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Going for Growth

Promoting Access to Wealth Building Financial Services in Massachusetts Gateway Cities

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Residents of the Commonwealth familiar with our economic past know the great contributions provided by historic mill cities, communities MassINC terms "Gateways" for their role as regional economic hubs and escalators to the middle class. Unfortunately, like so many others cities throughout the Northeast and Midwest, these communities have been hit hard in recent decades by both suburbanization and decline in domestic manufacturing.

MassINC and others have argued that the state could gain real benefits by helping Gateway Cities reinvent themselves to compete in a new era.[2] These 11 cities are engines in their regional economies, well-positioned to drive growth in other parts of the Commonwealth. They also disproportionately represent the young human talent that will provide the state's next generation of workers, along with lower-cost, higher density, transit-connected housing needed to accommodate our future growth.

New partnerships and policies are needed to help Gateway Cities leverage these strengths and reposition for the Commonwealth's 21st century economy. This paper —the third in MassINC's *Going for Growth* series— focuses on helping Gateway Cities tap into the growing effort to connect low-income families with wealth-building financial services.

This topic belongs at the top of the Gateway City growth agenda because financial services that help families build wealth give them greater economic security —stability that translates into more productive adults, and children more likely to gain the skills they need to succeed.

At present, many lower-income Gateway City residents rely on high-cost financial products that strip wealth. Too many families do not have bank accounts, which leaves them dependent on high-cost services like check cashers. Without bank accounts, families also have difficulty developing the credit history needed to qualify for low-interest loans. They turn instead to pawnshops, rent-to-own stores, and auto title lenders with much more costly interest rates and fees. At tax time, their valuable Earned Income Tax Credit (EITC) payments are reduced by tax preparers pushing costly Refund Anticipation Loans, products that directly undermine government attempts to make work pay.

Experts from the Brookings Institution and elsewhere have argued that lower-income families in communities like the Gateway Cities could save thousands of dollars annually by using mainstream banks instead of these high-cost providers. With incentives to direct their savings toward asset building investments, residents could create a stronger economic future for themselves and their communities.

Steps have already been taken by all sectors toward achieving this goal, and momentum behind these efforts continues to build. By exposing the need to foster responsible lending in lower-income communities, the current financial crisis adds even greater urgency. Many public, private, and nonprofit organizations are now focused on finding innovations that will improve wealth building opportunities. While current fiscal realities make it difficult to advance other Gateway City growth strategies, the energy around this issue makes the timing right for communities looking for opportunities to build partnerships and strategies that will not require large state and local investments.

This policy brief examines the current market for financial services in each of the Gateway Cities. We then summarize past efforts to promote access to wealth building financial services, and highlight emerging new opportunities. The brief concludes with a number of recommendations to help communities capitalize on innovative new pathways to high-quality financial services.

I. The Gateway City Market for Personal Financial Services

Efforts to connect Gateway City families to wealth-building financial services require a clear understanding of the complex market for personal financial services in these communities. Unfortunately, it is difficult to draw a complete portrait of these markets with readily available data. However, basic information gathered from phone books and other public sources provides a starting point with useful details about the relative density of high-cost financial service providers in each community. These data suggest many Gateway Cities have large concentrations of high-cost providers. These services cost residents, and Gateway City economies indirectly, millions of dollars each year. The data also show that, within these communities, high-cost providers compete directly with mainstream banks located in the same neighborhoods. These bank braches have the infrastructure to offer lower-cost basic financial services that can help Gateway City families save money and build wealth.

A. Providers of high-cost financial services are located throughout lower-income Gateway City neighborhoods.

Gateway Cities are home to large numbers of check cashers, pawnshops, and paid tax preparers (Table 1). This concentration of non-bank basic financial services suggests residents in these communities spend significant sums on high-cost financial products.

Check cashing is the most ubiquitous of these pricey services. Households without bank accounts often rely on check cashers to access their pay. While it is hard to know exactly how many Gateway City residents lack a bank account, estimates from other communities suggest approximately 30 percent of families in low-income urban neighborhoods do not have a checking or savings account.[3]

Currently, 43 check cashers serve the 11 Gateway Cities. These businesses are particularly concentrated in Springfield (19), Worcester (8), and Holyoke (4). To the extent that check cashers also offer services to send money abroad, larger immigrant populations in these cities may help explain higher concentrations in these three communities. Nevertheless, the compact size of Gateway Cities means that residents in most of these communities are fairly close to a check casher. Geographic analysis places

Table 1

Proximity to Providers of Alternative Financial Services

	CHECK CASHERS		PAWNSHOPS		TAX PREPARERS	
	NUMBER	AVG. DIST. (MILES)	NUMBER	AVG. DIST. (MILES)	NUMBER	AVG. DIST. (MILES)
Brockton	3	0.81	1	1.10	18	0.52
Fall River	1	1.39	6	0.60	11	0.39
Fitchburg	0	-	1	1.37	3	1.13
Haverhill	1	0.90	1	0.93	3	0.83
Holyoke	4	0.27	1	0.61	8	0.30
Lawrence	1	0.73	1	0.72	9	0.37
Lowell	1	0.93	2	1.01	8	0.58
New Bedford	3	0.67	1	1.59	12	0.40
Pittsfield	2	0.78	0	-	6	0.49
Springfield	19	0.46	6	0.77	20	0.35
Worcester	8	0.76	6	0.87	25	0.45
Gateway Cities	**43**	**0.77**	**26**	**0.96**	**123**	**0.53**

Source: MassINC's analysis of data from yellowpages.com the average resident within three-quarters of a mile of a check cashing outlet.

