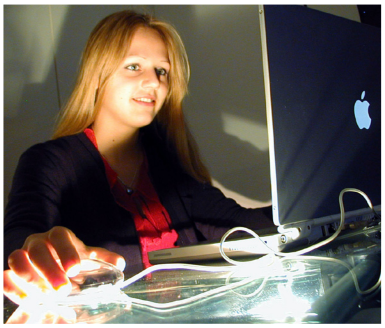
IDB

Banking the Unbanked



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August 15th, 2003

MIF
FOMIN

Inter-American Development Bank

“BANKING THE UNBANKED”

According to new estimates released by the U.S. Census Bureau, the Hispanic population in the United States reached 39.9 million on July 1, 2003, accounting for about one-half of the 9.4 million residents added to the nation’s population since Census 2000. The growth of the Hispanic population is enormous, projected to increase from 9 percent of the total population in 1990 to 16 percent in 2020.

A recently released study by the University of Georgia’s Selig Center for Economic Growth states that Hispanics nationally, both native and foreign-born, have a disposable income of $686 billion. By 2010, this is projected to double to $1.4 trillion.

U.S. Banks have begun to realize the significance of this market and are exploring various marketing strategies and business models to attract and integrate the Latin American immigrant into the financial mainstream. One of the marketing strategies employed by banks is the offering of bank accounts with ***remittance service*** features.

What are Remittances Services?

In 2004, according to the Multilateral Investment Fund (MIF) of the Inter-American Development Bank (IDB), an estimated $45 billion was remitted to Latin America and the Caribbean (LAC), of which $34 billion was sent from the U.S. to LAC. In 2004, as in the previous two years, remittances exceeded the combined totals of official development assistance and foreign direct investment received by the region.

Currently, more than 175 million separate remittance transactions are sent each year from all over the world to approximately 25 million LAC households, typically $100/$200/$300 at a time, and mostly outside the banking system.

How often do Latin American immigrants send funds back home?

At least 65 percent of Latin American immigrants in the United States remit funds back to their countries of origin monthly, and 20 percent do so slightly less frequently. This flow of funds has proven to be stable even during the economic downturn experienced in the U.S. in the years 2000 and 2001.

The IDB estimates over $2 billion in fees were generated by remittances services in 2003. Transaction costs to send these remittances have been cut in half over the past five years, but at 7 percent, still remain too high. Studies conducted by the MIF report that remittance dollar amounts are increasing ($300-$400), cost has declined due to increase competition as banks and credit unions are entering the market. However Latin American immigrants continues to describe themselves as lacking knowledge of newly available remittance products.

What are the various remittance products?

Remittances from the U.S. to Latin America are sent predominantly by large money transfer businesses (e.g., Western Union), with a growing percentage being sent by banks and credit unions.

The channels used to send remittances, include:

- Postal money orders
- Personal delivery systems
- Traditional wire transfers
- Cash to cash transfers
- Automated batch processing
- Account to account transfers
- Mobile ATMs
- Dual ATM cards
- Debit Cards
- Credit Cards
- Pre-paid Card
- Stored value cards
- Cellular phones
- Internet

How do most Latin American immigrants send money home to their families?

In 2004, according to a state by state survey of remittance senders conducted by Bendixen & Associates for the Multilateral Investment Fund:

- 78 % of Latin American immigrants send money home through international money transfer companies
- 11 % through people traveling back home
- 7 % through banks
- 2 % via mail
- 1 % through credit unions

It is obvious that there is a great deal of growth potential for banks and credit unions to enter this market.

Factors that can influence what channels will be used include:

- Language
- Cultural preferences
- Immigration status
- Financial education
- Relational trust with financial institutions
- Awareness of the available remittance options

- Cost of banking services
- Convenience of longer hours of operation by non-bank financial institutions vs. banks and credit unions
- The efficiency of the delivery system
- The existence of a modern banking system and financial infrastructure in the country of origin
- The income status of the sender and recipient

According to the 2002 Yankelovich/Cheskin Hispanic Monitor Study, Hispanics want to use financial services available in the United States but they are not aware of what these services are or where to go. Ninety-one percent of Hispanics surveyed in this study stated that they would like financial institutions to offer products with them in mind, and 85% want more information about savings and investing their money.

