U.S. House Subcommittee on Financial Institutions and Consumer Credit Hearing on:

"Examining Consumer Credit Access, Concerns, New Products and Federal Regulations"
July 24, 2012

By: G. Michael Flores, CEO
Bretton Woods, Inc.

Good morning. I'd like to thank the chairman and members of the subcommittee for the opportunity to testify today on a topic of growing concern to many in this room and one that I have followed closely over the past four years. My name is Michael Flores and I am CEO of Bretton Woods, Inc., a management advisory firm specializing in financial institutions including banks, credit unions and alternative financial services providers. With more than 30 years of experience, I have witnessed the evolution in the financial services marketplace. In 2008, this country woke to the worse economic crisis since the Great Depression. Four years later, I believe we have reached a decision point in how to deal with the credit needs of the 60+ million of Americans marginalized by the traditional banking model.

Based on my most recent study, "Serving Consumers' Needs for Loans in the 21st Century," I would argue that consumers, notably those in the low- to-moderate-income range, would stand to benefit from a new financial paradigm that recognizes the potential of alternative financial services providers. Many, but certainly not all of these consumers are part of the 60+ million Americans who are either unbanked or underbanked and who present a particularly complex challenge. In addition, there is a growing class of debanked or moderate- to-middle-income consumers who have chosen to leave traditional banking because of increased fees or because they need an unsecured personal loan, a product no longer offered by most traditional banks.

Access to credit has been an ongoing problem that has largely gotten worse with time. Difficulties for unbanked and underbanked consumers to obtain smaller-dollar loans have been the subject of increasing debate, including in a number of congressional hearings. But it's not just about low- to-moderate-income consumers because the fact is bank customers, many with what you and I would consider healthy bank accounts, are coming up short as well.

Since the 1980's, banks have used credit card lines, home equity lines and overdrafts to provide consumer credit. These are now less viable due to the poor economy and increased regulations. Overall, the community banks' focus on consumer lending has declined significantly since 1985 according to the FDIC, and during that period, unsecured installment loans all but disappeared from bank product suites due to profitability, risk and regulatory concerns.[1] Today, loans of under $5,000 are all but nonexistent and with good reason. Given their legacy cost structure and slow adoption of new technologies, banks aren't capable of making loans of under $5,000 profitably and so they don't. .

New federal regulations have played a role in adding to the burden of maintaining growth or at the least, stability and as a result, banks are examining their customer base. As my study details, the traditional banking business model relies on scale to be profitable. According to JPMorgan Chase, about 70 percent of customers with less than $100,000 in deposits and investments will be unprofitable following

[1] "Community Banking by the Numbers," FDIC Community Banking Research Project, Feb. 16, 2012

regulations that cap lenders' fees.[2] Given the level of investment required to succeed in the 21st Century, it is only rational that banks target the most profitable customer segments. The potential fall out is significant and will likely add to a further retraction in the credit market. Limiting consumer and small business credit has a detrimental impact on local economies.

Consumer financial services are clearly at a crossroad and I believe that a new financial regulatory structure is warranted. The answer points to the capabilities of alternative financial services providers. Many have invested in more efficient and cost effective technology, but costs associated with regulatory variations in 50 states naturally inhibit their ability to offer a range of standard products particularly in the $750 to $5,000 longer-term loan range. Differing states' regulations deny alternative financial services providers the ability to achieve scale thereby reducing costs now associated with operating in all 50 states. Studies of the impact of restrictive regulations in other industries, most particularly the lack of federal preemption, repeatedly show these regulations limit options and increase costs to consumers. There is room for both federal and state approved lenders as is the model for state and national chartered banks.

I would further argue that the lack of a standard product nationally, in and of itself, creates "disparate impact" on consumers. That is, nothing more than a state line can cause consumers to have to meet their specific credit needs with less than optimal and more expensive alternatives.

I understand and appreciate the impact of regulations on the financial services industry, and while not a policymaker, I close by suggesting that the simplest way to expand access to credit is to bring all alternative financial services providers under the tent of federal regulatory licensing and oversight.

My thanks to the chairman and the subcommittee for your time and I would be happy to answer questions. I am submitting my study for the record.

[2] "JPMorgan Sees Clients with Less Than $100,000 Unprofitable," Laura Marcinek, Bloomberg, Feb. 28, 2012

Serving Consumers' Needs for Loans in the 21st Century

June, 2012

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About Bretton Woods, Inc.

Bretton Woods, Inc. is a management advisory firm specializing in financial institutions. Since 1988, Bretton Woods, Inc. has provided value-added services to its clients by applying business, technology, payments and earnings improvement strategies.

The firm has worked with clients on payment strategies, unbanked and underbanked issues and trends from cash and checks to card and electronic transactions. The work with insufficient funds and overdraft fees in banks and credit unions includes credit advances on debit cards and other alternative financial services offerings.

The firm continues to work with commercial banks in re-engineering efforts to attain profitability in today's regulatory environment.

About the Author

G. Michael Flores, CEO of Bretton Woods, has more than 30 years of financial institution experience through his employment in banking as well as consulting. Flores' consulting work focuses on the areas of strategic planning, fee income strategies, payment systems, process improvement through enabling technologies and alternative financial services.

Flores has testified before House and Senate sub-committees on underbanked issues raised in white papers he authored on alternative financial services, spoken to industry groups and authored several articles for industry publications. He has been a faculty member with the Pacific Coast Banking School in Seattle, Washington and the Graduate School of Banking in Madison, Wisconsin where he taught Technology's Role in Community Banking curriculum for bankers in the graduate school.

Flores received a BBA in Accounting and Management from the University of Notre Dame in 1973 and in 1974 attended the Commercial Lending School at Georgia State University. He is a Certified Mediator with the Center for Dispute Resolution, Boulder, Colorado and also with the American Arbitration Association in Atlanta, Georgia.

Executive Summary

Bretton Woods, Inc. has been advising clients and researching payments and small dollar loan alternatives since 1999. The residual impact of the 2008 economic crisis and the ensuing legislative response have resulted in a financial services market unable to adequately meet the credit needs of an increasing number of Americans. An estimated 73 million low- to-moderate-income consumers are either unbanked or they are underbanked, defined as having a checking or savings account, but relying on alternative financial services such as payday loans, rent-to-own agreements or pawn. Less well understood is a growing class of "debanked" or moderate- to-middle-income consumers who have chosen to leave traditional banking because of increased checking account fees or they need an unsecured personal loan, a product no longer offered by most traditional banking institutions. Together, the unbanked, underbanked and debanked constitute an enormous challenge for regulators and the financial services industry moving forward.

This report looks at the historical perspective of the traditional banking system, explores the credit market including trends, options and providers and details the relationship of consumer credit to economic growth. A comprehensive examination confirms a void in current banking and alternative financial services, in particular for unsecured installment loans from $750 to $5,000, and concludes that there is a demonstrated need for a more efficient and innovative financial system.

Key Findings

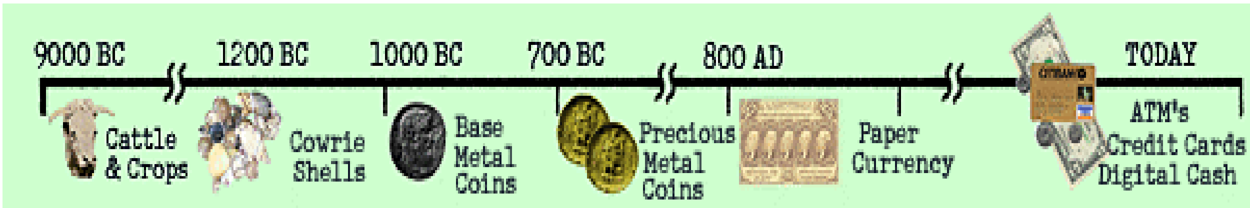
- **Consumer loans under $5,000 are unprofitable under the traditional banking model and as a result, the credit needs of low- to-moderate-income individuals and small businesses are no longer fulfilled by most community banks and credit unions.** Impediments include the industry's legacy cost structure, reliance on brick and mortar service delivery outlets and slow adoption of new technologies embraced by younger consumers.

- **Some alternative financial services providers have built more efficient and cost effective technology, but typically offer only low-dollar products which are limited in availability due to differing states' regulations.** Impediments include inconsistent product offerings among states, elimination of certain products based on state law, and increased compliance costs for companies operating in multiple states.

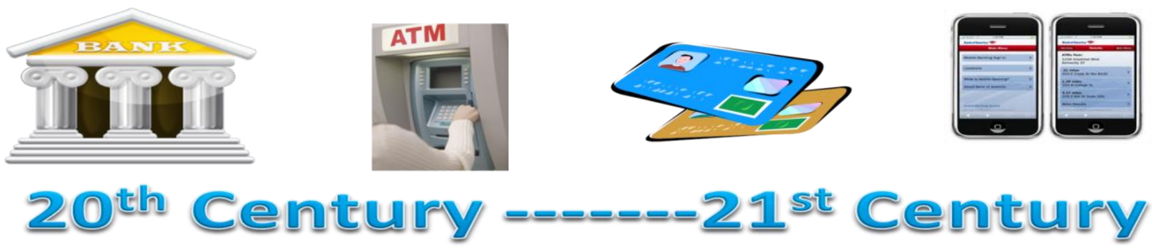
- **A new banking model for low- to-moderate-income consumers must be built to better serve this community which has been marginalized by traditional banks.** While alternative financial services providers may serve as a foundation for a new consumer banking model, the myriad of state regulations inhibit the introduction of a standard product. Studies of the impact of restrictive regulations, including the lack of federal preemption, repeatedly show these regulations limit options and increase costs to consumers.

State of Legacy Banking

Throughout the history of mankind, paying for goods and services has evolved from barter in various forms to the minting of coins and the production of currency to digitized money.



The advent of banks as a financial intermediary between savers and borrowers has also evolved from the stately marbled edifices to a more self-service model with ATM's, debit and credit cards and mobile banking.



Traditional banks are maintaining all of these service delivery elements at a significant cost. Adding to these costs are the additional regulatory burdens that considerably hamper community banks, those banks under $1 billion of assets. There are 6,290 commercial banks under $1 billion as of December 31, 2011[1]. They represent the following:

- **93% of all banks**
- **17% of all assets**
- 21% of all bank employees
- 20% of all loans
- 19% of total deposits
- 20% of interest income
- 28% of interest expense
- 14% of deposit service charges
- 18% of premises costs
- 13% of net operating income

FDIC data from December 31, 2011 indicate that banks under $1 billion of assets are much less efficient than larger banks. The efficiency ratio (noninterest expense, less the amortization expense of intangible assets, as a percent of the sum of net interest income and noninterest income) for banks over $1 billion is 60.26% versus 71.12% for banks between $100 million and $1 billion and 78.11% for banks under $100 million. In essence, it costs smaller banks more to generate a dollar of revenue.

[1] http://www2.fdic.gov/sdi/

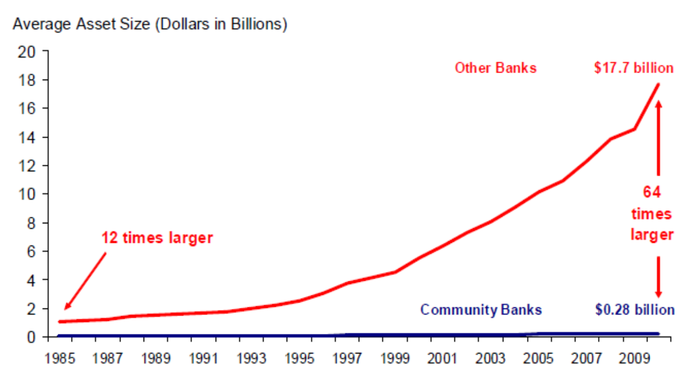
The following chart indicates the elements of profitability for these banks based on December 31, 2011 FDIC data.

