

DOUBLE DUTY:

Payments Cards as a Doorway to Greater Financial Health

CFSI Center for
Financial Services Innovation



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DOUBLE DUTY:

Payments Cards as a Doorway to Greater Financial Health

The same systems that made electronic payment possible can also help people understand and plan their financial lives.

Executive Summary

Electronic payments are growing by leaps and bounds, overtaking paper as preferred payment mechanisms. Governments at all levels have embraced this change, often not just encouraging a move from paper checks but even requiring it. Electronic payments have advantages for all parties. Governments lower the cost of distribut-

ing benefits. The payments industry realizes further economies of scale and greater revenue from wider use of the payments network. For individuals, electronic payments lower the incidence of lost checks and potentially improve efficiency and convenience.

Electronic payments 1.0 is a success story. Electronic payments spare government the cost of writing and distributing checks while delivering funds to recipients more safely and reliably. But electronic payment methods can do more—and defining “more” will be the next chapter in the story.

By far, most recurring government electronic payments, such as Social Security and unemployment benefits, are made via direct deposit. However, direct deposit does not work for people without bank accounts. Payment cards—prepaid debit cards with a 16-digit number, magnetic strip, and network logo—are an electronic option that does not need a bank account. When state and federal governments require recipients to receive their benefits electronically, those who do not choose direct

deposit receive the default choice instead—a prepaid debit card. And this is where the next chapter begins.

Electronic government payments can serve as an entry into lower-cost, broader-function payment tools that support recipients' financial lives. They can offer increased choice among financial services and a range of financial service functions. Above all, they have the potential to help people improve their financial health and capability, whether through access to more information or a transition to greater use of higher-quality, more effective services. The same systems that made electronic payment possible can also help people understand and plan their financial lives.

Government payers can model the best possible payment delivery vehicles. In selecting default payment mechanisms, they can ensure that government payees use high-quality products, considering functionality, low fees, and consumer protections.

Electronic payments can supply all these things, but will they? This report lays out ways to go beyond getting government payments into the hands of recipients, ultimately strengthening household financial security. Three broad strategies are key: increased choice, expanded functionality, and improved financial capability.

Increased Choice

Those who opt for direct deposit can choose among all the accounts offered by banks and other financial institutions. Those who receive a prepaid card as the default option have no choice—they get the card that results from a government contract with a designated card provider. This product has the features established in the contract between the government and the financial institution.

There is an alternative to selecting a single winning bidder for a government contract. Instead, the government could specify a set of features and allow multiple providers to

build products to meet—or exceed—those specifications. Financial institutions could provide a range of appropriate prepaid products, or state and federal governments could work with financial institutions to design products and features; and recipients could then choose among products and providers. This choice process allows for some standardization by requiring key features, but also allows for some customization and segmentation of features.

Expanded Functionality

Government payers could include functionality such as reloadability, portability, fund transfers, or savings buckets to government-delivered payment vehicles to turn them into fuller-featured financial accounts.

Direct deposit puts government payments into a bank account, where additional funds can be added from other sources. In the language of the prepaid card environment, these are “reloadable” accounts. In contrast, a government payment recipient who opts for a prepaid debit card generally does not gain access to a fully reloadable account to which funds can be added from any source. For example, the Direct Express card issued on behalf of the federal government is reloadable only with funds from Social Security and other recurring federal payment programs.

It is possible to expand the functions of a prepaid card by adding a subaccount for additional funds—called a “dual purse” in the industry—to bridge the gap between close and full functionality. Reloadable dual-purse cards may be the shortest route to being banked for many unbanked government payment recipients. One card can serve as a way to access two accounts, one for payments from the government program that issued the card, and the other for non-government payments.

Improved Financial Capability

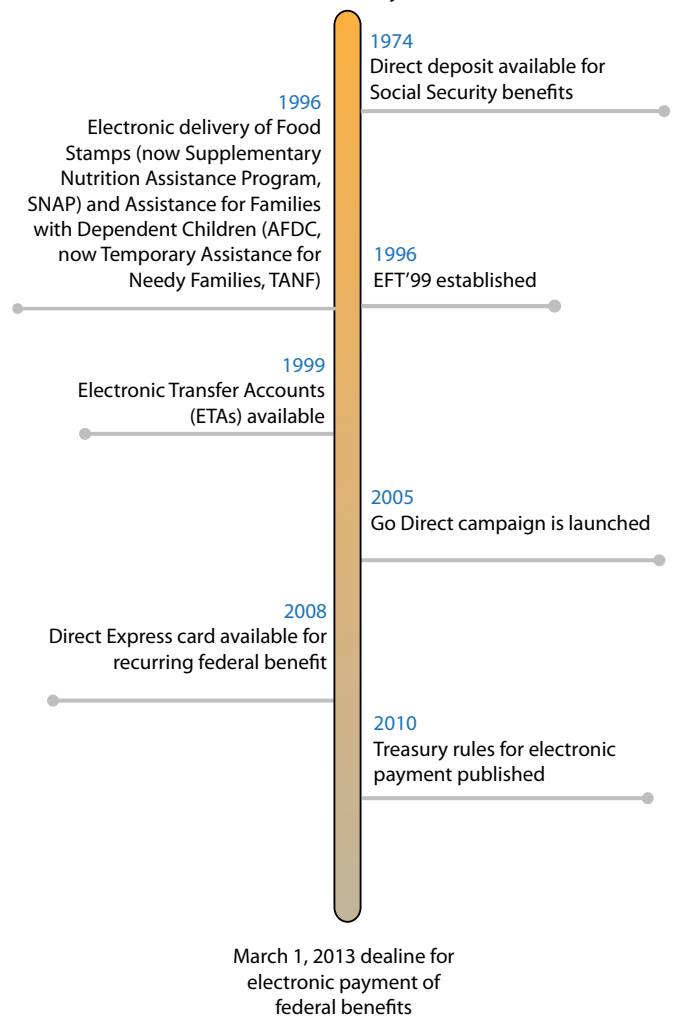
We have all experienced the declining cost of information technology. Search engines have put a seemingly infinite number of facts at our fingertips. The cost of gathering and distributing information that supports better financial decisions is also falling. For example, many bank accounts and prepaid cards offer low-balance alerts—when a transaction reduces an account below some predetermined limit, a text message alerts the cardholder, enabling the person to make an informed decision on future spending.

We are just beginning to learn how technology can increase financial capability and help people improve their financial health.¹ It can be used to create decision aids and support systems that enable consumers not only to accomplish financial transactions but also to achieve financial goals. These can be simple goals like having enough money to last through the month, or longer-term goals like saving for an education or retirement.

Conclusion

Because of tremendous variation in how the 50 states, the federal government, and other countries are tackling these issues, we have an opportunity to proceed carefully and deliberately, learning from multiple experiences. This paper describes where electronic government payments stand today and into the future. It identifies how governments, participants in financial systems, and allies of payment recipients can help fulfill the promise of electronic payments. It also identifies further areas for study and makes a few initial suggestions for what electronic payments 2.0 for government programs could include.

Electronic Payments



¹ CFSI defines financial capability as a set of consumer behaviors that lead to tangible improvements in financial health. It is measured through whether or not individuals can cover monthly expenses with income, track their spending, plan ahead and save for the future, effectively select and manage financial products and services, and gain and exercise financial knowledge. According to CFSI research, effective financial capability interventions must be relevant, timely, actionable and ongoing in order to have impact.

INTRODUCTION

The Opportunity

Thanks to digital technology, many tasks that once required paper now use electronic formats. Checks are nearly a thing of the past, debit cards have surpassed both checks and credit cards as the most common payment method, and the use of prepaid cards is growing at double-digit rates.² Electronic payments make up three-fourths of all non-cash payments by number and more than half by value.³ The greater efficiency and convenience of electronic formats have driven this transformation.

Government payment cards can be viewed as potential bank accounts waiting to be opened.

For most consumers, electronic payments mean direct deposit of pay or benefits into a checking or savings account in a bank. For those who lack bank accounts, payment cards have become an alternative entry point into the digital world. Payment cards have solved the problem of how to make electronic payments to people without bank accounts, enabling government agencies to reduce costs. But cost reduction is only one aspect of electronic payments; other aspects—safety, convenience, and the opportunity for consumers to improve their financial health and capability—are equally important.

