

# EBT Interview:

## EFT '99: A MEANS TO EMPOWER THE POOR IN ASSET BUILDING

Michael A. Stegman

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*From June 1993 through June 1997, he served in the Clinton Administration as assistant secretary for policy development and research at the U.S. Department of Housing and Urban Development (HUD). At HUD, Prof. Stegman headed the department's urban policy initiatives; oversaw preparation of the administration's national urban policy reports; and founded HUD's Office of University Partnerships, which supports more than sixty college and university community-building collaboratives.*

*Prof. Stegman received his B.A. degree from Brooklyn College, City University of New York, and holds M.A. and Ph.D. degrees in city planning from the University of Pennsylvania.*

*In this interview he discusses the potential impact of "EFT '99," the shorthand term for the federal initiative to replace virtually all federal payments now made by paper checks with various Electronic Funds Transfer (EFT) methods, including the Electronic Transfer Accounts (ETAs) that will be designed to support "unbanked" recipients of federal payments like Social Security Annuities.*

**It is generally accepted that EFT and EBT are more efficient ways for federal and state government to move money into the hands of individuals who are receiving entitlements and benefits. Beyond these quantifiable reasons for EBT and EFT, what other advantages do you see in introducing these payment methods?**

If all of the pieces came together, EFT could do for the delivery of affordable financial services to low-income people in low-income communities essentially what the Community Reinvestment Act (CRA) has done for providing affordable mortgage credit in these same under-served communities. The CRA has proven to the financial community that this under-served market can be served profitably. We are at the front end of that same kind of discovery process for financial services. It's the EFT mandates that are forcing us to look at how technology can be used to serve this community more effectively.

**What problems do you see in implementing EFT '99?**

It requires training people who have never used debit cards on how to access funds, and how to use an ATM card or debit card. However, the foundation of EFT and EBT is a citizenry more informed and educated about financial management and about the whole range of costs of dealing inside and outside the financial mainstream. There are also accessibility issues to consider—what to do about the areas without bank branches or ATMs. This is one of the reasons why the EFT rule lets the benefit recipients themselves determine whether to sign up for direct deposit or continue receiving their benefits by check. So there are enormous public education and access challenges associated with this new technology, and with bringing several million individuals outside the financial system into that system. But the benefits of doing so will be substantial—for them and for the country.

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**Why do you think it is so important to link EBT/EFT with asset-building initiatives? What is your larger vision for these programs?**

We have a very serious problem with under-saving in this country. As Senator Bob Kerrey has said, "in a global economy, your economic health and security is measured by what you own, in addition to what you earn." About thirty percent of American households have no financial assets, and about half of all children in the United States are growing up in families that have no financial assets. Along racial lines, the difference in asset building between white Americans and African Americans is far, far greater than the difference in their incomes. Under-saving for retirement investment is another big problem. By bringing millions of "unbanked" people into the financial mainstream, EFT will facilitate savings, but it does nothing to encourage or help people to save. We have a golden opportunity to expand EFT's impact by linking it with a national economic literacy campaign and a new savings initiative targeted at the working families of America who don't benefit from existing savings incentives.

This country has a long, proud tradition of helping and encouraging middle- and upper-income Americans to build assets, most recently with Roth IRAs and with other kinds of tax-advantaged savings systems. These systems are not appropriate for the kinds of working families—the working poor and lower-income people who will be most affected by EFT—who can't take advantage of these tax breaks. Therefore, we need to create different kinds of incentives to encourage people who have not been part of this system of asset building to begin saving. Moreover, if we were able to connect the electronic benefits program that creates bank accounts for people with a savings program of any kind, this would help the economics of EFT by providing a pool of cheap deposits for the financial institution to invest and earn interest upon. Generating a little more float should help keep down the costs of the ETAs for benefit recipients, which have to be fee-based.