	All Commercial Banks 12/31/2011 $ in 000's	All Commercial Banks - Assets less than $100M 12/31/2011 $ in 000's	All Commercial Banks - Assets $100M to $1B 12/31/2011 $ in 000's	All Commercial Banks - Assets more than $1B 12/31/2011 $ in 000's
Number of institutions reporting	6290	2143	3633	514
% of Total Banks	100%	34%	58%	8%
Yield on earning assets	4.29%	4.88%	4.88%	4.23%
Cost of funding earning assets	0.67%	0.95%	0.98%	0.64%
Noninterest income to earning assets	2.01%	1.12%	0.97%	2.12%
Noninterest expense to earning assets	3.54%	3.97%	3.43%	3.55%
Net operating income to assets	0.87%	0.54%	0.57%	0.90%
Return on assets (ROA)	0.90%	0.59%	0.61%	0.93%
Pretax return on assets	1.28%	0.71%	0.79%	1.33%
Return on equity (ROE)	8.06%	5.03%	5.91%	8.28%
Retained earnings to average equity (YTD only)	2.91%	0.22%	2.43%	2.98%
Efficiency ratio	61.19%	78.11%	70.12%	60.26%
Assets per employee ($ millions)	6.48	3.47	4.06	6.92
Cash dividends to net income (YTD only)	63.90%	95.70%	58.98%	63.99%
Equity capital to assets	11.12%	11.59%	10.58%	11.16%
Core capital (leverage) ratio	8.93%	10.94%	9.86%	8.82%
Tier 1 risk-based capital ratio	12.65%	17.33%	14.50%	12.43%
Total risk-based capital ratio	15.03%	18.46%	15.73%	14.93%

These community banks are at a clear disadvantage with higher interest expense, lower service charges and lower operating income than the 500+ banks over $1 billion. A clear indicator that larger banks benefit from scale is the amount of assets ($ million) supported by employees. For banks over $1 billion, one employee supports almost $7 million of assets versus $4 million of assets per employee for banks between $100 million and $1 billion, and $3.5 million of assets per employee for banks under $100 million.

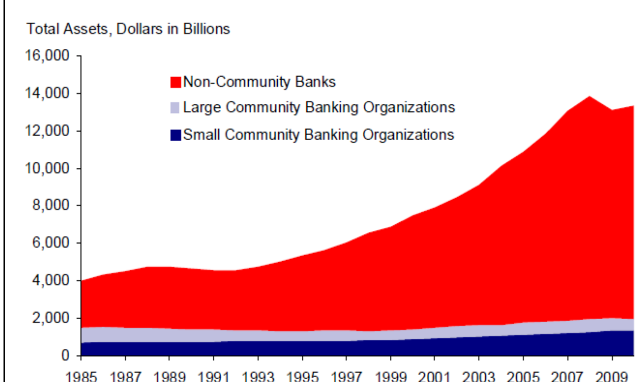
The disparity is even more profound when you consider that the top 50 banks represent .65% of all banks but control 65% of all deposits. Large banks were, on average, 12 times larger than community banks in 1985. The difference has grown to 64 times in 2010.

Community banks tend to be small, and the size disparity with other banks is growing.



Source: FDIC Community Banking Research Project

The total assets of non-community banks have grown much faster than those of community banks since the early 1990s.



Source: FDIC Community Bank Research Project

BearingPoint produced a white paper [2] on *"ARE YOU TRANSFORMING OR JUST TRANSACTING? THE MODEL FOR THE 21ST CENTURY RETAIL BANK".* The following table highlights the changes banks must pursue to survive:

STRATEGY AREA	20TH CENTURY	21ST CENTURY
CUSTOMER SEGMENTATION	• Customer relationship understood in relation to products held • Limited understanding of customer profitability	• Customer-oriented/structured institution providing full range of financial product on customer-defined basis (transaction to full-service) accessible to customers on their terms and requirements and with focus on customer service
CHANNEL	• Siloed channel with limited process or data integration • Employee interaction focused on servicing	• Multichannel delivery with human relationships/sales focus and automated servicing/support • Branch as retail and/or advisor function • Channel-integrated rather than siloed
SERVICE	• Priority on sales/efficiency rather than satisfaction • Disparate service between channels and products and disjointed problem resolution	• Enterprise service platform across channels with combination of automated and human service support based on customer preference, but with design to incentive automation
SALES	• Reactive/mass market sales focus • Focus on direct mail • Product focus, sales campaigns in branch • Uncoordinated between channels • Open loop between marketing and sales	• Development with sales/service role for all front-office staff with human resources/training/compensation linked to both customer satisfaction/sales • Automated origination to improve customer service (processing time) • Integration/coordination of marketing and sales process
PRODUCT	• Product differentiation focused on pricing • Slow time-to-market for new products	• Ability to bundle/wrap products with rapid time-to-market for new products and ability to offer customizable products
COMPLIANCE/ RISK	• Regulation-specific reporting • Manual/spreadsheet-based data analysis/ collection • Business-level risk systems	• Enterprisewide compliance-consistent processes/data management platform with automated reporting that can meet evolving compliance requirements and provides benefits to other functions • Consistent/top-down manageable process for sales (for risk management/compliance)
PAYMENTS	• Siloed payment systems by product • Manual processing	• Minimal paper/human interaction in payment and process (exceptions management) across checks and existing electronic payments, with access to payments across all channels
OPERATIONS	• Multiple points of data re-entry • Manual processes • No consolidation/central view of processes • Separation of operations center and channels	• Single point of capture/data entry • Automated processes • Enterprise content management allowing multisite processing • Consolidation view of operations/site/workforce optimization/workload balancing

Banks are trying to serve two constituencies. In addition to older customers who still want to use bank branches and paper transactions, banks are attempting to build a more virtual service delivery model for younger consumers. Many in the industry question the viability of community banks under $1 billion in assets.

[2] http://www.finextra.com/Finextra-downloads/featuredocs/BearingPoint_21st%20Century%20Retail%20Bank.pdf

Only the largest banks with the necessary resources will be able to make the changes outlined. The traditional banking business model clearly relies on scale to be profitable. Given the level of investment required to succeed in the 21st century, it is only rational that banks target the most profitable customers segments.

According to JPMorgan Chase & Co.[3]:

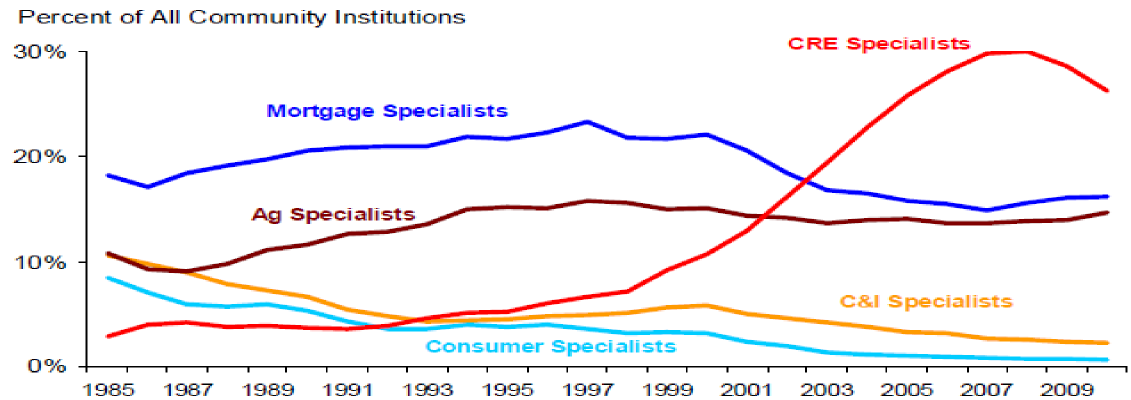
> "…said about 70 percent of customers with less than $100,000 in deposits and investments will be unprofitable following regulations that cap lenders' fees."
>
> The biggest U.S. banks are grappling with lost revenue from regulations that cap debit interchange fees and overdraft charges, making customers with low deposits more expensive for lenders to manage. JPMorgan, run by CEO Jamie Dimon, sees its greatest opportunity with affluent customers that have more relationships with the company.
>
> "Lost revenue has to be replaced with higher share of wallet and customer penetration," Maclin said. "You have to get your costs and where you spend your time, to the fullest extent possible, more in line with where the opportunity is."

[3] http://www.bloomberg.com/news/2012-02-28/jpmorgan-views-clients-with-less-than-100-000-to-invest-as-unprofitable.html

Consumer Credit

Since the 1980's banks have used credit card lines, home equity lines and overdrafts to provide consumer credit. Overall, community banks focus on consumer lending has declined significantly since 1985 according to the FDIC[4].

Change in percent share among main community bank specialty groups, 1985-2010



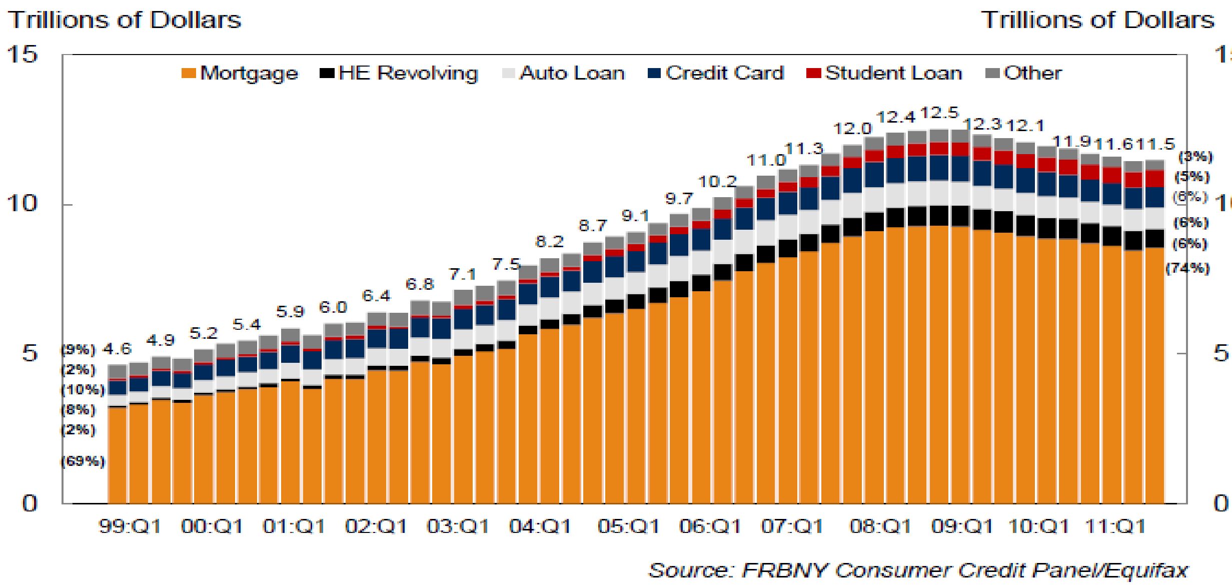
Source: FDIC Community Banking Research Project

During that period, unsecured installment loans all but disappeared from bank product suites due to profitability, risk and regulatory concerns.

