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8 Banking the Unbanked: Connecting Residents of Social Housing to the Financial Mainstream

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INTRODUCTION

In today's economy, it is increasingly important to have access to a basic bank account and mainstream financial services (Summers 2001). Without bank accounts, families often pay high fees — as much as US\$15,000 over a lifetime — to check cashers and other fringe bankers to conduct basic daily financial transactions (Hawke 2000). More importantly, banking status has profound implications for families' long-term self-sufficiency. People with bank accounts are more than twice as likely to hold savings as are people who are unbanked and are more likely to add to their savings on at least a monthly basis (Dunham 2001, cited in Kim 2001). In fact, controlling for income and other factors, lower-income individuals with bank accounts are 43 per cent more likely than those who are unbanked to have positive net financial assets of any kind. Indeed, for more than half the unbanked (54 per cent), their only asset is their car (US Department of the Treasury 2000). This is why community advocates and US policymakers should be concerned that, despite the longest economic expansion on record during the 1990s, 10 per cent of all American families —

including 25 per cent of African Americans and Hispanics, a quarter of all families with incomes under \$20,000, and nearly half of all families moving from welfare to work — have no bank accounts (Kennickell et al. 1998).

The problem of growing financial exclusion and asset-deprivation has global dimensions, and is closely tied to the themes of this book. For instance, one in every six adults in Britain - around 2.5 million people - does not have a bank or building society current account, and British households are becoming increasingly asset-poor (Meadows 2000). The ratio of British households without any assets doubled between 1979 and 1996, and 50 per cent of all people have less than £500 of disposable financial wealth.¹ More than 80,000 adult Glaswegians are also ‘unbanked’ — ‘16.5 per cent - compared with 15 per cent for Scotland overall, and 8 per cent for England and Wales.’ (Levine 2000) As in the US, minority groups in Britain are more vulnerable - people of Indian, Pakistani or Bangladeshi origin are twice as likely as white people not to have an account (Meadows 2000).

Financial exclusion is also a problem in Eastern Europe. According to one account, only 54 per cent of Poles are active users of banking services (in 1998) (*Cards International*, 27 September 2000), while about one-third of Hungarian households are unbanked, including a quarter of all households in Budapest, and 45 per cent in outlying villages (*European Banker* 2000).

While the incidence of so-called cash deserts, or neighborhoods without convenient access to banks, is generally greater in core cities and remote rural communities, residents of social housing in various locations are also more likely to be unbanked. Confirming the link between this essay and the larger themes of this compilation, research sponsored by the Britannia Building Society recently pointed out that

People who live in local authority or housing association housing are roughly twice as likely not to have an account than otherwise similar people who are owner-occupants (Meadows 2000). ...Those without accounts although the same as those who have them, are likely to be part of social networks concentrated in social housing in major urban areas where the predominant form of money management is cash, and where use of mainstream financial services is relatively uncommon (Meadows 2000).

This essay traces the rise of financial exclusion in the US and abroad, and discusses how a decision designed to save the taxpayer money by delivering government benefits electronically, has the potential to improve peoples' lives by helping them open a bank account and bring them into the financial mainstream. The essay begins with an overview of the US government's transition to electronic funds transfer (EFT), including the factors that motivated this policy, and its current status. This is followed by a discussion of global trends in the banking sector, marked by a decline in the number and concentration of commercial banks, and the explosive growth in the number of 'fringe banks', most notably

check cashing outlets and payday-or money-lenders. This latter, parallel banking system, increasingly serves, and preys upon, the poor and financially disenfranchised, including residents of social housing. Policies that complement the transition to EFT and support more asset-based social policies are then discussed in the next section.

With the government transition to EFT potentially increasing the commercial viability of low-income consumers to private-sector commercial banks, the next section describes several innovative banking products and strategic alliances entered into by commercial banks that are designed to bring more unbanked people into the financial mainstream. The essay concludes with a call for closer links between government EFT programs, asset-based social policies, and financial institutions' strategies to profitably develop the lower income market, including that consisting of residents of social housing.

THE SIGNIFICANCE OF THE MOVE TO EFT

In my book, *Savings for the Poor* (Stegman 1999), I suggest how a cluster of new public policies — most importantly, the federal transition to electronic funds transfer (EFT) or the delivery of government benefits through direct deposit — present new opportunities for financial institutions to better serve unbanked and marginally-banked populations in the United States, and to help people save. Because of EFT, the Treasury Department has undertaken several initiatives to stimulate the development of new, low-cost banking products for unbanked federal benefit recipients. As part of this transition, Congress has also required all fifty US states to convert their food stamp programs to electronic payment by 2002, using point-of-sale (POS) terminals at participating retailers. And, while not

required by law, more than forty states have added their emergency cash assistance programs to the plastic food stamp cards so that welfare benefits will be accessible at ATM and POS networks.

Although the move to convert millions of benefit checks to electronic payments was begun to save American taxpayers money — as much as \$100 million a year according to one estimate — EFT could be the first step toward greater financial independence for millions of low-income Americans. If partnered with financial literacy and savings initiatives for working people, EFT could help the poor build assets and become a critical link in the nation's transition from entitlement programs to policies that promote and reward work, self-sufficiency, and wealth accumulation.

