OFFICE OF
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UNITED STATES POSTAL SERVICE

WHITE PAPER

Providing Non-Bank Financial Services for the Underserved

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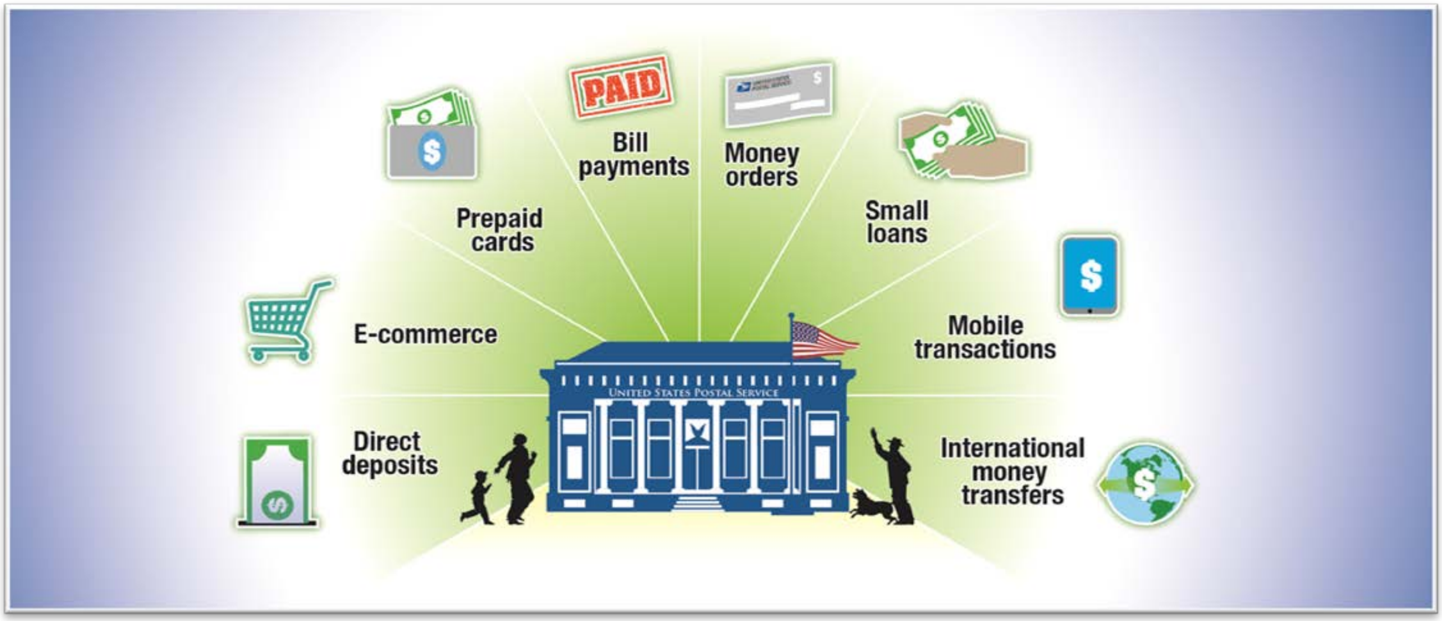

Report Number: RARC-WP-14-007

EXECUTIVE SUMMARY

Providing Non-Bank Financial Services for the Underserved

Millions of Americans do not have a bank account, or use costly services like payday loans and check cashing exchanges just to make ends meet. The entire underserved population comprises more than a quarter of all U.S. households — some 68 million adults. They are an economically diverse mix of working and middle class families, poor and unemployed people hurt by the recent economic crisis, young people, immigrants, and others who are trying to make it paycheck to paycheck. Together, they represent a huge market. In 2012, they spent about $89 billion just on interest and fees for alternative financial services.

Highlights

One in four U.S. households lives at least partially outside the financial mainstream — without bank accounts or using costly services like payday lenders.

The average underserved household spends $2,412 each year just on interest and fees for alternative financial services.

Postal financial services may appeal to many customers who feel abandoned by major financial institutions. Postal organizations have an unmatched ability to reach consumers from diverse backgrounds.

Many international posts are already garnering significant new revenue and keeping citizens connected by offering financial services.

Financial services have been the single best new opportunity for posts to earn additional revenue. For the Postal Service, this might ultimately translate into $8.9 billion per year.