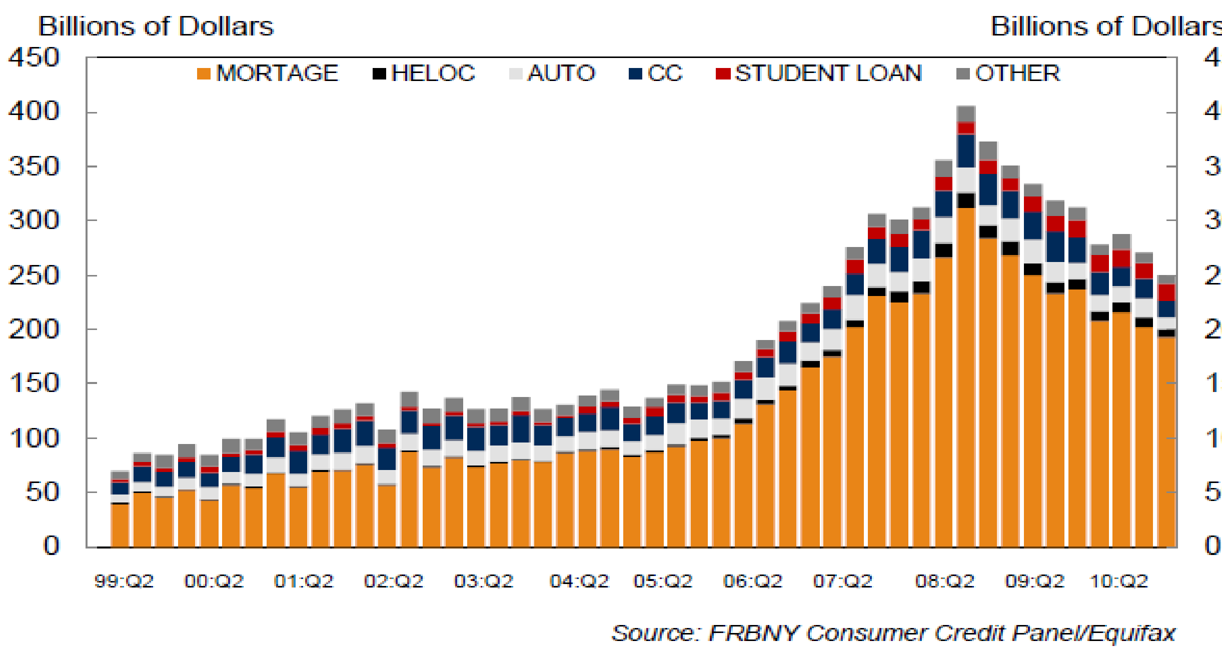
[4] http://www.fdic.gov/news/conferences/communitybanking/community_banking_by_the_numbers_clean.pdf

Trends in Unsecured Consumer Installment Credit

The following data from the Federal Reserve Bank of Richmond[5] depicts total debt balance and its composition from 1999 to 2011. While total consumer credit has more than doubled, unsecured consumer installment credit has fallen from 9% to 3% of the total.

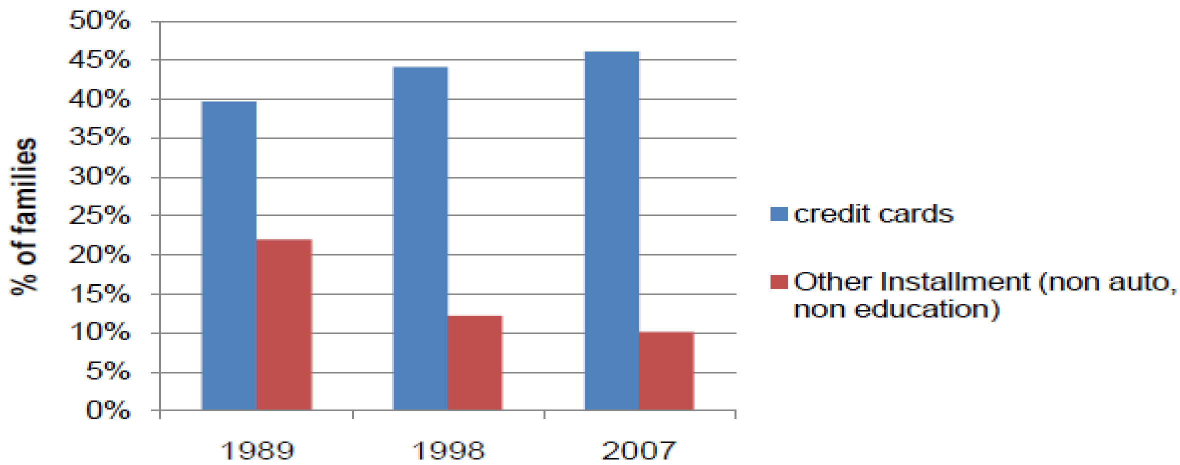


Additionally, delinquent balances by loan type for unsecured consumer credit have remained fairly stable.



[5] http://www.richmondfed.org/research/regional_economy/regional_view/macheras/2011/pdf/2011-07-19_macheras_slides.pdf

Unsecured installment credit has been supplanted by credit cards since 1989.



Source: Survey of Consumer Finance 2007 Chartbook

Types of Available Consumer Credit

The following outlines the types of available consumer credit. Auto and home loans are not included since the focus of this study is on loans for purposes other than the acquisition of longer term assets.

Need	Product	Collateral	Amount	Duration	Benefit	Risk	Availability
Unanticipated	Overdraft	Unsecured	< $500	Less than 30 days	Less expensive that bouncing a check	High cost for low dollar overdraft	From banks in all 50 states
Anticipated	Payday,	Unsecured	< $500	Less than 30 days	Immediate access and less expensive than an overdraft	Multiple rollovers	AFS providers in 31 states
Anticipated	Installment Loan	Unsecured, Closed end	$500 - $5000	Closed end – 6 – 36 months	Less expensive than short-term options	With appropriate underwriting, there are limited risks with this product	Very few banks and limited from AFS providers due to different state regulatory environments
Anticipated	Credit Card and Revolving Line of Credit	Unsecured, Open end	$500 - $5000	Open-ended	Less expensive than short-term options but may be more expensive than installment	Extended repayment and cost if minimum payments are made	From banks based on the credit score, lines and balances are increasing. This is not an option to many consumers with poor credit.
Anticipated	Pawn	Secured	Varied	Less than 30 days	Quick access	Loans amounts are a low percentage of collateral value. Potential loss of collateral	Widely available from AFS providers depending on state regulations
Anticipated	Title	Secured	Varied	Varied - Up to 44 months or more	Option for consumer with no access to unsecured installment credit	Limited amount based on value of collateral	From AFS providers in approximately 20 states

Credit card, bank overdrafts and home equity lines of credit have substantially replaced installment loans due to the more cost efficient means of delivering these types of credit and the tax advantage of home equity advances. Economists from the Federal Reserve noted "revolving credit, particularly credit card debt, has substituted for small installment loans because of its ease of use and availability…"[6]

Credit cards appear to be the primary source of low-dollar, unsecured credit for consumers, but not necessarily the best choice in some situations. That is, many consumers would prefer to match a loan for a specific need with a defined payback schedule. Credit cards make it too easy to default to the minimum payment and are subject to a change in terms – both which extend the cost of credit well beyond a fixed payment term.

FDIC Small-Dollar Loan Program

Most banks do not offer unsecured low-dollar consumer loans. In our consulting practice, we have advised banks since the 1990's to set a minimum loan amount that can profitably be offered to the consumer. Our break-even model indicates loans of $5,000 are the minimum loan amounts that can be profitable. The amount varies based on the unique cost structure of the bank. To address this issue, banks offered credit cards and overdraft programs to fill the need for unsecured consumer credit. Consumers with homes could use HELOCS (home equity lines of credit) for secured loans, but with the dramatic loss of real estate value, HELOCS are no longer a viable option for many.

In February 2008, the FDIC began a two-year pilot project to review affordable and responsible small-dollar loan programs in financial institutions. The pilot was a case study designed to illustrate how banks can profitably offer affordable small-dollar loans as an alternative to high-cost credit products such as payday loans and fee-based overdraft protection.

An excerpt from the report discusses the costs associated with offering this product:

"…pilot bankers indicated that costs related to launching and marketing small-dollar loan programs and originating and servicing small-dollar loans are similar to other loans. However, given the small size of SDLs and to a lesser extent NSDLs, the interest and fees generated are not always sufficient to achieve robust short-term profitability (emphasis added). Rather, most pilot bankers sought to generate long-term profitability through volume and by using small-dollar loans to cross-sell additional products."

In the longer term, *"About three-quarters of pilot bankers indicated that they primarily used small-dollar loans to build or retain profitable, long-term relationships with consumers and also create goodwill in the community. A few banks focused exclusively on building goodwill and generating an opportunity for favorable Community Reinvestment Act (CRA) considerations, while a few others indicated that short-term profitability was the primary goal for their small-dollar loan programs."*

It is clear that on a stand-alone basis these loans were not profitable to originate, underwrite and process.

[6] http://www.federalreserve.gov/boarddocs/rptcongress/creditscore/creditscore.pdf

This is consistent with our models that indicate that individual consumer loans under $5,000, depending on cost allocations, are unprofitable for the traditional bank to offer. Exhibit II depicts a model that only considers direct costs of origination and processing with no overhead allocation for systems, space, compliance and management. **The minimum loan amount is just over $5,000.**

Consumer Loan Activity

Key findings according to an Equifax press release[7] in July 2011 stated:

Auto

Auto loan originations rose nearly 17 percent year-to-date in April and are up nine percent month-over-month. While both banks and captive financiers are originating more auto loans, banks are being much more cautious in the subprime sector. Captive finance sources (e.g., Ford Motor Credit, etc.) issued almost 25 percent of new loans to buyers with scores under 600 in April. The comparable bank subprime number is about eight percent.

Credit Cards

Notable within the data is the rebound in the number of bankcard originations to subprime borrowers, with an 80 percent increase in originations for April 2011 vs. April 2010 alone. New subprime bankcard origination levels for January-April 2011 are up more than 66 percent over 2010 levels. This is of note when compared to the 63 percent YOY (Year over Year) decrease the industry witnessed for the same period from 2008 to 2009. Total new bankcard limits have risen as well, with increases of more than 27 percent (January - April 2011), and new subprime bankcard credit limits experienced an increase of 68 percent.

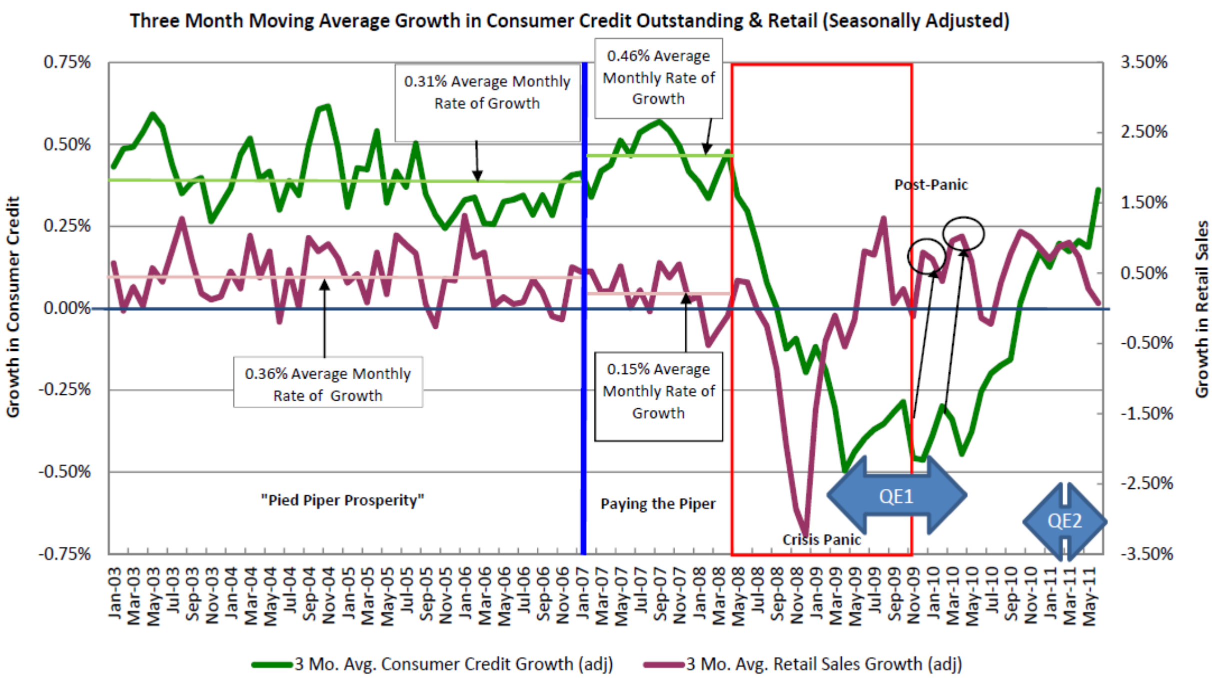
Consumer Finance

New consumer finance credit loans grew 3.5 percent year-to-date and two percent month-over-month in April, and - like bankcards and autos - show increases in subprime. In fact, loans to customers with scores below 599 - 41 percent - are up about two percent over 2010 and almost 10 percent over 2006.