And the opportunity is sizable. For example, in January 2013, more than 62 million consumers received Social Security or Supplemental Security Income (SSI) benefits totaling more than \$70 billion.⁴ Of these, 95 percent of the Social Security and 86 percent of the SSI payments were made electronically to bank accounts or via Direct Express, a prepaid card for federal benefit recipients. Supplemental Nutrition Assistance Program (SNAP) benefits, formerly known as food stamps, deliver more than \$74.6 billion annually to nearly 22.3 million households via monthly loads to payment cards.⁵ Overall, more than a quarter of all Americans live in a household that receives a regular, usually monthly, government payment or benefit.

² See “Consumers’ Use of Prepaid Cards: A Transaction-Based Analysis,” a publication of the Federal Reserve Bank of Philadelphia and CFSI (August 2012), at www.philadelphiafed.org/consumer-credit-and-payments/payment-cards-center/publications/discussion-papers/2012/D-2012-August-Prepaid.pdf.

³ See the “2010 Federal Reserve Payments Study” at www.frb-services.org/files/communications/pdf/press/2010_payments_study.pdf.

⁴ See Social Security’s Monthly Statistical Snapshot at http://www.socialsecurity.gov/policy/docs/quickfacts/stat_snapshot/index.html.

⁵ USDA Supplemental Nutrition Assistance Program FY 2012 statistics at <http://www.fns.usda.gov/pd/34SNAPmonthly.htm>.

Many state and federal benefit recipients lack bank accounts. According to the 2011 FDIC National Survey of Unbanked and Underbanked Households, 8.2 percent of households (about 17 million adults) are unbanked, and an additional 20.1 percent (about 51 million adults) are underbanked—that is, they may have a bank account but also rely on alternative financial systems, such as check cashers, money orders, and payday loans.⁶ The same survey reveals that among those who report having a prepaid card, 87 percent are unbanked. Thus, these prepaid cards may be the only part of their financial lives that involves the electronic payment system.

To be part of the financial mainstream, individuals need the capacity that usually comes with a bank account—a safe place to deposit and store money and ways to make payments and save. Payment cards can provide these capacities. Payment cards and related technologies for government payments could give unbanked recipients broader access to financial services. And extending the reach of government payment card programs could allow consumers to obtain additional services at a relatively low cost (see Appendix A, Prepaid Card Primer).

Indeed, government payment cards can be viewed as potential bank accounts waiting to be opened. Government payments can serve as an entry into lower-cost, broader-function payment tools that enhance recipients' financial lives. These payments can increase choices among financial services and provide a range of financial service functions. Their greatest promise lies in their potential to help people achieve a higher level of financial health, whether through access to more information or a transition to increased use of higher-quality, more effective financial services. The same systems that made electronic payment possible can also provide tools that help people understand and plan their financial lives.

⁶ "2011 FDIC National Survey of Unbanked Households," www.fdic.gov/householdsurvey/

THE GROWTH OF GOVERNMENT ELECTRONIC PAYMENTS

As of March 2013, the federal government's official policy is that paper checks are no longer available for programs that provide recurring payments.

Federal Payments

The federal government first used electronic payments to deposit benefits directly into bank accounts. Social Security beneficiaries have had the direct deposit option since 1974; by the early 1990s, more than half opted for direct deposit.

In the early 1990s, pilot programs were established for electronic delivery of food stamp benefits and certain cash programs such as Aid to Families with Dependent

Children (AFDC, now TANF, Temporary Assistance for Needy Families). Recipients used electronic benefit transfer cards (EBT) to obtain food stamp benefits at point-of-sale (POS) terminals in grocery stores and cash benefits at ATMs and POS terminals. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 established electronic delivery for food stamps (now SNAP) and for TANF payments.

Congress took electronic delivery of federal payments beyond the realm of welfare via the Debt Collection Improvement Act of 1996. A portion of the bill that became known as "EFT '99" declared that by January 2, 1999, the Department of the Treasury would have to use direct deposit for all recurring federal benefits, such as payments for Social Security, SSI, veterans benefits, and railroad retirement (nonrecurring payments can also be delivered electronically). The law was intended to save tax dollars by eliminating checks.

Treasury's final rules for implementing EFT '99 stopped short of mandating direct deposit. Instead, consumers could choose to receive their benefits through direct deposit; a check; or a special account, the Electronic Transfer Account (ETA). Consumers have not warmed up to the ETA; only about 167,000 ETAs were active in 2012.

Starting in the early 2000s, the federal government promoted direct deposit as simple, safe, and secure through its Go Direct campaign. The campaign also declared that direct deposit gives consumers convenience and control—they can use any account type offered by the financial institution of their choice.

But not every payment recipient has a bank account, and those who do not have bank accounts cannot

take advantage of direct deposit, no matter how much the government encourages it. The development of prepaid debit cards by the financial services industry created a way for people without bank accounts to migrate from paper checks to electronic payment.

Since June 2008, recipients of recurring federal payments such as Social Security have had the option of receiving their payment via the Direct Express card. Treasury contracted with Comerica Bank to provide the card nationwide. The card carries minimal fees (see Box 1, Direct Express Fees).

In 2010, Treasury issued rules requiring that recipients of recurring payments from the federal government receive their payments electronically. New benefits recipients are signed up for either direct deposit or a Direct Express

BOX 1. Direct Express Fees

Standard Free Services

SERVICE	FEE
■ Purchases at U.S. merchant locations	Free
■ Cash-back with purchase	Free
■ Automatic deposit notification**	Free
■ Automatic low balance notification**	Free
■ Web account access	Free
■ ATM balance inquiry	Free
■ ATM denial	Free
■ Customer service calls	Free
■ Cash from bank tellers	Free
■ Card replacement - one free per year	Free
■ ATM cash withdrawal in the U.S. including the District of Columbia, Guam, Puerto Rico, and U.S. Virgin Islands. ?Surcharge by ATM owner may apply	One free withdrawal with each deposit to your Direct Express Card Account*

* For each federal government deposit to your Card Account, Comerica Bank will waive the fee for one ATM cash withdrawal in the U.S. The fee waiver earned for that deposit expires on the last day of the following month in which the deposit was credited to the Card Account.

** The customer can request this service upon receiving the debit card.

The ONLY Fees You Can Be Charged

OPTIONAL SERVICE	FEE
■ ATM cash withdrawals after free transaction are use in U.S. including District of Columbia, Guam, Puerto Rico, and U.S. Virgin Islands. Surcharge by ATM owner may apply	\$0.90 each withdrawal (after free transactions are used)
■ Monthly paper statement mailed to you	\$0.75 ea. mo.
■ Funds transfer to a personal U.S. bank account	\$1.50 ea. time
■ Card replacement after on free year	\$4.00 after one (1) free ea. yr.
■ Expedited delivery of replacement card	\$13.50 ea. time card
■ ATM cash withdrawal outside of U.S. Surcharge by ATM owner may apply	\$3.00 plus 3% of amount withdrawn
■ Purchase at merchant location outside of U.S.	3% of purchase amount

card; existing benefit-check recipients were encouraged to sign up for the Direct Express card. As of January 2013, there were 2.7 million Direct Express cards in use, accounting for 3.6 percent of payments. About 90.8 percent of federal payments are made via direct deposit to a bank account and 5.6 percent are made via check. The full implementation date for electronic payments was set as March 1, 2013, although recipients who had not signed up for direct deposit or Direct Express by that date continue to receive their checks.

Electronic payment helps bolster the Social Security program. Each Social Security recipient who signs up for direct deposit allows the program to avoid \$205 in costs over the period they receive benefits.⁷ Social Security trust funds are estimated to be \$12 billion higher because of the cumulative impact of moving to electronic payment.

State Payments

SNAP and TANF are federal benefits distributed at the state level, sometimes combined with additional state-level assistance. States issue magnetic stripe cards to program recipients, who then swipe their cards at POS terminals to make a purchase. The terminal copies identity information from the card and transmits it to the contractor that administers the program. Electronic systems verify information, debit the amount from the recipient's allocation, and relay the approval back to the merchant.

States began EBT delivery in the 1980s, and by 2004 every state had adopted EBT cards. The result is a large cohort of people, many at the margins of the financial system, who have mastered the technology of using a magnetic stripe card at a POS terminal. Many have also learned how to deal with a POS terminal that requires a decision about which benefit should be accessed for the current transaction.

