was very unhelpful and would not return calls. The bank eventually offered to open a new account and to try to trace the £380 which had disappeared.

A North of Scotland CAB reports of a client whose bank reduced his credit card limit to below the amount that he owes. The client had reached an agreement with his bank to pay £5 a month for a credit card debt. The credit card had a £3000 credit limit. The client received a letter from his bank stating that his credit limit would drop from that day to £550 – he owed £570.89. In another letter received on the same day he was asked for the full £20.89 limit plus charges.

A West of Scotland CAB reports of a client who received unsympathetic treatment from her bank when repaying her loan. The client has a repayment arrangement in place with her bank that was due to be reviewed in October 2008. The client received a worrying phone call from the bank saying that there is no way that the present arrangement will continue after October and offered a final settlement figure of £9,000 for a debt of around £11,000. They suggested if she did not take advantage of this offer "her house would be involved".

58. A common response from a bank to a client who is reporting financial difficulty is to increase the amount that a client can effectively borrow, for example by increasing credit limits or authorised overdrafts. This can give a client breathing space in the short-term, but can ultimately represent irresponsible lending as the client still cannot afford to repay what they owe and end up with a higher amount of debt.

A North of Scotland CAB reports of a client whose bank continually raised his credit card limit despite his precarious financial situation. The client has never had permanent work, yet has a credit card limit of £11,200. The client was only able to keep paying minimum payments on his credit card debt each month by taking cash withdrawals from his card. As a result of never missing a payment his credit limit was increased on a number of occasions, thereby allowing the client to get into deeper debt.

A North of Scotland CAB reports of a client whose credit card limit has been increased to £7,050 despite the client being unable to maintain payments during the past few years. The client has been on Income Support for 17 years and has a debt of £25,000. She has numerous debts which she has not been paying for a number of years as she is awaiting legal action to allow her to apply for bankruptcy. The bank's reaction to her financial situation has been to extend her credit limit allowing the client opportunity to get further into debt.

An East of Scotland CAB reports of a client who asked for help from her bank in repaying a loan to them. Their response was to raise her overdraft limit substantially. The client had had a series of loans from her bank since the 1980's, which was rescheduled as a £25,000 loan in 2006. When the client returned to the bank for help as she was not able to cope, the bank's response was to raise her overdraft limit from £300 to £2,000.

## Right of 'set off'

59. The right of set off allows banks to legally transfer cash from current or savings accounts to pay credit card or loan arrears without account holders' permission. Citizens Advice Bureaux have seen cases of people having their pay or benefit payments removed from accounts, leaving them unable to meet priority debts, like mortgages and council tax, and in greater financial difficulty.

A North of Scotland CAB reports of a lone parent whose bank took £400 from her account to repay debts without her permission. The client has credit card and overdraft debts with her bank, with whom the bureau has been in contact with to negotiate repayments. The bank took £400 from her current account after her wages had been made in, leaving the client with no money with which to live. The client contacted her branch who denied having any contact with the bureau, and who stated that if the client moved her account to another bank they would take her to court.

## Sale of associated products

60. Another way in which a bank can put pressure on clients to repay is to encourage them to take out further products as part of their repayment. Once this offer is in place, it can be difficult for the client to reject the product and negotiate with the creditor. The types of related products that clients can be under pressure to agree to include further loans, consolidation loans, credit cards, and overdrafts.

A West of Scotland CAB reports of a client who made a repayment offer to her creditors, and was instead offered a further loan. The loan would have helped the client to avoid default, but would have cost a further £2700 in interest and charges. The client rejected the offer, and decided to stick to the repayment plan prepared by the bureau.

An East of Scotland CAB reports of a client who was offered a refinancing loan after making an offer of repayment. The bureau had helped the client to set up a repayment agreement with his bank six months previously with interest frozen on the account. When the arrangement expired, the bureau wrote to the bank with the same offer of repayment as the client's circumstances had not changed. The client then contacted the bureau to say that his bank had contacted him offering a refinancing loan. The bureau explained to the client that the loan would put him more in debt and he would not receive any money.