Latin American immigrants can gain economic benefits by using bank-offered remittances products. As shown in Table 1, the cost of bank-offered remittance products, on average, to Mexico are less than those charged by other providers.

Table 1.
Charges for the transfer of remittances to Mexico

Channels used to transmit	***Charges (fee and exchange rate*)**
FedAch International	$ 5.00
Debit card withdrawal at ATM	$ 6.06
U.S.-based bank remittance with pickup at Mexican Bank	$15.70
Cash to cash transfers	$19.03
Traditional wire transfers	$39.75

Source for data on debit card withdrawal through traditional wire transfers: Manuel Orozco, Changes in Atmosphere? Increase of Remittances, Price Decline and New Challenges", Inter-American Dialogue Research Series, March 2003.

How can U.S. Banks improve Latin American immigrants' access to the financial system?

- Promote a financial education program that incorporates the ***Spanish*** language and is sensitive to the Latino culture, and offers participants the opportunity upon completion to open a low cost, no minimum balance checking or savings account with debit card access to pay bills and remit funds back to their countries of origin
- Partner with community-based organizations to educate the immigrant community about the U. S. banking system and insured deposits
- Promote employer-based education and outreach programs for the opening of direct deposit accounts and other banking services

- Sponsor community-based tax preparation services linking the earned income tax credit with the opening of a direct deposit account
- Hire bilingual and bicultural individuals from within the community
- Create within the institution a warm and people-friendly environment that cultivates a relational trust between the immigrant community and banking personnel
- Develop specialized loans to assist the immigrant establish a credit history
- Promote Individual Deposit Accounts
- Familiarize tellers, branch managers, loan officers and operational staff with specialized remittance service accounts, and the regulatory precepts regarding the opening of bank accounts

Why are remittances services of interest?

The Board of Governors of the Federal Reserve, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration (collectively, “the Federal Banking Agencies) agree that the sale of remittances can provide an important service in low-and moderate-income communities, and help financial institutions access a new, or expand an existing, consumer base that may not have used traditional banking services in the past.

The Federal banking agencies also agree that remittance services by wire transfer and through automated clearinghouse would receive consideration as a retail service under the ***Community Reinvestment Act (CRA)***; and may also qualify as a ***community development service*** if they serve to increase access to financial services by low-and moderate-income persons.

CRA requires federal banking agencies to evaluate how financial institutions meet the credit needs of their entire communities, including low-and moderate-income neighborhoods.

What are the regulatory requirements and banking concerns for opening new accounts?

By law, financial institutions are required to know their customers, the source of their funds, and report suspicious activity.

THE BANK SECRECY ACT (BSA)

The BSA was amended to include Anti-Money Laundering (AML) Regulations in the USA PATRIOT Act. The BSA requires all financial institutions to adopt a written internal compliance program, approved by the board of directors and noted as such in the board minutes; to designate a BSA compliance officer with day-to-day responsibility for all aspects of the compliance program, oversight of employee training, and compliance with all BSA regulations; develop and implement a Customer Information Program for

new accounts; provide for an on-going employee-training program; and an independent audit and testing of its compliance program.

THE USA PATRIOT ACT

The Act was established to detect, prevent, and prosecute anti-money laundering and terrorism; and requires under Section 326 that banks, saving association, credit unions and certain non-federally regulated banks ("bank") implement a written Customer Information Program ("CIP") appropriate for the size and type of business.

The CIP must include account-opening procedures that specify the identifying information that will be obtained from each customer, and must also include reasonable and practical risk-based procedures for verifying the identity of each customer.

Customer Information Required: The CIP must contain account-opening procedures detailing the identifying information it must obtain from each customer.[1] At a minimum, the bank must obtain the following basic information from the customer prior to opening the account[2]:

- Name
- Date of birth
- Address
- Identification number[3]

Customer Verification: The CIP must contain risk-based procedures for verifying the identity of the customer within a reasonable period of time after the account is opened, "using the identifying information obtained by the bank". A bank need **<u>not</u>** establish the accuracy of every element of identifying information obtained but it must verify enough information to form a reasonable belief that it knows the true identity of the customer.