[7] http://news.equifax.com/index.php?s=18010&item=97085

Relationship of Consumer Credit to Economic Growth

Daniel Alpert, Managing Director of Westwood Capital, LLC[8], analyzed the growth of consumer credit which is growing at the highest rate in the last decade. The following chart depicts the relationship trend between consumer credit and retail spending since January 2003.



Some would argue that that too much consumer credit is harmful to both the individual and to the economy, but access to credit is a necessity to most. Credit is useful not only when the individual's transaction demands are uncertain but also when the individual tries to plan purchases. Credit provides a tool against unanticipated changes to income or spending and for financing transactions where sales or other promotions can reduce the overall cost of a transaction.

Utilization of consumer credit could increase savings and provide consumers with the ability to purchase goods or services at an earlier time period or fulfill other needs when cash is not available.

Use of credit, savings or increased wages drive consumer spending. One argument is that excess leverage by consumers helped to fuel the financial crisis beginning in 2008. There are, however, economists who state that consumers' access to credit is the quickest way to spur economic growth. From a Reuters article dated January 9, 2012[9]:

> "Outstanding consumer credit increased by $20.37 billion during the month, the Federal Reserve said on Monday. That was the biggest gain since November 2001 and nearly three times the median forecast in a Reuters' poll.

[8] http://www.westwoodcapital.com/wp-content/uploads/2011/08/Back-to-the-Future-Again-080911.pdf
[9] http://www.reuters.com/article/2012/01/10/us-usa-economy-consumercredit-idUSTRE80823O20120110

"Revolving credit, which mostly measures credit-card use, increased $5.60 billion, a third straight monthly increase. 'Credit growth is a positive sign for the recovery in that it signals increasing demand and willingness to spend,' said Paul Edelstein, an economist at IHS Global Insight in Lexington, Massachusetts…"

Sizing the Market

Underbanked Individuals

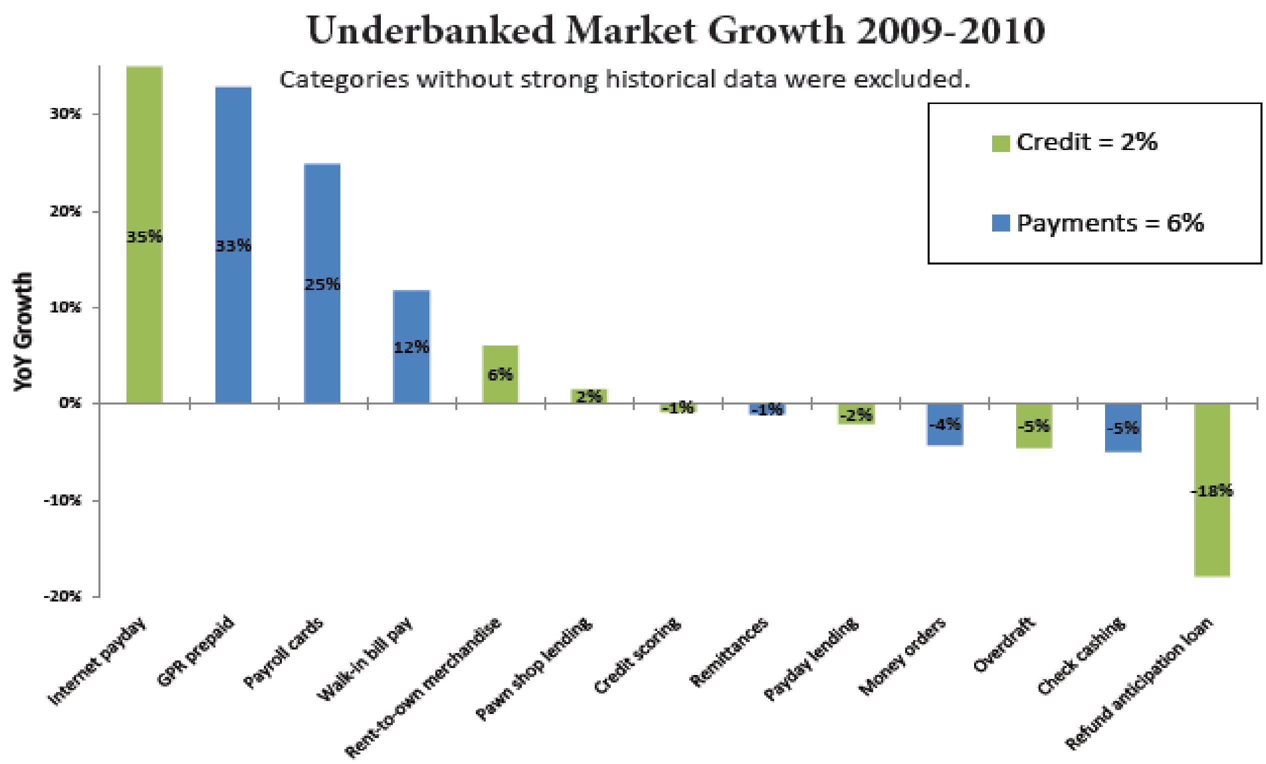
The most widely quoted metric for the number of unbanked and underbanked in the United States comes from the 2009 FDIC National Survey of Unbanked and Underbanked Households. It stated there are 9 million unbanked and 21 million underbanked. An update to this report is due to be released later in 2012. A report from Core Innovation Capital and CFSI[10] estimates the number of unbanked and underbanked to be 60 million. The U.S. Postal Service Office of Inspector General published a report[11] in October, 2011 that estimated 40 million households (73 million individuals) are either unbanked or underbanked.[12]

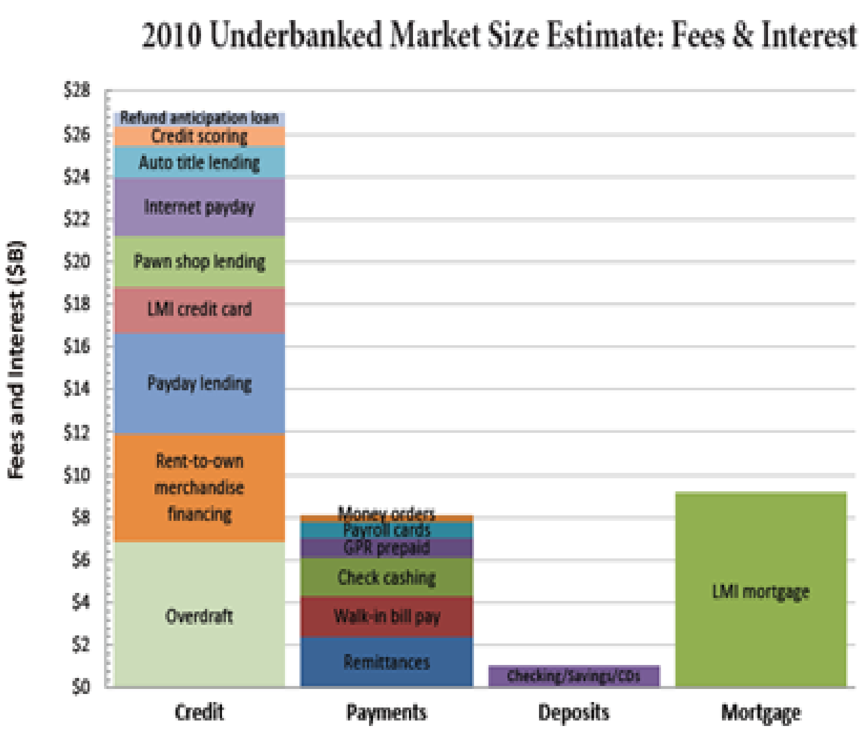
Data[13] developed by the Washington Credit Union League found:

- One unbankable baby born every 7 seconds
- One bankable/account-holding adult death every 13 seconds
- One unbankable international immigrant every 27 seconds
- Net gain of one unbankable person every 11 seconds or 2.8 million every year

[10] http://cfsinnovation.com/system/files/09-11,%20Marketscan_final.pdf
[11] U.S. Postal Service Office of Inspector General October 3, 2011
Digital Currency: Opportunities for the Postal Service RARC-WP-12-001
[12] http://www.uspsoig.gov/foia_files/RARC-WP-12-001.pdf
[13] http://www.slideshare.net/JosephSam/serving-the-unbanked-wcul-ppt

A report[14] by Core Innovation Capital and CFSI, *2010 Underbanked Market Size,* shows the annual growth of services used by the underbanked from 2009 to 2010.

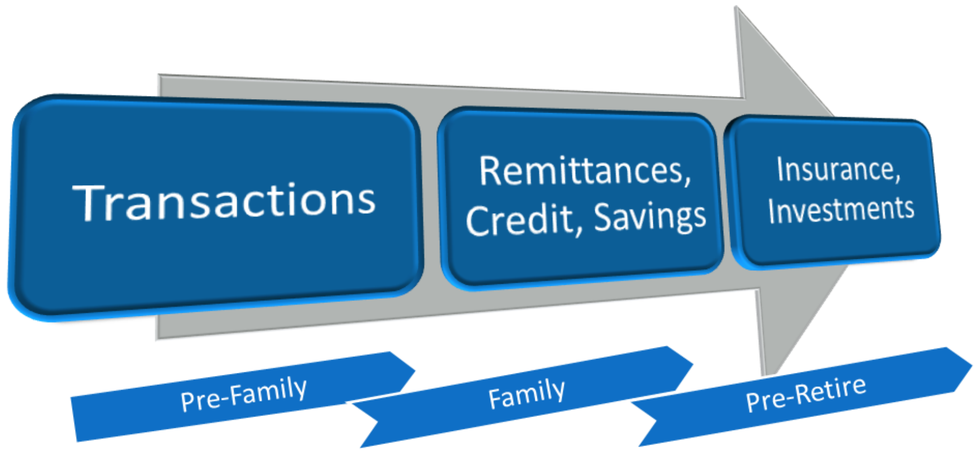




The credit category represents products and services that allow consumers to borrow funds on a short-term basis. The payments category is comprised of products and services that allow consumers to send funds, transact with funds, and convert funds into another form such as cash or a money order. The deposit category consists of traditional bank depository products. Mortgages have been placed in their own category because, although they function as a credit product, they can also enable consumers to build assets through equity accumulation.

[14] http://cfsinnovation.com/system/files/09-11,%20Marketscan_final.pdf

Financial Services Life Cycle



Many tend to think of moderate-income consumers in terms of individual services rather than a holistic view. That is, these consumers have needs for a variety of financial services and these needs tend to be cumulative over a lifetime.

A study[15], "The Regulation of Consumer Financial Products: An Introductory Essay with a Case Study on Payday Lending", with Howell Jackson, Brigitte Madrian, and Peter Tufano, Chapter 7 in Nicolas P. Retsinas and Eric S. Belsky eds. Moving Forward: The Future of Consumer Credit and Mortgage Finance, Brookings Institution Press, dated September 2010, quantifies the financial holdings by income strata.

The following charts depict families in the lower-to-moderate income strata whose holdings include transaction accounts, CD's, savings bonds, stocks, pooled investment accounts, retirement accounts and life insurance. Installment and other non-real estate consumer credit are the primary credit drivers for these income strata.