The transition to EFT is not limited to the United States. For example, the Australian government makes 6 million welfare payments by electronic transfer each fortnight (Westbury 2000), and ambitious plans are underway in Great Britain to make the transition to EFT between 2003 and 2005. Like the US, the driving force in Britain is cost-efficiency rather than individual empowerment. Excluding actual benefit payments, administrative costs - including, security, printing, postage, and payment of a fee to the Post Office - amount to

79p a payment for girocheques (around a million payments a week) and 40p for each order book counterfoil (around 14.5 million payments a week). By contrast,

payment by credit transfer is very cheap — only 1p a time according to the Department's estimate.

Conversion to direct deposit of social security benefits in Britain, including the creation of a 'universal bank' that would be operated by the British Postal Service to serve low income individuals who are poorly served by commercial banks 'would save taxpayers an estimated £540 million a year (Economist 2000). Another important motivation for a Post Office-run bank is to make up some of the £400 million in lost revenues from the posting of benefit checks that will no longer be necessary when electronic welfare delivery put in place. While officials were are still working on the details when this essay was written, it is expected to offer accounts from which holders can pay bills, withdraw money from cash machines and receive electronic payments.

THE FUTURE OF COMMERCIAL BANKING

As suggested in the introduction, campaigns to reduce the number of unbanked and expand financial literacy and savings incentives come at a time when access to financial services for low-income families has become increasingly problematic. The interplay of many factors — among them the deregulation of interest rate ceilings in the 1980s, new technology, and growing competition from nondepository institutions — has led to a significant decline in the number of financial institutions in the United States and abroad, and has driven banks to charge for services that they formerly subsidized with cheap, regulated deposits. In the US, for example, the number of federally insured banks and thrifts declined by forty-three per cent over the last fifteen years, and the number of credit

unions fell by nineteen per cent in the 1990s (Stegman 1999; FDIC). At the same time, the banking industry is restructuring to focus on higher-income markets.

Thus, while the total number of banking offices has increased by 29 per cent during the last twenty years - nearly all of this growth has occurred in middle-and high-income areas -low-income neighborhoods in the US saw a 21 per cent decline in branch facilities (Avery et. al. 1997).

The same forces at play in the US are also changing the global banking landscape. In Australia, for example, an average of five branches per month are closing in regional and rural New South Wales alone (totaling 137 in NSW over the last two years) (Westbury 2000), while in Great Britain, over 4,500 bank branches have closed in the last decade, and consolidation is still underway. In April 2000, Barclays announced 172 branch closings, according to one account, putting businesses at risk and increasing social exclusion in disadvantaged communities (Benham 2000:7).

Growing competition with nonbanks such as money market funds and mutual funds, and technological advances have also been important factors in the move to fee-based banking. In the twenty-first century, banks in the US and abroad will meet their bottom lines more by charging fees for specific services than by living off the interest spread between taking deposits and making loans. This trend, which has important implications for lower-income consumers, is already discernible.

By October 1997, some 35 per cent of the total revenue for American banks came from fees, almost double the proportion in 1980 (*Economist* 1997). In practical terms the results of this phenomenon are higher transaction fees, charges for speaking with a live banking representative instead of an automated voice response telephone unit, or higher minimum balance requirements. For example, ‘the cost of using another bank’s automated teller machines has nearly tripled in the past four years to \$2.86 (U.S.) up from \$1.01 in 1996, when ATM surcharges were first allowed in most states.’ (*Washington Post*, 30 March 2001: E02)

Wells Fargo, which recently merged with Norwest Bank, now gives checking account customers three free calls into its automated-voice-response telephone lines and then charges 50 cents for each additional call. To speak to an agent to shift funds or ask questions, customers are charged \$1.50 per call (Perman 1998).

Like the other banking trends discussed earlier, the growth of fee-based banking and its implications for small depositors also transcends national borders. In 2000, New Zealand’s Commerce Minister called for an investigation into rapidly rising bank fees (*Dominion (Wellington)* 2000), while Industry Canada reports a distressing trend among Canadian banks to require higher minimum monthly balances to qualify for low-cost banking (Prentice 2001). Sociabank, for example doubled the minimum monthly balance required to avoid bank charges from \$1,000 to \$2,000, ‘which is the equivalent of an open-ended \$2,000 loan to the bank. At five per cent interest, that’s a \$100 – a-year cost to the customer’(Prentice 2001). Despite record profits, ‘Hong Kong’s biggest lenders, HSBC

and Hang Seng Bank, are ending free banking (*Deutsche Presse-Agentur*, 27 February 2001). Punjab National Bank in India has announced plans to increase fee-based income from its present level of 14 per cent of the bank's revenue to bring it closer to the 40 per cent benchmark of foreign banks (*Hindu*, 26 December 2000). Similarly, 'Bangkok-based Bank of Ayudhya aims to double its fee-based income to 20 per cent of total revenue over the next few years in order to compensate for the shortfall of income from lending.' (*Bangkok Post*, 6 October 2000)