A North of Scotland CAB reports of a client whose bank will only accept an offer of repayment if the client takes out a new consolidation loan. The client is deeply in debt, and the bureau made offers to her creditors for repayments. The client's bank replied to the bureau saying that they will 'accept' her offer of £175 a month but only if she has a 'new line' opened, i.e. takes out a consolidation loan. If the client were to accept this, she would continue to pay interest and charges on the debt.

## Debt collection

61. Bureau clients often complain of intimidation or harassment from creditors chasing repayments on a debt. This includes creditors or debt collectors who put pressure on clients to increase repayments through phone calls, letters, and home visits.
62. Phone calls from banks are often intimidating to clients and can happen so often that it becomes a form of harassment. Clients are reporting receiving multiple calls every day, including late at night, early in the morning, and on weekends. The content and tone of the conversations can also be threatening to the clients.

A West of Scotland CAB reports of a client who received phone calls at all hours from his bank after falling into arrears. The client received calls into the evening and from 8am. His wife often took the calls and sometimes they were 'silent', but the client was sure they were from the bank. The bureau wrote to the bank complaining on behalf of the client. The reply stated that all customers who get into arrears receive phone calls like this, but the system is unable to cope with requests not to call at certain hours. Some calls start out as silent as the operator can't always respond immediately. These administration difficulties at the bank cause unfair stress and worry for clients.

## Third party dealings

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63. Scottish bureaux have reported banks that have refused or delayed recognising a bureau as representing a client. The consequence of this is that the bureau cannot act on behalf of the client while banks continue to request payments from them. This can result in clients feeling pressurised to agree repayments without the benefit of an adviser's input.
64. The OFT's guidance on debt collection defines refusing to deal with authorised third parties, such as Citizens Advice Bureaux, as 'deceptive and/or unfair'. However, bureaux have reported a number of cases in which a bank either does not recognise a bureau as representing a client or actively takes action against the client in response to bureau involvement.

A West of Scotland CAB reports of a case in which a major bank refused to recognise a Citizens Advice Bureau as representing a client. The client had asked the bureau for help to re-claim bank charges on his account. The bureau contacted the bank by letter with a signed mandate from the client. The response stated that the bank 'is under no statutory obligation to record this information and therefore I am unable to assist further with your request'. The bureau contacted the bank again to request information relating to the bank charges, and were asked to forward another signed mandate from the client. The bureau received no reply, so sent the letter and mandate again, but were told on the phone that the bank had not received a mandate. The bureau received a letter from the bank six months after first sending a letter, advising that 'with effect from 23 April 2007 it became an offence to provide claims management services without authorisation.' It further reads that after checks they were 'unable to confirm your company have the required authorisation.' The letter went on to say that the bank would deal directly with the client.

An East of Scotland CAB reports of a retired client with a loan who was upset by the harassment she felt she was receiving on the telephone while she was trying to negotiate a solution to her debt problems. The client had approached the bureau for help, but the bureau found that creditors were taking a long time to respond to their letters while continuing to contact the client directly. The client was told on the phone that her bank did not deal with third parties, including the citizens advice bureaux. The bureau contacted the head office of the bank who advised that this was not the case and that the original offer of repayment would now be accepted.

65. A recent trend reported by bureaux has been banks freezing clients' accounts after a citizens advice bureau has made contact on behalf of a client. The reasoning behind this action is that the banks are protecting their own funds in case the client gets further into debt. This seems counterintuitive, especially as many UK banks encourage customers to visit a bureau if they are in financial trouble in their correspondence to clients.

A North of Scotland CAB reports of a client who had her current account closed after making a reduced offer on her loan repayments. The client was in financial difficulty and the bureau made a reduced offer of repayment and sent her financial statement to the bank. The bank responded by immediately closing the client's bank account, which caused the client to lose her State Retirement Pension of £380 which was due to be paid in that day. The bureau called the bank who were unhelpful and would not return calls. The client was left with no money whatsoever.

