Date of Hearing: April 19, 2010

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Mike Eng, Chair
AB 2581 (Bradford) – As Introduced: February 19, 2010

SUBJECT: Banking development districts.

SUMMARY: Establishes a Banking Development District (BDD) program with the state Treasurer's office, which would encourage the establishment of bank branches and/or new bank services in specially designated geographic locations where there is a need for banking services. Specifically, this bill:

1) Makes findings and declarations regarding the status of unbanked and underbanked consumers, as well as, the need for baking services in underserved communities.

2) Provides that financial institutions, as defined, may seek to participate in the BDD program if they do either of the following:

   a) Open a new outlet in a lower income, underserved area: or,

   b) Develop and market a new product line or group of services in an existing outlet in an underserved community.

3) Defines "underserved community" as a remote location or impoverished area that lacks banking services commensurate with the services provided to higher income areas with a population of similar size.

4) Defines "Banking Development District" as a specifically designated geographic location where there is a demonstrated need for banking servicers that has been designated as such by the Treasurer and the Department of Financial Institutions (DFI).

5) Provides that a local agency in conjunction with a bank shall submit an application to the Treasurer and DFI in order to participate in the BDD program. This application shall request that specific underserved community be named as a BDD.

6) Allows for the Treasurer, DFI and local agencies to compile list of underserved communities or regions that lack a concentration of banks and services in order to provide banks with a clear demonstration of those areas that are in most need.

7) Specifies that the application for participation in the BDD program shall include the following components:

   a) Clearly defined current and anticipated bank product and service needs of the community;

   b) Demonstrate that those needs are not currently being met by existing institutions; and,

c) Demonstrate that the bank applying for acceptance can meet the needs of the community as identified.

8) Requires the Treasurer and the DFI to set forth selection criteria to evaluate a bank's application. The criteria shall meet the following:

   a) Result in needed and responsible bank products and marketing of those products to local consumers;

   b) Be flexible and allow for differences in local markets; and,

   c) Encourage viable business practices.

9) Provides that the Treasurer and DFI shall evaluate and approve applications and designate BDDs to the extent that participating banks can accomplish the following:

   a) Help unbanked Californians open starter accounts that include no monthly balance requirements, low cost overdraft protection plans and second chance accounts;

   b) Build the financial literacy of low income customers;

   c) Provide effective ways for low income customers to build savings and a credit record;

   d) Provide competitively priced mortgage and auto loans;

   e) Offer microloans and micro lending products and services;

   f) Provide products to assist small businesses; and,

   g) Provide specialized marketing, and specialized training for staff.

10) Requires the Treasurer and DFI to develop and provide a range of incentives to encourage banks to participate in the BDD Program that shall be valuable to banks and significant enough to encourage banks to locate in underserved communities.

11) Provides that a bank that is located in a BDD and that has been designated as such, shall be eligible for a range of incentives including, but not limited, to:

   a) Access to priority of deposits of public funds and access to below market-rate public funds as deemed appropriate and approved by the Treasurer; and,

   b) Incentives offered by local agencies as deemed appropriate and approved by the Treasurer.

12) Allows the Treasurer to work with local agencies and economic development officials to develop additional local incentives for participating banks including, but not limited to, the following:

a) Local agency deposits;

b) Assistance in locating suitable commercial real estate space for branches;

c) Local tax incentives; and,

d) Workforce development.

13) Requires the Treasurer and DFI to adopt rules and regulations for the establishment of the program, as well as, development a performance review process.

EXISTING LAW provides for the regulation of state banks and credit unions by DFI.

FISCAL EFFECT: Unknown

COMMENTS:

In 1998, the state of New York, under Governor George Pataki, created the first BDD program in the nation. BDDs were designed to provide communities with a resource to assist in providing economic development opportunities and incentives to financial institutions to locate in underserved communities. According to a 2006 Wall Street Journal Article, Citibank executives acknowledged that without the below-market-rate deposits from the state and city, the bank would continue to lose more than $350,00 a year operating a three story branch in a neighborhood where 38% of the residents live below the poverty line. The goal of AB 2581 is to spur increased and enhanced banking services in under-served communities that will spur greater financial inclusion. The desired outcome is that more Californians will enter the financial mainstream and build savings and wealth through participating banks' offerings and marketing of appropriate transactional, loan, and credit products that can lead to long-term wealth building opportunities.