THE EXPLOSIVE GROWTH OF 'FRINGE BANKS'

Though less well understood, studied, or regulated, there is a parallel system of financial services providers that primarily serve lower-income working class communities in the US and elsewhere in the world who are benefiting from these global banking trends while putting the poor at risk. The core of this 'fringe banking' industry, as it is commonly referred to by consumer advocates in the US, is a national network of check cashing centers and payday lenders that cash more than 180 million checks a year with a face value of \$55 billion (Stegman 1999). A study by the New York Office of the Public Advocate found that a customer with an annual income of \$17,000 will pay almost \$220 a year at a check-cashing business for services that would cost \$30 at a bank (O.N.E.: 5). The Federal Reserve Bank of Kansas City reached similar conclusions: A family with an annual income of \$24,000 will spend almost \$400 in fees at a check cashing outlet for services that would cost under \$100 at a bank. The Massachusetts Division of Banks found that, depending on the customer's income, the cost of cashing a weekly payroll check and writing money orders are 3.2 to 40.5 times more expensive at a check casher than if she used a low-cost

Basic Checking Account offered under the Commonwealth's basic banking program (Massachusetts Division of Banks 1999). These high fees add up. Over the course of a lifetime, ONE estimates, 'the cost of using a check cashing outlet . . . is more than seven (7) times the cost of using a basic checking account.'(O.N.E.: 5) Reliance on fringe bankers also has serious wealth implications. According to ONE, if the difference in fees saved by using a basic checking account instead of a check-cashing outlet were deposited in a standard savings account, a person would be able to save more than \$17,000 over an average lifetime of work (O.N.E.: 5).

Sometimes operating in standalone storefront facilities, and sometimes co-located with check cashers, payday lenders are an important part of the parallel banking system. Payday loans are high-interest, short-term sources of credit backed by post-dated personal checks, which borrowers promise to repay out of their next paycheck (Riccobono 2000).

No matter how the size of the industry is measured, the statistics are striking. Where virtually no payday loan outlets existed 10 years ago, industry analysts estimate there are now up to 10,000 of them, with total loan originations of between \$8 billion and \$14 billion in 2000 alone.² At an average of \$350 per loan, this translates to between 23 million and 40 million individual payday loan originations in 2001. Experts anticipate that a steady growth in loan demand to about \$20 billion a year by 2004 will fuel expansion at a rate of about 100 new payday loan outlets a month across the country (Blackwell 2000; CFSA).

The payday loan industry defends its high fee structure — my state of North Carolina, for example, sets a ceiling of \$300 on the amount that can be borrowed at any one time, limits fees to 15 per cent of the amount borrowed (which works out to \$45 on a \$300 loan), and provides for a maximum term to maturity of 31 days (North Carolina Cash Checkers Act 1998) - largely on the grounds that ‘small loans are relatively more costly per dollar to originate and service than are large consumer loans.’(Ellihausen and Lawrence year: 3) Because, the argument goes, payday loans are one of the few accessible sources of very short-term, *occasional* credit for hard-pressed consumers and are *not* intended to be a source of longer-term credit, the annual percentage rate (APR) is not a fair way of assessing the reasonableness of the cost of a two-week loan. In North Carolina, for example, the median APR for a payday loan in 2000 was 419 per cent.

The most urgent policy and regulatory challenges posed by payday lending relate to the repeated use of such loans. Rollovers occur when a borrower cannot repay a loan that becomes due and so renews it for another short term by paying another fee. Because of the high fees and very short terms, after just a few rollovers, ‘borrowers can find themselves owing many times the amount they originally borrowed.’(Riccobono 2000: 1)

That rollovers are a widespread problem is documented in audits by state regulators, studies, and academic research. For example, regulators found that 77 per cent of payday loans in Indiana are rollovers, with the average payday customer taking out more than 10 loans per year (DFI 2001). The average customer in California takes out 11 payday loans a

year,¹ while repeat usage is even greater in Illinois, where the typical customer averages more than one payday loan per month (PIRGs and Consumer Federation of America 2000). A typical payday loan customer in North Carolina took out about seven loans in 2000, a sizable increase over the 1999 level of 5.8 loans (North Carolina Check Cashers Act 1998).

The payday loan industry has its counterpart in countries across the globe, drawing its ‘customers from groups who find it difficult or inconvenient to borrow from banks and other mainstream financial institutions.’ (Meadows 2000) The British press has coined a new term — cash deserts — to describe communities in East London and elsewhere where banks have pulled out, forcing small merchants and others to turn to ‘cheque-cashing companies to get money, and face commission charges of 10 per cent or more.’(Andrew 2000) Another sign of the times is in Bristol, where loan sharks ‘take benefit books so they can demand repayment as soon as the benefit is claimed.’(*Bristol Evening Post*, 9 February 2001: 12)

Abuses in the parallel banking system are also evident in Borneo (Gunsika 2001), in Scotland, where the Office of Fair Trading has launched an investigation into extortionate agreements with money lenders (Hunter 2000: 9). And in the former Czech Republic, where small loans to welfare recipients by money lenders at interest rates of up to 100 per cent per month have become wide spread (CTK News 2001).