The EBT model has had spillover effects on other programs. In other state-administered programs that provide money to recipients—for example, child support and

unemployment insurance—states have moved more rapidly than the federal government to a policy of no longer offering paper checks. Generally, recipients can opt for direct deposit to a bank account; however, some have no choice but to receive payment via a card (see Appendix B for state-by-state detail on payment options under unemployment, TANF, and child support). Some state programs use EBT cards as the only delivery model, as opposed to the opt-in approach that Treasury and the Social Security Administration used to move participants from paper to electronic payments.

States follow one of two models in combining SNAP with cash assistance programs. In one model, a single card serves as an electronic benefit card that can access both SNAP and the cash assistance program (most often TANF). The funds remain the government's until a transaction uses the funds. In the other model, the cash benefit gets transferred to the individual's account at the beginning of the benefit period. The card is a reloadable debit card (although reloadable only with the next period's payment from the government program). Thirty-five states combine SNAP with TANF, providing recipients with one card to access both cash benefits and SNAP funds to buy eligible foods.

The largest benefit for government is cost savings. Besides the efficiency of reducing paper use, the government saves on postage, bank fees, and staff who deal with mis- or undelivered payments. The payments industry can better realize economies of scale from the complex and expensive computer systems that make electronic payments possible. Prepaid cards also provide an opportunity for banks to realize interchange fees—fees charged to merchants for acceptance of credit card transactions—on purchases made using cards that function as debit cards. The interchange fees banks receive are, according to a recent study by the Federal Reserve Bank of Philadelphia and the Center for Financial Services Innovation, an important source of revenue and make possible such features as no monthly fees for consumers.⁸

⁷ Hanns Kuttner, "The Move to Digital Payment: When the Check Is No Longer in the Mail," Hudson Institute (2011), hudson.org/files/publications/Hannspaperfinal4web.pdf.

⁸ See "Consumers' Use of Prepaid Cards."

The federal government has also piloted work on electronic delivery of nonrecurring payments, such as income tax refunds. While many refund recipients opt for direct deposit to bank accounts, unbanked households do not have that option. For the past several years, tax preparers have offered prepaid cards for tax refunds. In 2011, the Treasury Department initiated the

MyAccount program to deliver tax refunds via reloadable prepaid card accounts. The pilot provided some important lessons learned, and a redesign of the program is in process (see Box 2, The MyAccountCard Pilot).

BOX 2. The My AccountCard Pilot

During the 2011 tax-filing season, the Treasury Department carried out a demonstration project that targeted low- and moderate-income taxpayers with a prepaid card that could be used for direct deposit of income tax refunds. The demonstration made a direct mail offer and tested responses to three features: a monthly card fee of \$4.95 versus no fee; with and without a linked savings account; and messaging that focused on either the convenience or the safety of the card.

Among those who were most likely to be unbanked, the response rate was 0.8 percent—more than twice as high as the overall response, but still lower than expected. Among those who were issued cards, however, 33 percent used it within six months. Of those who used the card, 48 percent used it to receive their income tax refund.

There were mitigating factors for the low response rate, suggesting the trial was not an adequate basis for determining the card's utility. Many low- and moderate-income households pay the fee of a tax preparer using a refund anticipation check or loan. Opting for the prepaid card meant forgoing that option, effectively limiting the product to those who had the ready cash to pay a tax preparer's fee. Also, the mailing list had a 12.5 percent return rate, nearly 50 percent higher than the level expected in direct mail. Low- and moderate-income taxpayers file returns earlier in the filing season. A hiccup in the mailing process showed that offers mailed later yielded lower responses.

The demonstration produced a number of lessons, including:

- Monthly fees matter. The difference in response rate to an offer of an account with a fee and one without implied that each 10 percent higher monthly cost reduced applications by 2.6 percent.
- A monthly fee reduced card longevity. Those offered a card with a monthly fee were 55 percent less likely to be active users six months later.
- Neither the savings offer nor messaging about safety or convenience led to a higher response rate.
- Most users paid some fees. Fees could be incurred by using a non-network ATM or adding money at a participating retail location. Fees decreased as time holding the card went on.
- Added steps reduce use. While the card was intended as a device to receive income tax refunds, receiving the refund on the card required having the card in hand when preparing a tax return or meeting with a preparer. Of cards issued, only one in five resulted in a direct deposit of an income tax refund to the card.

Source: Caroline Ratcliffe and Signe-Mary McKernan, "Tax Time Account Direct Mail Pilot Evaluation," Washington: Urban Institute, 2012. <http://www.urban.org/UploadedPDF/412623-Tax-Time-Direct-Mail-Pilot-Evaluation.pdf>.

LEVERAGING GOVERNMENT PAYMENT CARDS: STRATEGIES

All approaches outlined here would provide unbanked individuals with capabilities that come with a bank account.

Unlike EBT, prepaid debit did not develop to solve a government payment problem, but once it emerged, it did solve the problem of providing payments electronically to people without bank accounts. As the technology evolves, opportunities are emerging for recipients to leverage government payments to obtain other financial services. With electronic payments now the norm for state

and federal programs, it's time to look at what the next generation of these payments can provide—government payments 2.0.

Here, we propose three interlocking strategies to consider: increased choice, expanded functionality, and improved financial capability.

Increased Choice

The field of behavioral economics has popularized the concept of a consumer-friendly default option. The classic example is automatic enrollment in a retirement savings plan. For Social Security and SSI, the default option is the Direct Express card. But default options are not the only solution. The government could set up a forced-choice framework that requires consumers to choose among payment options. The policy question to be addressed is which structure is better for consumers. Consumers who sign up for direct deposit of federal and state benefits have a lot of choices. They can choose the bank or credit union they use. And they can choose

from all of the possible accounts that institution offers, with a range of features and fees. However, consumers who receive their government benefits on a prepaid card—many of whom are unbanked—have no choice. They receive the card with the features and fees the government provides through a card issuer, usually a bank.

As an alternative, instead of contracting with a single financial institution, the government could specify a set of basic features and fees for a prepaid card program. Financial institutions could choose to offer this basic product but could also provide additional features and services to address a wider variety of consumer financial service needs. Thus, for example, an account might allow more ATM withdrawals per month than the basic account. Other products could have a linked savings account that would allow for splitting monthly payments between one account for current expenditures and another for saving for irregular, costly purchases or longer-term needs. The additional features—and any accompanying fees—would be driven by consumer needs, and consumers could choose among the range of card providers and programs.

Offering multiple products requires a deeper and more nuanced understanding of consumers, their motivations, and their financial lives. Current products are often structured to yield no costs for certain consumers. For example, the Direct Express card has no fees for someone whose cash needs can be met by a single monthly ATM withdrawal and cash back on purchases with the card. This works well for some people, but others may prefer a set monthly fee in exchange for a larger number of ATM transactions. The set fee would mean they don't need to think about fees with every additional ATM transaction.

Interestingly, Treasury initially tried a version of this “free to choose” approach when setting up the electronic transfer account (ETA) as part of the EFT '99 initiative. The time may be ripe to revisit this approach as part of a next generation initiative. Prepaid cards were still relatively new in 1999; today they are ubiquitous. The ETA had clear product specifications that could not

be varied—a one size-fits-all approach; a next-generation card could offer “add-ons” to a basic account structure to allow consumers to customize their account. Because the ETA did not have a network brand (MasterCard or Visa), functionality was limited. A next-generation product could be usable in the card networks.

Treasury developed a website for consumers to search for an ETA by entering their zip code and matching that to banks offering ETAs.⁹ But in 1999, many consumers who might be targets for ETAs—including many unbanked consumers—lacked access to computers. Today's consumers are more likely to have access either via computers or, more likely, mobile devices, and should be better able to search out and connect with an appropriate prepaid card provider. Moreover, the next-generation website could match consumers not only with local providers but also with products that have the features that best meet their needs (see Box 3, *Steering Versus Rowing: How it Could Work*).

⁹ See <https://www.eta-find.gov/>

BOX 3. Steering Versus Rowing: How it could Work

When governments steer, they provide strategic direction to a program. Delivering payments electronically is an example of steering. When governments row, they more narrowly get into delivering the products for those programs. Contracting with a single financial institution to provide a specified product or service is an example of rowing. Arguably, the comparative advantage of governments is to steer rather than row. Federal and state governments could set standards they expect government payment products to meet and then turn to a public-private partnership to do all the rowing: determine what products will be offered, educate recipients about choices, and sign them up for the products recipients choose.