In the modern financial arena consumers are faced with a confusing myriad of choices and options. This confusion is amplified by the financial illiteracy of most consumers, and what has been a traditional lack of outreach by financial institutions to certain communities. Recently, the untapped market of those without a banking relationship has become an intriguing opportunity for those offering financial services. However, as many studies have shown, the unbanked and underbanked often do not feel comfortable dealing with financial institutions that are not located in their neighborhoods.

The Unbanked : The unbanked, or those without a transaction account with a financial institution constitute approximately 22 million, or 20% of Americans. This population spends $10.9 billion on more than 324 million alternative financial service transactions per year. Bearing Point, a global management and technology consulting company, estimates that the unbanked population expands to 28 million when you include those who do not have a credit score. In addition, Bearing Point, puts the underbanked population, defined as those with a bank account but a low FICO score that impedes access to incremental credit, at an additional 45 million people. Although estimates find that at least 70% of the population has some type of bank account, these individuals continue to use non-bank services, ranging from the purchase of money orders, use of payday lenders, pawn shops or sending of remittances. The Federal

Reserve Board has noted that 50% of current unbanked households claim to have had an account in the past.

In California, 28% of adults do not have a checking or savings account, according to the U.S. Census. In San Francisco, the Brookings Institution estimated that one in five San Francisco adults, and half of its African-Americans and Hispanics, do not have accounts. Recent market research indicates that Fresno and Los Angeles have the second and third highest percentages of un-banked residents in the country.

Nationwide, the unbanked are disproportionately represented among lower-income households, among households headed by African-Americans and Hispanics, among households headed by young adults, and among renters. A Harvard Poll of Hurricane Katrina evacuees in the Superdome found that seven out of ten did not have a checking or savings account.

The unbanked poor pay more to conduct their financial lives. Check cashing outlets can charge between 2-3% of the face value of a check. So, an individual who makes $30,000 a year can pay $800 a year in fees to cash their payroll checks and pay their bills. The lack of access to mainstream banking costs both consumers and society, as well as, the financial community that misses out on this untapped market.

Families without accounts don't have a safe place to keep their money. They may walk around with wads of cash in their pockets, or keep it at home in a coffee can. Robberies are more prevalent around check cashing outlets. A burglary, or a fire, could cost them their life's savings in a matter of moments. A bank account helps people take the first step onto the path of savings and mainstream financial products. Without an account, it is much more difficult to get well-priced car loans, credit cards, or mortgages-the exact financial tools needed to climb up the economic ladder. Stable societies are built on financially stable families who have access to high-quality, low-cost financial services.

In January 2009, the FDIC sponsored a special supplement to the U.S. Census Bureau's Current Population Survey (CPS) to collect data on the number of U.S. households that are unbanked and underbanked, their demographic characteristics, and their reasons for being unbanked and underbanked. The following are the findings from the survey:

1) An estimated 7.7 percent of U.S. households, approximately 9 million, are unbanked.3 At least 17 million adults reside in these unbanked households.

2) The proportion of U.S. households that are unbanked varies considerably among different racial and ethnic groups, with certain racial and ethnic minorities more likely to be unbanked than the population as a whole. Minorities more likely to be unbanked include blacks (an estimated 21.7 percent of black households are unbanked), Hispanics (19.3 percent), and American Indian/Alaskans (15.6 percent). Racial groups less likely to be unbanked are Asians (3.5 percent) and whites (3.3 percent).5

3) In addition to the unbanked households, an estimated 17.9 percent of U.S. households, roughly 21 million, are underbanked.

4) Certain racial and ethnic minorities are more likely to be underbanked than the population as a whole. Minorities more likely to be underbanked include blacks (an estimated 31.6

percent), American Indian/ Alaskans (28.9 percent), and Hispanics (24.0 percent). Asians and whites are less likely to be underbanked (7.2 percent and 14.9 percent, respectively).

5) Taken together, at least 25.6 percent of U.S. households, close to 30 million, are either unbanked or underbanked. Approximately 60 million adults reside in these households.

6) Overall, almost 54 percent of black households, 44.5 percent of American Indian/Alaskan households, and 43.3 percent of Hispanic households are either unbanked or underbanked.