The Postal Service is well positioned to provide non-bank financial services to those whose needs are not being met by the traditional financial sector. It could accomplish this largely by partnering with banks, who also could lend expertise as the Postal Service structures new offerings. The Office of Inspector General is not suggesting that the Postal Service become a bank or openly compete with banks. To the contrary, we are suggesting that the Postal Service could greatly complement banks' offerings. The Postal Service could help financial institutions fill the gaps in their efforts to reach the underserved. While banks are closing branches all over the country, mostly in low-income areas like rural communities and inner cities, the physical postal network is ubiquitous. The Postal Service also is among the most trusted companies in America, and trust is a critical element for implementing financial services. With affordable financial offerings from the Postal Service, the underserved could collectively save billions of dollars in exorbitant fees and interest. This could make a big difference to struggling families — on average, people who filed for bankruptcy in 2012 were just $26 per month short of meeting their expenses.

Using posts to expand citizens' financial options and access is not a novel idea; many international posts already succeed in providing financial services. Much of their success is due to the ubiquity of their networks and the trust the public places in them. In addition, the U.S. Postal Service already offers some types of financial services, like money orders and international money transfers, so it has an established presence. Moreover, expanded financial offerings would be in the spirit of the organization's founding mission to support commerce and serve citizens.

This paper identifies specific opportunities for the Postal Service to offer non-bank financial services. These services could include reloadable prepaid cards with features that encourage people to save money, mobile transactions, and products that help the underserved take part in e-commerce. They also could include new ways of transferring money both domestically and internationally, and perhaps even include small loans that would help customers overcome unexpected expenses. As society becomes increasingly cashless, the Postal Service's ability to provide a physical link to the new digital economy will become more and more vital.

Many people could benefit from the Postal Service expanding its presence in the financial services market. The millions of citizens currently struggling would have new ways to conduct their financial transactions. Non-bank financial services from the Postal Service could help these people to gain more financial security, and help foster a culture of savings. In addition, by partnering with banks and other financial institutions, the Postal Service could create a "win-win" situation. Postal financial services could complement the current offerings from banks by helping banks reach customers in geographic areas where they lack a physical presence, by offering products to customers who were not previously a main focus of banks, and by helping some customers transition to traditional bank savings or checking accounts. In addition, financial services could result in major new revenue for the Postal Service. If even 10 percent of what the underserved currently spend on interest and fees instead went to more affordable offerings from the Postal Service, it could lead to $8.9 billion in new revenue per year.

A suite of financial services from the Postal Service could be a powerful new tool to help the underserved become more financially secure. As a first step, the Postal Service could explore services similar to those it is already authorized to provide, such as money orders and international money transfers. In addition, small market tests in key geographic areas could help to demonstrate new products' viability. Although some financial services may have a longer development period, others have the potential to be a big hit right away. A quick victory or two could help garner stakeholder support for additional postal financial services. There is a clear market need for innovative financial products, and millions of families would benefit from more affordable solutions. The Postal Service could be exactly what they are looking for.

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Providing Non-Bank Financial Services for the Underserved

Introduction

Banks and other financial institutions play a critical role in American society. Accounts at federally insured depository institutions provide safety and security, protect households from theft, help families save money, and can open the door to affordable credit. Yet, more than a quarter of American households are left outside or on the fringes of the traditional financial system. Some have no bank account whatsoever. Others have a checking account, but do not qualify for traditional forms of credit, forcing them to use costly services like payday loans and car title loans — which can often do more harm than good. Many of the 34 million financially underserved households — representing 68 million adults — are treading water very close to the economic edge.[1] Unexpected expenses can push them over the brink into homelessness or bankruptcy, which come with broad social and economic costs. In addition to this at-risk population, there are many other Americans who are simply looking for new financial options.

Many interested parties have been trying for years to bring the underserved into the traditional financial system, and have made progress. In 2005, Congress required the Federal Deposit Insurance Corporation (FDIC) to conduct biennial surveys of the financial habits of underserved Americans and banks' efforts to reach them.[2] These reports provide strong evidence that the unmet need for banking services is nationally wide and deep. In many countries, policymakers have turned to postal organizations to increase the level of financial inclusion. While federal law currently places restrictions on new non-postal products and services, the U.S. Postal Service already offers money orders, international money transfers, and other relevant financial products.

