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Bringing More Affordable Financial Services to the Inner City: The Strategic Alliance between Bethex Federal Credit Union and RiteCheck Cashing, Inc.

A Case Study

by

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Introduction

This case is an examination of an innovative corporate-community development alliance. It involves a cooperative program between a community development credit union, Bethex Federal Credit Union, and licensed check cashing outlets (CCOs) in the Bronx, New York. RiteCheck, which owns eleven check cashing locations in inner-city Bronx and Manhattan neighborhoods, has taken the lead among New York check cashers in building this partnership. A RiteCheck store is the first CCO involved in the pilot, and other RiteCheck locations will become involved as the project grows. Other check cashing firms have expressed an interest in participating, and it is anticipated that, when fully operational, the pilot will involve 14 CCOs owned by as many as three firms.

The pilot project was implemented in April 2001 after more than four years of planning. Because it has only been in operation for a short while, all of the benefits of the partnership as discussed here are projected. There has not yet been time to assess the results of the arrangement, but because it is both unusual and cutting edge, it bears examination, as it exhibits several promising features of 'win-win' practices. Moreover, despite the fact that the concept offers expanded business opportunities for both partners as well as increased access to basic banking services for people in low-income neighborhoods, it is not without its critics and controversy. These concerns—the reason the concept took so long to become reality—will be discussed in the case as well.

Having realized that they share a customer base that is chronically underserved by other financial institutions, each of the principals in this case was already thinking of the other as a partner by the time they met in 1997 and began discussions. The express purpose of the strategic alliance is to make credit union services more accessible to lower income consumers living within the credit union's field of membership.[1] The partners hope that the capability to make deposits through a check cashing outlet, as well as the presence of credit union marketing materials in those outlets, will encourage check cashing customers who do not have bank accounts to open credit union accounts and thus become part of the financial mainstream. The partnership is also a strategy by an innovative credit union to increase its branch presence in underserved neighborhoods without incurring the expense of acquiring or building additional bricks-and-mortar facilities.

In fulfilling a branch role for the credit union, check cashers hope that the availability of deposit services will increase the walk-in traffic and thus expand the overall volume of transactions upon which their business depends. By allying themselves with an organization whose mission is to serve the needs of a low-income population, they also hope to improve their overall standing in the community and at least partially overcome the negative perception of their industry held by advocates for poor communities.

Technology is another critical feature of this partnership. Strategic alliances such as this one would not be possible without sophisticated technology and networks for conducting a variety of financial transactions. Today, the most advanced check cashing operations have access to the

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[1] Bethex is a community development credit union with a geographically defined field of membership in the South Bronx.

same technology and Automatic Teller Machine (ATM) networks that mainstream banks use. Indeed, RiteCheck has access to better technology than does Bethex, and the fact that RiteCheck can offer additional services to members is part of the advantage to Bethex in using CCOs as branches.

The Context

The partnership between Bethex Federal Credit Union and New York check cashing firms is particularly interesting because it taps into a number of concurrent trends in the financial services industry and public policy. Utmost are the recognition that low-income families need to build assets in order to break the cycle of poverty common in many inner-city communities and the corresponding effort to help them accumulate those assets by providing better access to banking services. Such services are often missing in inner-city neighborhoods because banks have found it unprofitable to operate branches with a large volume of small transactions.

The second financial services trend important to this case is the growth of the check cashing industry and the issues surrounding it. Check cashers have identified and filled a niche market, providing a variety of financial services to a primarily minority, urban, largely unbanked customer base. The industry is controversial, however; advocates for the poor have criticized its fee structure as harmful to the low-income communities in which CCOs primarily do business. So when a community-based financial institution (the credit union) sought out a strategic alliance with the perceived "enemy,"—swimming with the sharks, if you will—eyebrows were raised.

Yet partnerships between check cashers and more mainstream financial institutions are becoming more common, a trend that represents the third critical piece of backdrop for this case. Increasing competition in the banking industry and saturation of middle-class suburban markets have led banks to try to develop new markets in inner-city neighborhoods. Still reluctant to establish full branches in low-income neighborhoods, however, banks have sought various types of alternative alliances with check cashers. This has blurred the lines between the two industries, as banks come to look more like check cashers and vice versa.

The Need for Basic Financial Services

Despite the longest economic expansion on record and the lowest unemployment rates in a generation, 10% of all American families have no bank accounts. This includes 25% of African Americans and Hispanics, one-fourth of all families with incomes under $20,000, and nearly half of all families moving from welfare to work.[2] In recent years, advocates and policymakers have grown to understand that bringing the unbanked into the financial mainstream is important, because one's banking status has profound implications for long-term family self-sufficiency. "Even controlling for income and other factors, low-income individuals with bank accounts are 43% more likely to have positive net financial assets than those without."[3] Lack of savings is particularly important to low- and moderate-income families in general and to unbanked families

[2] Federal Reserve*, 1998 Survey of Consumer Finances*. http://www.federalreserve.gov/pubs/oss/oss2/scfindex.html.
[3] U.S. Department of the Treasury, "The First Account Initiative: Bringing the "Unbanked" into the Financial Services Mainstream," December 16, 2000.

in particular, because they are much less likely than other households to be covered by a retirement plan at work. In 1998, more than nine out of ten (92%) unbanked families were without a retirement account, compared with less than half of banked families (47%). Indeed, for more than half of the unbanked (54%), their only asset is their car.[4]

At least part of the reason so many American families do not have bank accounts is the simple fact that there are no banks in the neighborhoods where they live. Because of mergers and increased competition from nondepository institutions, the number of financial institutions in the United States has declined significantly. Between 1975 and 1995, the number fell from about 18,600 to 12,200, a decline of about 35%.[5] Continuing to fall steadily through the late 1990s, the number dipped below 10,000 by the end of 2000, representing an additional 17% decrease over the six-year period.[6]

A decline in the number of banks does not automatically lead to a loss in local banking offices. During the same 1975–95 period, the total number of branch offices increased by 29%, with an additional 10% growth by 2000, but virtually all of this growth occurred in middle-income areas.[7] In contrast, low-income neighborhoods saw a 21% decline in branch facilities.[8] While nationwide branches were growing, New York State underwent a small (3%) decline between 1995 and 2000.[9] Within New York City, however, Brooklyn lost around 14% of its bank branches between 1978 and 1995 and the Bronx about 20%; a disproportionate share of these closings occurred in the poorest neighborhoods.[10]

The Rise of the Check Cashing Industry

While the number of banks is decreasing, providers of alternative financial services are growing. With an estimated $200 billion in annual transactions, this fringe banking industry—which delivers a host of financial services from cashing checks to issuing money orders and short-term "payday loans"—is both very big and highly profitable (see Sidebar 1).[11] Payday lending, also called payday advance (or deferred deposit by the check cashing industry) allows a customer to receive a small, short-term loan against his or her next paycheck. The customer writes a personal check for the advance amount plus a fee, in exchange for cash in the amount of the advance. The lender agrees to hold the check for a specified period of time, usually about two weeks, at the end of which the check is deposited or the customer returns with cash to reclaim the check.