7) While 17.9 percent of U.S. households are known to be underbanked, another 4.1 percent of U.S. households, or roughly 5 million, are banked and may also be underbanked, but their use of Alternative Financial Services (AFS) could not be determined because of missing data. The number of adults that reside in these households is estimated to be 11 million.

8) The proportion of unbanked and underbanked households varies across different regions of the country, with the highest incidence in the Southern United States.

9) A substantial percentage of lower-income households are unbanked. Nearly 20 percent of lower income U.S. households—almost 7 million households earning below $30,000 per year—do not currently have a bank account. Households with earnings below $30,000 account for at least 71 percent of unbanked households.

10) The proportion of unbanked households declines with education and age. Households more likely to be unbanked than all U.S. households have less than a college education or a householder under age 45.

11) Not having enough money to feel they need an account is the most common reason why unbanked households are not participating in the mainstream financial system.

12) The 9 million unbanked households are approximately split between households that have never had a bank account (46.9 percent) and households that were previously banked (49.0 percent).

13) A considerable proportion (an estimated 41.1 percent) of unbanked households believes that opening a bank account in the future is "not likely at all." However, among all unbanked households, the previously banked are more likely to consider opening a bank account in the future. About 16 percent of previously banked households believe that they are "very likely" to open a bank account, compared with 4.8 percent of those that have never been banked.

14) About 66 percent of unbanked households use the following alternative financial services AFS: nonblank money orders and non-bank check-cashing, pawn shops, payday loans, rent-to-own agreements (RTOs), and refund anticipation loans (RALs). About one-quarter of unbanked households do not use any AFS, suggesting a strong reliance on cash transactions.

15) Approximately 12 percent of unbanked households have used a general spending prepaid card, and an estimated 3.1 percent receive their income through a payroll card.

16) The underbanked rate declines with age of the householder but is more evenly distributed across most educational and income groups. For example, middle-income households (those with annual income between $30,000 and $50,000) are about as likely as lower-income households (those with annual income below $30,000) to be underbanked. The proportion of underbanked households is considerably lower among the highest education level of the householder (at least college degree) and the highest income group (at least $75,000).

17) The AFS products used most frequently by underbanked households are non-bank money orders (an estimated 81.1 percent of underbanked use money orders) and check-cashing (30.0 percent) transaction services. Underbanked households also use on payday lenders (16.2 percent), pawn shops (15.8 percent), RTO services (13.0 percent), and RALs (13.2 percent) for credit services from non-banks.

18) The survey data indicate that the majority of underbanked households that go to nonbanks for money orders and check cashing do so primarily for convenience. Speed and cost were also reasons underbanked households use these non-bank transaction services.

19) Many underbanked households that use payday loans or pawn shops rather than banks for credit services do so primarily because it is easier to qualify for a loan from the AFS provider or because it is more convenient.

20) Approximately 16 percent of underbanked households have used a general spending prepaid card and an estimated 4.2 percent receive their income through a payroll card.

Following up on the aforementioned survey, in February 2009, the FDIC released the results of a survey of insured institutions regarding the unbanked and underbanked as required by Section 7 of the Federal Deposit Insurance Reform Conforming Amendments Act of 2005. Here is a sample of those results:

1) Seventy-three percent of banks are aware that significant unbanked and/or underbanked populations are in their market areas, but less than 18 percent of banks identify expanding services to unbanked and/or underbanked individuals as apriority in their business strategy. Over three quarters of banks (77 percent) have not conducted research on this potential opportunity in their Community Reinvestment Act (CRA) assessment areas. The 25 largest banks are more likely than smaller banks to identify expanding services to these groups as a priority, although fewer than half of larger banks (46 percent) have done so.

2) When asked to rank-order the three most effective ways of educating and reaching out to unbanked and/or underbanked customers, banks identified “Providing financial education sessions” as most effective, followed by “Participation in other organizations,” and “Outreach visits.” Almost all banks (98 percent) rank “Participation in other organizations” or “Outreach visits” among the top three most effective programs.

3) Sixty-three percent of banks provide financial education materials to unbanked and/or underbanked individuals, often in the form of brochures and pamphlets. Basic banking or savings program educational materials for unbanked and/or underbanked customers are provided by about 39 percent and 34 percent of banks, respectively.