Reports from Uganda, suggest that ‘you can’t fail to bump into a money lender any 100 metres you walk in Kampala today,’ (Buwembo 2001) while business is booming for

¹“Sop Legal Loan Sharks.”

India's money-lenders, who are euphemistically known as 'blade' since the high rates of interest (of up to 3,650 per cent) are sharp enough to slit your throat.' (*Business Line* 2001)

The same can be said for Korea's more than 1,400 loan sharks - which account for about one fourth of that nation's 5,200 financial institutions (*Korea Herald*, 26 March 2001).

Further indication of the prolific growth of the parallel banking system is in Malaysia, where the Federation of Malaysian Consumer Associations recently urged Government to expedite approval of a proposed Consumer Credit Act to more effectively monitor money-lending activities.' (Malaysia General News 2001)

COMPLEMENTARY POLICIES TO EFT

A number of new US policy initiatives that complement EFT promise to further enhance the economics of serving unbanked and under-banked populations. The most important of these involve savings initiatives for working families like those being piloted in Individual Development Account (IDA) programs across the country that are discussed more fully below. Matched savings programs like IDAs can make EFT and related banking initiatives not only more powerful forces for individual empowerment; they can also significantly improve the economics of low-cost account products for banks. A few of these policy initiatives are discussed below.

First Accounts

In December 2002, the US Treasury Department expanded its EFT campaign with the launch of First Accounts, a \$10 million pilot program designed to encourage mainstream banks to target the other half of the unbanked — individuals without bank accounts who do not receive government checks. The goal of First Accounts is to move a maximum number of ‘unbanked’ low- and moderate-income individuals to a ‘banked’ status with either an insured depository institution or an insured credit union through the development of financial products and services that can serve as replicable models in other communities without the need for ongoing public subsidies. <<http://www.treas.gov/firstaccounts/>>

Recognizing the difficulty that mainstream banks have in reaching unbanked low and moderate income individuals, and the importance of achieving scale economies, Treasury believes that depository institutions are more likely to succeed if they forge strategic alliances with partners who have more direct access to the target market than they do, including employers, labor unions, faith-based organizations and other nonprofit organizations whose workers, members, and neighborhoods, respectively, include large numbers of unbanked individuals (Department of Treasury 2001).

Welfare Reform

American-style welfare reform is more widely recognized for ending the federally-guaranteed entitlement to means-tested public assistance for impoverished families than it is for legitimizing government’s role in helping the poor build assets. The rationale for an asset-based social policy is that assets promote a longer planning horizon by the poor, and a

variety of positive attitudes and behaviors, including household stability, community involvement, and political participation (Mills et al. 2000).

Welfare reform not only led to new rules that liberalized asset limits — North Carolina, for example, raised its limits from \$1,000 to \$3,000 — but it also encouraged savings by promoting Individual Development Accounts, or IDAs. IDAs are special savings accounts for low-income families and are restricted to the first-time purchase of a home, to higher education, and to small business capitalization. IDAs are like tax advantaged retirement accounts (commonly referred to as 401(k)s, after the section of the tax code that created them), except that IDAs provide an incentive to save by matching account holders' deposits instead of giving them the kind of tax breaks that are incorporated into 401(k)s. Participants are usually required to complete financial education courses provided by nonprofit organizations as part of the IDA programs (Corporation for Enterprise Development 1998: 1). The welfare reform law also permits states to use their welfare block grants to fund IDAs and account balances in eligibility determination for all means-tested federal benefits (Corporation for Enterprise Development 1998: 1). A total of thirty-one states have enacted legislation to support IDAs, with most of this legislation occurring since 1995 (Corporation for Enterprise Development 1998: 5).

Welfare reforms and asset building strategies are also under discussion in Europe. Press reports from France, Germany, and Italy suggest widespread recognition that soaring welfare budgets cannot be sustained (Crooks 2000). A recent public opinion poll found 'majorities in Germany, Italy and Spain supported the option of privatizing their social security retirement, while the French narrowly rejected the idea.' (Crooks 2000) Reforms in

the United Kingdom are also focused on driving people off benefits and into work (MacLeod 2000) and a new form of means testing, which the Labour Party refers to as ‘progressive universalism’ (Watson and Miles 2001), and a new emphasis on asset-building.

Individual Development Accounts (IDAs)

The most important thing that banks and communities should know about IDAs is they are proving that, with appropriate support and incentives, poor people *can* save. Two-year results from the nation’s largest national demonstration in fourteen US communities found that participants with incomes at about 130 per cent of poverty are saving an average of about 3 per cent of their income, or \$24 a month (Schreiner et al. 2000). Another study of eleven IDA programs showed that average account balances per participant were \$903, including both deposits and accrued match, ranging from a high in \$2,361 in Raleigh, North Carolina, to a low of \$362 in Chicago (Mills et al. 2000: 63).

