TESTIMONY OF

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BEFORE THE U.S. SENATE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

DEVELOPING OPPORTUNITIES FOR AFFORDABLE LIFELINE BANKING FOR LOWER-INCOME CONSUMERS

THURSDAY MAY 2, 2002

My name is Marva Williams. I am the Senior Vice President of the Woodstock Institute. I am grateful to Chairman Sarbanes, Ranking Member Gramm, and other Members of the U.S. Senate Committee On Banking, Housing and Urban Affairs for this opportunity to discuss expanding opportunities for lifeline banking for lower-income consumers. I am also pleased to join my fellow panelists, the Honorable Sheila Bair, Michael Barr, Fran Grossman, Rufino Carbajal, and Jaye Morgan Williams.

The Woodstock Institute, in partnership with Chicago-area banks, is expanding opportunities for lower-income consumers to establish deposit accounts, improve their financial literacy, and develop assets. The Woodstock Institute has a 29-year record of policy research, public education, and technical assistance to promote access to safe and sound capital and credit in lower-income and minority neighborhoods. The Institute has a specialized knowledge of lower-income families' use of financial services and has expertise on the quality and quantity of basic retail services that financial institutions provide to lower-income consumers.

Importance of Lifeline Banking

Limited access to the financial mainstream and poor financial literacy skills are major barriers to asset development. Poor financial literacy has a detrimental impact on personal financial management—affecting the consumer's ability to own a home, find employment, buy a car to get to work, purchase life insurance, rent an apartment, or pay tuition. Consumers without a relationship with a mainstream financial institution also pay high transaction fees at check cashers. According to a Woodstock Institute study, check cashers charge up to three times as much as financial institutions for basic financial services but do not provide key services like savings accounts and financial advice. In addition, some check cashers offer predatory services with exorbitant fees, including payday loans.

Lifeline banking is also the foundation of asset development. Consumers need affordable means to cash checks and pay bills. In addition, retail products enable and encourage savings habits and can help build credit.

Challenges to Lifeline Banking

Prior to developing remedies, we conducted research to identify the reasons that lower-income consumers remain "unbanked" or dissatisfied with mainstream financial institutions. These barriers include:

Limited Access: Bank branches have abandoned many inner-city communities. Bank mergers involving institutions with overlapping branch locations have caused a decline in the number of bank branches per capita in lower-income communities as the newly merged institutions close branches to reduce costs. Further, banks often have inconvenient hours and are not accessible on evenings and weekends. Finally, residents of lower-income communities may also have problems accessing automatic teller machines (ATMs). Community Reinvestment Act regulations provide an opportunity to promote increased access. The Service Test, which assesses the market penetration of a bank's retail products, record of opening and closing branches, and other factors. The Service Test examination should be strengthened to include an assessment of the income and other characteristics of a bank's account holders to determine if they are meeting the service needs of their assessment area.

Costs: It can be prohibitively expensive for lower-income people to maintain bank accounts. They may face high minimum balances, initial deposits or monthly service fees.

Credit status: Some banks conduct credit checks and scoring for applicants. Consumers with little or no credit or a slightly blemished credit record can be disqualified from opening a bank account.

Trust: Some 'unbanked' consumers may have attempted to access bank services in the past and been repelled for a variety of reasons. Some may worry that financial institutions share account information with others, including creditors. In addition, poor communication regarding account guidelines can also lead to misunderstandings for account holders. Some consumers may feel uncomfortable continuing a relationship with a bank that has denied them a loan.

Financial literacy: Lifeline banking requires significant person-to-person training and education on balancing checkbooks, planning monthly finances, using an ATM, etc. Without the skills to manage accounts, consumers may be faced with high fees for non-sufficient funds and other transactions. They might become frustrated and close their accounts. In addition, some consumers are uncomfortable using electronic technologies that are associated with many lower-cost accounts, including ATMs, Point of Sale terminals (POS), and Internet banking.

Lack of information or poor marketing: Many banks have affordable accounts that are directed to lower-income consumers. However, the account features are not well marketed to lower-income communities and people are not aware of affordable options.

Lifeline Account Features

Establishing checking and savings accounts with traditional financial institutions can be a major challenge for lower-income consumers. The following features of a model lifeline checking account mitigate the barriers that many unbanked consumers face:

- No credit check
- Flexible ID requirements.
- Ten dollars or less opening requirement
- No minimum balance
- No monthly service fee
- No teller charges
- Unlimited check writing
- Free withdrawals from bank-owned ATM machines
- Promotion of direct deposit of paychecks and government benefits

Intermediate Products Checking account products may not be suitable for all consumers. In fact, one of the reasons that people frequent check cashers is that they serve as one-stop-shops for cashing checks and paying bills. However very few financial institutions provide inexpensive electronic bill payment services. The North Side Community Federal Credit Union, a Chicago community development credit union, and First Bank of the Americas allows owners of savings accounts to pay utilities and other bills electronically.