Typically check cashers set rates at the maximum legal level. Unlike many states, Massachusetts does not impose limits on check cashers.[4] The average rate charged by check cashers nationally is 4.5 percent for payroll and 3.2 percent for government checks. This translates to $80 per month in fees for the median income unbanked household with a full-time worker.[5]

In contrast to check cashers, which generally offer a service similar to mainstream banks and credit unions only at a higher cost, the short-term loans provided by pawnshops are often the only credit option for lower-income families struggling to manage daily expenses.[6] But the inefficient pawnshop business model, coupled with limited regulation, mean customers relying on these loans often pay exorbitant interest rates. While in theory Massachusetts usury laws do restrict interest on pawnshop loans, historically lax oversight of pawnshops has led to much higher fees. A 2007 *Boston Globe* investigative report found pawnshops charging annual interest rates over 100 percent in urban areas throughout the state.[7]

Geographic analysis of phone book data indicates the average Gateway City resident lives less than a mile from one of the 26 pawnshops operating in these 11 communities. But pawn loans provided by jewelry stores and other retailers are difficult to distill from phone book listings. High-cost lending is probably much more widespread than this total suggests. Still, phone books show high concentrations of pawnshops in many Gateway Cities. Fall River, Worcester, and Springfield each have six outlets making high-cost loans.

Tax preparation is another financial activity associated with harmful lending in Gateway City neighborhoods. In recent years, state and federal governments have increased income support to low-wage earners through earned income tax credits (EITC). This results in much larger tax refunds, which has led to the proliferation of paid tax preparers in low-income communities. Too frequently, tax filers choose to utilize the Refund Anticipation Loans (RALs) offered by these commercial tax preparers. This service gives tax filers instant access to refunds rather than waiting a few days for a check to arrive by mail.

Tax preparers assume virtually no risk since the loan is backed by a government refund, but interest rates range from 50 to 500 percent APR. Estimates suggest the average taxpayer opting for a RAL forfeits 8 percent of their return in fees.[8]

Gateway Cities have 123 tax preparers. This high concentration places residents within a half mile of these costly services. Worcester (25) and Springfield (20) have the highest number of tax preparers, followed by Brockton (18) and New Bedford (12).

Across the Gateway Cities, the financial services provided by check cashers, pawnshops, and tax preparers are relatively concentrated in lower-income neighborhoods. However, check cashers and pawnshops are particularly more likely to locate in struggling neighborhoods. The average median family income of neighborhoods where check cashers locate is a third lower than the average Gateway City neighborhood's median family income (Figure 1).

The tendency for these services to serve lower-income families explains at least some of the variation in the concentration of these high-cost services across Gateway Cities. Haverhill, the city with highest median income, has just 0.3 check cashers and pawnshops per 10,000 residents. At the other end of the spectrum, Springfield is home to

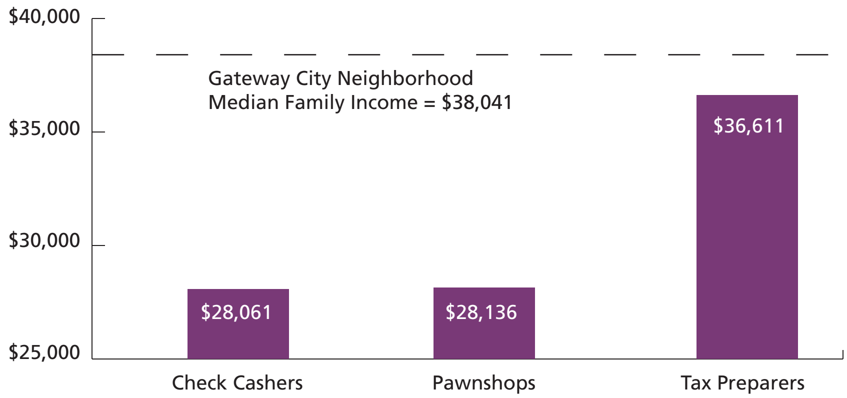
These services cost residents, and Gateway City economics millions of dollars each year.

ABOUT THE ANALYSIS

This section describes the location of both mainstream and alternative providers of financial services in Gateway City neighborhoods following the approach taken by Matt Fellowes and Mia Mabanta in a 2008 Brookings Institution report that looked at the distribution of these services in neighborhoods nationally. The analysis relies on publicly available listings from the Federal Deposit Insurance Corporation (FDIC) and the National Credit Union Association (NCUA). Only full-service branches are included. To describe the locations of check cashing outlets and pawnshops, MassINC relied on data gathered from yellow page listings.

Figure 1

Neighborhood Median Family Income by Financial Service



Source: MassINCs analysis of data from US Census Bureau

Table 2

Low and High-Cost Financial Services by City

CITY	LOW-COST SERVICES BANKS & CREDIT UNIONS PER 10,000 RESIDENTS	HIGH-COST SERVICES CHECK CASHERS & PAWNSHOPS PER 10,000 RESIDENTS	RATIO OF LOW-COST TO HIGH-COST SERVICES
Brockton	2.90	0.43	6.8
Fall River	3.85	0.77	5.0
Fitchburg	2.01	0.25	8.0
Haverhill	2.50	0.33	7.5
Holyoke	3.02	1.26	2.4
Lawrence	1.28	0.29	4.5
Lowell	2.13	0.29	7.3
New Bedford	2.18	0.44	5.0
Pittsfield	4.89	0.47	10.5
Springfield	2.60	1.67	1.6
Worcester	2.64	0.80	3.3
Gateways	**2.66**	**0.72**	**3.7**

Source: MassINC's analysis of data from FDIC, NCUA, and yellowpages.com

1.7 check cashers and pawnshops per 10,000 residents. Income, however, does not fully explain differing market dynamics across the 11 communities. In Lawrence, where the median income is similar to Springfield, the concentration of these non-bank services is actually lower than Haverhill (Table 2).

Aside from income, a number of factors shape demand for non-bank financial products. First, in some communities, local banks may simply not offer services well-suited to the needs of low-income customers, which increases the market for alternative providers. Second, communities may have large immigrant populations. The unique barriers to banking that these residents face creates additional demand for non-bank products (see text box). And third, some communities may deter providers of these high-cost services by establishing interest rate limits and strictly enforcing regulations. Additional research is needed to better understand the variations in demand for these services across the Gateway Cities.

B. Gateway City economies lose approximately $72 million a year to providers of these high-cost financial services. This large transfer of wealth has a significant impact on local economic growth.

While it is difficult to estimate accurately the total market for high-cost financial services in Gateway Cities, by combining national averages with available local data it is possible to develop some conservative estimates for both check cashing and tax preparation (Table 3).

