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BRIEFING FOR MEMBERS

FINANCIAL INCLUSION AND OVER INDEBTEDNESS: STATE OF PLAY AND CHALLENGES

What is "financial inclusion"?

The European Commission recognises that basic financial services are inaccessible for 30 million people, i.e. 7% of its population[1].

Achieving financial inclusion is aiming to counterbalance this phenomenon by opening **access** (for example people are entitled to have access to a credit or a bank account) and appropriate **use** (people may have access to a service, but it may not be appropriate to their needs or they may be using it ineffectively) of financial services to all people, regardless of their socio-economical or legal status, living on a territory. This is based on an understanding of banking services as public goods, essential to social participation and therefore to the achievement of social cohesion.

Initially, financial inclusion was understood mainly in opposition to financial exclusion seen as the geographical difficulty to access services. The concept of financial exclusion has then widened to be "*a process whereby people encounter difficulties accessing and/or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal social life in the society in which they belong."*[2] ("Mainstream market" is understood here as "non stigmatizing" providers).

If debates persist as to a clear definition of "financial inclusion", academic research and policy makers help to precise the definition as they generally identify four mainstream financial products as central to financial inclusion: banking, credit, savings and insurance[3]. These products are deemed to be central to financial inclusion as they are instruments of social participation.

What is Over-indebtedness? How does this relate to "financial inclusion"?

Household over-indebtedness can be defined as a *"temporary or permanent disequilibrium in the budget of a household resulting from expected or unexpected expenditure increases or from the household's income decreases"*[4]*.* Literature distinguishes 3 categories of causes for over-indebtedness: change in life, gradual over-commitment, reaching a reasonable standard of living. Other studies insist that the main cause is clearly to be found in the occurrence of a disruptive event for the household budgetary equilibrium (change in life).

Over-indebtedness should not be disconnected from the issue of financial inclusion. As underlined by G. Gloukoviezoff[5], over-indebtedness is one of the aspects of financial exclusion. It therefore relates to financial

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[1] Flash Eurobarometer 282, Consumers' Views on Switching Providers, European Commission.
[2] Financial services provision and prevention of financial exclusion, European Commission, March 2008
[3] World bank (1995) as refereed in EC Financial services provision and prevention of financial exclusion, March 2008
[4] Toward a common operational European definition of over-indebtedness, European Commission, February 2008
[5] GLOUKOVIEZOFF G., « From Financial Exclusion to Overindebtedness : The Paradox of Difficulties for People on Low Income ? », in ANDERLONI L., BRAGA M.D., CARLUCCIO E. (eds), New frontiers in banking services. Emerging needs and tailored products for untapped markets, Berlin : Springer Verlag, (forthcoming, 2006)

inclusion strategies. Financial exclusion and over-indebtedness are two sides of the same coin as they both relate to banking problems, and both have for consequence the deprivation of all or part of financial services.

The European household debt has been on the rise since the 1980's. In 2007, even before the start of the Financial and economic crisis, household debt in the European Union had increased on average by almost 19% [6].

Why is this relevant now?

Firstly, the increasing unemployment, and decreasing levels of social protection resulting from the **economic and financial crisis** have increased the number of vulnerable people and therefore potentially exposed to financial exclusion and over-indebtedness. Meanwhile, the types of debts and the characteristics of over-indebted households and lenders are also changing, while demand for such services is increasing. Eurodiaconia members providing debt-related services will have to increase their efficiency, adapt to new demand, and develop integrated approaches (ideally encompassing health, legal and social aspects of the demander's needs).

Secondly, the 2010 **"Europe 2020 strategy**", Europe's latest strategy for smart, sustainable and inclusive growth, has set five ambitious objectives on employment, innovation, education, social inclusion and climate/energy - to be reached by 2020. It presented "inclusive growth" as one of its three core priorities, therefore establishing social cohesion as a main concern. Financial inclusion consequently came back on the agenda as a necessary step toward a better social cohesion.