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[1] When an individual opens a new account for an entity that is not a legal person or for another individual who lacks legal capacity, the identifying information for the individual opening the account should be obtained. By contrast, when an account is opened by an agent on behalf of another person, the bank must obtain the identifying information of the person on behalf of whom the account is being opened.

[2] For credit card customers, the bank may obtain identifying information from a third-party source prior to extending credit.

[3] An identification number for a U.S. citizen or legal resident is a taxpayer identification number (TIN) (or evidence of an application for one) or a social security number. For a ***non-U.S. resident it is one or more of the following: a TIN; a passport number and country of issuance; an alien identification card number***; ***<u>or</u> the number and country of issuance of any other unexpired government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard.***

Recordkeeping: At a minimum, the bank must retain the identifying information (name, address, date of birth for an individual, tax identification number (TIN), and any other information required by the CIP) obtained at account opening for a period of five years after the account is closed.

Comparison with government list: The CIP must include procedures for determining whether the customer appears on any federal government list of known or suspected terrorist or terrorist organizations.

What is the Legal Status of Latin American immigrants?

A MIF survey of 3,802 individuals in 37 states and the District of Columbia as shown that 24 percent of remitters are U.S. citizens; 39 percent are legal residents; and 32 percent are undocumented. (Bendixen & Associates)

Can banks serve undocumented individuals?

Per Section 326 of the USA PATRIOT Act regarding identification requirements for opening new accounts for non-residents, financial institutions may accept a passport, alien identification card, or other official unexpired government-issued document evidencing nationality or residence, and bearing a photograph or similar safeguard. This does not need to be a US-government issued document.

Is the acceptance of an unexpired foreign government issued document, such as the Matricula Consular card, a reliable source for establishing the identification of a non-US person?

The U.S. Department of the Treasury, mandated by Congress to oversee and monitor the implementation of the USA PATRIOT Act, reported to Congress that Section 326 of the Act does not discourage bank acceptance of the ***Matricula*** Consular card.

What is a Matricula Consular Card?

The Matricula card is issued by the Consulates General of Mexico as proof of Mexican citizenship and is valid for five years. The Matricula bears a serial number, picture of its owner; name, date, city and state of birth (in Mexico); current U.S. address; issue date; expiration date; and the location of the consulate that issued the card. In 2002, the Mexican consulate upgraded the Matricula card to a digital version to protect against and detect the counterfeit use of the document. To obtain a card, applicants must present an official birth certificate and official photo identification.

A passport, military service card, Mexican voter card, record of clearance from the police department, driver’s license, and expired Matricula card qualify as official photo identification.

Other Latin American Countries such as Guatemala and Honduras either have or are in the process of developing a National Identification Card to assist their immigrants in accessing the U.S. banking system.

What is the FDIC's position on the use of *Matricula* card?

FDIC's position on the use of Matricula card by financial institutions is consistent with The U.S. Department of the Treasury's policy. Essentially, accepting the ***Matricula*** card is a decision for banks to make. Moreover, the FDIC's position has been that, regardless of the type of identification card used, it is incumbent upon the bank to establish procedures relative to what forms of identification are acceptable and to articulate the terms and conditions under which those forms of identification will be honored.

Some financial institutions serving remitters with the intent to migrate the Latin American immigrant to traditional banking products have incorporated in their written ***CIP*** that under certain circumstances the combined acceptance of the Matricula card or comparable form of government issued photo ID and an Individual Taxpayer Identification Number (ITIN) would be appropriate documents for opening interest-bearing bank accounts.

On June 13, 2002, FDIC Chairman Donald E. Powell, before the National Association of Affordable Housing Lenders 2002 Industry Conference in New York, stated that "the ability of banks to now accept Individual Taxpayer Identification Numbers - or ITINs- issued by the Internal Revenue Service (IRS) and, in many places, the ***Matricula*** card issued by the Mexican consulate when opening new accounts, means that tapping into that market is much easier than it use to be".

What is an Individual Taxpayer Identification Number?