Check cashing is clearly a costly service, but it is also hard to quantify since check cashers are lightly regulated, fees vary, and it is impossible to know for certain the size of the market. However, a rough estimate based on national averages suggests Gateway City residents incur at least $38 million in check cashing fees annually.[9]

The cost of paid tax preparation is easier to quantify because the IRS collects detailed data through the tax filing process. For all 11 Gateway Cities in the 2006 tax year, nearly 73,000 residents (17 percent of all tax payers) paid to receive their refunds more quickly in the form of a Refund Anticipation Loan (RAL).[10] This led to an estimated $13 million in interest and service fees.[11]

In addition to the direct cost to families, these tax services have an indirect cost on local economies. One recent study found the flow of federal EITC transfers generates $1.58 in local spending for every refund dollar received.[12] In Gateway Cities, recapturing lost EITC dollars would lead to an additional $20 million in economic activity each year.

The combined $72 million lost to check cashing, refund anticipation loans, and EITC associated economic activity are very conservative estimates of the total cost for these fringe financial services. Others would include the high fees low-income workers often pay for basic tax preparation, along with rent-to-own and auto title lending, other costly services utilized by families with limited wealth and credit histories. To put just this $72 million into perspective, state EITC payments to Gateway Cities in the 2006 tax year totaled $25.8 million annually. If families retained just half of the dollars that flow out through high-cost financial services, it would equate to more than doubling the value of the state EITC.

Table 3

Direct and Indirect Cost of Check Cashing and Refund Anticipation Loans ($ millions)

CITY	CHECK CASHING FEES	RAL FEES	EITC MULTIPLIER	TOTAL COST
Brockton	3.5	1.4	2.2	7.1
Fall River	4.1	1.1	1.8	6.9
Fitchburg	1.6	0.5	0.7	2.8
Haverhill	2.4	0.6	0.9	3.9
Holyoke	1.6	0.6	0.9	3.1
Lawrence	2.6	1.6	2.5	6.6
Lowell	3.9	1.2	1.8	6.9
New Bedford	4.0	1.2	1.9	7.1
Pittsfield	2.1	0.5	0.8	3.3
Springfield	5.8	2.6	4.1	12.6
Worcester	6.8	2.0	3.2	12.0
Gateways	**$38.3**	**$13.1**	**$20.8**	**$72.2**

WHY NOT BANK?

The reasons why low-income families have difficulty connecting to low-cost financial services are multiple and complex. According to national surveys, the most common explanation given for not having a checking account is dislike of banks (25 percent) followed by those who do not feel they write enough checks (19 percent). Other survey respondents list high bank fees (12 percent) and minimum balances (8 percent) as the deterrents. Smaller numbers do not use a bank account due to issues with credit (7 percent), or because there is not a bank branch with a location or hours convenient for them (1 percent).[15]

In very low-income communities, a cash economy may reduce the utility of checks. Surveys have found that many landlords in these neighborhoods will not accept personal checks. Providers of non-bank financial services may simply offer products that better serve the needs of low-income families, particularly recent immigrants who benefit from bilingual staff and money transfer services to send remittances abroad.[16] Even in communities where banks offer comparable products, residents may not trust banks or have limited knowledge of the services provided by them. Distrust based on experience with inflation and corruption in less stable economies is common among immigrants.

Non-citizens also faced identification challenges after the passage of the USA Patriot Act in 2001, which mandated stricter identification requirements for financial institutions. While the act allowed for the use of Individual Tax Identification Numbers (ITIN) issued by the IRS as an alternative to social security numbers, for a time, many Massachusetts did not accept ITINs as an alternative form of identification, although reports suggest this issue may have largely been resolved.[17]

Forgoing the services of a bank has a variety of costs in addition to the fees incurred by reliance on check cashers. Families without bank accounts have more difficulty saving, which makes it harder to weather a crisis brought on by job loss, injury, or other unfortunate event. Without savings, buying a home or financing education is more challenging. Bank holdings also help individuals develop credit to qualify for lower interest rate loans.

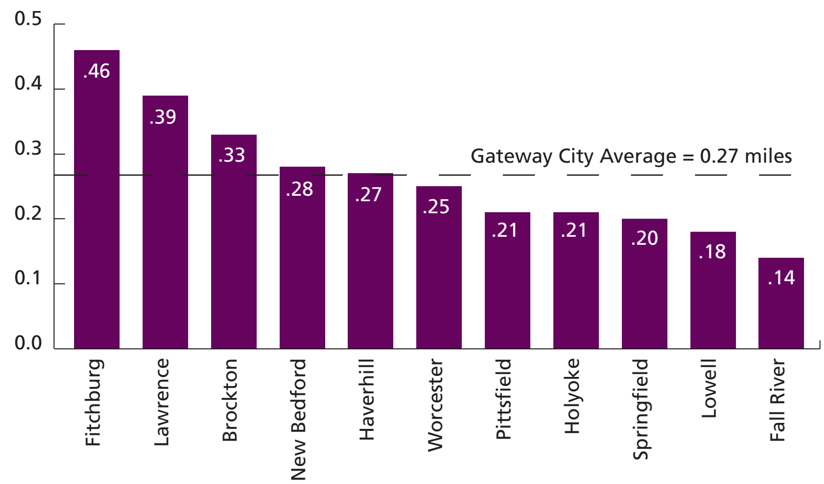
Others have an entirely different view of why low-income families avoid traditional banks. They believe these consumers make appropriate decisions given their personal circumstances. When a family is living paycheck to paycheck or earning inconsistent wages, the fees from overdrafts, not maintaining a minimum balance, or making late payments may be enough to drive a family away from mainstream financial products. In these circumstances, the weekly fee necessary to access a payroll check through a check-cashing outlet may seem more affordable and appealing.[18]

C. Most unbanked Gateway City residents live near a bank or credit union with the infrastructure to offer basic financial services that help lower-income families build wealth.