This paper aims to explain how the Postal Service could expand its offerings to include a broader suite of non-bank financial services and products. These new offerings could not only bring financial stability and flexibility to the underserved, but also could yield broad benefits to the U.S. economy, the financial services industry, and the Postal Service itself. We contracted with a team of experts in the U.S. financial services industry, international postal operations, and other relevant areas to help conduct our analysis.[3]

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[1] Federal Deposit Insurance Corp. (FDIC), *2011 FDIC National Survey of Unbanked and Underbanked Households*, September 2012, http://www.fdic.gov/householdsurvey/2012_unbankedreport.pdf, pp. 4-10.

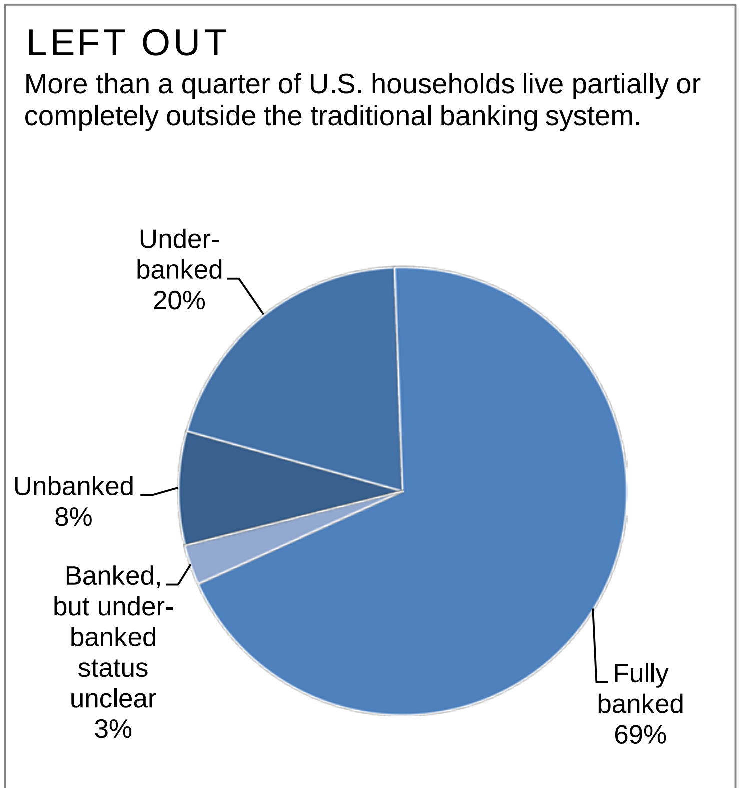
[2] Both studies are available on the FDIC's website at http://www.fdic.gov/unbankedsurveys/ and http://www.fdic.gov/householdsurvey/.

[3] For this project we contracted with Decision/Analysis Partners, who assembled a team of experts including: Hans Boon, a world-renowned expert on postal operations and financial inclusion strategies who has helped implement postal financial services in various countries, formerly with ING and the Netherlands Postbank; Jean Philippe Ducasse, an expert on postal strategies, formerly with the European Commission, La Poste, and the Universal Postal Union (UPU); James Pérez Foster, a former VP with Merrill Lynch and Morgan Stanley Smith Barney, who has recent experience as an expert on banking services for underserved communities; and Ana Harvey, the former head of the Small Business Administration's Office of Women's Business Ownership.

Who are the Underserved?

The underserved are a geographically, economically, and demographically diverse group of people who, by choice or circumstance, operate partially or completely outside the traditional banking system. We define underserved as primarily consisting of two main groups: the unbanked, who have no checking or savings account, and the underbanked, who have a bank account but also used at least one non-bank financial service during the past year. These non-bank financial services include check cashing, money orders, remittances, payday lending, pawnshops, rent-to-own agreements, and other similar products and services. We refer to them in this paper as "alternative financial services." In addition, there also are many fully-banked consumers who are unhappy with their current options and are seeking alternatives.