One scenario could build on web-based selection system, similar to the Medicare Part D plan-finder site. After providing information required to determine eligibility, consumers would be able to choose payment delivery either via direct deposit to their bank accounts or via a prepaid card.

Those who opted for the prepaid card would then see a screen providing information about the prepaid card program. Users would have the opportunity to see more screens about how prepaid cards work or could move directly to screens that explain what products were available. The range of choices could take into account where the consumer lives as well as the range features consumers need and want, as well as information about “add-ons” and fees, enabling consumers to make their own feature/fee trade-offs. This could lead to a set of customized choices for the consumer: “Based on the information you provided, the product that best fits your needs is ...”

This public-private “steering and rowing” partnership might allow a faster product innovation cycle than would be available under a more-traditional government payment contract which typically lasts five years or more.

Expanded Functionality

Reloadability

A reloadable card allows a consumer to add funds. Cards such as Direct Express and the prepaid cards used by states in one sense are reloadable, since they can receive funds many times on the same card. But only the government agency may load funds onto the card.

In contrast, general purpose reloadable (GPR) cards, like bank accounts, allow funds to be loaded from multiple sources (government, employers, individuals) and in multiple forms (cash, check, direct deposit, etc.). By expanding reloadability to non-governmental sources, government payment cards can offer recipients a more powerful financial management tool. Cards could be portable, so that they remain useful even if government payments end (e.g., unemployed workers could use the same card for payroll deposits once they start working again). That would be convenient for consumers, but there would be trade-offs.

One issue is that the government agency acting as a card program manager and its issuing bank would take on additional risks in opening their cards to outside deposits. For example, today’s issuing banks know the source of funds: the government program. They would not have that same level of knowledge about the sources of other funds that come from program participants. Banks would need to mitigate against the potential fraud risks, including standard anti-money-laundering protocols, relating to other sources of funds.

As more banks issue GPR prepaid cards outside of the government benefits systems, they are gaining experience in developing the extensive computer systems that support these cards. Reloading networks, remote deposit capture, and mobile financial services all help to enhance banks’ ability to serve these accounts,

opening the possibility that banks could provide enhanced services to government payment recipients. Some expanded functionality, however, may be limited as a result of the Durbin Amendment, a provision in the Dodd-Frank legislation that places some limits on interchange fees that banks can charge merchants.

The expanded functionality that comes with reloadability could be achieved via different combinations of number of cards and number of subaccounts on the card (see Appendix C, Summary of Potential Strategies for Government Payment Cards).

One Card, One Account

This strategy builds on the high degree of government involvement in setting the terms for the Direct Express cards and the cards issued for state programs. Government programs could revise their policies and allow the banks that issue the cards to permit cardholders to deposit funds from other sources to their government-issued card in the same account. For example, Social Security recipients who continue to work could have their pay deposited to their Direct Express cards. Workers who receive unemployment compensation could use the same card after getting a job, now for direct deposit of their pay. Child support recipients could have income tax refunds deposited directly to their cards.

Commingling funds from multiple sources can make it more difficult to deal with policy restrictions regarding garnishment and wage assignment (for example, Social Security payments are not subject to assignment). Some states have concerns about recouping erroneous payments when payments go to accounts that commingle government payments and private funds. And financial institutions would have to explore a feasible business model and fair fee structure for these accounts. But from the consumer perspective, the unified strategy is the simplest—it is more straightforward and easier to use, since it most closely resembles a standard checking account or GPR prepaid card account.

Reloadability might make for more complex procurement decisions. An offeror might structure fees for non-government reloads to allow it to more aggressively price the government contract. Ideally, governments should want to offer a competitively priced product to demonstrate they are providing benefits to consumers and not steering consumers into “predatory” products.

One way to reduce risks associated with reloadability would be to make it a feature that had to be unlocked. Instead of automatically issuing reloadable government payment cards to all cardholders, a bank could require that a cardholder contact the financial institution before funds could be deposited. This would enable the bank to go through its usual customer identification protocols and would reduce any risk the bank might perceive from having many “latent customers,” cardholders who could at any moment show up, either in person or via an electronic transfer, and become a customer without being subject to those protocols. It would also allow the financial institution to separately price the products—for example, charging a different fee for customers who wanted the reloadability option while continuing to price the government-only account without a monthly fee, as Direct Express and many state cards do.

Another way to reduce risks would be to limit reloadability to specific sources of funds—for example, income tax refunds or payroll funds (the mandate for federal electronic payments does not extend to income tax refunds). The once-a-year payment for an income tax refund, surely a secure source, is a natural extension of government payments onto a government benefit card.

Opening government prepaid cards to payroll deposits would accommodate a primary income source for many users. Allowing deposits from a payroll source would also be less risky, and thus less costly, than opening the card to deposits from any source, making it a more reasonable compromise between cost and functionality for both government and industry.

Depositing cash or checks sent to consumers might be more challenging. Online banks have demonstrated that mail and remote deposit via image capture can mitigate the lack of local branch locations. Consumers might be less interested in a small or remote branch network. An advantage may go to providers who set up relationships with retailers (check cashers, grocery stores, prepaid cellphone sellers) to expand their retail reach.

One Card, Multiple Accounts

In a multiple account structure, at least two accounts would be accessible from one card—one for the government cash payment and the other for non-governmental funds. Cards like these are sometimes called “dual purse” cards. This arrangement would be similar to providing SNAP and TANF benefits on a single card, as many states currently do. Recipients swipe a card at a POS terminal and then select the account to be used for the purchase. The segregation of funds would avoid any issues that might arise with an account that commingled government and other funds.

Multiple accounts might reduce risk and regulatory burden for the issuing bank, meet the original purpose of the payment card (getting dollars from the government to consumers), and improve usability for the consumer. Banks would need to consider pricing structures for a multi-account card. One option would be to price services for the non-government account appropriately, without cross-subsidies across the two sets of accounts. It is likely that pricing would still be more favorable for these cards than GPR cards consumers obtain elsewhere, because customer acquisition costs would be lower.

Consumers would need to pay attention to the source of funds to be used at each purchase. For example, parents who have a child support account and a payroll account accessed from the same card would need to pay attention to which “purse” they used for which purchase. At the same time, separate accounts might increase a card’s usefulness. Some economists have argued that

consumers sometimes behave as though the amounts held in separate accounts are not fungible. This notion of “separate mental accounts” suggests that consumers might feel better off financially with this structure. A cardholder might view the funds in the government payment account as money for necessities, while those in the other account are available for extras. Multiple accounts would allow consumers to tag purchases and track spending by category, such as food or clothing. For example, child support recipients report that payment cards help them track costs relating to their children.

Multiple-account cards might also allow joint venturing between financial institutions. A large financial institution might find the scale of government payments well matched to its scale of business but not have a substantial retail presence in some markets. In this case, the large, payments-oriented bank could join with smaller, regional banks or credit unions to offer “one card, two accounts” to take advantage of the smaller bank’s footprint in some areas. This approach could also allow smaller financial institutions that lack the scale required for the government payments business to reach the market of government-payment recipients.

Multiple-account cards might also enable some efficiency in providing a broader range of benefits and payments. As indicated, SNAP and TANF benefits are often delivered on the same card. Many recipients also receive state and federal income tax refunds, and may receive child support and unemployment benefits as well. For example, Utah recently started providing multiple benefits on a single card (see Box 4, *Utah: One Card, Multiple Programs*).

With a multi-account card, separate purses can keep all these funds segregated without requiring the consumer to carry five or six cards. But some government officials are concerned that product complexity and multiple accounts could lead to consumer confusion and dissatisfaction. Participants would have to be attentive to how much money of which type they had or accept the possibility of re-executing a denied transaction to obtain funds from another account.

Joint Marketing -- Two Cards, Two Accounts

A joint marketing approach joins enrollment in a government program with an opportunity to sign up for a GPR card from the same issuing bank that provides the government card. With two cards, two accounts, there would be no need to integrate government payments with other sources of funds on a single card. If financial institutions had lower customer acquisition costs, a substantial cost in many GPR programs, they might be able to lower the cost of the card to

consumers. The GPR card could be offered at enrollment or in the mailer that delivers the government card itself.