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[4] Federal Reserve Board, Survey of Consumer Finances (1998) and calculations by the authors.
[5] Robert B. Avery, Raphael W. Bostic, Paul S. Calem, and Glenn B. Canner, "Changes in the Distribution of Banking Offices," *Federal Reserve Bulletin* 83, no. 9 (September 1997, online).
[6] FDIC Statistics on Banking, http://www.fdic.gov/bank/statistical/statistics/sectionb.html.
[7] Avery, et. al, "Changes in Distribution," 2, 18; FDIC Statistics on Banking, http://www.fdic.gov/bank/statistical/statistics/sectionb.html.
[8] Avery, et. al, "Changes in Distribution," 2, 18.
[9] FDIC Statistics on Banking.
[10] Louis Jacobson, "Bank Failure: The Financial Marginalization of the Poor," *The American Prospect*, no. 20 (Winter 1995), p. 8.
[11] Scott Shepard and Elliot Jaspin, "An 'Unholy Alliance'? Check Cashers and Banks Seen Profiting in Paperless Era," *Philadelphia Inquirer*, September 28, 1998, online.

The core of the fringe banking industry is the network of stores across the country that classified their primary business as check cashing. In 2000, this numbered an estimated 9,500, up from 7,100 just two years earlier; another 1,300 stores listed check cashing as their secondary line of business.[12] All told, the industry cashes more than 180 million checks a year,[13] with a total face value of $60 billion, producing about $1.5 billion in fees.[14]

The industry's growth has been reflected in the New York metropolitan area. Between 1995 and 1999, the number of check cashing stores in New York City rose 11%.[15] The New York State Banking Department indicates that the city's CCOs cashed more than $14.5 billion in checks in 1999, up from $11.4 billion two years before. During the same period, annual net income for the industry rose from $3.7 million to $11 million.[16]

In contrast to conventional banks, CCOs historically have been concentrated in inner cities rather than outlying urban areas and suburbs, although this is changing.[17] Many check cashers are now establishing locations in suburban strip centers where banks have closed.[18]

Because they do not have the stand-alone buildings and big lobbies, CCOs have lower facility costs, enabling them to survive in areas where banks have struggled.[19] Surveys also suggest that "customers are satisfied with the services they receive from check cashers, which include convenient locations, flexible hours, short lines, ancillary services such as bus passes and lottery tickets, and, perhaps most important, immediate cash without waiting for a check to clear."[20] Market research by mainstream banks such as Chase Manhattan confirm check cashers' competitive advantages. Chase's Kenneth Rosenblum points out, "Check cashers are far superior to banks in terms of the days and hours they are open for business and their ease of access."[21]

Bank–Check Cashing Partnerships

Technology and competition have prompted banks to rethink their use of traditional branches and begin forming partnerships with third parties to deliver financial services without heavy investments in bricks and mortar. Banks are looking to supermarkets, high-volume discount stores, community development organizations, and check cashers to provide cheaper locations and greater expertise in reaching consumers they have been unable to reach in the past.

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[12] Data from InfoUSA, cited in Survey of Non-Bank Financial Institutions. Dove Consulting, for U.S. Dept. of the Treasury. April 4, 2000. Available at: http://www.treas.gov/press/releases/docs/nbfirpt.pdf.
[13] "Q&A – NaCCA Facts," National Check Cashers Association website http://www.nacca.org/q&a.htm.
[14] Survey of Non-Bank Financial Institutions.
[15] Richard A. Oppel Jr., "The Stepchildren of Banking," *The New York Times*, March 26, 1999, sec. C, p. 1.
[16] Heike Wipperfurth, "Check Cashers Buff Up Image," *Crain's New York Business*, November 27, 2000, p. 3.
[17] Caskey, *Fringe Banking,* 63.
[18] Joanne Gordon, "The Service Side of Strips," *Chain Store Age* (February 1998): 136.
[19] Stephen Wolf, Board Chairman for National Check Cashers Association, written comments to U.S. Department of Treasury on interim EBT rule, 61 Fed. Reg. 39253, November 25, 1996.
[20] Louis Jacobson, "Bank Failure: The Financial Marginalization of the Poor," *The American Prospect*, no. 20 (Winter 1995), pp. 63-70.
[21] *Financial Access in the 21st Century,* proceedings of a forum held on February 11, 1997 (Office of the Comptroller of the Currency), p. 46.

Economics and policy shifts have also led check cashers to seek out alliances with banks. The transition to electronic funds transfer (EFT) for delivery of welfare and Social Security benefits is reducing the volume of checks that need to be cashed, making check cashing a roller-coaster business. When New York replaced its electronic vouchers redeemable only at CCOs with debit cards that can be used at ATMs in 1999, the check cashing industry lost 20% to 30% of its income.[22] Seeking secure, steady business to make up for the loss of this previously assured volume, check cashers are forming alliances and serving an outsourcing role for banks.

Partnerships between banks and check cashers are blurring the lines between mainstream financial institutions and so-called "fringe banks," which operate without either significant consumer protections or community reinvestment obligations. As traditional financial institutions move to a fee-based services system and fringe banks adopt increasingly sophisticated technology and broaden their market appeal, banks are beginning to look more like check cashers, and check cashers more like banks. Proponents say these new alliances will provide more reasonably priced basic financial services to the unbanked and underserved, while critics predict that the alliances will only further exploit the poor and the debt-ridden. Ultimately, the value of these initiatives to society will depend in large part on whether they help the unbanked (as well as those who have abused, or been abused by, the consumer credit system) establish credit ratings so they can enter the financial mainstream.

Bank-check casher cooperative arrangements take a variety of forms (see Sidebar 2). Many banks have teamed with CCOs to offer complementary financial services. Others have chosen to compete head-to-head with check cashers by creating their own check cashing arms as a means to tap into the unbanked market and to generate brand recognition and loyalty among unbanked customers. Some arrangements are explicitly intended to serve as stepping-stones to mainstream banking.

Few bank partnerships, however innovative, use check cashers as a portal to their services or make an overt effort to provide a bridge into the financial mainstream for low-income unbanked customers. This highlights the uniqueness and significance of the partnership between RiteCheck and Bethex Federal Credit Union, a financial institution whose core mission is economic empowerment.

Bethex Federal Credit Union

In 1970, an adult education teacher named Joy Cousminer recognized her students' need for economic empowerment and began working with them to establish a cooperative credit union. The result was Bethex Federal Credit Union, a federally insured community development credit union (CDCU) (See Sidebar 3). Today Bethex's mission remains the economic empowerment of low-income individuals and households in the Bronx. Outreach has always been implicit in that mission, as Bethex strives to serve the maximum number of poor residents as possible.

As a result of its outreach efforts, Bethexhas grown from its original 600 members to nearly 8,000, and is continuing to add more than 1,000 new members per year. Bethex currently has

[22] Manny Levy, president of the 16-store N.Y.C. Check Express Inc., quoted in Wipperfurth, "Check Cashers Buff Up Image," p. 4.

assets of $8 million, dramatically less than the typical assets for a mainstream bank. In New York, banks average $298 million in assets per branch.[23] This gap highlights Bethex's need to use its assets efficiently while expanding its membership reach—just as it is seeking to do through partnership with check cashers.

Bethex has one main office/service center that operates six days a week and two full-service branches. One, the Roberto Clemente Credit Union, was acquired in the summer of 2000. Two additional full-service branches, one in the Hunts Point neighborhood and the other in the Mott Haven neighborhood, were due to become operational in May 2001. For the Hunts Point branch, Bethex partnered with the Hunts Point Economic Development Corporation and a coalition of local businesses. The Mott Haven branch received a boost in the form of a $200,000 construction and operating grant from the New York Empowerment Zone Corporation. Also in May 2001, Bethex was in the process of acquiring the Columbia-Barnard Credit Union, which was anticipated to bring an additional $1.5 million in assets and nearly 1,000 members under the Bethex umbrella. When fully operational, these will be full-service branches open five days a week; the Mott Haven branch will offer the added convenience of a 24-hour, wall-through ATM.