Figure 1: Banked Status of U.S. Households



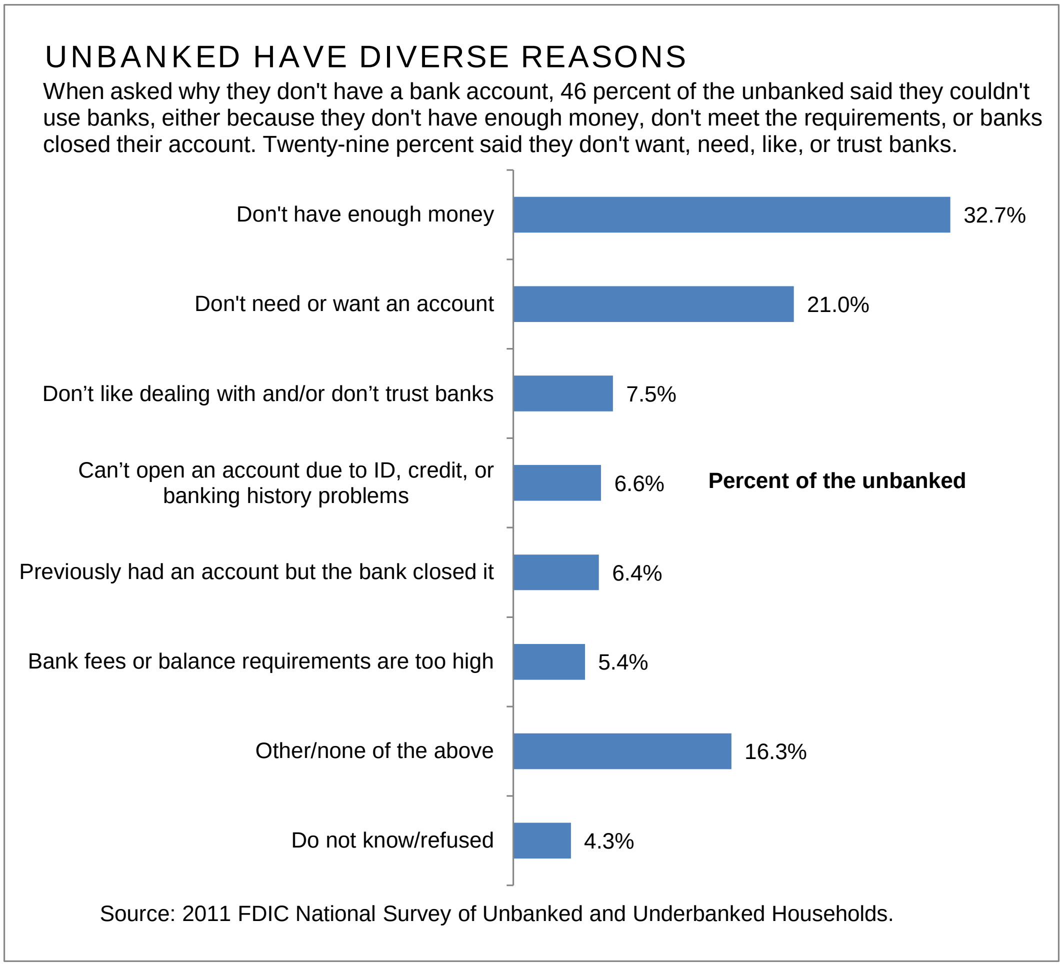
Source: 2011 FDIC National Survey of Unbanked and Underbanked Households.

There are about 34 million underserved U.S. households, comprising more than a quarter of all American families, as Figure 1 illustrates. Being underserved often comes at a hefty price. The average underserved household has an annual income of about $25,500 and spends about $2,412 of that just on alternative financial services fees and interest.[4] That amounts to 9.5 percent of their income. To put that into perspective, that is about the same portion of income that the average American household spends on food in one year.[5] In 2012 alone, the underserved paid some $89 billion in fees and interest.[6]

[4] Based on 34 million households, earning an average of $25,500 per year, spending a total of $82 billion in 2011. KPMG, *Serving the Underserved Market*, 2011, http://www.kpmg.com/US/en/IssuesAndInsights/ArticlesPublications/Documents/serving-underserved-market.pdf, p.1, and Center for Financial Services Innovation (CFSI), *2012 Financially Underserved Market Size Study,* December 2013, http://www.cfsinnovation.com/content/2012-financially-underserved-market-sizing-study, p.1.
[5] Based on average before tax income of $65,596 and average food expenditures of $6,599. Bureau of Labor Statistics, *Consumer Expenditure Survey*, 2012, http://www.bls.gov/cex/2012/combined/income.pdf, p. 1.
[6] CFSI, *2012 Financially Underserved Market Size Study,* p.1.

People are unbanked for a wide range of reasons.[7] Figure 2 gives a breakdown of the key reasons people cite for their unbanked status.