Thirdly, **Technological developments** are influencing the banking and financial services to move toward a cashless economy. This trend is reinforced as the economic process seems to reduce more and more all exchanges (e.g. goods, services, information) into financial instruments. This **"financialization"[7],** joined to technological developments, impact on households as it catalyses social exclusion of those excluded from access or use of the financial services and banking. They are *de facto* marginalized by being excluded from access and use of the tools enabling social participation and interaction, such as internet banking transfers and payments, credit cards, mobile phone payment, etc.

Finally, technological developments have also facilitated the access to credit inappropriate use of credit for vulnerable users (e.g. sms loans, online gambling, etc). It is therefore necessary for public authorities to address this issue now.

Why are these issues important to Eurodiaconia and its members?

Firstly, Eurodiaconia's members, based on their **Christian ethos**, have a role to play against the current process of financialization, through a double approach. On the first hand, members can demonstrate that all

[6] Explaining over indebtedness in the European Union, Julia Gumy, The research Group, July 2007

[7] Financiarisation et lien social : une analyse de l'exclusion bancaire à partir de l'institutionnalisme de J.R. Commons G. Gloukoviezoff et V. Dutraive

values do not stand in finances, growth, consumption and ownership. On the second hand, studies have shown that credit is now becoming a common way of fulfilling needs which were previously met by state solidarity or family solidarity. In this context, Eurodiaconia members can also offer another way and provide services to the most "risky" or "unprofitable" clients, such as alternative banking or financial services, training and education skills, etc

Secondly, Eurodiaconia has incidentally observed that over the past 3 years members have had to face an **increase demand for services** consecutive to the impact of the financial and economical crisis. The highest increase seems to have been for services related to food banks, emergency financial support and debt counselling, with the most striking move up for debt counselling services.

Thirdly, Eurodiaconia monitors social policies at EU level and observes that in view of the increasing financial exclusion and unprecedented growth in personal debts, much **more safeguards should be established for a better financial inclusion and the protection of individuals and families** against over-indebtedness. Eurodiaconia and its members, together, can work for governments and EU official to be reminded of the social consequences and economic benefit at stake through financial inclusion.

What is happening at European Level?

There is a need for more comparative data on over-indebtedness and its relationship to financial exclusion as a better understanding of this complex and interlinked relationship (as over-indebtedness can appears as one of the causes and consequences of social exclusion) would facilitate an integrated approach, more targeted policy making and a better inter-governmental cooperation on this topic.

Financial inclusion and over indebtedness are mostly related to National competence. However, the European Union can be involved in many different ways, for instance by legislating on the achievement of the internal market, by encouraging research in a specific area or by political pressure on a member state to match some minimum EU standards.

The European Commission is working on the topic of over-indebtedness through three of its directorates: Employment, Social Affairs & Inclusion (DG EMPL), Health and Consumer Policy (DG SANCO) and Internal Market & Services (DG MARKT).

DG EMPL, the directorate for Employment, Social Affairs & Inclusion mainly works on this matter through the Open Method of Coordination. It encourages Member States to set up common targets and then follow-up on the implementation of such targets. It also supports research in this area, and provides financial support.

DG SANCO, Directorate General for Health and Consumer Affairs also work toward reinforcing knowledge in this area. Besides, it looks at the issue of debts through the eye of consumer protection. The consumer credit directive (2008) established some principles such as the duty to explain, duty to check if debtor can pay the credit and a compulsory delay allowing the revocation of the agreement. This directive is currently being implemented in EU Member States. DG SANCO also aims to equip consumers, empowering them, especially through consumer education for instance with the self education tool www.dolceta.eu, or a European diary for students, giving advice and tips on financial management. Finally, it works toward the standardization of information, to help consumer understand and make informed choices.