The CU also provides service to members one or two days a week at six "teller stations" located in churches, a senior citizens center, and an animal hospital. Bethex also has a high concentration of phone and mail transactions. The majority of Bethex's clientele (60%) are welfare and SSI recipients and senior citizens; the remaining 40% are generally low-income earners who do not work for a specific employer and thus do not have payroll deductions or direct deposit contracts.

Bethex's commitment to expand in order to serve low-income residents is reflected in its innovative ways of doing business. To keep lending rates and service fees as low as possible, Bethex accepts donated equipment from banks and larger credit unions and relies on rent-free office space. Bethex has moved so many times in its thirty-year existence that members once called it "Gypsy Federal." The CU also pays lower employee salaries than other comparable institutions. Cousminer feels that minimizing costs and passing the savings along to members is an integral part of its goal, to economically empower its members.

Bethex's Goal Saver account/loan program is designed for people who have difficulty saving money but are accustomed to repaying loans. A member establishes a goal to reach in a specified period of time, and Bethex puts in the goal amount in the member's Goal Saver savings account, which earn 3% interest—1% higher than most of Bethex's accounts. The accountholder then pays an agreed-upon amount monthly to pay off the loan at 6%. Withdrawals from the account can only be made for the amount of equity that has been accrued. This program helps people build credit and develop the habit of saving and making monthly payments and prepares them to borrow on a larger scale. .

Bethex offers a 2% dividend on accounts. Mortgages are available through a partnership with a New Jersey credit union. Bethex makes consumer loans up to $10,000 and is a Small Business Association (SBA) guaranteed lender for small business loans—currently the only small CDCU in the country with this designation. The relationship took five years to set up, but Cousminer

[23] FDIC Statistics on Banking, http://www.fdic.gov/bank/statistical/statistics/sectionb.html.

says the SBA is now considering designating fifty other small CDCUs. Bethex markets its SBA loans through local small business centers and community colleges. Bethex's complete rates and fees are shown in Table 1 below.

Table 1: Bethex Federal Credit Union Fee Schedule

Service	Rate/Fee	Notes
Lending		
Personal/Consumer loan	16.5%	Unsecured, can be taken out for an unspecified purpose; often used for emergencies
Special purpose loan	15%	Short-term, taken out for purposes such as paying taxes; typically extended to someone who already has a loan outstanding with Bethex, but is sometimes used to attract new members or start a payroll deduction
Business purpose or good debt consolidation loan	11.75%	
Car loan	8%	
IDA and Goal Saver	6%	
Savings		
All share accounts	2% quarterly	
CDs	5%	One-year minimum, including IRAs; $3,000 minimum balance
Goal Saver account	3%	
Services		
Membership	$5	One-time fee
Membership cancellation	$5	Exception in case of death—no fee
Returned check	$15	
Checking account	$3/month	Unlimited checking
Money order	$1	

RiteCheck Cashing

Joe Coleman manages eleven RiteCheck check cashing outlets in the Bronx and Manhattan. His stores exemplify the model of a volume-based, a la carte, fee-for-service transaction business functioning as a one-stop shop for a variety of financial services. In addition to check cashing, CCOs offer, among other things, wire transfers, lottery tickets, payment for utility bills and traffic citations,, and sales of public transit passes, all efficiently processed by very specialized high technology equipment.

Table 2: RiteCheck Services, Fees and Technology

Service	Fee	Technology
Checks Cashed	1.4%	
Money Orders	$0.89	On line Delta Money Order dispenser
Authorized Agent -- Con Edison & Verizon	Free or $1.00	CashPoint or Pay-O-Matic Bill payment system (some are on line real time, some are batch process.)
Almost all Utility / Telephone / Cable Bills	$1.00	As above
EBT	$1.50	Personal Teller Machine (PTM)
Parking Tickets	$1.00	Electronic Batch Process
MetroCards	No Fee	
Western Union / Quick Collect	Scaled fee	Dedicated PC
ATM	$1.50	
PTM (Personal Teller Machine)	$1.50	NYCE / Lynk / Chase Point of Banking
Telephone Calling Cards	Retail mark up	
Lotto, Instant Tickets	6% state wide (all merchants)	NYS provided on line lotto machine
PayNet	Scaled fee	On line (uses 2 bill payment systems above)
Postage Stamps & Stamped Envelopes	No mark up (free service to customer)	
Merchant Coin & Currency Sales	$0.25 per roll, $1 per strap	

The range of services offered by RiteCheck is characteristic of the check cashing industry and offers many of the basic financial services low-income people need. Check cashers also tend to be open longer hours in order to serve low-wage workers. For example, RiteCheck outlets are open as early as 7:30 a.m. and close just before 6 p.m. on weekdays, and are open 8 a.m. – 1:50

p.m. on Saturdays. Coleman says several CCOs in New York are now open 24 hours a day. RiteCheck's service menus are also available in Spanish, and the stores' cashiers reflect the language and culture of the neighborhoods where they operate.

Based on these factors of service, convenience, and comfort, check cashers perceive their enterprises as uniquely suited to fulfilling the financial services needs of the poor and unbanked. An indication of this perception is the recent name change of the National Check Cashers Association (NaCCA), a trade association of CCOs, to the Financial Services Centers of America (FiSCA). The industry contends that the check cashing business is the most logical and appropriate model for drawing the unbanked population into the financial mainstream. That argument is taken a step further by Coleman, who criticizes the basic assumption that bank accounts are the best solution for meeting the financial services needs of the poor.

A fundamental point of Coleman's argument is that transaction-based financial services, as he calls check cashing, is more appropriate for low-income customers than the relationship-based services of traditional banking. In his view, the conventional wisdom that bank services should simply be shrunk to the scale needed by low-income individuals is inappropriate because it won't work for banks. The fact that smaller scale—a high volume of very small transactions—is not viable for banks is a major reason banks have pulled out of low-income inner-city neighborhoods in recent decades. Rather, Coleman points out, the check cashers' business model accommodates the needs of the working poor and is thus more viable. Indeed, Coleman contends that CCOs are more economical for poor customers because they can pick and choose the services they want and then pay for only those, rather than paying monthly fees for a bank account, maintaining a minimum balance, and paying penalty fees for below-minimum balances or bounced checks.

Further, Coleman says that the check cashing business exhibits three elements essential for the long-term survival of institutions working to meet the financial needs of the poor: access, liquidity, and service. Check cashers provide better access than banks by being open on a schedule that suits the poor: before and after normal business hours and on Saturdays. They are also located in neighborhoods where low-income people live and work. Check cashers provide liquidity appropriate for people who live from paycheck to paycheck by paying immediate cash rather than putting a hold on funds in a customer's account until a cashed or deposited check clears, as banks do. Check cashers provide service by taking time with individual customers, by helping them conduct their transactions, and often by helping their large base of immigrant customers overcome language barriers. This transaction-based business model, which depends on volume, dictates that CCOs provide superior customer service so customers will keep coming back and conducting more transactions.