A common misconception is that low-income families rely on high-cost financial services because their neighborhoods lack traditional banking institutions. This is not generally the case. In surveys of the unbanked, a very limited number of respondents indicate that living far from a branch is a deterrent to having an account.[13] Moreover, studies consistently find banks are fairly evenly spread across neighborhoods with varying income levels.[14]

Figure 2

Average Distance to a Bank or Credit Union



Source: MassINC's analysis of data from FDIC

The average Gateway City family lives just over a quarter of a mile from the nearest bank or credit union. More than 80 percent of all Gateway City residents live within a half mile of a bank or credit union.

These data show that, within Gateway Cities, providers of low- and high-cost services compete in the same spaces. The average check cashing outlet is located less than a third of a mile from the nearest bank or credit union. This finding is also consistent with studies nationally.

Helping families move from high-cost providers to a low-cost bank nearby could generate significant savings. According to simulations developed by Fellowes and Mabanta, a typical unbanked full-time worker could save $41,600 in check cashing fees over the course of their career. Workers who invest the money saved by avoiding these check cashing fees in a Certificate of Deposit (CD), an Individual Retirement Account (IRA), or other interest bearing savings products could accumulate $90,000 in wealth by the time they reach retirement. While this would require drastic changes in the way families with tight budgets manage money, as described in the next section, leaders in the field are already experimenting with products that could bring about this dramatic change.

II. Expanding Access to Low-Cost Financial Services and Promoting Asset Accumulation

In recent years, foundations, community organizations, and governments at all levels have experimented with a variety of approaches to give low-income families greater access to mainstream financial services. This work has led to some success, but unfortunately, it has not been able to forestall competition from high-cost providers. This persistent challenge gives greater energy to ongoing efforts to connect low-income families with wealth building financial services. The current economic environment, marked by predatory lending, credit tightening, and family economic instability, has only added greater urgency to this goal.

Fortunately, heightened focus on this issue coupled with emerging innovations opens new opportunities. Promising new products are coming from a variety of sectors including high-cost providers facing increasing scrutiny, banks and credit unions competing for new customers, and government agencies working with renewed commitment to connect low-income families to wealth-building financial services. A review of these ongoing interventions and new innovations can inform strategies to help Gateway City families establish pathways to wealth building financial services in this rapidly evolving landscape.

A. Efforts to Increase Access to Financial Services in Low-Income Communities

Since the early-1990s, there has been a flurry of activity aimed at connecting low-income families to mainstream financial services. These efforts were spurred by Michael Sherraden's transformative 1991 book, *Assets and the Poor*, which argued social policy should advance from providing income support to helping low-income families achieve security by building their assets. Recent interventions include (1) improving legislation that encourages lending in low-income communities, (2) creating community development financial institutions (CDFI) charted to serve low-income neighborhoods, and (3) developing specialized products and services that engage low-income families more directly.

1. Legislation to encourage lending in low-income communities

One major avenue of attack to connect unbanked families to mainstream financial services has been to ensure an end of discriminatory practices that have historically hampered access for poor and minority households. The federal Community Reinvestment Act (CRA) was passed in 1977 in response to redlining, the overtly discriminatory practice by which banks denied borrowers in low-income minority neighborhoods access to loans without regard to their qualifications. Redlining contributed to disinvestment and decline in urban areas throughout the Northeast and Midwest, including Massachusetts Gateway Cities.

The CRA encourages banks to lend in all communities in which they take deposits. Its teeth are evaluations performed by bank regulators. When banks request permission to merge or open a new branch, CRA evaluations are considered. In the 1990s, a number of legislative changes, including deregulation of financial institutions, which set off a wave of bank consolidation, increased the effectiveness of the CRA. Between 1990 and 1998, CRA commitments grew from $1.6 billion to $812 billion annually.[19] These funds have supported a number of activities including loans for small businesses operating in low-income areas, the production of affordable housing, and the remediation of environmental contamination.[20] However, the CRA's impact on personal banking services is less certain.

Massachusetts adopted its own state-level CRA in 1982. While several states have CRAs, Massachusetts is the only state in which this law applies to both state chartered banks and credit unions.[21] Perhaps as a result of this regulation, financial institutions in Massachusetts have taken on initiatives to make their services more accessible to lower income individuals.

The Massachusetts Community and Banking Council (MCBC) was established in 1990 to coordinate the CRA efforts of member financial institutions with the work of community organizations. In 1994, MCBC developed "Basic Banking for Massachusetts" to help low-income families access checking and savings accounts. The program established guidelines for low-minimum, low-fee accounts now offered by 126 banks across the state.[22]

2. Financial institutions chartered to serve low-income neighborhoods

While the CRA has undoubtedly had a large positive impact, the law has not been able to catalyze the full infusion of capital neighborhoods suffering from decades of disinvestment require. The projects and products these communities need have been too complex for conservative profit-minded banking institutions. Parallel to the CRA, community development financial institutions (CDFIs) have evolved, charted specifically to take on these more demanding challenges.

Efforts to encourage reinvestment and reach underserved residents in low-income neighborhoods through community development banks trace back to the early-1970s and the founding of Shorebank in Chicago. The success of Shorebank sparked a community development finance movement. These

THE MASSACHUSETTS ASSET DEVELOPMENT COMMISSION

Governor Patrick formed the Massachusetts Asset Development Commission (MADC) in 2008 to investigate the impact of state policies on residents' ability to sustain and build assets. The MADC released a final report in June 2009. The recommendations focused on ensuring that income transfer policies promote rather than hinder asset accumulation, making financial education a priority, protecting consumers from predatory lending practices, and supporting targeted savings. Specific recommendations included increasing goal-oriented savings through the use of 529 college savings plans, IDAs, and the FSS program. While the report did not focus on the financial services sector, it did call for stricter regulation of fringe financial services. It placed particular emphasis on commercial tax preparers, citing a need for stricter laws on the transparency of loan agreements, more leeway from the federal government for states for stricter regulation, and a public awareness campaign on the high cost of RALs and free tax services that are available across the state.[46]

efforts received important federal backing in 1994, with legislation creating the CDFI Fund, which supports institutions providing capital in underserved neighborhoods.