15 http://www.google.com/url?sa=t&rct=j&q=state%20regulators%20for%20the%20alternative%20financial%20services%20industry&source=web&cd=7&sqi=2&ved=0CGUQFjAG&url=http%3A%2F%2Fweb.hks.harvard.edu%2Fpublications%2FgetFile.aspx%3FId%3D602&ei=jdh5T7mZA8rl0QH_wdmWDQ&usg=AFQjCNHs0mFe2Z2ly9LeRgpp6KD1pYHFPg&cad=rja

TABLE 1. Financial Holdings of U.S. Families in 2007

Family characteristic	Transaction accounts	Certificates of deposit	Savings bonds	Bonds	Stocks	Pooled investment funds	Retirement accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
	Percentage of families holding asset										
All families	92.1%	16.1%	14.9%	1.6%	17.9%	11.4%	52.6%	23.0%	5.8%	9.3%	93.9%
By income percentile											
<20	74.9	9.4	3.6	--	5.5	3.4	10.7	12.8	2.7	6.6	79.1
20 to <40	90.1	12.7	8.5	--	7.8	4.6	35.6	16.4	4.7	8.8	93.2
40 to <60	96.4	15.4	15.2	--	14.0	7.1	55.2	21.6	5.3	10.2	97.2
60 to <80	99.3	19.3	20.9	1.4	23.2	14.6	73.3	29.4	5.7	8.4	99.7
80 to <90	100.0	19.9	26.2	1.8	30.5	18.9	86.7	30.6	7.6	9.8	100.0
90 to <100	100.0	27.7	26.1	8.9	47.5	35.5	89.6	38.9	13.6	15.3	100.0
	Median value of holdings for families holding asset ($1000s)										
All families	$4.0	$20.0	$1.0	$80.0	$17.0	$56.0	$45.0	$8.0	$70.0	$6.0	$28.8
By income percentile											
<20	.8	18.0	.5	--	3.8	30.0	6.5	2.5	100.0	1.5	1.7
20 to <40	1.6	18.0	1.0	--	10.0	30.0	12.0	5.0	86.0	3.0	7.0
40 to <60	2.7	17.0	.7	--	5.5	37.5	23.9	5.2	59.0	4.0	18.6
60 to <80	6.0	11.0	1.0	19.0	14.0	35.0	48.0	10.0	52.0	10.0	58.3
80 to <90	12.9	20.0	2.0	81.0	15.0	46.0	85.0	9.0	30.0	10.0	129.9
90 to <100	36.7	42.0	2.5	250.0	75.0	180.0	200.0	28.1	90.0	45.0	404.5

Source: Bucks, Kennickell, Mach and Moore (2009) from the 2007 Survey of Consumer Finances

TABLE 2. Financial Liabilities of U.S. Families in 2007

Family characteristic	Secured by residential property: Primary residence	Secured by residential property: Other	Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Percentage of families holding debt						
All families	48.7%	5.5%	46.9%	46.1%	1.7%	6.8%	77.0%
By income percentile							
<20	14.9	1.1	27.8	25.7	*	3.9	51.7
20 to <40	29.5	1.9	42.3	39.4	1.8	6.8	70.2
40 to <60	50.5	2.6	54.0	54.9	*	6.4	83.8
60 to <80	69.7	6.8	59.2	62.1	2.1	8.7	90.9
80 to <90	80.8	8.5	57.4	55.8	*	9.6	89.6
90 to <100	76.4	21.9	45.0	40.6	2.1	7.0	87.6
	Median value of debt for families holding debt ($1000s)						
All families	$107.0	$100.0	$13.0	$3.0	$3.8	$5.0	$67.3
By income percentile							
<20	40.0	70.0	6.5	1.0	--	3.0	9.0
20 to <40	51.0	42.0	9.8	1.8	1.3	4.0	18.0
40 to <60	88.7	68.9	12.8	2.4	--	4.0	54.5
60 to <80	115.0	83.0	16.3	4.0	5.1	5.3	111.3
80 to <90	164.0	125.0	17.3	5.5	--	5.0	182.2
90 to <100	201.0	147.5	18.3	7.5	17.3	7.5	235.0

Source: Bucks, Kennickell, Mach and Moore (2009) from the 2007 Survey of Consumer Finances.

Alternative Financial Services

It is clear that the traditional banking, with community banks and credit unions meeting credit needs of consumers and businesses funded with insured deposits, will not work for a growing number of consumers. Consider a National Bureau of Economic Research published paper[16], "Financially Fragile Households: Evidence and Implications," which found that approximately one-quarter of Americans report that they would certainly not be able to come up with $2,000 in thirty days.

It is our contention that banking services not just for the 60 million underbanked, but also for the moderate-income, debanked consumers, must begin with a clean slate. Alternative financial service providers have built a more efficient, cost effective, technology-driven model to serve their constituency, the moderate-income consumer.

World Acceptance Corporation, for example, reported in its 10Q SEC filing on December 31, 2011, that general and administrative costs as a percent of revenue was 48.7% (cost to generate a dollar of revenue which is equivalent to banks' efficiency ratio). Due to the risk inherent with these loans, however, its loss provision was 26.6% of revenue (note that World Acceptance operates in only thirteen states).

AFS providers must operate more efficiently because of the higher risk in the market they serve.

Effective Date 12/31/2011

• WORLD ACCEPTANCE CORPORATION 10-Q 12-31-2011 • EXHIBIT 31.1 • EXHIBIT 31.2 • EXHIBIT 32.1 • EXHIBIT 32.2 • XBRL INSTANCE DOCUMENT • XBRL TAXONOMY SCHEMA DOCUMENT • XBRL TAXONOMY CALCULATION LINKBASE DOCUMENT • XBRL TAXONOMY DEFINITION LINKBASE DOCUMENT • XBRL TAXONOMY LABEL LINKBASE DOCUMENT • XBRL TAXONOMY PRESENTATION LINKBASE DOCUMENT

	Three months ended December 31,		Nine months ended December 31,	
	2011	2010	**2011**	2010
	(Dollars in thousands)			
Average gross loans receivable [1]	**$ 1,003,584**	903,622	**956,723**	850,961
Average net loans receivable [2]	**733,613**	663,183	**700,266**	625,999
Expenses as a % of total revenue:				
Provision for loan losses	**26.6%**	25.4%	**22.7%**	22.3%
General and administrative	**48.7%**	48.7%	**49.1%**	49.3%
Total interest expense	**2.5%**	3.0%	**2.7%**	3.2%
Operating margin [3]	**24.7%**	25.9%	**28.1%**	28.4%
Return on average assets (trailing 12 months)	**13.4%**	13.4%	**13.4%**	13.4%
Offices opened or acquired, net	**12**	20	**53**	64
Total offices (at period end)	**1,120**	1,054	**1,120**	1,054

(1) Average gross loans receivable have been determined by averaging month-end gross loans receivable over the indicated period.
(2) Average loans receivable have been determined by averaging month-end gross loans receivable less unearned interest and deferred fees over the indicated period.
(3) Operating margin is computed as total revenues less provision for loan losses and general and administrative expenses, as a percentage of total revenue.

[16] http://www.nber.org/papers/w17072

By comparison, according to December 31, 2011 FDIC statistics, there are 2,143 banks under $100 million in assets that have an average efficiency ratio[17] (the cost to generate a dollar of revenue) of 78.11% and 3,633 bank between $100 million and $1 billion in assets with an efficiency ratio of 70.12%.

One common misperception is that alternative financial service providers are unregulated when, in fact, they are heavily regulated by the states in which they operate. Exhibit I, obtained from the American Financial Services Association (AFSA) and the Financial Service Centers of America, Inc. (FiSCA), lists the various state regulatory requirements for consumer loans, payday loans and check cashers.

The myriad of state agencies and regulations create the following:

- Inconsistent product offerings among states
- Elimination of certain products based on state laws
- Increased compliance costs for companies operating in multiple states

Our sampling of bank and consumer loan web sites indicates that there is a void in the market of unsecured installment loans, particularly loans under $3,000 with monthly repayment terms, not currently filled by either banks or alternative financial service providers. For example, the five largest banks that represent 38% of all deposits in the United States offer the following:

Bank	Unsecured Personal Loan Product
Bank of America[18]	Credit Card Only
Citibank[19]	Personal Loan - $500 - $50,000 (Must be an existing customer with other qualifying requirements)
JP Morgan Chase[20]	Credit Cards Only
US Bank[21]	Premier Loan - $3,000 - $25,000
Wells Fargo[22]	Personal Loan - $3,000 Minimum

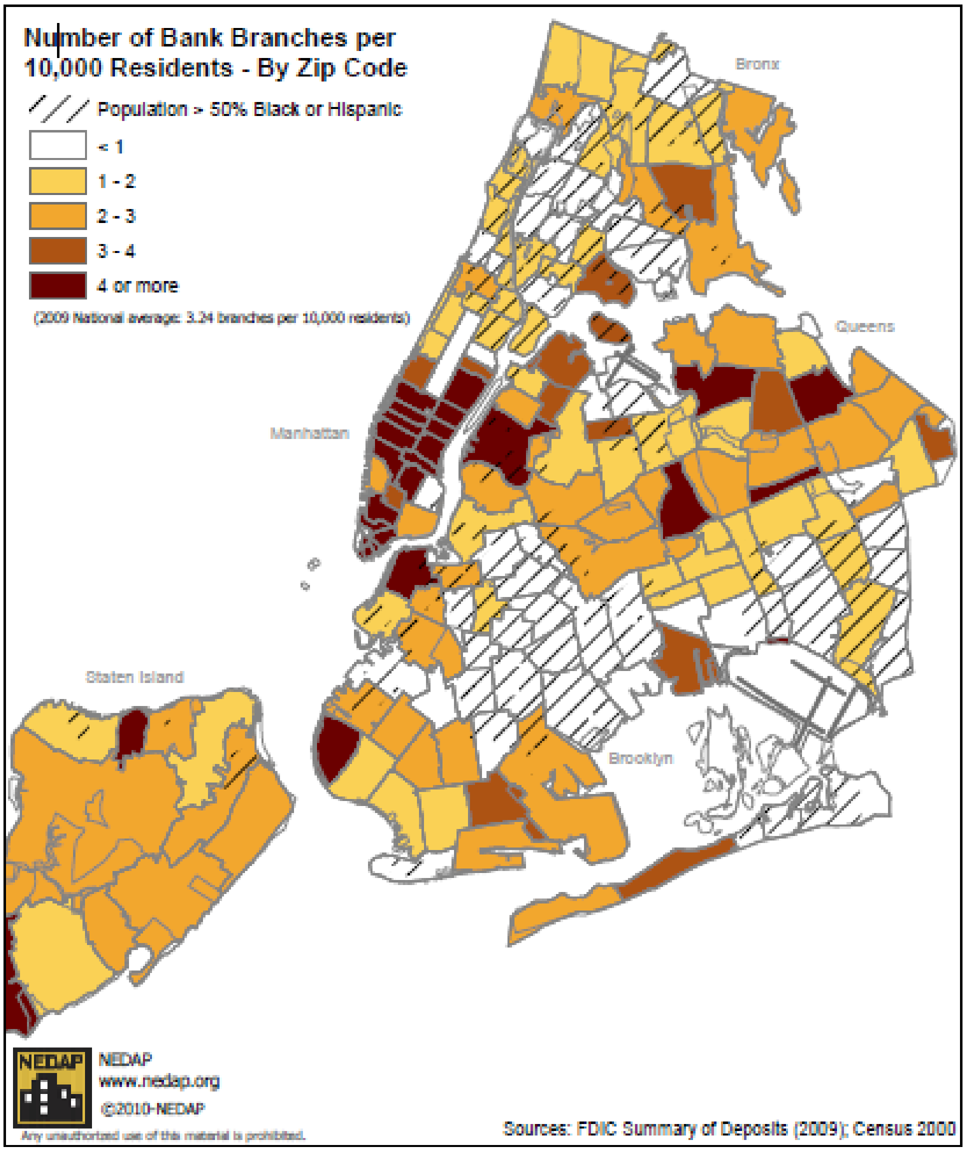
The reasons are straightforward – most banks cannot offer these loans due to their legacy cost structure and AFS providers are limited in their ability to provide a consistent product because of differing states' regulations.