Figure 2: Reasons for Being Unbanked



According to the FDIC, certain segments of the population are disproportionately underserved, including lower-income, black, and Hispanic households, as well as people under the age of 25. However, white households still account for half of the underserved. Geographically, the underserved live throughout the country. However, they are over-represented in the South, where poverty is more prevalent, and in inner cities.[8]

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[7] While the FDIC found that the most common reason people do not have a bank account is that they do not have enough money, a separate survey by the Federal Reserve found another leading cause: 24 percent of respondents said they do not have a bank account because: "I don't like dealing with banks." Board of Governors of the Federal Reserve System, *Consumers and Mobile Financial Services*, March 2012, http://www.federalreserve.gov/econresdata/mobile-devices/2012-appendix2.htm, Appendix 2.

[8] FDIC, *2011 FDIC National Survey of Unbanked and Underbanked Households,* p.15.

There also is a fair amount of economic diversity within the underserved population. While a bit more than half of underserved households earn less than $30,000 a year, more than a quarter earn at least $50,000. A full 57 percent are employed, just 10 percent are unemployed, and a third are not in the labor force — often because they are on disability or retired. Nearly half of the underserved have attended at least some level of college.[9]

Most payday loans carry extremely high fees that equate to an average annual interest rate of 391 percent.

The underserved tend to have very little savings. Just one unexpected expense, such as a car repair or a medical procedure, can quickly become a major crisis, forcing them to seek credit from the likes of payday lenders or worse. Payday loans are advertised as loans that must be repaid with the borrower's next paycheck. However, most borrowers cannot afford to pay the loan back in full, so they renew the loan repeatedly and are in debt for an average of 5 months of the year, all the while paying fees that typically equate to a 391 percent annual interest rate.[10]

Rather than giving borrowers the credit they need to climb out of a hole, these types of loans often dig borrowers deeper into debt. Research has shown that a majority of payday loan users are borrowing money for everyday expenses, rather than unexpected emergencies.[11] In essence, these consumers rely on overly expensive short term credit to balance out the ups and downs of their finances. This suggests a strong need for financial services that are more stable and affordable.

The Postal Service is Well Suited to Provide Non-Bank Financial Services

The Postal Service is an ideal fit for offering non-bank financial services, based on four basic guiding principles for potential new products. Figure 3, on the following page, highlights these four principles, each of which is explained below in more detail.

[9] Ibid.
[10] Pew Charitable Trusts, *Payday Lending in America: Who Borrows, Where They Borrow, and Why*, July 2012, http://www.pewstates.org/uploadedFiles/PCS_Assets/2012/Pew_Payday_Lending_Report.pdf, pp. 6-7.
[11] Ibid., p.13.

Figure 3: Guiding Principles for New Products

Market Need	Does the product fulfill an unmet market need?
Capabilities	Is the product consistent with the Postal Service's competencies and assets?
Public Purpose	Does the product fulfill an important public purpose?
Financial	Would the product cover its costs at full maturity?

Unmet Market Needs

There are many non-profits, financial advocacy groups, and government entities focused on improving financial access. While they have made significant strides, there is still a tremendous unmet market demand for financial services. As mentioned above, 28 percent of all U.S. households are either unbanked or underbanked. Millions of additional adults are open to new financial service options. In the current market, these people are missing the financial services they want and need.

Banks are closing branches across the country (nearly 2,300 in 2012).[12] Although the number of closings is only a fraction of the total number of branches, the closings are not spread evenly. The closings are heavily hitting low-income communities, including rural and inner-city areas — the places where many of the underserved live.[13] In fact, an astounding 93 percent of the bank branch closings since late 2008 have been in ZIP Codes with below-national median household income levels.[14] This leaves some communities stranded without physical access to quality financial services, and the problem could get much worse. Banking industry experts predict that banks will continue to shut branches, particularly in small communities.[15]

Even in neighborhoods that still have bank branches, there is no guarantee that the underserved will find what they need. Less than half (43 percent) of banks reported that they actively develop products and services for underserved consumers.[16] While free checking used to be a widespread offering from banks, it has become much less

[12] Robin Sidel, "After Years of Growth, Banks are Pruning Their Branches," *The Wall Street Journal*, March 13, 2013, http://online.wsj.com/article/SB10001424127887323699704578326894146325274.html.
[13] Nelson D. Schwartz, "Bank Closings Tilt Toward Poor Areas," *The New York Times*, Feb. 22, 2011, http://www.nytimes.com/2011/02/23/business/23banks.html?pagewanted=all&_r=0, and David Hayes, et.al., "Banks Follow the Money and Exit Lower-Income Areas," *SNL Financial*, April 27, 2012, http://www.snl.com/InteractiveX/ArticleAbstract.aspx?id=14485078.
[14] Frank Bass and Dakin Campbell, "Predator Targets Hit as Banks Shut Branches Amid Profits," *Bloomberg,* May 2, 2013, http://www.bloomberg.com/news/2013-05-02/post-crash-branch-closings-hit-hardest-in-poor-u-s-areas.html.
[15] Robin Sidel, "After Years of Growth, Banks are Pruning Their Branches," *The Wall Street Journal*.
[16] FDIC, *2011 FDIC Survey of Banks' Efforts to Serve the Unbanked and Underbanked*, 2012, http://www.fdic.gov/unbankedsurveys/2011survey/2011report.pdf, p. 4.