As waves of bank consolidation reduced the presence of local banks and relationship-based lending, CDFIs have become increasingly important in delivering personal banking services. Community development credit unions (CDCU) have been a particularly successful provider of these basic services in disadvantaged neighborhoods. According to the CDFI data project, in 2006, nonprofit CDCUs opened nearly 80,000 accounts for individuals who were previously unbanked and made loans to 27,000 people with no prior credit history.[23] Like all CDFIs, CDCUs struggle to find experienced leadership and capital, but those that are able to establish roots provide low-income neighborhoods with essential high-quality financial services.[24]

While Massachusetts has a robust CDFI movement, the focus here has not been the provision of basic financial services. The Commonwealth is home to just one of nearly 300 CDCUs currently operating in the US. According to an industry survey, less than one percent of total dollar volume invested by CDFIs in Massachusetts in 2006 went to financial services for individuals, whereas housing-related investments represented 86 percent of the state's CDFI financing; nationally, more than 14 percent of CDFI financing supported personal financial services, and housing made up 40 percent of CDFI activity.

3. Efforts to engage low-income families more directly

Encouraging banks to offer services to low-income families and forming community development financial institutions with the explicit goal of serving these families does not influence individual behavior or change the economic context that makes it hard for low-income families to access these services. To address these challenges, many communities are working to engage families more directly. These efforts include enrolling families in individual development accounts that facilitate saving, helping families access and preserve the full value of their EITC refunds, and giving families who rely on housing subsidies an opportunity to accumulate savings.

Many communities are working to engage families more directly.

Individual Development Accounts (IDA)

IDAs help lower-income workers, who can afford to save only modest amounts, amass more significant assets by matching savings toward a specific goal. For each dollar an account holder saves for assets (i.e. buying a home, building a small business, or paying for college), the sponsoring organization provides a match, often more than one-to-one and sometimes as high as three-to-one. The IDA is a central component of Michael Sherraden's poverty reduction strategy, which focuses on helping low-income families build assets that lead to greater stability and self-sufficiency. As a component of the program, sponsoring organizations typically require participation in financial education. Controlled studies have shown that this combination of financial education and matched savings has made IDAs a powerful tool for increasing homeownership, individual net worth, and participation in continuing education.[26]

In Massachusetts, matching IDA funds were provided by the state's Department of Housing and Community Development (DHCD) from fiscal years 2007 through 2009 in partnership with the Midas Collaborative, the Massachusetts Association for Community Action, and other community organizations.[27] IDA programs have also received federal support from the federal Administration for Children and Families Assets for Independence (AFI) grant program, and private donors such as the United Way of Massachusetts Bay and CVS stores.[28] Unfortunately, due to current financial constraints, IDA funding was eliminated from the state's 2010 budget.

In Gateway Cities, there are currently 120 account holders in state-sponsored IDA programs. IDAs are administered by private nonprofit and community based agencies, and the capacity of these organizations to serve IDA clients varies, as does the level of availability in different Gateway Cities. Currently, IDA investors reside in all 11 Gateway Cities, but program participation ranges from serving just five individuals in both Springfield and Fall River to 30 in Lawrence.[30]

Volunteer Income Tax Assistance (VITA)

Communities are also focused on the EITC as an approach to altering the economics of tight budgets that make it hard for low-income families to save. Because most families receive EITC payments in a lump sum at the end of the year, many are able to put some of these funds away. Community organizations focus on reaching residents with nonprofit tax services that promote savings, compared to private services, which often encourage discretionary spending by promoting consumer products.

The IRS provides resources, training, and funding for community organizations to offer free tax preparation through its VITA program, which trains and certifies volunteers to serve as tax preparers for low-income filers.

During the 2008 tax filing season, there were 14 IRS funded and regulated VITA providers operating in Gateway Cities. These services were offered in all 11 communities with the exception of Brockton.[31] The limited number of VITA sites in Gateway Cities returned $6.1 million in tax refunds, including $2.8 million in EITC payments. These services saved filers approximately $700,000 in tax preparation fees.[32] Unfortunately, limited capacity means this program serves only a small segment of the market. For each VITA agency located in a Gateway City, there were nearly 6,000 EITC returns filed. For comparison, in Boston there were 24 VITA locations, which breaks down the number of EITC returns to approximately 2,000 per site.[33]

Family Self-Sufficiency Programs

The Family Self Sufficiency (FSS) program is sponsored by the US Department of Housing and Urban Development (HUD) and administered by local housing authorities. The program is designed both to increase the earning capacity of households utilizing subsidized housing vouchers and residents of public housing, and to encourage them to save money for education, a vehicle, or a down payment on a home. As with IDAs, FSS participants receive financial education, along with other support services like job training, child care, and homeownership counseling.

Escrow accounts are created for each FSS household, and as their income grows, earnings that would go to pay for rent increases based on their higher wages are deposited into this account. Once a household successfully completes the FSS program, the escrow account funds are paid to them.[34] Unfortunately, quantifying the outcomes of these programs is challenging. Record keeping differs across local housing authorities, and often programs are designed to address varying goals.

There are currently 272 households in Gateway Cities participating in FSS programs.[35] However, these programs currently only serve residents of Brockton, Fall River, Holyoke, Lowell, Pittsfield, Springfield, and Worcester. Housing Authorities in other Gateway Cities could leverage funding from HUD to allow residents to participate in this program, and help them transition off of public support.

THE ROLE OF FINANCIAL EDUCATION

Bleak figures on financial literacy in the US demonstrate a need for additional financial education. On a recent national survey, only 36 percent of respondents correctly performed an interest rate calculation, just 35 percent knew that making minimum payments on a credit card would never eliminate debt, and only 7 percent could correctly identify the most affordable payment plan for an appliance.[47] Studies suggest financial education can have a real impact on family economic well-being by increasing savings and net worth, and reducing debit and lowering delinquency rates.[48]

Recently, a group of nonprofits, financial service providers, and government agencies came together to form the Massachusetts Financial Education Collaborative (MFEC) with the goal of coordinating and improving financial education across the state. The collaborative conducted a survey to assess the breadth of agencies that provide financial education services across the state. Of 185 survey respondents, 60 percent provided financial education courses and 68 percent of respondents reached 50 to over 1,000 people annually. Currently, the MFEC is working to establish a centralized entity to train financial education providers and advocate for stronger policies supporting financial education efforts, as over 70 percent of all survey respondents expressed interest in such an agency.[49] The organizations involved in MFEC are also supporting legislation to establish a financial education curriculum in Massachusetts's schools.