An advantage of the joint approach is its relative flexibility. Government payment product contracts tend to be for terms of five years or more, limiting innovation during the contract. A companion GPR card, however, can continuously innovate and improve, trying out new features and services. And once consumers become familiar with using their government prepaid cards, they may be more willing to try out a GPR card with

BOX 4. Utah: One Card, Multiple Programs

A single card can serve multiple government programs. Utah is about to launch a card that will be used in more programs than any other government card. It will be used for:

Cash assistance: Multiple government programs that provide cash payments, such as unemployment insurance and Temporary Assistance to Needy Families (TANF), will be routed to a single account. The card will be the sole alternative to receiving payments via direct deposit. The card will also be used to make payroll payments to state government workers who do not opt for direct deposit.

SNAP benefits: The card will also be the means for Utah residents enrolled in SNAP to access benefits. When they present the card to make a purchase, a display will appear on the point-of-sale terminal asking whether the funds from the purchase should come from the cash account or the SNAP benefit.

In-kind services: Child-care and training programs will also require participants to use the card. These programs will be, as with SNAP, part of a closed loop. The card will be usable at a defined universe of providers who have a relationship with the state agency. The card will support a “time and attendance”-like function, generating information about who was present at which program at what time. This reduces the cost of acquiring and submitting information required to make accurate payment to providers.

The card will not include all state programs. Most notably, child-support recipients who do not opt for direct deposit will continue to receive payments via a separate prepaid card. However, as systems evolve, other programs may join. The WIC program administered by the state health department, for example, faces a mandate to move from paper coupons to an electronic payment system. Utah supplements benefits paid under the Supplemental Security Income (SSI) program for some people, and the card may become the means for disbursing the state supplement.

Utah had previously adopted a common account number across the programs that participate in the card. This greatly simplified the process of linking individuals to a single card.

A single card has allowed Utah to realize scale and scope economies that reduce the cost of the payment system. For example, SNAP-only cases will cost 57 cents less per case per month. Utah expects to save \$1 million per year in the state’s administrative costs. If every state had a card that was as broad as Utah’s, savings to state governments could exceed \$160 million per year.

added functionality. A joint-marketing project could move forward by offering a GPR card to a subset of payment recipients to assess response rates and usage to help issuing banks determine pricing structures.

Private Cards – One Card, One Account

Consumers already can choose to have federal benefit payments loaded onto a private-label GPR card. The federal requirements are few: an account must come with FDIC insurance, it cannot be tied to automatic loan repayment, and it must have the protections, such as limited consumer liability in case the card is lost or stolen, afforded by Regulation E.

But just like shopping for a bank account, consumers need to shop for and compare GPR cards. One way to simplify the choice and reduce participants' fear of choosing the wrong card is through trusted allies—affinity groups that exist to serve specific populations. Examples include civic groups, veterans groups, and alumni organizations. A specific example is the AARP Foundation's reloadable, prepaid MasterCard, issued through GreenDot Bank. Consumers who already have the AARP prepaid card can sign up to have direct deposit of paychecks and government benefits, including Social Security, unemployment, and welfare.

Increased Financial Capability

Financial capability involves a set of consumer behaviors that lead to tangible improvements in financial health. Components include the ability to cover monthly expenses with income, track spending, plan and save for the future, effectively select and manage financial products and services, and gain and exercise financial knowledge. CFSI has found that effective financial capability interventions should be relevant, timely, actionable, and ongoing to have impact.¹⁰ Government prepaid cards meet all these criteria, providing an opportunity to establish best practices for promoting financial capability among consumers.

Government payments have the potential to help consumers build financial capability through a number of channels. Each monthly load provides an opportunity to send financial management messages and reminders. For example, with each text message telling Social Security recipients their funds have been loaded to their cards, there could be an additional reminder, such as “Have you checked your credit report this year? Visit www.annualcreditreport.com.”

But the underlying technology of prepaid cards can do more—from the simple, like checking balances, to the more complex, like tagging purchases and creating summaries of spending. Most prepaid cards can be monitored via online or mobile devices, delivering real-time financial information that enables consumers to make better-informed decisions.

Many cards today allow consumers to track spending in categories (food, clothing, entertainment, pets), to help them to make informed decisions and adjust spending. Some card issuers provide visual displays—charts, graphs, progress-trackers—on websites or within their mobile apps, showing consumers how much remains in their accounts or how much they've spent this month on coffee.

¹⁰ See “From Financial Education to Financial Capability: Opportunities for Innovation,” at www.cfsinnovation.com/system/files/Research_Paper_Financial_Capability_Mar2010.pdf.

Prepaid cards can also provide planning services, allowing consumers to set spending limits and receive text notices or emails when nearing those limits. For example, consumers who need help managing monthly payments across the entire month could get weekly spending-limit notices to help them manage their money throughout the month. These notices also work for saving, either automatically sweeping money into savings or reminding consumers to move money into a savings account. A logical next step is to help consumers connect with financial coaching and advice.

Some cards have partnered with organizations that use games and activities to reward consumers for online learning and improvements in spending and saving behaviors. So, for example, consumers are encouraged to set goals—a vacation, money for birthday presents, a back-to-school shopping fund—and work out a plan to achieve the goal and even win prizes.¹¹

¹¹ An example of this is the PayPerks program, in development; see <https://www.payperks.com/>.

CHALLENGES FOR EXPANSION OF GOVERNMENT PAYMENT CARDS

Consumer Protection

Expanding financial access is not the only consideration for government payment cards. To help low-income consumers improve their financial lives, the cards must provide strong consumer protections. Consumers also need to be confident that the money stored on prepaid cards is secure, and they need to understand the exact costs of using these cards.

Understanding what features potential users value is a new challenge for governments as well as their industry partners.

Monthly fees, for example, reduce benefits to consumers. Currently, many, but not all, payment cards used in government programs have no monthly fee. At least one state has a contract with the issuing financial institution that requires the consumer to pay a monthly fee.¹² Some cards leave consumers exposed to fees that can accumulate with particular patterns of behavior (e.g., making frequent, small ATM withdrawals from non-network ATMs, rather than getting cash back when making a purchase). Because understanding fees can be very important for consumers, disclosures are critical to help consumers readily find and understand the information they need to use their cards wisely. CFSI has developed a model fee disclosure box to recommend how to make the necessary information readable and easy to find (see Appendix D, Better Disclosures for Prepaid Cards).

¹² See National Consumer Law Center's 2013 Survey of Unemployment Prepaid Cards; <http://www.nclc.org/images/pdf/pr-reports/report-prepaid-card-2013.pdf>

Card issuers and program administrators are willing to make cards available at no fee to the consumer or the government because they expect to earn interchange fees from merchants who accept the card for payment. Changes that affect projected interchange revenues could lead to additional fees for consumers.

Other important consumer protections are provided under Regulation E of the Electronic Fund Transfers Act. Among other things, Regulation E gives consumers some liability protection if a card is lost or stolen, or if fraudulent transactions show up on an account. Regulation E also outlines dispute procedures so that funds may be restored to the consumer's prepaid card while an investigation proceeds.

CFSI's Compass Guide to Prepaid outlines core, stretch, and next-generation practices across all aspects of a prepaid account (see Appendix E, Compass Principles for Prepaid Cards). Ideally, government prepaid cards would follow all of the core and stretch practices and be a model for well-designed card programs.

Regulatory Issues

Making government prepaid cards reloadable may require other changes that would impact costs for financial institutions and consumers. Allowing non-government funds to be loaded onto the cards would require financial institutions to collect more personal information about cardholders because of increased regulatory requirements intended to limit money laundering and terrorism financing—the customer identification program and “know your customer” requirements. While the government agency carries out similar identification protocols for determining eligibility, there is no guidance for financial institutions as to whether they could rely on the government agency's due diligence.

Other rules may play a role in how accounts would be structured and priced. One is Regulation E governing

electronic fund transfers, including limitations on consumer liability. As of this writing, the Consumer Financial Protection Bureau is considering whether and how GPR cards should be covered. Garnishment rules also raise issues. For example, some benefit payments are protected from garnishment (e.g., Social Security payments), and accounts that commingle funds must be able to account for any garnishment activity.