Coleman suggests that financial services be viewed as a continuum rather than as discrete (bank accounts versus no bank accounts). Check cashers can provide a place for immigrants and the poor to get temporary, transitional financial help until they are ready for a relationship with a bank. He suggests that check cashers can and should do more to meet the financial services needs of these marginalized populations:

> What would be genuinely helpful would be a way of offering a few transitional bank-type services through check cashing locations without abandoning the basic model of transaction based fee for service. That would help those low-income customers who are ready … make the transition from transactional financial services (check cashers) to relational financial services (banking). I believe that the joint venture between check cashers and credit unions may lead to the evolution of a new kind of creature that without relying on charitable or government contributions, without requiring tax exempt status,[24] can thrive while at the same time provide the financial services that the poor genuinely need.[25]

The Business of the Partnership

As outlined briefly in the Introduction, the cooperative arrangement implemented in April 2001 between Bethex Federal Credit Union and RiteCheck Cashing consists of four provisions, with two primary components. First, Bethex members are able to make deposits and withdrawals through the check cashers' Point of Banking (POB) terminals at no cost. These POB terminals are essentially ATMs located within cashier windows, and customers and cashiers conduct transactions jointly. POBs are part of the NYCE regional financial exchange network sponsored by Chase Bank and are regulated according to the established network rules (see Sidebar 4).

Credit union members may also cash checks at participating check cashers without incurring a fee. Rather, the credit union absorbs fees at an agreed-upon discounted rate different from the maximum (1.4%) set by New York state law. In most cases, the resulting fee will be lower than the state limit, although the fee depends upon the amount of the check. (See Table 2 and accompanying footnotes.) It is the same fee structure that is extended to members of PayNet, a cooperative network of check cashers that have established a relationship with New York–area banks to cash payroll checks from some of the banks' large clients. Bethex joined PayNet to facilitate its participation in the pilot. As a result, checks issued by Bethex (e.g., loan checks) and presented at participating check cashers are eligible for the PayNet rates. In addition, Bethex members are able to cash payroll and other checks at participating CCOs for a 1.1% fee, discounted from the statewide 1.4% rate.

Under the other major provision of the partnership, Bethex marketing materials will be available in participating CCOs. A basic packet of information introducing the CU's mission and services, these materials will also contain applications for membership and loans that individuals may complete and mail back or drop off at one of Bethex's offices.

[24] Community development credit unions like Bethex are tax-exempt nonprofit organizations, while check cashers are not.
[25] Interview conducted by case study author, January 22, 2001.

Table 3: Partnership Fee Structure

Transaction	Cost to CU	Cost to Consumer	Net to Check Casher
Withdrawal	\$1.88	\$0.00[a]	\$1.88
Deposit	\$.70	\$0.00	\$.70
Check cashing (issued by Bethex) \$0–\$600[b]	\$4.50	\$0.00	\$4.50
Check cashing (issued by Bethex) \$601–\$1,000	\$5.50	\$0.00	\$5.50
Check cashing (issued by Bethex) over \$1,000	1%	\$0.00	1%
Check cashing (payroll and other checks)	\$0.00	1.1%	1.1%

[a] The check casher will surcharge as provided by NYCE network rules (currently \$1.50). Bethex will pay \$.38 interchange at time of transaction; customer will pay \$1.50, which will be reimbursed by Bethex.
[b] In its six years of operation, the average PayNet check cashing fee works out to be **less** than the regulated rate of 1.4%. This is because most of the checks that find their way into the PayNet system are greater than \$350. Since most Bethex checks are loan checks, it is a certainty that the PayNet rates will fall below the regulated fee amount.

Why It Makes Sense

Check Cashers' Perspective and Interests

The participating check cashers have two major business interests in the credit union partnership. The first is expanding their customer base. Volume is critical to the check cashing business, so if people can be drawn into CCOs with the offer of accessing their credit union accounts, they may then take advantage of other services such as bill paying, money wire transfer, etc.

Partnership with a credit union allows CCOs to offer access to depository accounts, a service that—without such an arrangement—would fall outside their legal range of activities. Coleman views such a partnership as an opportunity both for customers and for his own business. In an industry dependant on fee-based services geared mainly to low-income people with relatively small transactions, expanding the volume of transactions is critically important. Coleman and other check cashers hope that providing access to credit union accounts will draw more people into CCOs, where they then may find it convenient to take care of other necessary financial transactions and thereby boost the overall volume of the check casher's business.

Credit unions seem a logical alliance for check cashers. Unlike banks, they are already present and working in communities that are targeted by check cashers and thus offer a ready market for check cashers' convenient locations and hours. As indicated, Coleman and Cousminer recognized early on that they share a common customer base.

Additionally, Bethex's willingness to absorb fees incurred by its members' use of banking services made possible through the partnership allows check cashers, through POBs, to offer services they otherwise could not, thereby increasing their overall walk-in business volume without bearing the transaction costs for those additional services.

The other reason check cashers want to align themselves with credit unions is public relations. Coleman is a former president and active executive member of the Check Cashers Association of New York (CCANY). During his tenure as president in 1994–95, CCANY developed a strategic plan to guide the future direction of the industry in the state. That plan established three principal goals:

1. grow the core business by increasing the volume of checks cashed
2. form strategic alliances with banks and credit unions
3. become electronic

During that same time, Neil Levin, New York State Superintendent of Banks, was looking for innovative ways to draw the unbanked residents of low-income inner-city neighborhoods into the financial mainstream. Levin talked with Coleman and other check cashers about becoming more active in and integrated into the communities in which they operated, partly to improve public relations. Check cashers, he believed, needed to overcome their predatory image and make people more aware of the needed services they provide to low-income communities. Levin also saw fuller integration into communities as good business for check cashers; it would help them identify additional needs and the best ways to meet them.

The conversations with Levin struck a chord with Coleman, who regretted not being able to offer customers who came into his stores to cash their paychecks the opportunity to put some of that check away into a savings account and ultimately achieve longer-term economic improvement.

Credit Union Perspective and Interests

From Cousminer's perspective, building the broadest possible membership base is necessary to meeting Bethex's mission of serving the poor and those without access to financial services in the Bronx. A broader membership base also helps to make the credit union more viable and sustainable. Philosophically opposed to charging fees to recover operating and transaction costs, Cousminer believes organizations such as hers should make their money through the interest spread on loans. Expanding their membership helps achieve this goal.

In order to expand membership, Bethex was interested in establishing branches but had little money to do so. Cousminer, treasurer and manager of Bethex, thought of working with check cashing facilities both because CCOs have an abundance of convenient locations in low-income neighborhoods and because Bethex had done business with them in the past. In its first twenty years of operation, Bethex used check cashers because it had no real ability to keep cash safely and found that banks were rude and disrespectful to its members when they tried to cash their Bethex loan checks. As a result, Bethex started to send "ok to cash" checks to check cashers instead—an unofficial endorsement that signaled to the check casher that the checks wouldn't bounce.

Although Bethex was interested in branching to meet the banking needs of a broader segment of poor households in the Bronx, it soon discovered that cost constraints were prohibitive. "To build a branch, no matter how small, costs a lot of money, but there are check cashers on every corner," Cousminer points out.[26] She estimates that establishing a branch costs a minimum of $200,000, plus all of the ongoing operating costs—salaries for three full-time employees would run more than $60,000 annually, plus an additional $2,000 in bonding insurance beyond what Bethex currently pays. Then there are operational costs such as telephones, computers, etc. Paying a fee per transaction is comparatively negligible, Cousminer argues, and using check cashers is the most efficient way of acquiring new deposits. In addition, for people who already cash their payroll checks for free through the PayNet system, having access to credit union accounts could help them save.