B. Innovative Products to Link Low-Income Families with Wealth Building Financial Services

New innovations are connecting more unbanked households to low-cost financial services. These range from (1) efforts to provide families with prepaid cards that facilitate basic transactions to (2) efforts to help workers save, and (3) attempts by banks to offer loan products that will better serve low-income households.

1. Establishing a connection through prepaid stored value cards

Stored value cards (SVC), which first appeared as phone cards and were later adopted by retailers as gift cards, are probably the most significant innovation reshaping the financial services landscape for low-income families. SVCs have a very low-cost structure compared to traditional checking accounts. Initially, for-profit companies attempted to exploit this advantage by developing a profitable product that provides the unbanked with services very similar to a checking account. More recently, community-based and nonprofit organizations have developed their own SVCs in an attempt to offer lower-cost alternatives and maximize the benefits for low-income consumers. SVCs mark an important development because they offer a starter product that establishes a bank-like connection with unbanked customers. This relationship can evolve to include all the beneficial aspects (low-cost transaction, savings, credit building) of full-service accounts with mainstream financial institutions.

H&R Block's Emerald Mastercard was one of the first SVCs designed to provide basic banking services. The Emerald Card is a prepaid product, which users initially fill with tax refunds. The card can be reloaded with direct payroll deposits or through a network of check cashing outlets. Users may withdraw cash without fees when making purchases, or with a $1.95 charge at most ATMs. The Emerald Card can also link to a savings account.* Since 2007, H&R Block has opened 7 million Emerald accounts, loading more than $15 billion in funds. The company estimates these cards have saved unbanked customers more than $200 million in check cashing fees.[36] Other major for-profit providers of general purpose reloadable cards, such as GreenDot, charge one time activation fees (approximately $10) and monthly fees ($3-$10). These leaders are pursuing new opportunities to encourage savings, as well as the credit building potential of SVCs through partnerships with credit bureaus.[37]

From the nonprofit sector, the Community Financial Resources (CFR) Card is one of the more promising low-cost SVCs. The CFR Card was developed by the Campaign for Working Families in Philadelphia as a way to encourage savings at their community VITA sites at tax time. This product has a low $1 monthly fee, can be used anywhere VISA is accepted, includes free VISA bill pay, and has no minimum balance and no penalty fees. The card can be reloaded from a tax refund, through payroll deposits, or government benefits, or for no fee at any ATM machine within the Allpoint network, which includes 37,000 ATMs worldwide. The CFR Card can also be linked to a high-yield savings account, providing a direct link to an advantageous banking relationship.[38]

Moving forward, low-income communities may also see closer linkages between these stored value cards and the Electronic Benefit Transfer (EBT) cards used to deliver public benefits. While these systems have been designed to minimize costs, as technology develops, states may take advantage of this opportunity to develop a pathway to financial services for this population.[39]

2. Finding innovative approaches to help low-income families save

While the IDA offers an excellent model for helping low-income families save, the services involved, as well as the cost of matching funds, make it difficult to extend the reach of these programs. Financial services providers are increasingly experimenting with approaches from the field of behavioral economics to encourage low-income families to save.[40]

Prize-linked savings is one example. Peter Tufano, a professor at Harvard Business School and founder of the Doorways to Dreams Fund, a Boston-based nonprofit, has been promoting the potential of this approach. Internationally, prize-linked savings has a long history. In the UK, the same fraction of the population holds prize-linked savings as holds stocks. The first prize-linked savings program in the US was started recently by Indiana-based Central Credit Union. Following a successful 2006 pilot, the bank now offers

* While this product demonstrates important innovations, caution is important in interpreting the benefits it provides to unbanked low-income families, as it is offered by a commercial tax preparer in conjunction with high cost RALs that may erode the value of a cardholder's tax refund.

the product across all 22 branches with nearly $800 million in account balances. Across the country, other credit unions are beginning to offer prize-linked savings accounts.[41]

$aveNYC is another new model that relies on the large annual windfall families receive from EITC payments to encourage savings. In contrast to IDA programs, which have generally been high-touch and goal oriented, $aveNYC is an attempt to simply improve the financial stability of low-income families by encouraging savings on a much larger-scale.

Families receive a 50 percent match if they deposit funds received as a part of their tax refund, and maintain the initial deposit for at least one year. Though participants in this program were very low-income, more than three-quarters kept their accounts open for the full year. While additional evaluation will be required to judge the effectiveness of $aveNYC, early analysis suggests the program can be effective in encouraging savings behavior among families with very limited means.[42] This has important implications for the future of government-led efforts to help low-income families achieve greater financial stability.

Around the country cities are also taking impressive steps to brand and market opportunities to access low-cost banking services following the lead of the Bank on San Francisco program. With the endorsement of a coalition of state and local organizations, this approach has helped overcome the lack of knowledge and negative associations that often keep low-income residents from banking with mainstream institutions.

Over the last year, Governor Schwarzenegger has replicated the San Francisco model in four more California cities. The Bank on California program has more than 30 participating banks and credit unions that offer full service checking accounts with no minimum balance for less than $10 per month; customers who sign up for direct deposit pay no monthly fee. For unbanked residents with poor credit histories, the program also offers a "second chance" account after completion of a financial education course. The governor's goal of opening 100,000 accounts for previously unbanked households within two years was reached in just nine months.[43]

The National League of Cities (NLC) began an effort to expand the Bank on San Francisco model in 2008. With assistance from NLC, the FDIC, and the Clinton Foundation, dozens of communities around the country are now developing similar programs to reach the unbanked.[44]

3. Providing low-cost short-term loans

Financial service providers are also working hard to find cost-effective products that offer low-income families an alternative to the pawnshop, payday, and auto title loans that make it difficult for low-income families to build wealth.