And IDA savings don’t just displace savings families would otherwise accrue. For example, Stegman and Faris estimate that overall, the median participant in a national IDA demonstration saved \$117 more than she would have saved had she not enrolled in an IDA program (Stegman et. al. 2001). The mean savings increment is almost two-and-a-half times greater — \$285. The evidence suggests not only that low-income people can save, but that the resources offered by IDA programs are effective in helping people get into the habit of saving. These include financial education, peer support and encouragement, an

accessible and cooperating financial institution, and financial inducements in the form of matching funds.

The Assets for Independence Act (AFIA) enacted by the US Congress in October 1998 authorizes \$125 million in federal funds to support local IDA programs over a five-year period (Community Opportunities, Accountability and Training and Educational Services Act 1998). After appropriating \$10 million a year for AFIA in FY 1999 and 2000, in response to local program successes, Congress appropriated \$25 million for AFIA in FY 2001 (US Department of Health and Human Services 2001).

Congress has not yet passed the proposed Savings for Working Families Act (SWFA), which authorizes \$5-\$10 billion in federal tax credits for financial institutions and private sector investors to set-up, match, and support IDAs at financial institutions <<http://thomas.loc/cgi-bin/query/D?r106:1/temp/~r106CxPREY>>. Under SWFA, savings from any source would be matched on a 1-1 basis, up to \$500 per person per year. Financial institutions would be reimbursed for all matching funds provided, and for some of the banks' program and administrative costs (Corporation for Enterprise Development 2001). However, there continues to be strong bipartisan support for a national IDA program that would be funded on the tax side of the federal budget, and renewed efforts to pass SWFA are continuing.

As suggested above, interest in IDAs is also strong in Great Britain, with proposals focusing on children's savings accounts. One plan under study would include a state deposit of about £1,000 into a savings scheme for every child at birth, at a cost of £700

million a year (Grice 2001). Another would apportion £1,000 to every newborn baby and match savings contributions on a ratio of 3-1 for lower-income families. A third option would give a lump sum to young adults when they reach 18 and match the individual's contributions rather than those of their parents (Sherman 2001).

Programs to reduce the digital divide and help residents in social housing build assets

Most germane to the themes of this volume are two promising programs aimed at increasing the computer literacy and online access of residents of US social housing and motivating them to increase their labor market activity by dedicating earnings-induced rent increases to resident savings accounts.

Neighborhood Networks (NN)

Launched in 1995, NN is a community-based initiative by the US Department of Housing and Urban Development (HUD) that has thus far created more than 800 multi-service community technology centers in social housing. Tailor-made to fit each local community, NN centers open the doors — both on-site and via the Internet — to an infinite array of job opportunities, social services, microenterprise possibilities, and educational programs <www.hud.gov/nnwaboutnn.html>. While not directly linked to any government-sponsored banking initiative, because they provide online access, Neighborhood Network centers are a portal to a menu of electronic banking and financial education opportunities that increase the commercial potential of the social housing market to mainstream financial institutions.

The Family Self-Sufficiency (FSS) program

Created in 1990, FSS is an employment and savings incentive program for low-income families that receive either tenant-based rental assistance (housing vouchers), or who live in social housing (Sard 2001: v). The program is a combination of ‘case management services that help participants pursue employment and other goals, and of escrow accounts into which the public housing agency deposits the increased rental charges that a family pays as its earnings rise. Families that complete the program may withdraw funds from these accounts for any purpose after five years.’

Despite the fact that not all local housing authorities participate in the program, and not all social housing residents who enter the program, complete it, the results have are quite impressive. According to HUD, as of November 2000, almost half of the participants who had been enrolled in FSS for 12 months or more had positive escrow balances, which averaged about \$2,400. Even more impressive is the finding that these families were ‘adding to their accounts at the average rate of about \$300 per month.’(Sard 2001: vi) Furthermore, the families that ‘successfully completed the FSS program between the fall of 1999 and November 2000 received escrow funds averaging nearly \$5,000 per family.’(Sard 2001: vi)

INNOVATIVE PRODUCTS FOR THE UNBANKED

In the course of our research, we identified several account products that target the unbanked, which suggests that the industry is beginning to explore the commercial potential and behavior of this underserved market. Save for one technologically-advanced

product introduced by Standard Bank of South Africa, none have achieved the degree of market penetration necessary to capture scale economies and demonstrate commercial viability. The following brief descriptions of some of these products document the current state of practice and, hopefully, will encourage others to take a hard look at the business potential of serving the unbanked. As indicated above, some of these products are built around technology, while others are off-the-shelf products that are delivered through community development partnerships. Still others blend the products and services of fringe- and conventional-banks to help transition unbanked customers into the financial mainstream.

Technology-Based Products

Banco Popular's Acceso ETA and Acceso Popular Accounts

As part of the federal government's campaign to convert more government checks to direct deposit, the Treasury Department created a new, low-cost account called the Electronic Transfer Account, or ETA. The department hopes to attract unbanked recipients of Social Security and other federal benefits to open ETAs and then sign them up to receive their federal benefits by direct deposit.