An East of Scotland CAB reports of a client who had her current account frozen after a bureau contacted the bank with an offer of payment on behalf of the client. The client had been coping with her debts until her husband had had an accident at work. She decided to do the sensible thing and deal with her debts before they got unmanageable. The bureau sent out letters to the client's creditors offering repayments, but received no reply from the client's bank. On approaching her branch, the bank informed the client that the account was 'frozen' and she could not withdraw any money. The client had £461 in her account, and was therefore not in overdraft. The branch informed her that because she had involved the CAB, it was their policy to automatically freeze the account. The branch further told the client that she should have come to them for help, and not the CAB. The client duly informed them that she had approached them and asked for a loan to tide her over until her husband went back to work, which they had refused. The client then asked what help they could offer her, receiving the reply that as she had involved CAB, there was no further help they could give her. The client left the branch with no money, and two children under 10 to feed over the weekend.

# Conclusion

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66. Banks play a fundamental gateway role in nearly every person's life in the UK, so it is essential that the policies and practices of the banks allow customers to access this gateway without undue problems and hardship. However, Scottish clients are continuing to experience problems relating to their current accounts, overdrafts, use of credit, and management of arrears.

## **Opening and maintaining accounts**

- Clients are struggling to open basic bank accounts due to a lack of personal identification, previous debts with the bank, or the policies of the bank branch.
- Clients who are made bankrupt are losing their bank accounts and experiencing difficulties in opening another.
- Clients are experiencing difficulties when switching their account, which is dissuading other clients from considering switching

## **Bank charges**

- Clients are receiving disproportionately high bank charges after making small infringements in their overdraft, which unfairly penalises low income customers.
- Banks are using clients' much needed benefit payments to pay for overdraft charges.
- Clients are being hit with multiple charges - such as insufficient funds charges, unpaid item charges, missed payments charges, and interest - that 'snowball' into a high amount that forces the client into a cycle of debt.
- Clients have a poor understanding of the likelihood and level of charges involved in their overdrafts.
- Banks can be unhelpful in their responses to clients who try to negotiate a solution to their overdraft problems.

## **Irresponsible lending**

- Low income clients need affordable credit, but are often given unaffordable and substantial credit that puts them into a cycle of debt.
- Substantial credit is being given to clients with no obvious ability to repay, including those who rely on benefit payments, are retired, or have existing financial commitments.
- Clients who already have substantial debt can be given further loans which worsen their situation.

- Clients can be pressured into taking loans they had not intention of asking for, and be persuaded that taking a further loan can act as a solution to arrears.

### **Third party dealings**

- Scottish bureaux have reported banks that have refused or delayed recognising a bureau as representing a client, running contrary to OFT Guidance on Debt Collection.
- A recent trend has been banks freezing clients' accounts after a citizens advice bureau has made contact on behalf of a client.

67. The events of the last two or three years, including the OFT test case in the High Court and the financial problems induced by the Credit Crunch, have triggered great interest in the banking sector. This has highlighted many of the policies and practices that have adversely affected customers in the last few years.

68. This interest also represents an opportunity for banks, government, and regulators, to look at the way in which the banking sector is run. Many remedies have already been proposed and some already implemented. However, for any remedy to be successful it needs to take into account the impact on the individual. This is an opportunity for a new agreement to take place between government, banks, and customers – one in which banks make their revenue in a fair and transparent manner, and customers can access the services that they need without the problems and the charges that they currently face.

Citizens Advice Scotland and its member bureaux form Scotland's largest independent advice network. CAB advice services are delivered using service points throughout Scotland, from the islands to city centres.

**The CAB service aims:**

to ensure that individuals do not suffer through lack of knowledge of their rights and responsibilities, or of the services available to them, or through an inability to express their need effectively

**and equally**

to exercise a responsible influence on the development of social policies and services, both locally and nationally.

The CAB service is independent and provides free, confidential and impartial advice to everybody regardless of age, disability, gender, race, religion and belief and sexual orientation.

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