In 2007, the FDIC issued guidelines to encourage banks to offer these alternatives products. These guidelines call for small loans of up to $1,000 at a 36 percent maximum APR with low origination fees. Banks that offer these loans receive CRA credit. In 2008, the FDIC began collecting data from 31 banks participating in a pilot, including the Washington Savings Bank in Lowell.[45]

Credit unions are also working hard to offer small, short-term loan services that compete more directly with payday lenders. These "salary-advance" products are similar to payday loans, but carry lower fees. In many states, credit unions are working together to reduce

SYRACUSE COOPERATIVE FEDERAL CREDIT UNION

Syracuse Cooperative Federal Credit Union (Cooperative Federal) is a model Community Development Credit Union working to help families build wealth in a midsize city struggling with industrial change. Cooperative Federal provides a variety of products that meet the needs of their members, including very low-cost accounts, services aimed at allowing low-income individuals to build assets, and products that help customers avoid fringe financial services. Cooperative Federal offers a very low-cost savings account ($5 account minimum with no monthly fees). Members that maintain an average minimum balance of $50 are eligible to earn dividends. For a $20 annual fee, checking accounts are available with no minimum balance. To transition unbanked residents to lower-cost services, Cooperative Federal offers a continuum of services to non-members. These basic transaction products, which include international remittances, check cashing, and money order sales, allow customers to avoid high-fee fringe services.

Since its founding in 1982, Cooperative Federal has provided over $65 million in financing to Syracuse's underserved low-income residents. The credit union has also delivered training to owners of nearly 800 small businesses, as well as credit and homeownership counseling to over 1,000 individuals.

the cost of developing and marketing these services. Examples include the Better Choice Loan in Pennsylvania and the StrechPay loan in Ohio.

III. Recommendations

Connecting Gateway City residents to lower-cost, wealth building financial services is a fundamental component of a comprehensive growth strategy for these communities. The power of this approach is that it complements existing strategies, and leverages individual savings with public dollars, helping families accumulate assets. By helping families develop financial stability, over time these services will lead to stronger neighborhoods and more productive workers.

Fortunately, many pathways toward asset building have already been charted. Leadership and effort is needed now to see that the promise of this approach is realized in Gateway Cities, where limited capacity often makes it difficult to implement effective strategies. Toward that end, MassINC offers policymakers committed to these communities the following recommendations:

• **Develop a better understanding of Gateway City markets for financial services and metrics to evaluate progress toward asset building goals.** Relative to the focus placed on this topic, city-level data on the use of banking services and individual asset holdings is limited. While reliance on high-cost services can be inferred from their presence in these communities, it is difficult to draw a complete picture of how residents actually use financial services. This information is critical to design and target efforts. Fortunately, Massachusetts has a variety of organizations, including the Federal Reserve Bank, UMass public policy centers, and financial services nonprofits, well-positioned to perform the survey work required.

Data are also vital to chart progress toward asset building goals. Interventions, like state supported IDA programs, need standardized outcome measures. As the asset building field has grown, work has been done to develop standardized measures for success. Notably, the Asset Support Center in California has studied outcome-based evaluation of asset building programs across the country.[50]

• **Encourage collaboration between financial institutions and community leaders.** Providing lower-cost financial services and promoting saving in Gateway Cities will require collaboration in many different forms. Partnerships among existing community organizations could lead to the opening of a new CDCU, or to an existing depository financial institution receiving CDFI certification to obtain federal funding, which could lead to new products targeted at lower-income consumers. Banks can also play a valuable role in VITA efforts, by serving as tax sites, incentivizing employee volunteerism, or providing financial support. Financial institutions in other parts of the country have found that efforts like these benefit participants, build community goodwill, and add to their client base.

• **Support Community Development Financial Institutions that provide Gateway City residents with access to low-cost personal financial services.** Grants from the CDFI Fund and resources allocated through other sources, such as the New Markets Tax Credit, offer capital and technical assistance to community development credit unions. With public support, existing Gateway City credit unions may be able to qualify as CDCUs and collaborate to offer products that help lower-income residents build wealth.

• **Create new pathways toward asset building.** As experimentation with new approaches like prize-linked savings demonstrates effective ways to implement these strategies, aggressive steps should be taken to ensure that Gateway City residents have the opportunity to benefit from these advances.

• **Vigorously promote asset building among families receiving public assistance.** State agencies should have a coordinated strategy to help families build assets through improved access to low-cost financial services, beginning with a plan to move recipients of EBT payments toward traditional bank accounts. The state could also explore ways to ensure that families that have earned income and receive public benefits file for tax refunds through VITA programs.

Following on the recommendation of the Massachusetts Asset Development Commission, the state work to help the Department of Housing and Community Development (DHCD) provide more support for both the federal Family Self-Sufficiency Program (FSS) and the Moving to Work (MTW) Housing Choice Voucher Program. These efforts help residents of public and subsidized housing save toward specific goals without facing sanctions in the form of reduced housing assistance.

Notes

[1] Lynn Sanders is a master's student at the Heller School of Social Policy and Management at Brandeis University. Formerly, she served as a staff member at the Boston EITC Coalition. Lynn completed the bulk of her research for this brief as a MassINC Summer Graduate Student Policy Fellow.

[2] See Mark Muro and others, "Reconnecting Massachusetts Gateway Cities: Lessons Learned and an Agenda for Renewal," (Boston, MA: MassINC, 2007); Radhika Fox and Miriam Axel-Lute, "To be Strong Again: Renewing the Promise in Older Industrial Cities," (Oakland, CA: PolicyLink, 2008); Andre Leroux and Lorlene Hoyt, "Voices from Forgotten Cities: Innovative Revitalization Coalitions in America's Older Small Cities," (Boston, MA: Citizens Housing and Planning Association, 2007).

[3] Ellen Seidman and others, "A Financial Services Survey of Low- and Moderate-Income Households," (Chicago, IL: Center for Financial Services Innovation, 2005).

[4] Massachusetts Office of Consumer Affairs, Division of Banks.

[5] Matt Fellowes and Mia Mabanta, "Banking on Wealth: America's New Banking Infrastructure and its Wealth Building Potential," (Washington, DC: The Brookings Institution, 2008).