The Durbin Amendment, included in the Dodd-Frank Act, restricts the interchange fees banks can receive from electronic debit transactions, including prepaid cards. However, the rules exempt some cards, including small issuers (those banks with assets less than \$10 billion), government-administered programs (those issued by federal, state, or local governments), and certain reloadable cards (for example, cards issued to access flexible spending accounts, when the card is the only means to access those funds).¹³ For some financial institutions, limiting the ability to capture interchange fees may limit the cards' appeal.

It is clear that any multiple-purse card loaded with non-government funds (such as wages or salary) would be covered by the Durbin Amendment's interchange fee limits. Not only might this be a disincentive for financial institutions but it might also limit innovation. Data from the Federal Reserve show that in the last quarter of 2011, exempt transactions accounted for 82 percent of the number of prepaid card transactions and 83 percent of the dollar value of prepaid card transactions. On average, covered prepaid transactions had a lower value compared with exempt transactions (\$31.35 versus \$33.61).¹⁴

Consumer Acceptance

The prepaid card market is still relatively new, and we continue to learn about how consumers relate to these products and services. Unlike private card programs, in which consumers choose the card, consumers typically do not choose the card for government

¹³ The details of the rules implementing the Durbin Amendment can be found at www.gpo.gov/fdsys/pkg/FR-2011-07-20/pdf/2011-16861.pdf.

¹⁴ “2011 Interchange Fee Revenue, Covered Issuer Costs, and Covered Issuer and Merchant Fraud Losses Related to Debit Card Transactions,” www.federalreserve.gov/paymentsystems/files/debitfees_costs_2011.pdf.

payments – it is chosen for them. It would be helpful to learn more about use patterns to better match card services and features with consumer needs.

In a study by CFSI and the Federal Reserve Bank of Philadelphia, use patterns took the shape of a U. That is, a lot of consumers used the card only once to get most or all of the cash from it (a “one and done” profile) while many others made extensive use of the card; there were very few in between.¹⁵ Some consumers make sparing use of ATMs. Some are comfortable using digital formats to pay bills (online or mobile bill paying), while others prefer tangible methods such as money orders or cash. While some consumers will be enthusiastic about additional prepaid opportunities, the attitudes and views of those who do not will require careful study. Those who mistrust banks may be more trusting when government is involved.

As more people develop a history with prepaid cards, acceptance among government payment recipients will likely increase. Also, a generational factor may be at play—younger consumers who are “digital natives” may be more experienced and comfortable using prepaid cards, and may actually prefer them.

The availability of technology to consumers to make transactions without banks raises the question of whether the unbanked vs. banked distinction will matter in the future.

NEXT STEPS

Government payment cards have a tremendous potential to enhance financial inclusion for millions of U.S. consumers. However, for those who administer payment card programs, greater financial inclusion is either not part of what they perceive as their mission or not a current priority. Making the leap will require pioneers or entrepreneurs willing to demonstrate how the concepts work. Leadership might emerge from anywhere—the public sector, organizations that are trusted intermediaries of payment recipients, social entrepreneurs who see an opportunity to leverage new paths to financial inclusion, and private industry, motivated by profit, seeking to better meet consumer needs.

Federal Programs

The federal government is poised to be a leader in moving people to electronic payment. Its electronic-only policy for recurring payments that took effect in March 2013 was a milestone in moving millions of individuals from paper checks to electronic payment. There are several opportunities on the horizon for expanding the federal government’s role in the payments arena relating to Direct Express, income tax refunds, and coordination among federal-level programs.

¹⁵ See “Consumers’ Use of Prepaid Cards.”

Direct Express

The solicitation for the next round of Direct Express payment cards provides an opportunity to put this agenda to work. For example, financial institutions could offer a basic prepaid card product with government-specified functions while also offering add-ons to address a wider variety of consumer needs. Direct Express could be reloadable with government funds only or with non-governmental funds as well. The government could partner with industry and nonprofit groups to provide benefit recipients with tools and services to improve financial capability. Whether the government makes a single product or multiple GPR products available to benefit recipients, the products would have to meet certain consumer protection and quality standards.

Income Tax Refund Payments

Because many refund recipients are unbanked, tax refunds account for a large number of federal paper checks. In 2011, the Treasury Department piloted the MyAccountCard, designed to deliver tax refunds via a reloadable prepaid card, with mixed results. The experience with a payment card for nonrecurring, periodic payments like income tax refunds shows the need for a closer understanding of how taxpayers think about refunds and other parts of their financial lives. Options for next steps include:

- Carry out consumer research about attitudes and preferences that will better specify a more appealing card product to improve the targeting, delivery, and consumer adoption of the prepaid card account.
- Allow tax filers to sign up directly on the tax form, or incorporate sign-up into tax filing software.
- Specify basic features and fees for the card program and offer a choice among multiple cards that meet consumer protection and quality standards. Card offers could be keyed to the consumer's zip code to allow local banks to compete for these consumers.

Coordination Among Federal Programs and the Federal-State Nexus

In terms of their relationship with the federal government, state program administrators operate across a wide spectrum. At one end, the TANF program is a block grant, and the federal government provides little guidance.¹⁶ At the other end, states must clear payment system RFPs for SNAP ahead of time with the U.S. Department of Agriculture. In the middle is unemployment insurance, where the Department of Labor has issued a best practices document.¹⁷

None of the agencies has suggested that a state could use the payments system to promote financial inclusion and improve financial capability. In part this reflects the goals and priorities of those who administer federal programs. Some involved with government payment policy read the history of government trying to get away from paper checks as a story in which simplicity succeeds and complexity fails. Leadership from outside program agencies could increase the likelihood that something will happen. It might come from some other agency or from a change in federal law or policy to make leveraging opportunities for financial inclusion part of agency administrators' jobs.

States have realized economies from combining SNAP and TANF onto a single card. Broadening benefit cards to include other features, such as a reloadable purse and access to tools that help build financial capability, is a next step. Other options for the federal government include:

- Provide guidance outlining a vision for the future of payment cards in state programs, addressing such issues as integrating multiple programs on a single card, reloadability, and other approaches to broaden financial inclusion and the financial capability of recipients. An interagency memorandum of understanding between the federal agencies with cash benefit programs administered by states—the

¹⁶ *The strong exception is a provision contained in the Middle Class Tax Relief and Jobs Creation Act of 2012, signed on February 22, 2012. That legislation responded to media accounts of locations where recipients accessed funds and requires that states assure that funds not be accessed at liquor stores, casinos or gaming establishments, or retail establishments that provide adult-oriented entertainment in which performers disrobe or perform in an unclothed state for entertainment.*

¹⁷ *Employment and Training Administration, "Best Practices for Payment of Unemployment Compensation (UC) by Debit Cards," Unemployment Insurance Program letter No. 34-09, August 21, 2009.*

Departments of Agriculture, Health and Human Services (HHS), and Labor—would serve as a model of interagency cooperation and collaboration.

- Issue best practices guidelines for card programs and identify problematic practices for consumers. These guidelines should address consumer and regulatory issues (e.g., how to meet “know your customer” requirements). This would require interaction across arms of the federal government that have not had reason to interact before: those that administer programs (Agriculture, HHS, Labor, Treasury) and those responsible for supervising financial institutions (CFPB, FDIC, the Federal Reserve Board, National Credit Union Administration, Office of the Controller of the Currency, State Banking Supervisors).
- Conduct or fund research to better understand consumer preferences with regard to prepaid card products and to identify best practices in their design and delivery. Program agencies such as HHS and Agriculture administer programs that seek to increase self-sufficiency, an outcome with a financial component. This overlap should lead to cooperation among agencies to develop a joint research agenda.

State Programs

Electronic payment is now the norm for benefits administered by states. Every state offers some options for a card alternative to paper checks or direct deposit in at least one of its programs that transfer cash. At least four states have moved ahead with non-reloadable tax-refund debit cards: Connecticut, Louisiana, Oklahoma, and South Carolina.

States face strong incentives to design prepaid programs that work for citizens. Any product that generates negative attention, either from informal views shared among participants or from media reports, can lower participation. Understanding what features potential users value is a new challenge for states and their partner card issuers.

As with other innovations in services provided by government, state agencies learn by watching, with many states holding back until they see how the concept works in

at least one other state. Thus, a state moving ahead with a particular model creates momentum among others.

In general, states have opted for “one card, one account,” and the card is not reloadable except with funds from the program that issued the card. The major exception is states that have made both TANF and SNAP available from the same card.