**Since the people at which this is aimed are poor and lower-income individuals, where is the initial money coming from that they're to save and use to build their assets?**

The issue of beginning to save a little on a regular basis as part of a longer term program is very important. There is a growing body of literature that suggests that not only do low-income people have the discipline to save, but also that they respond just as higher-income people do, although at lower levels of magnitude, to incentives to save. For example, one of the largest savings incentive programs in the country is the federal government's Thrift Savings Plan, in which the federal government matches on a dollar-for-dollar basis the first three percent of savings that federal employees put away, then matches the savings on a declining scale after that. Forty-four percent of covered federal employees who earn under \$20,000 a year participate in the Thrift program. This is twenty times higher than the rate of low-income American workers who participate in IRAs where there are no direct matches and direct incentives and where the money isn't deducted from a paycheck.

This data, as well as anecdotal evidence from some of the federal pilot programs on direct benefit payment, suggest that low-income people can and will, under appropriate conditions and incentives, begin to put some money away. I would like to see the federal government match

the savings deposits of low-income people. There are various ways of accomplishing that.

**In the current environment of welfare reform and a relatively healthy economy, is it more difficult to gain the attention of government policy makers on initiatives to help the poor, such as the Individual Development Account (IDA)?**

I don't think so. For one thing, the welfare reform law removed all kinds of disincentives to save, and several states are already funding their own IDA programs—Indiana and Pennsylvania have invested more than \$1 million each in IDA pilots, and my own state of North Carolina has three IDA demonstrations underway. More importantly, Congress enacted a national IDA pilot that the president signed into law on October 27. The Assets for Independence Act authorizes the Department of Health and Human Services to conduct a five-year \$125 million national IDA demonstration, and appropriated \$10 million for initial start-up costs.

I was asked by Senator Joseph Lieberman of Connecticut to prepare legislation called the Savings for Working Families Act, which he is preparing to introduce in the 106th Congress. It would provide tax credits against the corporate income taxes of any federally regulated financial institution that sponsors and provides matching funds for IDA programs. It is during a period of strong economic times that these kinds of programs have the best chance of passage, and national work- and asset-based incentive programs are exactly what policy makers are looking for.

**What role would EBT and EFT play in making IDAs more widely available?**

The two programs complement each other. By bringing unbanked families into the financial mainstream, EFT/EBT enables benefit recipients to save, while the IDA gives them the incentive to start saving for the first time in their lives. Moreover, both require more economically literate populations to succeed; so Treasury's EFT economic literacy campaign can serve double duty—helping people understand the benefits of EFT, and motivating them to enroll in an IDA program.

The connection with EFT and EBT also depends on the further evolution of the U.S. Treasury Department's ETAs. But most important is the evolution of the EBT card into one that provides savings options for families. The EBT card is a debit card. While it uses the banking system's networks of ATMs in addition to the point-of-sale systems, it does not necessarily connect anybody with a bank account, or a means of saving.

We should note that several states have begun to put their cash assistance onto EBT cards, but at the same time offer the recipient the option of receiving cash assistance through direct deposit. More effort should be made into not only delivering cash benefits electronically, but also connecting people who are moving from welfare to work into the financial banking system. Potentially, the EBT debit card provides the first contact with a future banking customer whose income will rise over time.

**Since EBT deals largely with the distribution of food stamp benefits, how do you see EBT fitting into your vision of asset building?**

Recently, I was at a meeting with a number of people that the

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Treasury Department called on to deal with recipients who don't have bank accounts. A representative of the Department of Agriculture mentioned that a number of states have actually applied to the Department of Agriculture for waivers under the EBT food stamp delivery system to allow the accumulation of unused balances, that is, a mini-savings account, to remain available to families. Under the current policies, it's hard to do that; those accounts get swept. Even in the narrowest strictures of EBT delivery of food stamps, there seems to be increasing interest as people are brought into this electronic system on focusing in a more disciplined way on budgeting and allocating resources and perhaps even beginning to save.