Woodstock Institute Experiences with Lifeline Banking

Bank One Alternative Banking Program The Woodstock Institute and the Chicago CRA Coalition negotiated a CRA agreement with Bank One when it purchased First Chicago Bank in 1998. In addition to increasing small business and residential lending and community development grants and investments, Bank One agreed to increase services to unbanked consumers. Working with members of the Chicago CRA Coalition, the bank developed the Alternative Banking Program (ABP). ABP is a safe, convenient and inexpensive alternative to using check-cashing services. Customers who do not meet Bank One's traditional credit scoring criteria, due to borderline credit or no credit history, may be eligible to establish an ABP account due to its more flexible credit scoring criteria.

ABP is not a separate banking product—customers have access to Bank One checking and savings accounts that have features similar to a model lifeline account:
- $10 opening deposit
- Low or no minimum balance
- Low or no service fee
- Unlimited check writing
- Unlimited use of Bank One ATMs
- Some free teller transactions, depending on account
- Free financial literacy training

The account features were designed to address many concerns that lower-income unbanked consumers express. It is low-cost, accessible at all Bank One branches and ATMs, and includes the availability of financial literacy classes for account holders. Further, although applicants with a credit history must have suitable credit scores, people with no or borderline credit may open accounts. In exchange for a more flexible credit scoring criteria, the Bank did establish some modest restrictions on the ABP. However, after one year, account holders can apply to upgrade their accounts to traditional account products.

The ABP is not only an innovation for Bank One—it is also a means for bank staff to learn more about providing services to lower-income consumers. Therefore community reinvestment staff held two focus group meetings with account holders to learn how the program was faring. Focus group participants identified several important concerns, including the need for access to telephone banking to obtain information on account balances and withdrawals, and the importance of providing alternative bill payment mechanisms for savings account holders.

ABP has allowed thousands of consumers, many with no credit record, to establish checking and savings accounts. In addition, the Bank has cross-sold other products to ABP customers, including consumer loans, certificates of deposit, and installment loans. ABP has also influenced the establishment of more flexible criteria for other Bank One retail accounts.

However ABP is only available at 8 branches in the City of Chicago, and should be expanded to reach more unbanked consumers.

Financial Literacy and Lifeline Banking Partnerships The Coalition has also developed relationships with Fifth Third Bank, Charter One Bank FSB, and LaSalle Bank. Unlike Bank One, these banks have accounts that meet many of the criteria for lifeline checking accounts. In these cases, the Chicago CRA Coalition helped the banks to (1) develop financial literacy curricula suitable for lower-income consumers, and (2) establish relationships with community partners to identify workshop topics and market and co-sponsor workshops.

These efforts have resulted in the integration of financial literacy programs within each bank's retail banking divisions. Fifth Third retail management staff have joined with community reinvestment staff to offer financial literacy programs and have developed several creative marketing and program partnerships with community organizations. Charter One retail and community reinvestment staff have participated in "train the trainer" financial literacy workshops offered by a local cooperative extension office and are currently developing a financial literacy curriculum.

LaSalle and the Coalition developed an exemplary financial literacy curriculum that addresses the financial management concerns of lower-income consumers. The Chicago CRA Coalition also helped LaSalle establish a very fruitful partnership with Chicago Commons. Chicago Commons is a multi-service settlement house that provides job-training services through its Employment and Training Service Center (ETC) to lower-income people moving from welfare to work. The Bank teaches its financial literacy curriculum in eight classes over a period of about two weeks. Approximately 32 students participate in each course, which culminates in a trip to a local LaSalle branch where accounts can be opened. The partnership is ongoing.

Community Development Credit Unions Community development credit unions (CDCUs) focus on providing financial services and loans in lower-income communities. The Woodstock Institute has documented several innovative financial service partnerships developed by CDCUs.

Central Appalachian Peoples Federal Credit Union operates in 23 rural counties that are among the poorest and least educated in the nation (see Figure 4). Isolated from larger cities, the community is poorly served by traditional financial institutions and unemployment is high. The credit union leverages deposits with government and private funding to provide much needed access to home mortgages, small business and consumer loans, and deposit services.