Two state-administered programs—unemployment insurance and child support—have particular potential as a platform for greater financial inclusion. Prepaid cards for unemployment insurance benefits could be leveraged to serve as a payroll card for consumers returning to work. A similar option exists for child-support recipients who opt for a payment card over direct deposit. In both cases, the state government could bargain for better terms and protections than currently exist.

Utah has demonstrated that one card can serve multiple programs. But other states may have issues to resolve before a combined card becomes practical. For example, procurement cycles for payment products vary across programs, and some computer systems may not work well across multiple programs. In addition, state laws restricting garnishment may pose a challenge.

Some options for states include:

- Try new models. State policy entrepreneurs have multiple options to connect payment recipients with financial services and increase financial capability. The experience of states over time will show how different models perform. Efforts at the state and local level that pursue reloadability can only work if federal regulators solve conceptual issues that might keep financial institutions from participating.
- Synchronize procurement cycles. In many states, each program has its own contract with a financial institution for payment products. Innovation bringing more programs onto one platform is almost impossible unless states move programs to a common renewal cycle.
- Combine multiple government benefit program payment tools into one larger contract. This can leverage more economies of scale. Explore

broader access by asking financial institutions for proposals to extend the reach of payment cards through access to reloadable products.

- Learn more about what features users value (making research done by the federal government, industry, or the research community helpful). As the federal government's experience shows, to develop an accepted product requires listening to what people want and presenting it to them in a way that encourages them to choose it. Launch and market products accordingly.

Industry

Expanding reloadability introduces concerns for government program managers and issuers. Rather than having funds loaded by a single entity (the government), financial institutions would have to deal with more, and more variable, sources. As a result, banks would likely rethink their business case for this market segment. What additional risks and costs would the bank face? How could it recover those costs? Would there be opportunities to recover the costs from cardholders who used the reloadability feature? If there were limited opportunity to recover the costs, how would banks change the terms they offered governments in their responses to government contracting requests? Of course, if states moved from offering a single card to offering a choice of cards, the problem would be different.

Government payments are computer-system intensive and have become associated with larger banks. Innovation in prepaid cards, on the other hand, has been associated more with smaller banks. These smaller institutions have narrower product offerings than the large banks. Reaching the unbanked who participate in government programs will be a relatively small market in the overall pattern of prepaid use. Innovative partnerships may be necessary to encourage smaller banks to get involved.

Sharing with Government

Financial institutions know much more about technology and consumer financial behavior than do government officials who administer payment systems. Their experiences can help government understand the potential and use payment cards to do more for users. Industry can help educate government by sharing these experiences:

- Share insights and research on consumer preferences to help state and federal programs better understand how to structure and deliver prepaid card accounts to participants.
- Share the latest trends and best practices in the government payments industry with state and federal programs, as well as background on relevant emerging technologies.
- Inform government stakeholders about new, relevant payment technologies and show concrete ways they could be applied to payment cards to expand financial access.
- Encourage states and the federal government to adopt reloadability or other strategies for extending the reach of government cards both formally (through the RFP process) and informally (individual conversations, conferences, marketing materials, etc.). Not only is there a market opportunity here (broader customer acquisition and higher revenue from higher card use both as accounts and over longer time periods), but also government cards can be market movers with new technologies.

Nonprofits/Academics/ Consumer Advocates

Much of industry knowledge is proprietary—there is little public knowledge about payment recipients and their financial behaviors. Furthermore, the path to a payment system that gives choice to government payment recipients and provides a path to more capable payment products may be better paved by others than by government.

Payment recipients may be better served, with more choices and access to a wider range of financial products, if governments “row” rather than “steer.” Nonprofits, academics, and consumer advocates can be more flexible and more nimble than government in doing the following:

- Research and obtain more data on consumer preferences and behavior with payment cards to help governments build appropriate expectations and inform product development and rollout.
- Support governments with this work to enhance the chance that the development and deployment of more financially inclusive government payment cards will succeed.
- Form an organization that can take over the “rowing” from government—one that will work with financial institutions to develop consumer products or administer a process for offering qualifying products. Government could turn to this organization to provide a range of products to payment recipients, because a nimbler organization could allow smaller or more geographically limited institutions to reach them.

CONCLUSION

Governments at all levels have embraced the changes brought about by new payment card technologies. And electronic payments have advantages for all parties: governments lower the cost of distributing benefits; the payments industry realizes further economies of scale and greater revenue from wider use of the payments network; and individuals have the security of knowing the check won't be "lost in the mail."

But electronic payment methods can do more. They can serve as an entry into lower-cost, broader-function payment tools that support recipients' financial lives. They can increase choices among financial services and provide a range of financial service functions. Their greatest promise lies in their potential to help people improve their financial health, whether through access to more information or a transition to increased use of higher-quality, more effective financial services. The same systems that made electronic payment possible can also provide tools that help people understand and plan their financial lives.

Government payers can model the best possible payment delivery vehicles. As governments select default payment mechanisms, they can ensure that government payees are using high-quality products, taking into account functionality, fees, and consumer protections. The relationship of technology and financial inclusion will shape the potential of government payment cards and other tools that look different from traditional bank accounts. This is the next generation of payment cards and financial inclusion products.

APPENDIX A: Prepaid Card Primer

Consumers used to have two payment choices: pay now (with cash, check, or a debit card that accesses money in a bank account) or pay later (with a credit card that accesses a line of credit). But now consumers have a third choice: pay before. Consumers can place funds on a prepaid card that they can access in the future to make payments at stores or online.

A prepaid card can be used in a **closed loop** or an **open loop**. In a **closed loop**, the information encoded on the card passes between a card reader and one issuer. Examples include cards for a single store or group of stores, such as a gas station chain, gift cards that can be used for a single company, or transit cards. In the government sector, **electronic benefit transfers (EBT)** such as the SNAP program (Supplemental Nutrition Assistance Program, formerly food stamps) administered by state governments are a variation of a closed-loop, in that the card can only be used for designated food items.

An **open loop** describes **general-purpose cards**, that is, cards that have a network logo and can be used at any merchant who accepts the card. Visa, MasterCard, and American Express are common examples. A merchant may be a brick and mortar store, an online store, or a service provider—a category that ranges from doctors' offices to taxi cabs. Some general-purpose cards are single-load cards – for example, rebate or gift cards that have a network logo. Virtually all cards can be used at point of sale and online. Many can be used at ATMs to get cash; in addition, it is possible to get cash back with a purchase – for example, you buy \$100 of groceries but ask the clerk to ring it up as \$150, keeping the additional \$50 in cash and avoiding an ATM fee.

General-purpose reloadable cards (GPR) are gaining in popularity, with a growth rate of 46% per year.¹⁹ Consumers can add funds to a GPR once they have registered it with the issuer (this characteristic is called “reloadability”). Employers have adopted GPR cards as a means to make payroll payments to employees who do not have, or who do not wish to use, bank accounts for direct deposit of earnings. State and federal governments work with financial institutions to issue GPR cards to deliver benefits to program participants. These government-issued cards differ from the more widely available GPRs in that funds are only reloadable by the government, not by the consumer.

While most prepaid card make use of a magnetic stripe on the back of the card to access payment networks, **smart cards** have an embedded integrated circuit (called a **chip**). The chip allows much more data to be carried on the card than on the magnetic stripe cards. Some states use smart cards in the Women, Infants, and Children (WIC) nutrition assistance program. The card stores information about individual benefit packages, a complexity unique to WIC.

Payment Networks. Payment networks provide an electronic connection between someone who wants to make a payment, a financial institution, and the payment recipient. The most common electronic payment experience today involves swiping a magnetic-stripe card at a point-of-sale terminal. However, other technologies are becoming more common. Near field communication (NFC) provides a contact-free way to connect to payment networks—transit systems, states that use EZPass, or the “wave and pay” systems at some gas stations, for example. Many smart phones are equipped with NFC technology as well. The magnetic-stripe card may someday give way to the mobile phone biometric identification, using voice recognition, iris scans, or fingerprints to access payment networks.

¹⁹ See *Consumers' Use of Prepaid Cards*.