[17] Noninterest expense, less the amortization expense of intangible assets, as a percent of the sum of net interest income and noninterest income.
[18] http://www.bankofamerica.com/vehicle_and_personal_loans/index.cfm?template=overview
[19] https://online.citibank.com/US/JRS/pands/detail.do?ID=LLInstallmentLoan
[20] https://www.chase.com/ccp/index.jsp?pg_name=ccpmapp/individuals/home/page/pf
[21] http://www.usbank.com/loans-lines/unsecured/premier-loan.html
[22] https://www.wellsfargo.com/personal_credit/products/options/unsecured_loan

Also, banks have moved out of the neighborhoods on the low- to-moderate-income consumer as depicted in this map of the New York metro area[23].

Absence of Bank Branches in Communities of Color

New York City (2009)



A report[24] from The Financial Services Roundtable, "*The Compliance Function in Diversified Financial Institutions",* dated July, 2007 is an excellent study in the analysis of the burden of sometimes conflicting regulations with unclear standards and expectations as well as lack of coordination among the agencies.

One excerpt clearly defines the issue:

[23] http://www.nedap.org/programs/documents/2009BankBranches.pdf
[24] http://www.fsround.org/publications/pdfs/ComplianceFunctioninDiversifiedFinancialInstitutions.pdf

> *Congress should consider moving toward a more productive form of federalism which properly balances state and federal interests.*
>
> *Uniform national standards and preemption of state laws should be considered in certain areas in order to allow financial services institutions to operate on an interstate basis without having to comply with multiple, conflicting laws. Any national standard enacted should ensure that consumers are adequately protected.*

Credit Unions have been touted as the vehicle to serve moderate income consumers. They still enjoy a tax advantage over commercial banks but increased compliance costs and lack of scale imperil their ability to adequately serve the consumer.

An article[25] in the Credit Union Times dated April 12, 2012 that recapped a meeting of the Credit Union Association of the Dakotas stated:

> "…at a Sioux Falls roundtable, a string of top managers from South Dakota credit unions and small banks complained that the 'mountain of new regulations-18,000 pages over the past three years - coming out of Washington D.C.' is driving numerous mergers of smaller institutions unable to bear the cost.
>
> "'During 2011 we saw five credit unions--almost 10% of the total-- involved in mergers and in each of the five mergers, management and volunteers cited regulatory burden as a primary reason to merge,' declared Schmidt who also serves as the state's chairman of CUAD's Governmental Affairs Committee.
>
> "'I am sure that it isn't a shock to you Mr. Cordray or anyone else at the CFPB that credit unions are subject to substantially more regulation now than just a few years ago but what I think might surprise you is that of the 46 credit unions left in South Dakota, 24--more than half--have six employees or less,' said Schmidt. 'The wave of new regulations has overwhelmed the staffs of these small credit unions prompting them to look for mergers,' he said."

While there is a place for low-dollar, short-term loans, the missing link are those personal, unsecured loans up to $5,000 with a term up to 36 months and monthly payments at a reasonable rate. Since most banks are not offering these loans, alternative financial service providers are filling the gap based on individual state regulations.

There is an opportunity either through strategic alliances or through vertical integration, for AFS companies to become a one stop shop for the financial services needs of underbanked and debanked consumers. Bretton Woods recommends that options be reviewed to provide better access to installment loan credit.

Role of Technology

Financial intermediaries act as the proverbial "middleman" by bringing together those with surplus funds who want to lend and those with a shortage of funds who want to borrow.

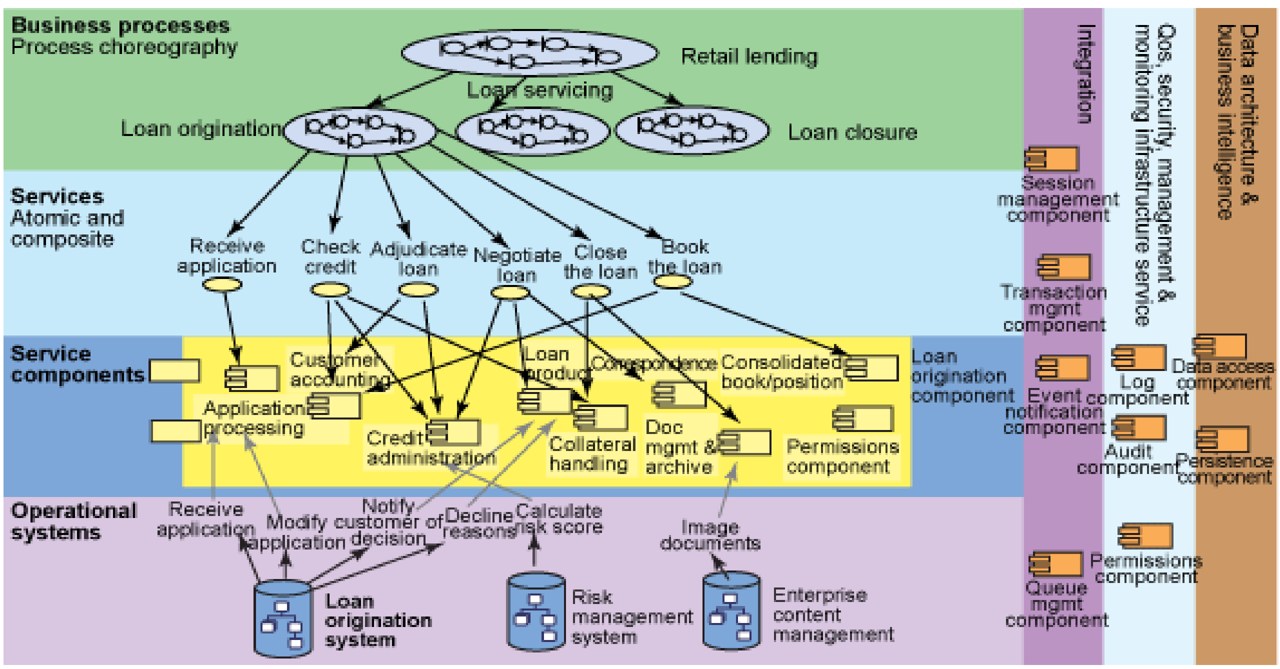
[25] http://www.cutimes.com/2012/04/12/dakota-credit-unions-air-compliance-gripes-at-spec?ref=hp

The bank, with its physical presence, provided a safe and secure facility for the deposit of funds as well as the knowledge of risk management to underwrite credit applications from those in need of loans.   Banks also serviced these loans by processing payments and collecting delinquent accounts.

The risks to this model are new enabling technologies. That is, the ability to match those with funds to those in need of credit. There are a number of fledgling entrants into this ecommerce space and the growth and acceptance of peer-to-peer lending will very much depend on the positive (or lack thereof) experience of the participants.

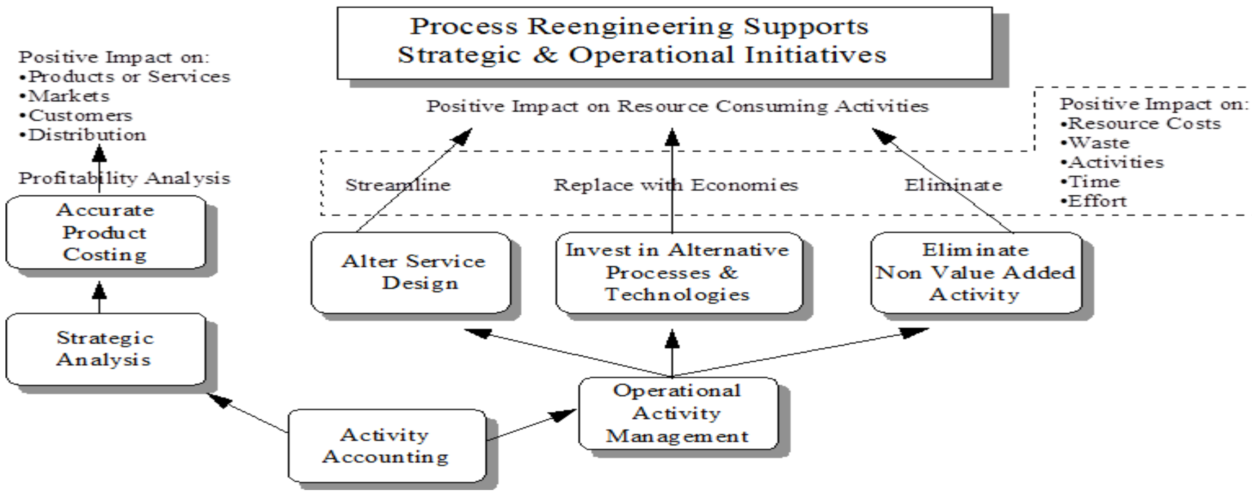
For the traditional banking system to succeed, it must embrace these new technologies. However, embedded processes, legacy technologies and cultural inertia can dramatically slow adoption.

A typical consumer loan origination process can look like the following[26]:



Any familiarity with Six Sigma or Lean Process methodologies allows one to visualize a process flow and identify tasks and activities that either do not add value or can be automated for efficiency.

26 http://www.ibm.com/developerworks/websphere/techjournal/0809_col_simmons/0809_col_simmons.html



New technologies can significantly simplify the process and eliminate many human interventions.

Alternative Financial Service providers are typically not hampered with these constraints. An equally important issue is the industry's knowledge and understanding of its clients and its culture to provide service that a typical bank does not support. This is represented in a study [27]by the Kansas City Fed, *"A Study of the Unbanked & Underbanked Consumer in the Tenth Federal Reserve District"* dated May 2010:

> "…Participants reported turning to retailers before banks due to simpler identification requirement, more transparent pricing, no hidden fees or penalties and immediate funds availability…"

Another study[28], *"Public Policies to Alter the Use of Alternative Financial Services among Low-Income households"* by Rebecca M. Blank, University of Michigan and Brookings Institution in March 2008 stated:

"Formal financial institutions provide services that are ill-fitted to the financial needs of low-income households. About 40 percent of payday loan recipients have bank accounts, suggesting that their payday loan provides a service that is not available from their bank (Elliehausen and Lawrence, 2001). About half of payday loan recipients claim to have considered a bank loan; many of these said that the payday loan involved an easier process; some also cited the convenient location of payday providers. Short-term loans to lower-income customers are simply not available through many local banks…"

[27] http://www.fdic.gov/about/comein/KCfed.pdf
[28] http://www.brookings.edu/~/media/Files/rc/papers/2008/0416_low_income_blank/0416_low_income_blank.pdf

The Future

Consumer financial services are clearly at a crossroad. Traditional banks have marginalized the low- to-moderate-income consumer and the myriad of state regulations inhibit alternative financial service providers to offer a standard product, achieve scale and reduce costs by operating in all 50 states in a consistent manner.

Studies of the impact of restrictive regulation at a local or regional level repeatedly show these regulations limit options and increase costs to the consumer. For example, a research report, "*The Economic Impact of Eliminating Preemption of State Consumer Protection Laws*", from the JOURNAL OF BUSINESS LAW, 2009[29] states:

- Preemption generates many clear economic benefits for banks and their customers.
- Uniform national laws, and the court and regulatory determinations pursuant to them, have been used as a device to open markets, thwart state-sponsored protectionist measures, reduce the price of credit, increase the availability of credit, and increase the efficiency of national banks. Consumers, small businesses, and the U.S. economy have been the ultimate beneficiaries.
- Critics of preemption are misguided in their attempts to link instances of predatory lending associated with the subprime crisis to federal preemption of state consumer protection laws. The vast majority of subprime loans at issue were originated by finance companies that have been outside of the purview of federal bank regulation but subject to state financial regulation. Concerns that preemption risks the dissolution of the dual banking system are also misguided.
- Case studies from the U.S. wireless and wine industries provide empirical evidence that the imposition of uniform, national regulations for interstate commerce increases economic efficiency. The implication is that any business, including banking, that crosses state boundaries should be regulated at the national level.
- From a policy perspective, elimination of preemption would jeopardize the significant economic benefits created by a uniform regulatory environment. However, preemption does not imply a laissez faire approach to regulation of the financial industry: advocating for preemption is not the same as advocating for deregulation. Policymakers should create new federal rules for the problem areas while taking advantage of the gains uniform national standards can offer the lending industry and the economy.