Northeast Community Federal Credit Union (Northeast Community FCU) provides a safe place to save for lower-income San Franciscans. Organized in 1981, the credit union is committed to serving the unmet financial needs of low-income community residents, many of who are recent immigrants or refugees from cultures where financial institutions are not accessible or trustworthy. Further, some members are concerned that maintaining a deposit account will violate citizenship or immigration regulations. Northeast Community FCU works with local community organizations to provide financial literacy regarding the practices of US financial institutions. It also educates members about the disadvantages of taking out high cost loans that are heavily marketed in this community.

Since its founding in 1981, Quitman County Federal Credit Union (Quitman County FCU) has focused on reaching its African-American, low-income community base. The membership is largely made up of single women, minorities, and public aid recipients. Quitman County FCU also manages a youth credit union program that not only helps young people save but also encourages them to serve their poverty-stricken community in rural Mississippi. Its members run the Youth Credit Union. They elect their own Board, hold monthly meetings, and operate various committees to manage the credit union's affairs. The Youth Credit Union program offers financial workshops that explain the hazards of using sub-prime lenders, manual and computer bookkeeping and accounting techniques, and checkbook balancing among other financial topics.

Lessons in Lifeline Account Programs

Financial Literacy Barriers related to trust, low financial literacy, and marketing can be addressed through effective financial literacy training. Banks should work in partnership with community and other nonprofit organizations to provide financial literacy workshops and counseling. The workshops should include the following topics:

- Budgeting and personal finance management skills.
- Tools to make informed decisions when choosing accounts, applying for loans, or credit cards, etc.
- Skills needed to manage accounts, such as balancing checkbooks, managing funds availability timetables, and using electronic banking services.
- Information on investment and savings options.

Program Marketing Financial institutions' marketing of these new products should include not only information on account features and advantages, but should also include outreach and information on how the products are preferable to check cashers and the other benefits of a mainstream banking relationship. In addition, marketing strategies should be developed with community-based organizations and in cooperation with organizations involved in consumer credit issues. Targeted marketing efforts, such as community newspapers and radio ads, should be considered as well.

Program Diversity It is also important to understand that there is a diversity of 'unbanked' consumers. For instance, minority consumers are more likely than other consumers to be dissatisfied with the quality of their financial services are. When asked by a 1999 survey (conducted by the Metro Chicago Information Center) how well their banking needs were being met, 16 percent of African Americans and 25 percent of Latinos responded 'not too well' or 'not at all,' compared to only 7 percent of whites. Recent immigrants often experience great difficulty developing savings. Many have poor literacy skills, distrust financial institutions or may have concerns about their legal status that keep them isolated.

Bank Staff A major component of the success of the program hinges on the enthusiasm of bank staff to work with lower-income consumers. For instance, one of the recruitment techniques is for tellers to encourage people who cash checks at the bank to apply for checking or savings accounts. Banks should use their in-house communication mechanisms to inform staff of new programs and branch managers should hold short orientation meetings with customer service staff explaining the importance of the bank's efforts to address the financial service needs of its community. Management should also set performance goals and incentives.

Reducing Consumer and Bank Expenses Inexperienced account holders should have accounts that allow some protections from NSF fees. Further, many retail account products are not profitable. According one expert on financial services, financial institutions make 80% of their profit on retail products from only 20% of their customers. Therefore it is also important to consider how banks can cut costs:

- Phone banking: Banks should provide information on account balances and other account activity by phone so that account holders can avoid NSF fees. This will also reduce teller expenses.
- Electronic access: Banks can also improve services and decrease costs by enabling low-income consumers to conduct financial transactions electronically. Services may include Internet banking, smart ATMs, electronic bill payment and money order machines and debit cards.
- No overdrafts: All checks that will cause a negative balance should be returned.
- Limit withdrawals: ATM withdrawals should be limited to $50/day.
- Funds Availability: Account holders may not be able to access funds deposited by check for up to two business days. However, immediate access should be allowed for cash and direct or electronic deposits.
- Second-day approval for new accounts: To reduce criminal exploitation of lifeline accounts, banks should impose a waiting period of 24 hours to establish new accounts. This will allow the bank to more fully investigate applicants and deter fraud activity.

Account Disclosures: It is important that consumers understand account provisions. Therefore they should be translated from "legalese" into standard language, making it understandable for readers of all levels. In addition, many of the materials should also be translated into Spanish or other languages as appropriate.

CRA Service Test: In 1995, the Community Reinvestment Act (CRA) was amended to concentrate on bank performance in three areas: lending, investment, and services. Creative and innovative bank products and services, such as the establishment of lifeline accounts and financial literacy workshops, can help a bank achieve a satisfactory rating under the Service Test. Further, the Woodstock Institute encourages the strengthening of the Service Test by requiring banks to collect and report information on the income and race of deposit account holders.