[6] In many states, payday lenders are also a major source of short-term high-interest loans to consumers with limited credit. Massachusetts usury law technically prohibits these high-cost loans. Despite the state ban, many experts suggest these loans are still offered in Massachusetts.

[7] Donna Roberson, "State Fails to Curb Usurious Pawnshop Rates," *Boston Globe* (April 30, 2007).

[8] Michael Barr, "Banking the Poor: Policies to Bring Low-Income Americans into the Financial Mainstream," (Washington, DC: Brookings Institution, 2004); and Chi Chi Wu and Jean Ann Fox, "Big Business, Big Bucks: Quickie Tax Loans Generate Profits for Banks and Tax Preparers While Putting Low-Income Taxpayers At Risk," (Boston, Massachusetts: National Consumer Law Center, 2009).

[9] This calculation is built on three conservative assumptions: First, that 10 percent of Gateway City households are unbanked, which is the rate nationally and is likely significantly lower than the actual rate in Gateway Cities; second, that these unbanked residents have the same demographic profile as unbanked households nationally (See Fellowes & Mabanta, 2008); and third, Gateway City residents pay national average fees for these services. These assumptions are fairly conservative. Unbanked Gateway City households may earn slightly higher wages working in the Northeast. Limited regulation in Massachusetts may also mean Gateway City residents actually face check cashing costs above these averages.

[10] Tabulated using data provided by The Brookings Institution's EITC Interactive data tool.

[11] Tabulated using data provided by The Brookings Institution's EITC Interactive data tool, and estimates on the average cost of paid tax preparation and RALs from: Reuters, "Tax Preparation Fees Still Affordable, Says National Society of Accountants," (2007); and Michael S. Barr, "Banking the Poor: Policies to Bring Low-Income Americans Into the Financial Mainstream," (Washington, DC: The Brookings Institution, 2004).

[12] Alan Berube, "Using the Earned Income Tax Credit to Stimulate Local Economies," (Washington, DC: The Brookings Institution and the Living Cities Initiative, 2006).

[13] Seidman and others (2005); Fellowes & Mabanta (2008).

[14] Barr (2004).

[15] Brian K. Bucks and others, "Changes in US family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances," *Federal Reserve Bulletin*, vol. 95 (February 2009), pp. A1-A55.

[16] "The Unbanked Latino: Expanding Banking Access for Latinos in Massachusetts," (Boston, MA: Office of Senator Jarrett T. Barrios, 2005). In conversations, local banking officials reported to the authors that ITIN challenges have largely been addressed since the release of the Barrios report.

[17] According to a 2004 report, 22 of 27 Massachusetts banks survey did not accept the ITIN. See "The Unbanked Latino: Expanding Banking Access for Latinos in Massachusetts," (Boston, MA: Office of Senator Jarrett T. Barrios, 2005).

[18] See Douglas McGray, "Check Cashing Redeemed," *New York Times Magazine* (November 7, 2008).

[19] Eugene Ludwig and others, "The Community Reinvestment Act: Past Successes and Future Opportunities," (The Federal Reserve Banks of Boston and San Francisco, 2009).

[20] See Joint Center for Housing Studies, "The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System," (Cambridge, MA: Harvard University, 2002).

[21] Massachusetts Division of Banks, Accessed at http://www.mass.gov/?pageID=ocaterminal&L=5&L0=Home&L1=Consumer&L2=Banks+%26+Banking&L3=Selecting+Banks+%26+Credit+Unions&L4=Community+Reinvestment+Act&sid=Eoca&b=terminalcontent&f=dob_cra&csid=Eoca, on July 1, 2009.

[22] Massachusetts Community and Banking Council. Accessed at http://mcbc.info/basic_participating on July 1, 2009.

[23] "Providing Capital, Building Communities, Creating Impact, Sixth Edition," (Arlington, VA: CDFI Data Project, 2007).

[24] Geoff Smith and others, "Collaborators or Competitors: Exploring the Relationships between Community Development Financial Institutions and Traditional Lenders in Small Business Finance," (Washington, DC: US Department of Treasury, CDFI Fund, 2008).

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[26] Gregory Mills and others, "Evaluation of the American Dream Demonstration Program," (Cambridge, MA: Abt Associates, 2004).

[27] "Individual Development Accounts (IDAs)," (Massachusetts Executive Office of Housing and Economic Development, 2009).

[28] Accessed at http://www.massassets.org/work.html on July 6, 2009.

[29] Tabulated using data provided by MassCAP and the Midas Collaborative, two major intermediaries helping non-profits provide IDAs statewide.

[30] Ibid.

[31] Tabulated using data provided by the Massachusetts Tax and Assets Consortium and the Massachusetts Association of Community Action Agencies, IRS VITA grantees for Massachusetts.

[32] Tabulated using data provided by The Brookings Institution's EITC Interactive data tool, and estimates on the average cost of paid tax preparation and RALs from: Reuters, "Tax Preparation Fees Still Affordable, Says National Society of Accountants," (2007).

[33] Tabulated using data provided by The Brookings Institution's EITC Interactive data tool and the Massachusetts Tax and Assets Consortium and the Massachusetts Association of Community Action Agencies.

[34] US Department of Housing and Urban Development, http://www.hud.gov/offices/

pih/programs/hcv/fss.cfm, accessed on: June 26, 2009.

35 Tabulated using data provided by the US Department of Housing and Urban Development, as of June 26, 2009.

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38 Background provided by Jessica Cook of the Boston EITC Coalition, and additional information accessed at https://www.enrollcfr.org/cfr/Home.aspx, January 13, 2010.

39 Barr (2004).

40 Recent research in the field of behavioral economics introduces new theories about financial decision making. They advance the idea that low-income people do not opt out of the banking system because they distrust institutions or do not understand the potential benefits. Rather, people mentally account for the stress caused by situational barriers like restrictive hours or formal environments lead the poor to choose other service over banks. To overcome these barriers, low-income people must see more of a benefit to banking, which may be achieved by providing incentives to open accounts, or by making opening a bank account and having paychecks directly deposited the default option when a person gets a job. See, for instance, Marianne Bertrand and others, "A Behavioral-Economics View of Poverty," *The American Economic Review* 94(2) (2004).

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