DG MARKT, the Internal Market and Services Directorate General, coordinates the Commission's policy on the **European Single Market** and seek to remove unjustified obstacles to trade, in particular in the field of services and financial markets. It is involved on the issue of over-indebtedness through the Mortgage credit initiative and rules on advertising. The European Commission published a legislative proposal on "Credit agreements relating to residential property" in March 2011. This text aims to create an internal market in mortgage credit with a high level of consumer protection and to promote financial stability by ensuring that mortgage credit markets operate in a responsible manner. It is discussed by the European Parliament, and is likely to be adopted in March 2012.

Finally, in June 2011, the college of commissioners (the 27 EU commissioners) decided to give up the idea of a legislative initiative on basic financial services to replace it by a non-binding recommendation, focusing on access to a basic account. However, the deadline for the implementation of the Commission's recommendation to member states is July 2012. It appears that if Member States have not started to implement seriously the European Commission recommendations then, it is likely that the European Commission will then propose a binding legislation.

How does this relate to your organisation at national level? What can you do?

As many of the commitments made by national governments rely on "soft-law", their implementation will partly depend on political pressure. Therefore, it is **important** for the European Commission **to be informed about what is really happening in your country** regarding the actual facts and the implementation of its legislation and recommendation. You can monitor what is happening in your country, lobby directly at national level and/or report on any evolution to the European Commission. Referring to the Commission's recommendations or decisions, you can remind your governments of the standards and target agreed on at EU level.

For instance, the recommendation on access to a basic account is currently a "soft option" that is to say it relies on political pressure for Member States to follow the EU recommendation. You can remind your governments that the European Commission invites Member States to ensure that basic and affordable bank account become available to individuals, regardless of their country of residence in the EU or their financial situation. The European Commission will assess the situation in one year's time and propose any further measures as necessary, including legislative measures. It is very important if you can monitor what is happening in your country and inform us about it. **Your report might differ from what your government will say, and this is very precious information for the European Commission**.

What is Eurodiaconia doing?

Eurodiaconia has been following the debate on financial inclusion for years for instance by responding to the consultation on access to a bank account in 2009 and writing to president Barosso and Commissioner

Michel Barnier in July 2011, regarding the decision to only issue a non-binding recommendation on access to a bank account[8].

In 2011, Eurodiaconia started to work actively on the matter of over-indebtedness, following the increasing demand for debt-related services to its members across Europe. Eurodiaconia Marginalisation and Exclusion network prepared policy recommendations which were then took up to the European Parliament on the occasion of a working seminar co-organised by Eurodiaconia and the EU research agency Eurofound on household over indebtedness in the context of the crisis.

In 2012, Eurodiaconia will keep working in partnership with other organisations and MEPs to raise the importance of the issue of financial inclusion and over-indebtedness. Eurodiaconia secretariat will also be working with Eurodiaconia members to monitor the implementation of the recommendation on financial inclusion and prepare an assessment for the European Commission.

Eurodiaconia will continue to work with Eurodiaconia members to assess the state of play of financial exclusion and over-indebtedness, and the related financial inclusion strategies at national level to relay these information at EU level, to the European Commission and Members of the European Parliament.

Further information and links

Explaining over indebtedness in the European Union, Julia Gumy, The research Group, July 2007

Financial services provision and prevention of financial exclusion, European Commission, 2008

Toward a common operational European definition of over-indebtedness, European Commission, 2008

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People on Low Income ? », in ANDERLONI L., BRAGA M.D., CARLUCCIO E. (eds), New frontiers in banking services.

Emerging needs and tailored products for untapped markets, Berlin : Springer Verlag, (forthcoming, 2006)
Data on 'Population and social conditions — Living conditions and social protection'
http://epp.eurostat.ec.europa.eu/portal/page/portal/income_social_inclusion_living_conditions/data/ad_hoc_modules

[8] Eurodiaconia's letter - withdrawal of Commission's legislative proposal on financial inclusion
http://www.eurodiaconia.org/images/stories/Letter_to_Mr._Barroso_on_access_to_a_basic_payment_account.pdf