Moreover, 36 states and the District of Columbia have decided to take advantage of their EBT platform by also converting their emergency cash assistance programs to electronic delivery. So we are now changing the way that millions of families receive their income, and EBT presents new possibilities for saving.

As the public assistance departments begin to think more of the importance of people who enter the world of work having a bank account, of not operating solely in a cash economy, they are beginning to develop financial literacy classes and opportunities for families to actually open bank accounts and establish a more formal system of cash management.

**As financial institutions become more involved in making IDAs available, do you see the federal and state governments increasingly sending payments to a direct deposit account or IDA rather than to an EBT card?**

There are several states, including Missouri, Massachusetts and Texas, that are actually doing direct deposit now, and others are considering it. Missouri gives the choice to a family of receiving their cash assistance through the EBT card or of opening an account--a savings account or a checking account--at a local bank and signing up for direct deposit as most federal employees do and many millions of private employees do. They would be earning interest; they would not have ATM fees if they make withdrawals from their own bank's ATM system. They would, for the first time, really be eligible as part of that bank's customer base to receive a wide range of services.

Welfare benefits have declined 30 percent over the last two to three years. That affects the number of people who are receiving food stamps and cash assistance through the EBT card, which in turn affects the economics of the contracts that EBT vendors have with the states. As the customer base declines, I think it's in everybody's interest to figure out how banks can continue to meet the financial services needs of this population, earn fees, and profit from it.

**The U.S. Department of the Treasury has indicated that it will "liberally apply" waiver provisions in implementing EFT '99. What are the implications of this decision?**

Both the law and the proposed regulations that Treasury issued to implement the law stated in no uncertain terms that the millions of current benefit recipients who don't have bank accounts and who don't sign up for direct deposit on their own would be assigned to ETAs. Well, that really was not feasible. There are millions of recipients who for one reason or another don't have bank accounts. For example, they are suspicious of banks, don't think they really need the services of banks, think

banks don't really welcome them, or have various barriers such as language, cultural, or physical disabilities. So Treasury learned that to assign bank accounts to eight to ten million unbanked recipients in a year or two and make EFT '99 work as the law suggested would be an enormous challenge. As Treasury began to work more closely with the banking industry, with consumer interests and with community organizations, it wisely, but with significant implications, decided first of all to slow this process down. Secondly, Treasury realized it couldn't just mandate this to happen and demand that the banking industry create these accounts. Treasury also realized that individuals who might be harmed by a rapid transition from paper checks to electronic delivery should be exempted for at least some period of time from this mandate.

As the process unfolded, Treasury for a variety of reasons ended up with, in my own view, too liberal of a policy. Essentially, Treasury has converted EFT '99 from a mandatory program to a voluntary one. The final regulation that was published on September 25 provides any benefit recipient who feels that the conversion from a paper check to an electronic delivery system would prove to be a hardship can simply exempt themselves out of the requirement. This has many implications for the kind of economies-of-scale for Citibank and other banks that were thinking about providing these accounts. For example, when the federal government mandates an electronic delivery program, there's a market of several million accounts. When it provides a very liberal waiver policy and allows anybody to opt out, financial institutions lose the economies-of-scale and the guaranteed, aggregate market for these new accounts. That's the bad news.

The good news is that now financial institutions have to provide a service to these unbanked recipients. They now have to treat them as customers. They have to go after the business. Within the next few weeks, Treasury will issue a notice in the Federal Register proposing the features of ETAs, including a fee structure and a set of services. This proposal will solicit comments from the financial industry and from consumers to determine what's the most appropriate and affordable mix of services that this part of the population is willing to pay for and receive.

What's even more interesting is that the new account services and products that come out of EFT '99 will not be limited to unbanked federal benefit recipients. What we're looking at here is the challenge of how to use technology to meet the needs of a portion of the population that the industry hasn't been meeting and hasn't been able to meet, in their view profitably, in the past. So that's the good news of the liberal waiver policy. We'll let the market and competition determine that mix.