4) Thirty-seven percent of banks participate in financial education or outreach efforts with other organizations to expand services to unbanked and/ or underbanked individuals. Examples of such efforts include working with employers that use payroll cards, government entities that use electronic benefit transfer (EBT) or prepaid cards, and faith-based groups that provide cash assistance. The largest 25 banks are more likely to participate in such efforts.

5) About half (53 percent) of banks teach financial literacy and education sessions targeted at unbanked and/or underbanked individuals. Larger banks are more likely to offer such educational sessions. Among banks that do provide such sessions, the topics most likely to be covered are basic banking and savings programs.

6) Fifty-eight percent of banks conducted off-premise financial education and outreach visits during 2007, most commonly at high schools and community- based organizations.

7) Thirty-eight percent of banks work with corporate or business customers to provide services for unbanked and/or underbanked employees. Larger banks are more likely to work with businesses to promote services for the unbanked than smaller banks.

8) A quarter (25 percent) of banks use targeted marketing to reach unbanked and/or underbanked individuals. Larger banks are more likely to engage in targeted marketing. Among banks that target a specific demographic segment, Hispanic Americans are most frequently cited. Perceived Challenges to Serving Unbanked and/or Underbanked Customers

9) When asked to rank order the challenges banks face in serving or targeting unbanked and/or underbanked individuals, banks list “Profitability issues” first, followed by “Regulatory barriers,” and “Fraud concerns.” Regulatory impediments are perceived by 40 percent of banks, reflecting concerns related to maintaining compliance with the Patriot Act and the Bank Secrecy Act.

10) Over half of banks offer limited extended hours and foreign language capabilities at their retail branches. Fifty nine percent of banks offer extended branch hours, typically after 5:00 p.m. on weekdays and after 1:00 p.m. on Saturdays. Among brick and mortar branch locations, 81 percent offer extended weekday evening hours, 16 percent offer Saturday afternoon hours and 5 percent offer Sunday hours. Fifty two percent of banks have hired staff with foreign language capabilities.

11) Almost two-thirds (64 percent) of banks report that they have modified their retail operations in the last five years to make the bank more appealing or convenient for unbanked and/or underbanked customers. Almost three quarters (73 percent) of these banks reported doing this by offering Internet or mobile banking. Forty seven percent of banks have installed external automated teller machines (“ATMs”) and 43 percent have added off-premise ATMs. Thirteen percent of banks added non-traditional locations in community centers, supermarkets, etc. and 20 percent of banks added branches in low-to-moderate income (LMI) areas.

12) When asked what efforts banks make as part of their branch strategies to serve unbanked and/or underbanked customers, less than half of banks identified providing check cashing (49 percent)and money order (41 percent) services. Far fewer banks identified bill paying

services (18 percent), prepaid card issuance and reloading (12 percent), and check cashing kiosks (less than one percent).

13) Banks provide limited check cashing opportunities for non-customers who may be unbanked and/or underbanked. Most banks (96 percent) will cash checks for non-customers drawn on the bank itself, but less than one-third will cash payroll and other business checks not written on the bank for non-customers.

14) Offerings of other transaction services to noncustomers who may be unbanked and/or underbanked are more limited. Bank checks/money orders and international remittances are available to non-customers at 37 percent and 6 percent of banks, respectively. Check cashing cards are offered by 2 percent of banks to non-customers.

15) Government-issued identification is required by most banks to open a new account. Most banks will accept either a driver's license (99 percent) or passport (92 percent) to open an account. Matricula Consular cards are accepted by 27 percent of banks and 38 percent of banks accept Individual Tax Identification Numbers (ITINs) during the process of opening a new account.

16) Unbanked and/or underbanked individuals with blemished account or credit histories often face challenges to opening new accounts. Most banks 87 percent) require a third party customer screen such as ChexSystems when opening a new checking account.6 A quarter (25 percent) of banks automatically reject a new account application that receives a negative result in the screening process and about half (49 percent) of banks are able to override a negative result at the branch location. A quarter (25 percent) of banks offer "second chance" accounts designed for individuals not qualified for conventional bank accounts.7

17) When asked to rank order the three most common reasons that a new account applicant is declined, banks identified "Negative account screening" first, followed by "Insufficient identification information" and "Low credit score." Deposit, Payment, and Credit Products and Services Offered to Entry-Level Consumers

18) Almost two-thirds (62 percent) of banks offer an entry-level checking account with no minimum balance. Another 8 percent of banks normally charge a minimum fee on their most basic checking account but will waive the fee if the customer uses direct deposit. When required, the median minimum balance with or without direct deposit was $100.