Cousminer also asserts that using check cashers is more efficient for Bethex's members. Because check cashers are so prevalent in low-income neighborhoods, CCOs are much more convenient for many credit union members than a full-service bank branch, which may mean a round trip of more than an hour and $3 or more in bus or subway fare. That round-trip fare often has to be paid by a low-income single mother traveling with her children or with the children of friends or family members who are in her care. Cousminer wants to help alleviate this time and financial barrier to accessing traditional financial services.

Beyond these direct effects, the partnership also has the broader potential of fostering name recognition both for Bethex and the credit union movement as a whole, positively impacting marketing and outreach.

Community Benefits

From a broader perspective, the partnership offers expanded delivery of credit union services to people who are currently unbanked, drawing more low-income people into the financial mainstream by counseling them on saving money, establishing a credit record, and applying for loans—thus helping them in a more fundamental way consistent with the credit union's mission. Providing low-income people access to basic financial services and thus entry into the economic mainstream has broad societal benefits as well. As these people acquire savings and credit history, they become consumers of additional goods and services, including more advanced financial services such as mortgage loans.

Moreover, a credit union-check cashers alliance may offer a uniquely effective way to reach the unbanked. In immigrant neighborhoods especially, many use check cashers because they have an established relationship with them, trust them, and feel comfortable with them. Many also turn to loan sharks when they need to borrow money (see Sidebar 5). By contrast, they mistrust mainstream banking institutions. Many come from countries where financial services often were corrupt or inflation very high, contributing to their mistrust of banks in general and possibly of any authority system. As evidence of that mistrust, Former NY Superintendent of Banks Neil Levin cites the failure of check cashing windows established by Chemical Bank in their branches.

Mainstream banks are rarely present in poor neighborhoods anyway, but even when they are—and even when they offer check cashing services—they are unable to attract low-income

[26] Quoted in Lauralee Ortiz, "Small CU Plans to Use Check Cashing Outlets As Branches," *Credit Union Journal* 4 , no. 44: 1.

unbanked customers. Coleman says banks fail to recognize that it is not simply a matter of services offered but of the more relaxed atmosphere in CCOs, somewhat like the difference between a fast food outlet and a fine restaurant. Low-income people are comfortable going into the lobby of a CCO in work clothes or with several small children, just as they would be going into a McDonald's. However, they do not feel comfortable walking into the lobby of a mainstream bank in the same circumstances, just as they would be uncomfortable walking into a restaurant and being greeted by a maitre d'.

Furthermore, Coleman says banks are unable to move past the relationship model of financial services. Even for check cashing services, Chemical wanted people to complete a form and join their "Checks to Cash Club". He contends that check cashers' transaction-based model appeals to poor customers; they do not need or want a relationship with a bank until they have enough income to keep some of it in a bank account. Until then, they do not want to provide personal information or otherwise establish a relationship with a bank; check cashers, who do not collect information, provide a level of comfort. It is hoped that this arrangement, by offering banking services through the familiar surroundings of established neighborhood CCOs, will help poor people make the transition to mainstream banking.

The Regulatory and Advocate Responses: The Issues Surrounding This Partnership of "Strange Bedfellows"

After more than four years of planning the pilot and working with regulators to obtain permission to enter into partnership, Bethex, and RiteCheck received letters of approval from the National Credit Union Administration (NCUA) in December 2000 and from the State of New York Banking Department (NYSBD) in February 2001. The proposed partnership raised a number of concerns among regulators and credit union advocates, and the terms of the partnership as approved are somewhat limited compared to the original concept. NYSBD, which oversees the state's CCOs, required that the check cashers involved provide monthly reports on the volume of transactions and fees associated with the partnership, as well as thirty-day advance notice of any changes in the services offered, the project's operations, or the participating check cashing establishments.[27]

In spite of the numerous reasons the partnership seems to make sense for the business of both principals as well as the community, there are a number of issues, questions, and possible negative outcomes arising from the credit union–check cashers partnership. These concerns fall into three categories. The first is a set of broad policy issues related to an alliance of any sort between the mission-driven credit union movement and check cashers, who are viewed among many credit union and other social policy advocates as preying on low-income communities for profit. The second is concern about possible expansion of the partnership to include other features or additional credit union partners in other geographic locations. Finally, there are questions about legal liability raised by check cashers conducting business on behalf of a credit union.

[27] Paul J. Fazio, Deputy Superintendent of Banks, State of New York Banking Department, letter to Gerald Goldman, General Counsel, Check Cashers Association of New York, February 14, 2001.

Public Policy Issues

Advocates such as the National Federation of Community Development Credit Unions (NFCDCU) express a concern over whether the underlying mission of the credit union movement is in fact being served by a credit union–check casher alliance. They worry that the credit union "brand"—its image as a positive social force—may be damaged by affiliation with an industry whose image is less than positive in terms of service to the disadvantaged. Moreover, the heart of the community development credit union movement is member education, with community empowerment the ultimate goal. Advocates doubt members will receive the same (if any) education through check cashers.

One advocate argued that if the major motivation for partnering with check cashers was the sheer prevalence of CCOs, which would enable low-cost CU branches, why not open branches in drugstores instead, since they are also numerous and present less risk to the credit unions' image and less harm to its members.[28] As Cousminer points out, however, there actually are very few drugstores in the poorest neighborhoods of Bethex's service area in the Bronx; they have been forced to close because of repeated robberies.

On the other hand, by aligning themselves with institutions that have a positive social agenda and image, check cashers may be able to improve their own image and parlay that into political legitimacy. NFCDCU officials speculate that the move may be a calculated effort by check cashers to elevate their public image as part of a broader attempt to legalize payday advance lending, currently not allowed in the state of New York. Credit union advocates oppose it because high fees are charged to borrow money for a short term; poor people frequently become mired in debt when they are unable to repay the full amount borrowed in the specified brief period of time. Because payday advance lending is illegal in New York, the credit union–check casher partnership is able to work. However, the check cashers' trade association is lobbying the New York legislature to legalize payday lending. If this happens, advocates wonder about the implications for the partnership.

NFCDCU officials worry that check cashers could even be employing a backdoor strategy to become essentially unregulated banks, taking deposits and making loans. Credit union advocates need to watch this partnership vigilantly, NFCDCU believes, and not lose their resolve in other policy areas regarding check cashers just because they now appear to be "good guys."

Partnership Expansion Issues

Considering all the positive impacts, this kind of partnership might work fairly well, NFCDCU representatives point out, especially in a state like New York where check cashers are strictly regulated. They are less certain, however, about expanding and transferring the partnership to other states. In states where payday advance lending is allowed, partnership customers could be confused between an application for a payday advance and one for a credit union loan. It is also possible that people who go into a CCO intending to apply for a credit union loan might be attracted by the immediacy of an advance and wind up in a debt situation that would be harmful to their overall economic status. In such a case, the credit union could be seen as a pre-developer

[28] John Reosti, "Teaming Up with Check Cashers," *American Banker*, October 25, 2000, p. 1.

of business for check cashers, rather than the other way around, and the credit union's mission of educating and empowering low-income individuals would be defeated.