**In your opinion, how could offering banking services to the poor be made economically attractive to financial institutions?**

I think we're underestimating low-income and working people and their ability to move up the income ladder and to become, over time, profitable customers to the financial community. We now have some inner-city banks that have made arrangements with third parties, such as American Express, to offer various kinds of investment vehicles to under-served inner-city residents who until now have not invested in the stock market or bought mutual funds and certificates of deposit. We're finding that there are creative opportunities for the industry to serve these communities profitably.

We also know that there are reasons why many people opt not to go to banks. What we want to do is understand those reasons and see if there are ways of overcoming some of the cultural and financial barriers. There's no question that in many cases the fees and the charges that people are paying today are higher than they are in mainstream financial institutions. But the unbanked are able to get their money immediately at a currency exchange. When recipients have a government benefit check, they shouldn't have to wait three days for the check to clear. So there are many practices and policies that institutions can change today, if they wanted to, that would make people feel more welcome. There are also partnerships that the banks are creating today that might make services more accessible.

Adding a saving incentive for working people would also help increase the float for financial institutions that want to serve this new market with an ETA product. Treasury's proposed EFT rule limited ETA accounts to unbanked benefit recipients, but the final rule permits non-recipients and anybody else who finds it attractive to sign up for a bank's ETA account. This considerably broadens the market for basic banking products among a potentially higher income customer base that is not currently part of the banking system. The ETA is the drawing card.

### **What would be your ideal vision for banking and financial services to the poor and lower-income individuals ten years from now?**

There is no question that technology is becoming increasingly important in the delivery of financial and banking services. Clearly, it is absolutely of the most importance, not just for the narrower issues that we're talking about, that there be no digital divide, that there be no isolation of low-income and inner-city communities from access to and full use of this technology. So I hope that ten years from now low-income people have the ability to secure banking and financial services using the technology of the day and that the technology is available and abundant in communities across the country.

I also hope that ten years from now basic financial literacy will be part of the elementary and high school curricula so that young people everywhere will learn more about the importance of credit, budgeting, and financial management, and the power of compound interest at a young age. I also envision more of our community development programs emphasizing asset-building and wealth accumulation than is presently the case, more savings for downpayment IDAs, community

development credit unions in public housing and empowerment zones—with technology-driven partnerships of financial institutions with community-based organizations providing access to financial services at the neighborhood level.

Finally, I hope that ten years from now the financial industry will have discovered a new customer base and that the technology and the delivery systems and the partnerships that the industry has forged in the communities will demonstrate that they can earn good returns by serving this community. EFT and EBT have given us an opportunity to think more about ways that we can create new markets and serve people in these communities.

### **What programs, if any, are in place now that give you hope for your vision of the future?**

One of the positive aspects of EBT and this whole electronic delivery mandate is that the federal government is putting an emphasis on and research into the creation of economic literacy curricula and materials, and helping to disseminate them across the country. Also, a number of financial institutions have joined together to support EBT educational materials and newsletters to help community-based groups and others who are trying to bring those services into their communities. In some cases, banks are working with community colleges and in conjunction with extension services to provide economic literacy curricula and services in rural and smaller communities. In my view, improving economic literacy and access to the financial services mainstream should become the foundation of all our community development policies, and EBT is moving us in that direction. Also, because of EFT, Treasury is investing in the kind of market research targeted at unbanked recipients that the financial industry normally funds for its customer base. We're going to learn in the next twelve-to-eighteen months more about this under-served population—why it stays outside the system, what products and services it needs and is willing to pay for, and how much it is willing to pay for basic financial services. Finally, while it is still too early to say this with any degree of certainty, I believe there is a great deal of innovative thinking going on in the financial industry about how to serve the EBT population at a profit. So, along with consumer development, there is a lot of market development work going on, and the results of these complementary efforts will be good for communities and for the financial industry. I think all of this is very positive—and it was stimulated by the EFT '99 mandate.