19) Nearly all banks (99 percent) charge a per-item overdraft fee on their most basic (lowest cost) transaction account. Overdraft fees range from $8 to $38 with a median of $25. While over half (60 percent) of banks offer some type of program that will cover or waive the fee, such programs frequently involve a line of credit or transfer and may not be available to underbanked customers. Over half of banks (57 percent) that charge overdraft fees automatically close an account after a customer has a certain number of overdrafts (ranging from one to 500) or after an account has remained in negative status for a given period of time (ranging from 10 to 180 days).

20) Nearly all banks (97 percent) offer low-balance (under $500) basic savings accounts, but few offer savings programs designed to help unbanked and/or underbanked customers. Seven

percent of banks offer savings accounts through work place based programs, eight percent of banks participate in or offer Individual Development Account (IDA) programs.

21) Less than a quarter (22 percent) of banks partner with organizations to promote savings products and about half (49 percent) of banks offer special savings clubs. The largest 25 banks were more likely to offer some of these programs. Funds availability from deposited checks at many banks, while in compliance with federal regulations, is slow relative to non-bank check cashing services. At least one-third of banks require at least a one-day wait for funds to be available from any check. Longer waits are frequently required for government or payroll checks and checks drawn on another bank.

22) Banks offer few advance or credit products tailored to LMI and/or unbanked and underbanked customers. Less than 6 percent of banks provide an advance on funds due to arrive by direct deposit or check. While over two-thirds (69 percent) of banks offer closed-end unsecured personal loans for amounts under $5,000, eligibility requirements may hinder access for unbanked and/ or underbanked customers.

23) Survey responses to a question asking whether banks offer "affordable small dollar loans" revealed confusion about the product since a number of banks counted overdraft programs with a line of credit in their affirmative responses.

Recent developments.

In October of 2009, the Los Angeles City Council approved a motion to establish a local BDD program by requiring the City Attorney and City Treasurer to draft an ordinance establishing the program. Additionally, the City Treasurer must set up a task force with department heads and council members to determine what modifications may be needed to adapt the New York BDD model program to Los Angeles.

On January 24, 2008, Governor Schwarzenegger announced an effort to assist unbanked and underbanked Californians. This program, called Bank on California, is built off of a pilot project in the City of San Francisco, known as Bank on San Francisco. The idea behind the Bank on California program is too increase the availability of starter checking accounts through partnerships with financial institutions. Additionally, this program creates partnerships between local officials, banks and community groups to raise awareness on the importance and benefit of entering the financial mainstream.

Questions.

1) What sort of incentives can be offered given legal requirements that the State Treasurer must maximize the return on investments and deposits?

2) The Bank on California program attempts to get more people banked. How could this bill assist that effort, or vice versa? Could this bill conflict with that effort? Are there statistics on the Bank on California program that demonstrate its effectiveness?

3) How many people have been assisted with banking accounts by the New York BDD program?

Amendments.

Committee staff recommends the following amendments to address inconsistencies in the language and to correct technical errors.

1) Page 4, lines 1 and 2, strike "a demonstrated need for banking services." Insert "an underserved community"

2) Page 4, line 5 strike "lower income, underserved area" and insert "an area designated as a banking development district."

3) Page 4, line 7 strike, "underserved community" and insert "in an area that is designated as a banking development district."

4) Page 4, line 21 strike "where there is a demonstrated need for banking services" and insert "comprising an underserved community."

5) Page 4, lines 33-37 (section 40002(c)) and move to new section 40002(b).

6) Change section 40002(b) to new section 40002(c).

7) Page 5, line 17 strike "viable business practices" and insert "safety and soundness"

8) Page 5, line 35 after "build" insert "or improve."

REGISTERED SUPPORT / OPPOSITION:

Support

New America Foundation (Sponsor)
Center for Responsible Lending (CRL)

Opposition

None on file.

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