Cousminer responds to this concern as well, arguing that the situation could be just the opposite: that check cashers offering payday lending could actually serve as pre-developers of business for their credit union partners. Given the choice between a payday advance and a credit union consumer loan, she says, most individuals would be attracted to the credit union loan—especially if the benefits are effectively marketed—because it carries availability of a larger amount, a lower interest rate, and a longer pay-off term. In addition, Bethex's small consumer loans are typically available on a same-day basis, offering cash within twenty-four hours. Cousminer points out that most people who use payday advances for emergency cash are probably in some sort of financial distress and could actually benefit from a larger, longer term loan. A credit union consumer loan can be a better solution to financial difficulties than a payday advance loan, which in her view perpetuates the difficulties and gets a person into a deeper hole.

Additionally, there is the question of whether CUs have adequate infrastructure to handle the additional demand for products and services generated by a partnership with check cashers. NFCDCU officials acknowledge that Bethex is probably in a good position to handle the increased demand for services but fear that smaller CUs may be overwhelmed. This raises the issue of the need for oversight and coordination, particularly when viewing partnerships on a broader scale.

Legal Liability Issues

With CCO employees being involved in CU members' business, a number of regulatory issues arise. The first and probably most significant issue is bonding. The National Credit Union Administration (NCUA), which approved the pilot, instructed Bethex to discuss bonding regulations directly with its bonding agency. Within the scope of the current agreement, bonding is not an issue. However, if the partnership expands to include additional activities, such as accepting account or loan applications, or disbursing loan checks, the bonding issue will need to be reexamined.

Another issue for advocates is liability: Since CCO employees would be handling cash deposits made by Bethex members, there was concern over who would be responsible if the money in the cashier's drawer did not match that handed over by the CU member. When a deposit is made, it is punched into the POB terminal in the customer's presence, the customer is given a receipt, and the information is automatically transmitted to Bethex over the NYCE network. A legal opinion by Steven Bisker, Bethex's attorney and former general counsel for NCUA, delineates that ultimate liability for end-of-day balance discrepancies lies with the bank as sponsor of the check casher's participation in the NYCE network:

> RiteCheck's participation in the NYCE network is based upon its contractual relationship with Chase Manhattan Bank ("Chase") as a "sponsored participant". As a federally insured depository financial institution participant in the NYCE network, Chase is authorized by NYCE to sponsor participants into the network. As a sponsor, Chase is liable to NYCE "and is obligated to accept settlement and billing, for the [t]ransactions of

> its [s]ponsored participants, and must ensure utilization of the NYCE Adjustment System for each of its [s]ponsored [p]articipants." In other words, Chase would be liable for any shortfalls in RiteCheck's network settlement account and for any failures by RiteCheck to properly notify an issuing participant (e.g., the Credit Union) of any checks deposited by cardholders (e.g., members) to their accounts that are returned for nonpayment.
>
> …deposits made at a POB terminal in a shared EFT network are immediately credited to the cardholders' (e.g., members') accounts at their respective financial institutions (e.g., credit union, bank, etc.). The terminal owner (e.g., RiteCheck) is required to have an amply funded network settlement account sufficient to cover all of the deposits credited to the cardholders' accounts. In the case of RiteCheck, any failure on its part to have sufficient funds in its settlement account would result in Chase being liable for such funding.[29]

Any expansion of provisions in the partnership could trigger the issue of liability again. For instance, in earlier versions of the partnership proposal, check cashing employees would be allowed to help customers complete applications for new accounts or loans; the applications would be submitted to check cashers and then forwarded to Bethex. For regulators, such a provision raises concerns over whether check cashing employees are adequately trained or skilled to meet the legal regulations imposed on credit unions, which include full disclosure and truth-in-lending requirements. Coleman envisions the partnership eventually incorporating this element, as well as a provision allowing check cashers to disburse loan checks. Since such activities go beyond electronic transactions that are covered by the NYCE network operating rules and backed by banks, such an expansion of the partnership would require additional regulatory scrutiny.

Conclusions: The Regulatory Environment—Impact of Regulators' Attitudes on the Partnership

The reason for so much regulatory scrutiny and hesitation in this particular case, as opposed to other partnerships involving check cashers, may lie more in perceptions about credit unions than in those about check cashers. Community development credit unions are seen as performing a service to disadvantaged people and communities, a positive good as opposed to a neutral entity (like banks and convenience stores, for example). For this reason the community development credit union sector is often referred to as a "movement." It is possible that regulatory hesitation to approve the alliance stemmed partly from fear of tarnishing the image of the whole movement by sanctioning its partnership with check cashers. The corollary is an uneasy feeling of giving check cashers an undeserved positive image via association with the CU movement. This is,

[29] Steven R. Bisker, Attorrney, representing Bethex Federal Credit Union, letter to Layne Bumgardner, Regional Director, Region I (Albany), National Credit Union Administration, December 12, 2000.

perhaps, where much of the tension about the partnership rests and the reason for wanting to limit it so significantly.

Sidebar 1: Check Cashers' Revenues and Profitability

Because most check cashing outlets (CCOs) are privately owned, there is little available information on the industry's revenues and profitability. A study done by Dove Consulting for the U.S. Treasury Department in 2000 provides a snapshot of the industry. Surveying CCOs in four major metropolitan markets —Atlanta, Boston, San Antonio, and San Diego.[1] Dove found that annual revenues vary among markets, from a little more than $84,000 in San Diego to almost $325,000 in Boston.

Two-thirds of all revenues are derived from check cashing fees, far exceeding the second-place service, money transmission (wiring money), at 18%. Fees charged for money orders contribute 10% of revenues. Overall, loans comprise only 3% of revenues in the four market areas studied. However, San Diego is the only market included in the study that allows payday advance loans; there, loans represent 16% of average store revenues. Two-thirds of CCOs' revenues pay for operating costs, with salaries and payroll expenses comprising the largest chunk at 27%, followed by rent (11%), cash and money services (9%), and bad debt (7%). In terms of profitability, overall pretax return on sales averaged 34% among the surveyed stores. The study also found that chain stores had higher average pretax income than independent stores ($65,000 compared to $39,000).

[1] Survey of Non-Bank Financial Institutions. Dove Consulting, for U.S. Department of the Treasury. April 4, 2000. Available at: http://www.treas.gov/press/releases/docs/nbfirpt.pdf.

Detailed financial information is available for Ace Cash Express (ACE), a publicly traded company that is one of the largest in the check cashing industry. ACE operates 1,200 stores (13% of which are franchised) in thirty states and the District of Columbia. Like most check cashers, ACE offers an array of transactional services, including short-term consumer loans through a partnership with California-based Community West Bancshares.

ACE's 2000 sales totaled $140.6 million, a 15% increase over the previous year and nearly double its ten-year average of $74 million. The 15% increase was actually a bit of a decline from the company's ten-year average annual growth of 24%. Net income grew by just 7% in 2000, though its five-year average growth in this respect is 36%. Company sales had profit margins of 6.8% and 5.9% in 1999 and 2000, respectively; reflective of the firm's ten-year average of 6%.[2]

ACE's return on assets (ROA) and return on equity (ROE) figures have remained rather stable in recent years. Its ROA was 4% in 2000, just down from 5.7% in the preceding year and 4.8% in 1998.[3] This is significantly higher than the average ROA for the nation's largest 100 commercial banks, which had average returns of 1.4% and 1.5% in 1998 and 1999.[4] ACE's ROE is also comparable to that of large banks;

[2] Ace Cash Express, Inc, 2001 Hoover's Company Profile Database–American Public Companies.
[3] Ace Cash Express, Inc. Disclosure Incorporated 2001 company report.
[4] Sheshunoff Information Services, data available at http://www.americanbanker.com.

its return has been consistently around 16.5%[5] over the last three years, while the average ROE of the twenty largest commercial banks was 18.6% in 1999.[6]

[5] Ace Cash Express, Inc. Disclosure Incorporated 2001 company report.
[6] Michael Blanden, "U.S. Commercial Banks: A Bumper Year But…" *The Banker* 150, no. 889 (March 1, 2000).