To encourage banks to offer ETAs, the Treasury Department compensates financial institutions \$12.60 for each new account that is opened. This one-time fee is intended to fully offset institutions' account set-up costs. Among the ETA's features are:

- Maximum cost of \$3.00 per month;

- Minimum of four cash withdrawals and four balance inquiries per month, to be included in the monthly fee, through any combination of proprietary ATM transactions or over-the-counter transactions;
- Access to the institution's online point-of-sale (POS) network, if available;
- No minimum balance, except as required by state or federal law;
- Account to be interest-bearing or noninterest-bearing, at the discretion of the financial institution;
- A written monthly statement. (Financial Management Service 2001)

The transition to direct deposit of federal benefits is much slower than the government had hoped. In the first year, only about 5,000 people had opened an ETA account. However, one particular bank - the \$18.4 billion asset of Popular Inc., Banco Popular de Puerto Rico - has distinguished itself as a model provider of high tech banking services to unbanked individuals who receive government checks (Daigle 2000).

As of 31 October 31 2000, Banco Popular (BP) had opened more than 3,000 ETA accounts, which is more than sixty per cent of all ETAs opened by all US banks (Daigle 2000; US Department of Treasury 2000) BP attributes its success to three factors: (1) serving the unbanked is a long and honored tradition of the People's Bank of Puerto Rico — its 2001 business plan calls for converting an additional 35,000 unbanked individuals; (2) it uses its most sophisticated technology and delivery systems to create low-cost, *and* low-risk accounts for financially marginalized populations, including debit cards without checking privileges to prevent overdrafts; and (3) despite low account service charges — ETA

charges are limited by the Treasury to \$3 a month—Banco Popular invested more than \$100,000 in a marketing campaign and provided financial incentives to employees for every ETA account they opened during the early months of the campaign.

Tracking Treasury's First Accounts program discussed above, BP has also created a companion account for other unbanked individuals, called Acceso Popular. Unlike its ETA product, the electronic Acceso Popular account includes a savings component. To simplify account management, reduce risk to both the bank and the account owner, and to avoid overdrafts, Acceso Popular provides for no check writing privileges or off-line credit transactions. Also, unlike Acceso ETA, this account features a savings plan option that permits the automatic transfer of a pre-specified amount of money each pay period from the transaction-side of the account into the savings-side.

Acceso Popular account holders have electronic access to the transaction purse through ATM and POS terminals, but to discourage savings withdrawals on impulse, there is no electronic access to the savings purse — all withdrawals have to be made in person at a bank branch. Introduced in March 2001, Banco Popular opened more than 59,000 Acceso Popular accounts by the end of the year, with fully half of the account holders having activated the savings component, giving further evidence that, once they enter the banking system, poor people are able to save.

Standard Bank of South Africa's Auto E-Bank

According to an analyst at McKinsey and Company, Standard Bank of South Africa is defying ‘the conventional wisdom of the financial-services industry: that the low-income market is at best marginal, at worst disastrous.’(Moore 2000) The bank created its E-Bank (later renamed E-Plan) program in the 1990s to serve a growing market of low-income, largely illiterate wage-earners who could no longer receive their pay in cash because of growing crime problems (Moore 2000). When employers switched to paying employees by check or direct deposits, Standard Bank was flooded by waves of unbanked customers (Moore 2000). Operating exclusively through a ‘fingerprint-secured’ debit card system and ATM network that is programmed to give operating instructions in each of South Africa’s eleven official languages, costs per outlet are 30 per cent to 40 per cent below those of traditional branches (Moore 2000). ATM technology greatly reduces the delivery and service expenses of transactions and sales (since there is no back office) and the bank minimizes unit cost of its ATMs by using education and incentives to maintain high transaction volume (Moore 2000). E-Plan grew to around 340,000 accounts by 1996. By 1999, the number of E-Plan accounts had grown to 2.6 million, with around 50,000-60,000 new accounts opened each month (Moore 2000).

FleetBank Boston Financial’s CommunityLink (CL)

Not all electronic banking initiatives are aimed at the unbanked. Because an online transaction costs just a fraction as much as an over-the-counter, branch transaction, financial institutions are developing marketing strategies and pricing policies to encourage more of their customer base to migrate from branch-based to online-banking. One particularly interesting effort, called CommunityLink, is being implemented by Boston-

based Fleet Bank to encourage lower income account holders - a more difficult market to reach - to move to online banking.

CL is a comprehensive community economic development initiative that is being implemented in up to five neighborhoods within Fleet's footprint and is intended to stimulate wealth creation by providing greater access to online financial services in low and moderate income (LMI) communities (Moore 2000). To participate in CommunityLink, households must have an annual income under \$50,000 a year (with a priority going to households under \$40,000), have a minimum Fleet Savings or Checking account in good standing for at least six months, currently not own a personal computer in the home, and be willing to participate in ongoing training and ongoing surveys.

In an effort to reduce the technology gap CL is providing state of the art computer hardware, software, and Internet service to the homes of up to 3,000 LMI customers at no cost, along with the necessary training and technical assistance to help people get online.³ Like One Economy, through this technology, CL will provide local information and culturally appropriate content to the pilot communities to increase their knowledge and to maintain an on-going customer relationship with them, using Fleet's online financial services and products.