Bretton Woods believes that a new banking model for the low- to-moderate-income consumer must be built to better serve this community. Some community banks may be able to restructure their costs and offer solutions for this market but that is only possible with management making a commitment and possibly foregoing more profitable products and services. Many alternative financial services providers are narrowly focused on a few products and do not operate on a national level. AFS providers have built a more cost effective business model and may serve as a foundation for a new consumer banking model.

[29] http://www.aba.com/NR/rdonlyres/71949FE8-BA04-40B8-BC61-AF9F612C679A/63659/Preemption_finalv1.pdf

Exhibit I – AFS Regulators

Small Loans

Regulated Negotiated Rate States	Rate Per $100 States Add-on Interest	Band-Based States	Credit Code Or "Insurance States"	Payday States	Loan Shark/Unlicensed
Characteristics					
For small loans (<$2,ooo) no state imposed interest rate caps	X% per $100 per year Ancillary products prohibited	"What you see is what you get" Generally, ancillary products prohibited "If X is the loan amount, then you pay Y per month"	Flat rate of X% per month plus ancillary products (e.g. insurance) Requires sale of ancillary products to achieve break-even or better	Rate limits unrealistic for small loans which results in no installment lending Only alternatives are payday, pawn or loan sharks	Rate limits are unrealistic for small loans which results in no installment lending Payday lending prohibited Loan sharks or unlicensed internet lending are only alternatives for small loans
Delaware	Hawaii (Discount)	Alabama	Alaska	Arizona	Arkansas
Idaho	Pennsylvania (Discount)	Colorado	Florida	California	Connecticut (Discount)
Illinois	Texas (Add-on)	Oklahoma	Georgia	Washington, D.C.	North Carolina
Missouri		Tennessee	Iowa	Indiana	Ohio
Montana			Kentucky	Kansas	Oregon
Nevada			Louisiana	Massachusetts	
New Hampshire			Maine	Michigan	
New Jersey			Maryland	Nebraska	
New Mexico			Minnesota	New York	
North Dakota			Mississippi	Rhode Island	
South Carolina			Oklahoma	Vermont	
South Dakota			South Carolina	Virginia	
Utah			West Virginia	Washington	
Wisconsin			Wyoming		

http://www.afsaonline.org/state_government_affairs/sga_resources.cfm?shownewfldr=y&cid=2&fldrid=22&pfldrid=0

Payday Loans

State Legislation	Permitted Fees	Permitted Period	Maximum Amount of Advance	Rollovers	Mandated Cooling Off Period	Statutorily Mandated Extended Repayment Option	Database Requirement
Alabama AI ST § 5-18A-1 et seq.	17.5% of the amount advanced	Min. of 10 days and max. of 31 days	$500	Limited to one	Next business day after rollover is paid in full	After rollover, if customer unable to pay, lender may offer extended repayment option of 4 equal monthly installments of remaining balance, but repayment option is mandatory if commencing legal action	State mandatory third-party database (no exclusive provider of database services) used to verify outstanding transactions do not exceed $500
Alaska AK ST § 06.50.010 et seq.	$15 per $100 advanced, plus max. of $5 nonrefundable origination fee	Min. of 14 days	$500	Limited to two	No	Lender must attempt in good faith to contact customer re: delinquency and offer payment plan (not exceeding 6 months) prior to assigning account to collection agency or initiating legal action; at least 5% is due when payment plan is signed	None
California CA FIN §23000 et seq.	15% of the face amount of the check	Max. of 31 days	$300 (max. amount of check)	Prohibited	None	For no additional fee, lender may may allow an extension of time, or a payment plan, for repayment of an existing loan	None
Colorado CO ST §5-3.1-101 et seq.	Finance charge of 20% on the first $300 and 7.5% on amount greater than $300; interest rate of 45% per annum (prorated refund is due to customer if loan is prepaid); monthly maintenance fee for each outstanding loan not to exceed $7.50 per $100 loaned (max. of $30); may charge an additional finance charge of 45% APR on a renewed loan	Min. of 6 months	$500	No limit, except the total amount financed cannot exceed $500 and there is at least a 30 day waiting period between loans	30 days	None	None
Delaware DE ST TI 5 §2227 et seq.	Rate of loan determined by parties	Max. of 59 days	$500	Limited to four	None	Permits borrower to enter into a workout agreement following no more than 4 rollovers	None
Florida FL ST §560.401 et seq.	10% of the amount of advance + max. $5 verification fee	Min. of 7 days and max. of 31 days	$500	Prohibited	24 hours	Lender must provide borrower with a grace period of an additional 60 days after original termination date without additional charge; borrower also required to meet with credit counseling agency	Industry-wide database
Hawaii HI ST §480F-1 et seq.	15% of the face amount of the check	Max. of 32 days	$600 (including fee)	Prohibited	None	None	None
Idaho ID ST §28-46-401 et seq.	Rate of loan determined by parties	Term of loan determined by parties.	$1,000	Limited to three	None	None	None
*Illinois 815 ILCS 122/1-1 et seq.	$15.50 per $100 loaned	Min. of 13 days and max. of 45 days	$1,000 or 25% of the consumer's gross monthly income, whichever is less	Prohibited	7 days if consumer is indebted on 1 or more loans for more than 45 days; if consumer is on a repayment plan, 14 days after the expiration of the repayment plan and payment of all outstanding loans	If customer has 1 or more outstanding loans after 35 days, a repayment plan is available under which he/she has at least 4 equal installments over a max. of a 90 day period (with a min. of 13 days between installments) to repay the loan without additional fees or charges. Borrower has until 28 days after the default date of the loan to request a repayment plan	Industry-wide database
Indiana IN ST 24-4.5-7-101 et seq.	15% on first $250 of the principal; 13% on amount greater than $250 up to and including $400; 10% on amount greater than $400 up to and including $550	Min. of 14 days	$550, subject to CPI change (cannot exceed 20% of monthly gross income, including fees)	Prohibited (If a loan is paid in full, a subsequent loan is not a rollover)	7 days after 5th consecutive loan is paid in full	If a borrower enters into an initial small loan followed by three consecutive loans, the lender must offer an extended payment plan that allows for the outstanding small loan to be paid in at least 4 equal installments over a period of not less than 60 days	Regulator instituted, mandatory 3rd party database
Iowa IA ST § 533D.1 et seq.	15% of the check on 1st $100; 10% on subsequent $100 increments	Max. of 31 days	$500 (max. amount of check)	Prohibited	Next day if total of amount loan repaid and new loan are greater than $500	None	None
Kansas KS ST §16A-2-404 et seq.	15% of the amount of cash advance	Min. of 7 days and max. of 30 days	$500	Prohibited	None	None	None
**Kentucky KY ST §286.9-010 et seq.	$15 per $100 on face amount of check.	Min. of 14 days and max. of 60 days	$500 max. loans proceeds per customer industry wide (no more than 2 loan transactions)	Prohibited	None	None	Industry-wide database
Louisiana LA R.S. 9:3578.1 et seq.	16.75% of the face amount of the check ($45 maximum); max. $5 documentation fee per transaction can be collected to cover the actual cost incurred by the lender	Max. of 30 days	$350	Prohibited, but can accept part. pmt. of 25%+ fee and then enter into new agreement	None	None	None
Michigan M.C.L.S. 487.2121 et seq.	15% on 1st $100 of the transaction; 14% on 2nd $100; 13% on 3rd $100; 12% on 4th $100; 11% on 5th and 6th $100;	Max. of 31 days	$600	Prohibited	None	Customer eligible for plan if unable to pay 8th loan with any licensee in any 12 month period; lender must advise borrower of repayment option when it is available	Industry-wide database
Minnesota MN ST §47.60	$0-$50 ($5.50 fee), $51-$100 (10%), $101-$250 (7% or $10 min.), $251-$350 (6% or $17.50 min.), plus $5 administrative fee	Max. of 30 days	$350	Prohibited	None	None	None
Mississippi (thru 12/31/11) MS ST §75-67-519	18% of the face amount of the check	Max. of 30 days	$400 (max. amt. of the check)	Prohibited	None	None	None
Mississippi (Effective 1/1/12) MS ST §75-67-519	$20 per $100 of amount advanced up to $250; $21.95 per $100 for amount advanced greater than $250 up to $500	Min of 28 days on loans more than $250 up to $500; max. of 30 days	$500, including fees	Prohibited	None	None	None
Missouri MO ST 408.500 et seq.	Total fees, including rollovers, cannot exceed 75% of initial loan amount	Min. of 14 days and max. of 31 days	$500 (max. amount outstanding to the lender)	Limited to six, but borrower must reduce principal by at least 5% with each rollover	None	None	None
Nebraska NE ST §45-901 et seq	$15 per $100 on face amount of check	Max. of 34 days	$500	Prohibited	Same day transaction with same lender not allowed unless lender can verify that prior loan was completed	None	None

State Legislation	Permitted Fees	Permitted Period	Maximum Amount of Advance	Rollovers	Mandated Cooling Off Period	Statutorily Mandated Extended Repayment Option	Database Requirement
Wisconsin W.S.A. 138.14	Rate of loan determined by parties	Term of loan determined by parties	$1,500 or 35% of borrower's gross monthly income, which is lower (inclusive of loans from more than 1 lender)	Limited to one	24 hours	At the end of the loan term, lender must offer the customer the opportunity to repay the outstanding balance of the loan in 4 equal installments with due dates coinciding with the customer's pay period schedule	Industry-wide database
Wyoming WY ST §40-14-362 et seq.	greater of $30 or 20% per month on the principal balance of the check	One calendar month	No statutory cap	Prohibited	None	None	None