Sidebar 2: Examples of Bank-Check Casher Partnerships

The move to paying government benefits by electronic funds transfer has increased a trend toward partnerships, as check cashers seek to hold on to their profits from cashing government checks while banks eye government beneficiaries as a pool of potential customers. At the intersection of these interests, several banks and check cashers have formed partnerships to provide complementary services. One of the largest such partnerships was established between the National Check Cashing Association (NaCCA, now the Financial Service Centers of America, or FiSCA) and Citibank. In 1999, the partnership unveiled a new electronic product called the NaCCA Preferred Card, which enables federal benefit recipients to open a special Citibank account into which their benefits will be electronically deposited.[1] They may then access their benefits at any ATM or participating check casher by using the debit NaCCA Preferred Card. Fees vary depending on the check casher; monthly fees range from $3 to $6, with withdrawals ranging from $1 to $4, depending on whether customers access their benefits at check cashers, ATMs, or point-of-sale terminals.[2]

InnoVentry, a joint venture between Wells Fargo and Cash America, owner of pawnshops and CCOs, is developing automatic tellers that cash paychecks for people with or without bank accounts. The terminals, called Rapid Pay Machines (RPMs), are essentially ATMs that rely on face-recognition technology. The earliest RPMs were located in convenience stores, discount stores such as Kmart, and some Kroger supermarkets. In May 2000, InnoVentry announced an agreement with Diebold to place similar machines in bank lobbies to enable unbanked employees to cash their payroll checks without having to stand in the teller lines; this would cut down on per-transaction costs for the banks.[3]

These examples highlight banks' desires to tap into and profit from the unbanked market without having to serve poor people directly, without having them stand in bank lobby lines, and without providing them access to mainstream financial services.

Other banks have elected to create their own freestanding check cashing operations. In an effort to become the principal financial services provider in the United States, Banco Popular established its own check cashing arm, Popular Cash Express (PCE), in early 1998.[4] PCE offers services typical of check cashing outlets as well as some expanded services, such as insurance and travel services, and is exploring offering credit cards and personal loans. As of late 2000, PCE operated seventy-five retail financial service centers in New

[1] "NaCCA Announces New Debit Card Program," NaCCA/FiSCA press release, January 11, 1999, available at http://www.nacca.org/pr6.htm.

[2] "NaCCA Preferred Card…Pilot Program Announced," *NaCCA Currents* (July 1998): 2.

[3] "InnoVentry and Diebold Form Marketing Alliance to Bring Banks ATM Check Cashing Solution for Non-Account Holders," *Business Wire,* May 17, 2000.

[4] Jose Riera, "Banco Popular and Popular Cash Express: Providing Financial Services to the Unbanked," *Community Developments* (Community Newsletter of the Office of the Comptroller of the Currency, U.S. Department of Treasury), Fall 2000, p. 11.

York, California, Texas, Arizona, Florida, and Washington, D.C.

Westamerica Bancorp started its own chain of check cashing outlets, called Money Outlet Inc., in late 2000. The northern California stores are cashing checks and selling money orders exclusively but plan to expand to other typical CCO services if they do well. Westamerica's relationship between its two businesses is virtually the polar opposite of Banco Popular's. Westamerica is not marketing bank accounts to Money Outlet customers; in fact, signs advertising the CCOs do not even acknowledge an affiliation with the bank. This separation is deliberate; Westamerica officials say they view check cashing as a completely different market that is not served by banks. This distinction makes perfect business sense to one investment analyst, who thinks Westamerica is wise to protect its reputation as a leading small business lender: "Check cashing is a different type of business, with a down-market customer who has a very different set of financial needs. You don't want to mix those brands, or you risk diluting the value of your brand."[5]

Union Bank of California, the state's third largest commercial bank, also has entered the business. Its Cash & Save is a hybrid program that goes beyond check cashing by using education and consulting services to encourage those accustomed to using check cashers to transition to traditional banking services. Begun at its Hawthorne location in south-central Los Angeles in 1993, 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 CCOs—what distinguishes Cash & Save is the range of banking services it provides. These include a discounted rate for buying a money order "plan" (six free money orders per month plus a 1% check cashing fee), no-fee low-minimum-balance basic checking and savings accounts, a secured credit card, and direct deposit for electronic delivery of government benefits. The bank estimates that 40% of Cash & Save's repeat customers had transitioned to traditional banking products such as checking and savings accounts by late 2000.[6]

In addition to its own check cashing outlets, Union Bank has entered into an alliance with Nix Check Cashing and Operation HOPE, Inc., a community-based nonprofit, to provide financial services in inner-city Los Angeles neighborhoods. Under the terms of the agreement, Union Bank acquired a 40% stake in Nix's parent company, Navicert Financial, Inc., with an option to acquire the remainder of the company in ten years, during which time Union Bank will give 5% of the company's equity to Operation HOPE.[7] Through participating Nix outlets, Union Bank offers applications for home mortgage loans, credit cards, checking and savings accounts; a dedicated phone line with

[5] R. Jay Tejera, senior analyst, Ragen MacKenzie, quoted in Katie Kuehner-Hebert, "California's Westamerica Enters Check-Cashing Biz," *The American Banker*, November 16, 2000, p. 1.

[6] "Banking, Financial and Educational Services Offered At Nix Check Cashing Stores," *Business Wire,* September 28, 2000.

[7] "Unique Venture Teams Nix Check Cashing, Union Bank of California and Operation Hope; 'We're Bringing Banking Back to the Inner City'," *Business Wire*, March 16, 2000.

access to a customer service representative; a full-service ATM with no surcharge for nonbank customers; and small business loan and deposit services. For its part, Operation HOPE offers mortgage assistance, consumer and business credit education information through brochures, and a direct phone lineto get information about and register for these financial education opportunities. . The partnership, seen by Union Bank as a way to provide poor people with a bridge into the financial mainstream, was implemented at three Nix stores in July 2000; the partners anticipate expanding the services to all forty-seven Nix outlets over the next two years.[8]

Union Bank's approach does not give low-income individuals access to the full range of mainstream financial services offered by the bank. While each Nix store in the pilot has a teller window bearing a Union Bank sign, the teller's job is to help people open Union Bank accounts and to direct them to information and automated services nearby. Basic banking transactions such as deposits, withdrawals, and check cashing, even for Union Bank accountholders, are only available through the Nix windows, at the check casher's normal rates. This situation leads some advocates to criticize Union Bank for continuing to relegate low-income neighborhood residents to second-class financial services.[9]

In response, Union officials point out that the bank is legally restricted from offering teller transactions through Nix outlets.[10] Beyond that limitation, however, turning Nix offices into Union Bank branches runs counter to the model the bank is pursuing, at least in the short term. The bank's experience has demonstrated that it is difficult for new branches in low-income neighborhoods to generate the volume of accounts necessary to sustain themselves. In the Nix partnership, Union has chosen to build on a fully financed and functioning platform so that the expected slow growth in accounts is offset by the revenues from typical check cashing fees provided by Nix.[11]

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8 "Banking, Financial and Educational Services," *Business Wire.*

9 Laura Mandaro, "Union Bank, Check-Casher Team Up," *The American Banker*, September 25, 2000.

10 Union Bank invested in Navicert without regulatory approval, taking advantage of the Gramm-Leach-Bliley Financial Modernization Act of 1999, which eliminated barriers to banks owning other financial businesses.