The IRS issues the ITIN to individuals required to file income taxes but who are not eligible for a Social Security Card. Increasingly, financial institutions are accepting these alternative ID forms. To date, over 70 banks with more than 2,900 branches in the U.S. have opened new bank accounts for Mexican workers using the ***Matricula*** and ***ITINs*.**

Bank efforts in this area have resulted in "about 400,000 new accounts", bringing upwards of approximately 40 million in cash for deposits. However, the accounts opened in the last three years represent only about "5" percent of the estimated eight million Hispanic immigrants who currently do not have bank accounts". (Orozco 2004)

What can be done to integrate more Latin American immigrants into the financial mainstream?

- Conduct demographic studies and focus group interviews to determine the needs of the community, and the best prospective locations for branch facilities

- Partner with community-based organizations to promote financial literacy, savings, homeownership, and investment building (See Appendix B for more information on this topic)
- Create and promote new banking products with remittance service as a feature to attract immigrants into the banking system
- Change the corporate short-term culture from that of accepting deposits and extending loans to one of investing time educating and empowering the Latin American immigrant's progression from non-traditional to traditional banking products
- Communicate in a consistent manner what type of ID forms are required to open banking accounts and apply for first-time home purchase loans
- Explore and implement new Information Technology developments to reduce the cost of remittance transfers and expand the distribution network
- Reduce costs and improve transparency on the prices for transmitting remittances. Total prices should be disclosed including all commissions and fees, foreign exchange rate applied, and execution time
- Familiarize senior and mid-level banking staff with the "Financial Life Cycle" of the Hispanic community

What is the financial life cycle of the Latino immigrant?

In the **FDIC Winter 2004** Outlook publication, the financial life cycle of Hispanics was defined as having four stages:

(1) Pre-banking services
(2) Basic banking services
(3) Advanced banking services
(4) Affluent banking services

Recent immigrants from Latin America, defined as those that have been in the U.S. less than ten years, are more likely to need financial services in one of the first two stages of the financial life cycle. As Latin American immigrants overcome their distrust of banks, fueled by memories of past bank failures in their home countries, and become less adverse to financial institutions they graduate to the higher stages of the financial life cycle.

***Stage 1, Pre-Banking Services:* "** First-generation (foreign-born) Hispanics are typically at the pre-banking services stage, often because they have had very few dealings with, or little confidence in, banks in their native countries". 4 It should be noted that in some Latin American countries only the affluent had checking and saving accounts. Consequently, a majority of first-generation immigrants have limited or no knowledge of checking, savings and investment accounts, financial planning, budgeting, credit management and home buying. In addition, past histories of bank failures in Latin America may have made immigrants wary of entering what they perceive as unstable or "cold" banks.

As a result of their limited experience with financial institutions and basic financial products and services, the availability of financial education in ***Spanish*** and ***English*** is a very important need for this segment of the Hispanic population. Financial institutions and regulatory agencies are already seeing economic and social development value changes by conducting financial education classes either as a stand-alone classroom curriculum or as part of an English as Second Language program.

These financial education classes are most often conducted in collaboration with community-based organizations have resulted in increased awareness of financial products and remittance services, increased access to financial institutions, the opening of new transaction accounts and an increase in first-time residential mortgage applications.

Stage 2, Entry-Level Basic Banking Services: At this level, Hispanics are not only seeking remittance services, but banking products that also meet their immediate needs and facilitate establishment of a long-term banking relationship. This group is likely to be first-generation Hispanics in need of a checking and/or savings account to conduct their daily affairs.

Stage 3, Advanced Banking Service: "This group consists of second-and third-generation Hispanics looking beyond basic banking services and focusing more on mortgage, personal and business lending products". 5

Stage 4, Affluent Banking Services: As Hispanics become better educated, accumulate assets and thereby create wealth, they will require higher margin banking products and services. "As their purchasing power continues to increase, they will have a significant need for credit cards, residential mortgages, consumer loans, and other banking products". 6 These
products may include certificates of deposit, money market accounts, individual retirement accounts, mutual funds, annuities, trust accounts, and life insurance.