Given the importance of the Internet as a cost-effective delivery channel and the fact 'the "easy" markets of well-educated, affluent knowledge workers are already wired up,' it is

probable that first-mover advantages can accrue to the institution that figures out how to best connect with CommunityLink's market segment (Cavanagh 1999).

Community Development Banking Partnerships

Chicago CRA Coalition and Bank One's Alternative Banking Program (ABP)

'The Coalition, which is convened by the Woodstock Institute...developed an agreement with Bank One when it purchased First Chicago Bank NBD in 1998,' that included a pilot program 'to promote deposit services to unbanked customers.' (Williams 2000) 'Rather than a separate product, 'the Alternative Banking Program (APB) incorporates into standard Bank One products features similar to a model lifeline account, including: \$10 to open an account, minimum balance as low as \$0...unlimited check writing, unlimited use of Bank One ATMs, and some free teller transactions, depending on the account.' (Williams 2000)

Bank One [also] conducts financial literacy workshops in cooperation with community partners to demonstrate cost savings over check cashers, improve financial management skills, and increase trust...with mainstream financial institutions. Although applicants with a credit history must have suitable credit scores, people with no or borderline credit may also open accounts. In exchange for more flexible credit criteria, the bank established some modest restrictions on the ABP. However, after one year, account holders can apply to upgrade to traditional account[s].

(Williams 2000)

Shore Bank's Extra Credit Savings Program

The nation's preeminent for-profit community development bank, South Shore Bank (SSB), and the Center for Law and Human Services created the Extra Credit Savings Program to encourage unbanked working poor to save a portion of their sizable Earned Income Tax Credit (EITC) refunds by providing them with low-cost savings accounts (Beverly et. al. 2000). Between January and April 2000, the Tax Counseling Project of CLHS offered free tax preparation assistance to EITC-eligible individuals two nights a week at a SSB branch (Smeeding 2000). On these evenings, SSB bankers invited individuals to join the ECSP. Those who chose to participate opened a no-fee, no minimum balance savings accounts and arranged to have some portion of their 1999 federal tax refunds directly deposited into the accounts. Funds in these accounts earn a market rate of interest, and include a no-fee ATM card to those who desire one. As encourage savings and discourage early withdrawals, participants receive a 10 per cent bonus on any funds remaining in their account at the end of the year (up to a maximum bonus of \$100 per account-holder) (Beverly et. al. 2000). Over the first two years of the program, this innovative partnership has attracted more than 200 account holders and initial deposits of \$200,000 (ShoreBank and the Center for Law and Human Services 2001).

The Big Issue and Bank of Scotland Banking for the Homeless Partnership

'Not surprisingly, homeless people are almost entirely excluded from banking services, yet they are among the most at risk of assault and robbery living as they do on the streets or in dangerous hostels.'(Guardian 2001) This is why the efforts by the Big Issue-Bank of Scotland partnership is so exciting. Set up in 1991 to give homeless people the chance to

make an income, Glasgow-based Big Issue ‘campaigns on behalf of homeless people and highlights the major social issues of the day.’ <www.bigissue.com/home.htm> Six years ago, The Bank of Scotland enabled Big Issue vendors and other homeless people to use its easy cash, no-frills accounts by accepting Big Issue vendor badges as proof of identity to open a bank account. But homeless people weren’t making full use of the services because they were embarrassed to go into ‘posh’ bank branches, and embarrassed to be depositing small amounts of money - £1 or £2 at a time — in such places. This led to the creation of Grand Central Savings — a ‘branch’ of Bank of Scotland for the exclusive use of homeless people, based in the Big Issue in Scotland’s Glasgow headquarters. In its first two weeks of operation nearly 60 homeless people opened bank accounts, and the organizers are confident that there will be 200 within the year.

Transitions to Mainstream Banking

Union Bank of California’s Cash & Save Program

Union Bank’s Cash & Save is a hybrid program that goes beyond check cashing by using education and consulting services to transition previous check-cashers users to traditional banking services (Stegman 1999). ‘[W]ith profit margins ranging from fourteen percent to fifty-one percent at its fifteen locations, Cash & Save [successfully] competes with other check cashing outlets.’ (Glassman 1996) ‘But what differentiates it is the way it tries to bring unbanked customers into the financial mainstream rather than simply exploiting profit from their financial alienation.’ (Glassman 1996)

Cash & Save provides a full range of services targeted to lower-income, ethnic markets with large contingents of unbanked workers. While each location provides basic check cashing services — at lower fees than those generally charged by [check cashers]—what really distinguishes Cash & Save from other check cashing operations is the range of banking services that it provides. Under its Money Order Plan, which carries a one-time fee of \$10, customers get six free money orders per month plus a 1 per cent check cashing charge. With Nest Egg Savings, a customer can open a no-fee, passbook interest rate savings account with an initial deposit of \$10 and a commitment to deposit \$25 monthly for at least one year. Cash & Save also offers a basic checking account for...as little as one dollar, a secured credit card for people who are repairing their credit rating, and a direct deposit option for the electronic delivery of government benefits.