11 Ibid.

Sidebar 3: What Is a Community Development Credit Union?

A credit union is a nonprofit, cooperative financial institution. Members (the equivalent of depositors to a bank) are the shareholders: They own the credit union and govern its operations. Credit union membership is restricted to a specific "field of membership," which may be based on where the members live, the company for which they work, or the organization to which they belong.[1]

A community development credit union (CDCU) is a geographically-based cooperative established by people in low-income communities as a way to pool their savings and make loans to each other. CDCUs are driven by a mission of reinvesting in distressed neighborhoods and communities and empowering poor families to become economically self-sufficient. To meet this mission, CDCUs provide basic financial services at low costs and access to credit to traditionally underserved populations.

Like all credit unions, CDCUs are:

- democratically controlled
- nonprofit
- insured and government regulated
- operated by volunteer boards of directors

CDCUs are distinct in their mission of serving low-income communities. Federal law and regulations support the CDCU mission by allowing these institutions to raise deposits and capital from nonmembers, including foundations, banks, faith-based institutions, and other social investors. CDCUs as a whole are often referred to as a movement because of their mission-driven orientation and because they have created a national organization to advocate on poverty issues as well as on policies that impact their operation. There are nearly 200 CDCUs serving urban and rural communities in forty states, spanning a broad spectrum of age, size, and operational sophistication.[2]

The movement began fifty years ago, with the first CDCUs organized to combat lending discrimination. The most recent ones were created in the 1990s to meet the financial service needs in neighborhoods where banks had downsized and closed branches.

Some CDCUs offer basic services one or two days a week in community facilities, such as church halls. Others have modern, full-service facilities, complete with ATMs.

All CDCUs offer small consumer loans. Some provide financing on a larger scale for housing, small and minority-owned businesses, and nonprofit organizations.

While providing their members capital for immediate needs, such as medical bills or a car to reach a distant job, CDCUs also help members save and borrow for long-term goals, such as buying a first home, starting a small business, or getting a college education.

[1] "Credit Unions and Banks: What's the Difference?" available at the Bethex Federal Credit Union web site, http://www.bethexfcu.org/difference.htm.

[2] "What are CDCUs?" Available at the National Federation of CDCUs web site, http://www.natfed.org/Home.html.

Sidebar 4: Point of Banking Terminals – A Critical Technological Link

Check cashers' ability to accept deposits from Bethex Federal Credit Union members is clearly the most critical feature in making this alliance unique and innovative. That ability is made possible by a financial transactions terminal called a Point of Banking (POB) terminal, found in RiteCheck and several other check cashing outlets in New York. Because of the critical role the POB plays in making banking services available through CCOs, it is important to understand its operation and implications.

What Is a POB?

In simplest terms, a POB is an ATM without a cash dispenser. It looks and functions in a manner very similar to Point of Sale (POS) terminals used in retail establishments to receive electronic payments. The POS is generally offered as a convenience to customers, and a merchant pays a fee (which is not passed on to customers) to route transactions over the POS network.

POBs provide consumers with remote access to banking services and initially were developed cooperatively by Chase Manhattan Bank, the NYCE network, and the check cashing industry in 1994. In their first incarnation, POBs could perform cash withdrawals, transfers between accounts, and balance inquiries; they have expanded to accept deposits as well, a feature that RiteCheck president Joe Coleman refers to as a quantum leap. In his words, "The deployment of POBs will enable ... storefront service centers (licensed check cashing outlets…) to offer banking products, from a variety of banks, in a convenient and cost effective, neighborhood setting."[1]

The Nuts and Bolts: How Do POBs Function?

A check cashing business wanting POB terminals enters into an agreement with Chase Manhattan Bank to deploy one or more POB terminals in a location. Chase sponsors the CCO in the NYCE network, with which Chase has a contractual agreement.

Here is how a deposit transaction works:
1. Customer enters CCO with a $200 payroll check from Employer Y and a debit ATM card from Bank X. Customer wishes to deposit the money from her payroll check into her checking account at Bank X.
2. Customer approaches one of the cashier windows, tells the cashier what she would like to do; she first cashes her check and receives $197.80 cash ($200 less the 1.1% fee for credit union members as part of the terms of the pilot partnership detailed in this case).
3. To deposit the cash, customer next swipes her card and enters her personal identification number (PIN) into the POB.
4. Cashier enters the appropriate information into the POB.
5. The POB routes this information via the phone line through the NYCE network to Bank X's computer.
6. Bank X sends back a confirmation that $197.80 has been deposited into

[1] Joseph Coleman, "Introducing *Point of Banking*," Document used as handout/primer for CCANY members, undated.

the customer's Bank X checking account, and the POB prints a receipt, which the cashier hands to the customer.

7. The customer can also purchase a money order, pay a bill, or receive part of her paycheck in cash in the course of this exchange. These transactions would simply be deducted from the amount deposited, and this information would be reflected on the receipt the customer receives. Combining steps allows customers to conduct multiple transactions at one place, which is different from (and, perhaps, more convenient than) ATMs. So, instead of taking a payroll check to a CCO, buying a money order, getting the remainder in cash and then taking the cash to an ATM for deposit, the customer is able to perform all steps at one cashier's window.

The customer receives a printed receipt confirming that the transaction has been recorded in her bank or CU account. If the cashier's drawer does not reflect the deposit at the end of the day, the liability lies with the check casher and, ultimately, with Chase as the sponsor of the check casher in the NYCE network.

Sidebar 5: Poor and Immigrants Turn to Loan Sharks for Debt Capital

Community development credit unions such as Bethex must compete with a way of borrowing that is entrenched in mostly poor, immigrant neighborhoods in New York and across the country—loan sharking. Loan sharks are informal lenders who provide debt financing to poor people, often to start small businesses. While New York law caps annual bank loan interest at 25% and person-to-person loans at 16%, the loan sharks' typical going rate of 2% to 5% weekly amounts to 104% to 260% annually.[1]

The ability of these illegal lenders to thrive, even in communities where mainstream banks are present, is a result of a combination of cultural factors. Many Latino borrowers come from countries where the poor usually do not have access to banks and have little money to save. Illegal immigrants particularly fear banks because of questions about their immigration status. They can't get a bank account without a Social Security number, so they don't go to banks for fear of being discovered and deported. Often, they do not keep the financial records necessary to apply for a commercial loan. Moreover, loan sharks tend to make loans more quickly, ask fewer questions, and be more understanding about a borrower's inability to pay.

Modern-day loan sharks are not linked to organized crime and do not use threats or coercion to force repayment. Instead, they tend to secure collateral to seize if the loan fails—often the property the borrower is trying to lease or buy. Some will hold jewelry or watches or the borrowers' immigration papers until the loan is repaid and as insurance that the borrower does not disappear.

[1] Dexter Filkins, "In Some Immigrant Enclaves, Loan Shark Is the Local Bank," *New York Times,* April 23, 2001, Section A, p. 1.