Check Cashing

STATE	STATUTORY CITATION	PERMISSIBLE CHECK CASHING FEES				LICENSE OR REGISTRATION REQUIRED	NOTABLE EXEMPTIONS TO REGULATION
		Public Assistance/ Social Security Checks/ Other Government Issued Checks	Personal	Payroll/Other Checks	Statutorily Authorized Account Set-up/Membership Fee		
Arizona	Ariz. Rev. Stat. §44-1361	3% of the face amount of the payment instrument or $5, whichever is greater, for cashing any payment instrument issued by an agency of the United States or of Arizona or any political subdivision of the United States or of Arizona.	No cap.		None.	A license or registration are not required.	Check casher means any person who engages in the business of cashing payment instruments more than 10 times in any calendar year and who receives compensation of at least $500 during any 30 day period for cashing payment instruments.
California	Cal. Civ. Code §1789.30	3% with valid identification for government checks, or 3.5% without identification, or $3, whichever is greater.	12% of the face value of a personal check.	3% with valid identification for payroll or government checks, or 3.5% without identification, or $3, whichever is greater.	Permitted to charge an amount not greater than $10 to set up an initial account and issue an optional identification card.	A permit is required.	The law does not apply to a retail seller engaged primarily in the business of selling consumer goods, including consumables, to retail buyers that cash checks or issue money orders for a fee not exceeding $2 as a service to its customers that is incidental to its main purpose or business.
Connecticut	Conn. Gen. Stat. §36a-580	1% for state drawn checks payable within the state to recipients of public assistance.	2% or $1, whichever is greater.		None.	A license is required.	The law does not apply to businesses that do not charge more than .50¢ for cashing a check, draft or other instrument.
Delaware	Del. Code Ann. Tit. 5 §2701	2%, or $4, whichever is greater, for cashing a check, draft or money order.			None.	A license is required.	The law does not apply when checks, drafts or money orders are cashed by any person as an incident to the conduct of any other lawful business where not more than 10¢ is charged for cashing each check, draft or money order.
Florida	Fla. Stat Ann. §560.303	3% or $5, whichever is greater, if payment instrument is for state public assistance or social security.	10% or $5, whichever is greater, for personal checks.	5% of the face amount of the payment instrument, or $5, whichever is greater; 10% or $5, whichever is greater for money orders.	None.	A license is required.	The law does not apply to persons engaged in the cashing of payment instruments that have an aggregate face value of less than $2,000 per person per day and that are incidental to the retail sale of goods or services whose compensation for cashing payment instruments at each site does not exceed 5% of the total gross income from the retail sale of goods or services by such person during the last 60 days.
Georgia	GA. Code Ann. §7-1-700	3% or $5, whichever is greater, for state public assistance or social security payable to the bearer of the check.	10% or $5, whichever is greater, for personal checks.	5% of the face amount of the check or draft or $5, whichever is greater; 10% or $5, whichever is greater for money orders.	None.	A license is required.	A business may register (rather than be licensed) as a check casher if it engages in cashing checks, money orders, or other drafts for a fee limited to the greater of $2 or 2% of the face amount of the check, whichever is greater. A registered casher of checks is not permitted to advertise its check cashing services.
Hawaii	Haw. Rev. Stat. §480F-1	3% of face amount of the check or $5, whichever is greater, for state public assistance or social security payable to the bearer of the check.	10% or $5, whichever is greater, for personal checks.	5% or $5 of face amount, whichever is greater, for all other checks; 10% or $5, whichever is greater for money orders.	Limit of $10 to set up an initial account and issue an optional membership or identification card.	A license or registration is not required.	The law does not apply to any person who is principally engaged in the bona fide retail sale of goods or services, and who, either as incident to or independent of the retail sale or service, from time to time cashes items for a fee or other consideration, where not more than $2, or 2% of the amount of the check, whichever is greater, is charged for the service.
Illinois	815 Ill. Comp. Stat. Ann. §315/2; 38 Ill Adm. Code 130.30	1.4% of face amount plus a service charge of $1 on all checks $100 or less; 2.25% on checks greater than $100.	1.4% of face amount plus a service charge of $1 on all checks $100 or less; 2.25% on checks greater than $100.	1.4% of face amount plus a service charge of $1 on all checks $100 or less; 2.25% on checks greater than $100.	None.	A license is required.	A merchant may offer check cashing services, in the course of such business and only as an incident thereto, and may charge fees for each check cashed provided that the check cashing services are incidental to the main business of the merchant. The merchant cannot charge fees in excess of the greater of .50¢ or 1% of the face value of the check cashed.
Indiana	Ind. Code §28-8-5	5% of the face amount or $5, whichever is greater.	10% of the face amount of a personal check or $10, whichever is greater.	5% of the face amount or $5, whichever is greater, for all other checks.	None.	A license is required.	The law does not apply to person principally engaged in the bona fide retail sale of goods or services if: (1) the person, either incidental to or independent of a retail sale of goods or services, from time to time cashes checks; and (2) the consideration charged for cashing checks does not exceed $5.
Kentucky	Ky. Rev. Stat. Ann. §286.9-010	No cap; licensee must conspicuously display a schedule of all fees and charges for authorized services.			None.	A license is required.	The law does not apply to any person who cashes checks without receiving, directly or indirectly, any consideration or fee. The law also does not apply to any person principally engaged in the retail sale of goods or services who, either as an incident to or independently of a retail sale, from time to time cash checks for a fee or other consideration.
Louisiana	La. Rev. Stat. Ann. §6:1001	2% of the face amount of the check or $5, whichever is greater, for government issued checks.	10% of the total amount of the check presented for cashing or $5, whichever is greater, for all other checks or money orders.		None.	A license is required (a person may engage in business at more than one location with one license).	The law does not apply to a business that cashes a check, draft, money order, or traveler's check, or other commercial paper if the fee charged does not exceed $2 and the currency exchange is incidental to the primary business.
Maine	Me. Rev. Stat. Ann. tit. 32, §6131	3% with identification, or 4% without identification, or $5, whichever is greater, if state public assistance or social security.	10% or $5, whichever is greater, for personal checks.	5% of the face amount of the payment instrument with identification, or 6% without identification, or $5, whichever is greater; 10% or $5, whichever is greater, for money orders.	None.	Registration is required.	The law does not apply to a person who is primarily engaged in the business of selling tangible personal property or services at retail and does not derive more than 5% of its income from check cashing.
Maryland	Md. Code Ann., Fin. Inst. §12-101	2% of the face amount of the payment instrument or $3, whichever is greater, for government checks.	10% or $5 of face amount of the payment instrument, whichever is greater, for personal checks.	4% of face amount of the payment instrument or $5, whichever is greater, for all other payment instruments.	A licensee may charge a one-time membership fee not to exceed $5.	A license is required.	The law does not apply to check cashing services where a fee of up to 1.5% of the face amount of the payment instrument is charged per payment instrument and that are incidental to the retail sale of goods or services by the person that is providing the check cashing services.
Massachusetts	Mass. Gen. Laws Ann. ch. 169A §1	No cap; schedule of fees and charges to be charged for the cashing of checks, drafts or money orders must be filed annually by each licensee with the commissioner.			None.	A license is required.	A license is required only if a person engages in cashing checks, drafts or money orders for consideration in excess of $1 per item.
Minnesota	Minn. Stat. Ann. §53A.01	No cap; fees charged by licensees at each location for check cashing services must be filed with and approved by the Commissioner of Commerce.			None.	A license is required. A license cannot be issued if the proposed place of business is located within one-half mile of another licensed currency exchange business.	The law does not apply to a person who provides check cashing services incidental to the person's primary business if the charge for cashing a check or draft does not exceed $1 or 1% of the value of the check or draft, whichever is greater.
Mississippi	Miss. Code Ann. §75-67-501 (sunset provision in effect until July 1, 2015)	3% or $5, whichever is greater, for government checks.	10% or $5, whichever is greater, for personal checks.	5% or $5, whichever is greater, for all other checks or money orders.	None.	A license is required.	Any person principally engaged in the retail sale of goods or services who, either as an incident to or independently of a retail sale, may from time to time cash checks for a fee, not exceeding 3% of the face amount of the check or $10, whichever is greater. The fee must be conspicuously posted for public view.

STATE	STATUTORY CITATION	PERMISSIBLE CHECK CASHING FEES				LICENSE OR REGISTRATION REQUIRED	NOTABLE EXEMPTIONS TO REGULATION
		Public Assistance/ Social Security Checks/ Other Government Issued Checks	Personal	Payroll/Other Checks	Statutorily Authorized Account Set-up/Membership Fee		
Tennessee	TN Code Ann. §45-18-101	3% or $2, whichever is greater of the face amount of the payment instrument, for public assistance or social security checks.	10% or $5, whichever is greater, for personal checks.	5% or $5, whichever is greater, for all other checks.	Licensees may charge a customer a one-time membership fee not to exceed $10	A license is required.	The law does not apply to persons engaged in the cashing of payment instruments which is incidental to the retail sale of goods or services whose compensation for cashing payment instruments at each site does not exceed 5% of the gross receipts from the retail sale of goods or services by such person during its most recently completed fiscal year.
Utah	Utah Code Ann. §7-23-103	No cap; a check casher is required to post a complete schedule of all fees for cashing a check in a conspicuous location at its premises that can be viewed by a person cashing a check.				Registration is required.	The law does not apply to a person that cashes a check in a transaction that is incidental to the retail sale of goods or services and for consideration that does not exceed the greater of: (i) 1% of the amount of the check; or (ii) $1.
Vermont	Vt. Stat. Ann. Tit. 8, §2500	2% of the face amount or $2, whichever is greater, for state public assistance or social security checks, if the customer cashing the payment instrument is the named payee.	10% or $5, whichever is less, for personal checks.	5% or $5, whichever is greater, for all other checks; 10% or $5, whichever is less, for money orders.	Licensees may charge a customer a onetime membership fee not in excess of $10	A license is required.	A seller of goods or services that cashes payment instruments incidental to or independent of a sale and does not charge for cashing the payment instrument a fee in excess of $.1 per instrument.
Virginia	Va. Code Ann. § 6.2-2100	No cap; registrant must file a statement of the fees charged at every location with the Commissioner. A notice stating the fees charged for cashing items must be conspicuously posted and displayed at all times.			None.	Registration is required.	The law does not apply to any person not holding himself/herself out to be a check cashing service, which is principally engaged in the bona fide retail sale of goods or services, who either as an incident to or independently of such retail sale or service, from time to time cashes items for a fee or other consideration, where not more than $2 or 2% of the amount of the item, whichever is greater, is charged for the service.
Washington	Wash. Rev. Code Ann. §31.45.010	No cap; a schedule of the fees and the charges for the cashing of checks, drafts, money orders, or other commercial paper serving the same purpose shall be conspicuously and continuously posted in every licensed location.			None.	A license is required.	Director of Financial Institutions may grant a total or partial exemption to persons not primarily engaged in the business of cashing or selling checks upon concluding that such an exemption would not be detrimental to the public.
Washington, D.C.	D.C. Code Ann. §26-301	2% of the face amount or $2, whichever is greater, for government issued checks.	10% of the face amount or $5 for personal checks.	4% or $5 of the face amount for payroll and all other checks; 10% of the face amount or $5 for money orders.	A licensee may charge a customer a one-time membership fee not to exceed $5.	A license is required.	The law does not apply to any person who cashes checks for no consideration or charge.
West Virginia	W. Va. Code Ann. §32A-3-1	1% of the face value cashed or $1, whichever is greater.			None.	A license is required. Merchants deriving more than 5% of gross revenues from cashing checks must obtain the proper license from state Division of Banking.	A merchant primarily in the business of making retail consumer sales may offer check cashing services at its stores to accommodate its customers in the course of said business, and may collect a fee for the service, if the check cashing service and any fees charged are incidental to the main business of the merchant. Where a merchant derives more than 5% of gross revenues from cashing checks, the check cashing services are not considered incidental to the main business of the merchant, and the merchant is required to be licensed.
Wisconsin	Wis. Stat. Ann. §218.05	No cap.			None.	A license is required.	None.

Exhibit II – Minimum Loan Calculator

Direct Variable Costs	Loan Officer *	Underwriter**	Processing***	Servicing****	Pull Through Rate *****			Total Other Costs
Productivity	75%	75%	75%	75%				
Salaries	$ 45.35	$ 33.34	$ 28.24	$ 26.81				$ 133.75
Applications Not Funded					49.25%			$ 65.87
TOTAL COSTS								$ 199.61
Net Interest Margin (Banks < $1 billion 12/31/2011) FDIC								3.90%
	Minimum loan amount to break even							$ 5,118.33

* Consumer Loan Officer I — $ 56,490.00 median salary plus 25% benefits = $ 34.01 cost per hour.
http://www.bls.gov/oes/current/oes132072.htm — Assumes 1 hour per loan at 100% productivity

** Consumer Loan Underwriter — $ 41,533.00 median salary plus 25% benefits = $ 25.01 cost per hour.
http://www1.salary.com/Consumer-Credit-Analyst-I-Salary.html — Assumes 1 hour per loan at 100% productivity

*** Consumer Loan Processor — $ 35,180.00 median salary plus 25% benefits = $ 21.18 cost per hour.
http://www.bls.gov/oes/current/oes_nat.htm#13-0000 — Assumes 1 hour per loan at 100% productivity

**** Consumer Loan Servicing — $ 33,390.00 median salary plus 25% benefits = $ 20.10 cost per hour.
http://www1.salary.com/Accounts-Receivable-Clerk-salary.html — ($33,390 X 1.25)/2353= $ 17.14

*******Pull through rate**
50.75% of all applications did not result in a closed loan although the time and costs of the loan officer and underwriter are still incurred

Notes:
The 2007 Cornerstone Report = Median 9 consumer loans originated per loan consumer loan officer per month, 93 consumer loans underwritten per loan consumer loan underwriter per month and 145 consumer loan applications processed per comusmer loan processing FTE per month. Use of these benchmarks
2007 Cornerstone Benchmark Analysis = 2,353 consumer loans serviced per servicing FTE