4-6: Jeffrey A. Ayers, Senior Analyst, Stephen L. Kiser and Alan R. Sanchez, Regional Economists "Banks Are Still Sizing Up Opportunities in the Growing Hispanic Market

Financial Institutions with a successful record of serving Latin American Immigrants

It is useful to examine the business models of several commercial banks, credit unions, and community banks that have been successful in serving Latino populations in the United States. These examples prove that servicing this community can be extremely profitable while also meeting all federal and state regulatory requirements.

El Banco de Nuestra Comunidad (El Banco) a subdivision of SunTrust Banks, Inc., headquartered in Atlanta, Georgia.

SunTrust is one of the nation's largest commercial banking organizations with an extensive distribution network primarily in Florida, Georgia, Maryland, North Carolina, South Carolina, Tennessee, Virginia, and the District of Columbia.

El Banco services the Latin American Community by providing non-traditional and traditional banking products in a Latin atmosphere. That is to say that all its employees are of Latino descent, speak ***Spanish***, and hired from within the community. This community tie cannot be over-emphasized. All Spanish-speakers are not alike; in a majority Mexican community the tellers should be Spanish speakers of Mexican descent to build maximum trust within the community. In addition, in many cases it is better to hire local figures prominent in the community and to train them in bank teller skills rather than bringing in workers with pre-exisiting teller skills from outside the community. Finally, El Banco has a full-time community liaison who spends time building trust with local Latin populations, up to visiting bank members in the hospital when they are sick.

El Banco has successfully integrated the retail store concept into a banking space. As a customer of the bank you can cash checks, purchase money orders, wire money back home via Western Union, purchase pre-paid phone cards, pay utilities bills, surf the net, open a bank account, apply for an Individual Taxpayer Identification Number, and secure an installment and first-time home purchase loan all under the same roof, in a family friendly environment. In addition, branches offer photo ID cards to members and sell El Banco branded T-shirts to make bank customers feel a part of a branch "family."

El Banco provides point-of-sale financial education, either when the customer is opening a banking account or when he visits a teller to cash a check; in this case, the teller will educate the customer on the benefits of opening a saving account and/or checking account that allows them to write and cash checks at no cost and helps them accumulate assets and establish credit.

El Banco protects its customers from overdrafting their account. Rather than charge exorbitant overdraft fees, they instead notify the customer in advance of an overdraft situation. This is accomplished using a software system to verify funds before cashing a check

El Banco has a proprietary software system for all non-banking transactions that monitors and records individual transactions over $3,000 dollars and single and aggregate transactions equal to or in excess of $10,000 dollars for internal audit purposes and compliance with the Bank Secrecy Act. This system also tracks and analyzes by customer name, identification number, payee and date, the dollar amount and volume of checks cashed.

El Banco also performs it own demographic surveys and focus group interviews to identify the needs of the community and prospective branch locations. It has 12 branches throughout the Atlanta area opened at times convenient for shift-laborers and those with long hours **6** days a week from ***10:00 am to 8:00 pm, and on Sunday from 2:00 pm to 5:00 pm.*** The branches are located predominantly in large Hispanic communities and strip centers catering to the needs of the Latin American immigrant. For example, branches are located next to butchers and bodegas providing Latin-oriented services.

El Banco has provided technical assistance and brand licensing to two banks that have recently opened branches to services the Latino Community. For example, Banco de La Gente, a subdivision of People Bancorp of North Carolina, Inc., adopted their business model and opened their first Latino branch in August 2004 in Charlotte, North Carolina and plans to open a second branch in the first quarter of 2005. First Security Group also adopted their model and opened two branches in Dalton, Georgia in the fourth quarter of 2004. – Primer Banco Seguro.

The Latino Community Credit Union ("La Cooperativa") Durham, North Carolina, is a community-based and member-owned non-profit institution that provides financial services to immigrants in the United States less than ten years, with its main office in Durham, and branch locations in Greensboro, Fayetteville, Charlotte and Raleigh.