APPENDIX B: State Programs and Prepaid Questions									
State	Unemployment Insurance			Temporary Assistance for Needy Families		Child Support Payments			Offers Info on fees before selection
	Direct deposit	Prepaid card	Checks	Prepaid Card	Checks	Direct deposit	Prepaid Card	Checks	
Alabama	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	Yes
Alaska	Yes	Yes (Optional)	Yes	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	No
Arizona	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Arkansas	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
California	No	Yes (Mandatory)	No	Yes (Mandatory)	Yes	Yes	Yes (Optional)	Yes	No
Colorado	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	Yes
Connecticut	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Delaware	Yes	No	Yes	No	Yes	Yes	Yes (Mandatory)	No	Yes
District of Columbia	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Florida	Yes	Yes (Optional)	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	Yes	Yes
Georgia	Yes	No	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Hawaii	Yes	No	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Idaho	Yes	Yes (Optional)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Illinois	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Indiana	No	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Iowa	Yes	Yes (Mandatory)	No	No	Yes	Yes	Yes (Mandatory)	No	No
Kansas	No	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	Yes
Kentucky	Yes	No	Yes	No	Yes	Yes	Yes (Optional)	Yes	No
Louisiana	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	No
Maine	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Maryland	No	Yes (Mandatory)	No	Yes (Optional)	Yes	Yes	Yes (Optional)	Yes	No
Massachusetts	Yes	No	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Michigan	Yes	Yes (Optional)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Minnesota	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Mississippi	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	NA

Note: Mandatory means that prepaid debit is mandatory for those who do not opt for direct deposit.

APPENDIX B: State Programs and Prepaid Questions

State	Unemployment Insurance			Temporary Assistance for Needy Families		Child Support Payments			Offers Info on fees before selection
	Direct deposit	Prepaid card	Checks	Prepaid Card	Checks	Direct deposit	Prepaid Card	Checks	
Missouri	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Montana	Yes	No	Yes	Yes (Optional)	Yes	Yes	Yes (Mandatory)	No	No
Nebraska	Yes	Yes (Mandatory)	No	No	Yes	Yes	Yes (Optional)	Yes	No
Nevada	No	Yes (Optional)	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
New Hampshire	Yes	No	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
New Jersey	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
New Mexico	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
New York	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	Yes	Yes
North Carolina	Yes	Yes (Mandatory)	No	No	Yes	Yes	Yes (Mandatory)	No	No
North Dakota	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Ohio	Yes	Yes (Mandatory)	No	Yes (Optional)	Yes	Yes	Yes (Mandatory)	No	No
Oklahoma	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Oregon	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Pennsylvania	Yes	Yes (Mandatory)	No	Yes (Optional)	Yes	Yes	Yes (Mandatory)	No	Yes
Rhode Island	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
South Carolina	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
South Dakota	Yes	Yes (Mandatory)	No	No	Yes	Yes	Yes (Mandatory)	No	No
Tennessee	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
Texas	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Optional)	Yes	Yes
Utah	Yes	Yes (Mandatory)	No	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Vermont	Yes	No	Yes	Yes (Mandatory)	No	Yes	No	No	NA
Virginia	Yes	Yes (Mandatory)	No	Yes (Optional)	Yes	Yes	Yes (Optional)	Yes	Yes
Washington	Yes	No	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	No
West Virginia	Yes	Yes (Optional)	Yes	Yes (Mandatory)	No	Yes	Yes (Mandatory)	No	Yes
Wisconsin	Yes	No	Yes	No	Yes	Yes	Yes (Mandatory)	No	Yes
Wyoming	No	Yes (Optional)	Yes	No	Yes	Yes	Yes (Mandatory)	No	No

APPENDIX C: Summary of Potential Strategies for Government Payment Cards

STRATEGY	NUMBER OF CARDS/NUMBER OF ACCOUNTS	DETAILS
One card - one account	Cards: 1 Accounts: 1	The government payment card allows access to a single account. The account serves two purposes: to receive the government payment and to accept deposits from the benefit recipient. The account continues even if the recipient no longer receives the government payment.
One card - multiple accounts	Cards: 1 Accounts: 2 or more	The government payment card allows access to two or more accounts. Government cash payment goes to one account or group of accounts that is not reloadable with funds outside government programs. In addition, there are one or more separate accounts for non-government funds. The account holder decides at the point of sale which account to use.
Joint Marketing	Cards: 2 Accounts: 2	The government payment card offers access to one account or an amount of funds that may be held in a larger account. In addition, the government facilitates access to a separate account. In one approach, enrollment in the program includes an opportunity to obtain a second card that is a general purpose reloadable card (GPRC). In another, the government allows the payment card manager to market a separate GPRC product to those who receive government payments via prepaid cards.
Private cards	Cards: 1 Accounts: 1	A private card program manager seeks to serve government payment recipients and enrolls them with no formal cooperation with government programs. Cards may be freestanding, or they may be marketed under an agreement with a group allied with benefit recipients (e.g., AARP). Cards may be limited in purpose to payments, or they may be part of a larger bundle of services (e.g., bundled with a mobile phone contract).

APPENDIX D: Better Disclosure for Prepaid Cards

Prepaid cards have a significant weakness—their consumer protections do not serve current and prospective users well. Their fee disclosures in particular need improvement. Companies typically disclose their fees in a list or box, but their design, content, and location vary widely and can be more consumer-friendly. Card users need to be able to more easily determine the true cost of a prepaid card and compare different products before deciding which to purchase. To help consumers make informed choices, prepaid cards should be offered with a well-designed fee box.

The Center for Financial Services Innovation (CFSI), which has been following the development of prepaid cards since 2004, has designed a model fee disclosure box based on research on current fee disclosure practices for GPR prepaid cards, best practices in disclosure for a variety of financial and nonfinancial products, and data on current prepaid card fees.

XYZ Prepaid Card Co.

Prepaid Card Fee Summary

Fee Category	Fee Type	Amount
Total Cost of Setup:	Monthly Fee	\$X.00
	Activation	\$X.00
Add Money:	Direct Deposit	Free
	Cash (at a Store)*	\$X.00
Get Cash:	ATM*	\$X.00
	Store Cash Back	Free
Spend Money:	Signature	Free
	PIN	\$X.00
Information:	Call Customer Service	\$X.00
	Online/Mobile Information*	Free
	ATM Balance Inquiry"	\$X.00
Caution:	Replacement Card	\$X.00
	Inactivity	\$X.00
	ATM Decline	\$X.00

Other fees may apply, see terms and conditions for details.

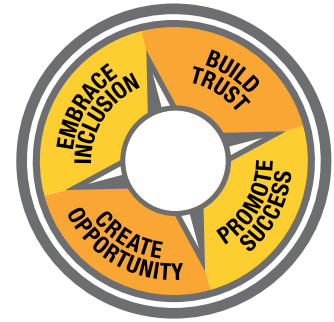
*Third party fees may apply.

www.XYZPrepaidCard.com

APPENDIX E: Compass Principles for Prepaid Cards

The U.S financial services industry faces several challenges, from increasing regulation to a fragmented marketplace where millions don't have what they need to manage their money in the short term while building assets for the future. Center for Financial Services Innovation, in partnership with a cross-section of industry participants, created the Compass Principles to help the industry take the lead in addressing these challenges.²⁰ The Compass Principles are aspirational guidelines that help providers work toward a vision for the future in which financial services are safe and actively contribute to improving people's lives:

1. Embrace Inclusion: Responsibly expand access.
2. Build Trust: Develop mutually beneficial products that deliver clear and consistent value.
3. Promote Success: Drive positive consumer behavior through smart design and communication.
4. Create opportunity: Provide options for upward mobility.



Working with an advisory group, CFSI used the Compass Principles to ask “what would a prepaid card look like if were designed around these principles?” The result was the Compass Guide to Prepaid, released in 2012.²¹ The Guide identifies Core Practices (standards for high quality cards), Stretch Practices (additional best practice ideas for providers looking to stretch beyond the basic requirements), and Next Generation Practices (these emphasize the need for new models that actively contribute to improving people's lives and deliver sustainable value to all consumers and providers).

For example, the Core Practices address issues of product functionality (FDIC insurance, loads, payments, and withdrawals), marketing and communications (fee disclosures, account term disclosures, and privacy policy), customer service and account information (access to balance and transaction history, customer service center, fraud and error resolution, and paper statements), and pricing design (pricing schedule and options, individual fees, and building a supportive customer-provider relationship).

²⁰ See the principles at www.cfsinnovation.com/content/compass-framework-and-tools.

²¹ Download the guide at www.cfsinnovation.com/content/compass-guide-prepaid.

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