(Glassman 1996: 80)

Almost one third of Cash & Save customers converted to traditional banking services in 1997, up from 14 per cent in 1996 (Comptroller of the Currency 1998).

Efforts to Reduce the Digital Divide and Encourage Online Banking

Several efforts are underway to reduce the digital divide, including the Neighborhood Networks program, discussed in the previous section, that targets residents of US social housing. Improved computer literacy and access to the Internet where they live, provides

residents of social housing a convenient and economical pathway to the world of e-commerce, including online banking services.

One Economy

Enterprising businesses and non-profit organizations have also begun to recognize the potential of the Internet to reach, educate and market a variety of goods and services to residents of social housing. One of the more ambitious developments in this area is the creation of One Economy, a national nonprofit organization headquartered in Washington, D.C. whose goal is to ‘maximize the potential of technology to help low-income people raise their standard of living and build assets.’ <www.one-economy.org/aboutus.asp> The core element of One Economy’s operation is the construction of a consumer web site called the Bee Hive <www.theBeehive.org> to provide, among other things, low-income individuals with a suite of Web-based products and services focusing on financial services, education, jobs, health care, and homeownership that help them build assets and raise their standard of living. <www.thebeehive.org/money>

CONCLUSION

We have a very serious problem with under-saving in the United States. As former Senator Bob Kerrey has said, ‘In a global economy, your economic health and security is measured by what you own, in addition to what you earn.’(Kerrey 1997) About 30 per cent of American households have no financial assets, and about half of all children in the United States are growing up in families that have no financial assets. Along racial lines, the difference in asset-holdings between whites and African Americans is far greater than the

difference in their incomes (Oliver and Shapiro 1995). Under-saving for retirement is another big problem. As it has done for generations of middle- and upper-income Americans, the federal government should create policies that make compound interest work for the poor and help those with lower incomes join the asset-building classes. This is why it is so important to use the transition to EFT as the vehicle for giving lower-income, low-wealth Americans — in Kerrey’s words — ‘a chance to own a piece of their country.’

By bringing millions of unbanked people into the financial mainstream, EFT can facilitate savings by providing recipients with bank accounts, but alone will not provide them with a concrete incentive to save. We have a golden opportunity to expand EFT’s impact by linking it with a national economic literacy campaign and new savings initiatives targeted at the working families of America who don’t benefit from existing tax-preferred savings incentives such as individual retirement accounts.

The growing political support for asset-based programs together with the advent of EFT present a critical opportunity for the nation to adopt a full-scale IDA program that will incorporate not only families in social housing, including those who are moving off welfare, but also the working poor. A national IDA program coupled with EFT would help millions of family develop an emergency cushion to help weather unemployment and other short-term setbacks as well as to build their long-term financial strength by investing in homes, job training and small businesses. While it might be possible to create a national program without linking it to EFT, coordinating the two together would improve partnership-building, outreach and education efforts.

There is a clear link between EFT and the banking partnerships discussed in this essay, and the IDA movement. To succeed, both require strong grassroots support and intensive outreach, education, and training in financial education. Treasury is sponsoring a two-pronged education campaign for EFT, one to a broad array of stakeholder groups emphasizing the benefits of direct deposit, and the other to unbanked benefit recipients on basic finances, including how to maintain a bank account and how to make the best informed choices. Hundreds of local community organizations are helping with the grassroots public outreach efforts (Hawke 1997).

A national IDA initiative could contribute to the success of EFT by providing benefit recipients with a substantial incentive to save. And by increasing the number and size of savings deposits, a national IDA program such as that envisioned by sponsors of the proposed Savings for Working Families Act, could also improve the economics of low-balance accounts by providing banks an inexpensive source of longer-term deposits, thereby increasing 'float'.

Finally, while not directly tied to EFT, but important nonetheless, IDAs can help keep hard-pressed workers out of the clutches of exploitive payday lenders if they permit early withdrawals to pay for family emergencies. IDA programs could allow accountholders to make up the difference within a specified amount of time to avoid losing previously earned matches.

NOTES

- 1 Gavin Kelly, Welfare: Nest Eggs: The Government is listening to new ideas from the US to invest money for each newborn baby as a way of helping people on low incomes save for the future, says Gavin Kelly, *The Guardian (London)*, 7 June 2000: 8.
- 2 Estimates vary; see, for example, Community Financial Services Association of America, at <www.cfsa.net/geninfo.html>. Downloaded April 27, 2001; Frank J. Diekmann, 'More Questions than Answers: Issues Related to Credit Unions and Payday Lenders Are Almost as Numerous as the People in Line', *Credit Union Journal*. 4 (48), 27 November 2000: 6; Rob Blackwell, 'Warning on "Payday" Partnerships', *The American Banker*, 28 November 2000: 32.
- 3 Although Community Link will include about 100 small businesses, the RFP addresses only the residential customers, which will number about 2900. Therefore, our research design addresses the impacts of CL on residential customer behavior, banking activities, and related issues.

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