La Cooperativa was chartered in February 2000 and opened its doors on June 26, 2000, with the goal of attaining 500 members in their first year of operation. La Cooperativa exceeded that goal with a first-year membership of 2,500. Today, as a result of their financial education classes, cultural sensitivity, and partnership with community-based organizations the credit union has more than 27,000 members of diverse ethnic backgrounds, with each member having on average at least 1 to 3 savings account per family unit. Prior to the opening of the credit union, 75 percent of the community's Latin American immigrant had no savings account or established credit history.

As of September 30, 2004, La Cooperativa's financial statement reflects a net worth of $1.8MM and total assets of $17.2MM, with assets primarily consisting of cash $5.2 MM and loans $10.6MM. Within the loan category, La Cooperativa has first-time home purchases aggregating $3.8MM, with zero delinquencies.

La Cooperativa's business model is completely community-based, providing services *for* the community *by* the community. All tellers and staff are local and members of the target customer population. La Cooperativa is also proactive in financial education,

creating their own curriculum based on Latin American schooling methods and English-as-a-second-language (ESL) coursework.

As evidenced by the success in opening accounts and providing loans to first-time homebuyers, La Cooperativa's customers have effectively applied the teaching objectives of the budgeting and credit management modules learned while attending La Cooperativa's financial education classes.

In 2004, Bank of America opened more than one million checking accounts for Hispanic customers and is the first major commercial bank in the U.S. to eliminate remittance and foreign exchange fees to Mexico from Chicago through its SafeSend service as part of a national rollout to be completed by year-end 2005.

Nationwide, customers who use SafeSend with a Bank of America checking account will not have to pay the usual three percent foreign exchange rate on transfers. By year-end, remittance fees will be completely eliminated nationwide.

SafeSend is a low-cost alternative to send money to Mexico when compared to money orders or traditional wire transfers. Customers can send money using the Internet or the phone anytime – 24 hours a day, 7 days a week. Customers have the option of either having the SafeSend Transfer Card sent to them or mailed to a friend or family member directly.

Once the friend or family member has the SafeSend Transfer Card, the customer can add money to the card electronically and the money is available in Mexico in less than six minutes. The SafeSend Transfer card can be used to withdraw money at 26,000 Plus or RED ATMs in Mexico, and to purchase goods or services wherever the Visa card is accepted.

In 2005, Bank of America plans to build 50 percent of its new stores in areas that will serve Hispanics neighborhoods, and recruit bilingual associates to assist in servicing the financial needs of the community. The hope is that the Safesend program will draw Latin American immigrants into the bank through remittance services so that branches can then cross-sell other services to customers.

In 2003, Citibank announced real time domestic and international account-to-account fund transfers through Citibank Global Transfers. This service affords Mexican immigrants the ability to send money home to their families or friends at a fixed rate of $5 dollars.

The funds are debited from the customer's account and credited to recipient's account in Banamaex *(*National Bank of Mexico) immediately. Citibank accepts the ***Matricua*** card as an alternative identification form to open bank accounts, and offers various types of banking accounts with no minimum deposit balances and low monthly service charges.

Wells Fargo offers international account-to-account fund transfers through its InterCuenta Express Account at a rate of $8 for transfer amounts up to as much as $3,000 per day. There are no minimum balance requirements, no monthly service charge, and no opening deposit requirement. The customer receives an ATM card to make deposits into the account. Funds deposited in the account by the remittance sender are transferred to the recipient's account at one of Wells Fargo's partner banks: BBVA Bancomer, Banorte or HSBC Mexico. The recipient can access the funds at any branch or ATM of the partner banks.

Appendix-A

Alternative Business Model

Hispanic entrepreneurs in South Dallas, Texas; Denver, Colorado; New York; Washington, D.C., and other predominately Hispanic marketplaces are starting their own community banks. Hispanic entrepreneurs are taking steps to bring banking service to the communities in which they reside. Their focus is on providing financial services that meet the financial needs of all segments of the Hispanic community inclusive of the low-to-moderate income individuals, small business owners, and affluent Hispanic professionals.

Nationwide there are currently seven Hispanic organizations soliciting investors and Federal regulatory approval for establishing Hispanic-owned financial institutions. Per the FDIC, there are 173 minority-owned financial institutions, 36 or 21 percent are Hispanic owned.

Appendix B
Financial Education

   

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