common. At the same time, banks have continued to increase existing fees and introduce new fees across a wide range of products and services.[17]

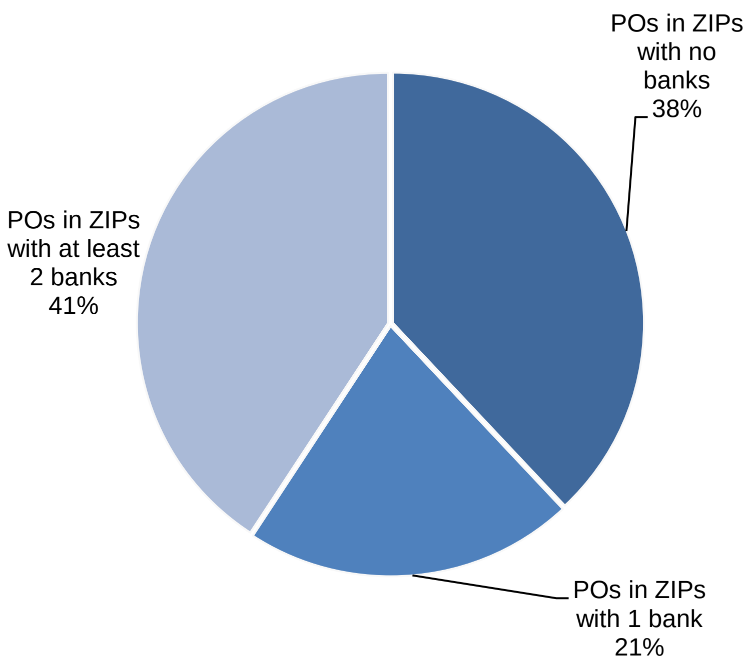
Competencies and Assets

The Postal Service has numerous competencies and assets that would be critical for providing non-bank financial services. The first and possibly most important factor is the sheer ubiquity of the Postal Service. The vast retail network of more than 35,000 Post Offices, stations, branches, and contract units is spread out across the country and is particularly well established in small towns. Banks and other financial institutions still maintain tens of thousands of branches and other locations across the country, but that network is fragmented among thousands of players and is inextricably linked to population density and centers of economic growth. The postal network, on the other hand, is a single, unified network that is linked to geography. As Figure 4 shows, 59 percent of Post Offices are in ZIP Codes with one or no bank branches.

Figure 4: Post Offices vs. Bank Branches

MOST POST OFFICES ARE IN BANK DESERTS

Fifty-nine percent of internally-managed Post Offices are in ZIP Codes with zero or one bank branch, illustrating that the Postal Service is geographically well-positioned to reach people with little-to-no access to retail banking services.



Note: Excludes Post Offices with unique ZIP Codes.

Sources: FDIC 2013 Summary of Deposits; Postal Service facilities database.

A second factor is Americans' trust and familiarity with the postal "brand." Trust is a crucial asset in financial services, especially when considering bank-wary unbanked and underbanked households that have been dealing with sometimes untrustworthy alternative financial services providers.

While banks operate efficiently and can reliably handle most consumers' financial transactions, the public's trust in banks to protect their personal information has

[17] Richard Barrington, "Bank Fees Survey Mid-2013: Free Checking Hits a New Low," *MoneyRates.com,* August 19, 2013, http://www.money-rates.com/research-center/bank-fees/.

declined since 2004, dropping from 48 to only 35 percent in that time.[18] In addition, a June 2013 survey found that only 26 percent of the public has much confidence in U.S. banks, and that this number has not risen above 40 percent since 2007.[19]

The public puts much greater trust in the Postal Service than in banks. While more than two-thirds of the public trusts the Postal Service, just 26 percent have much confidence in banks.

On the other hand, a recent market survey found that 68 percent of respondents agree or strongly agree that the Postal Service is reliable and trustworthy.[20] When it comes to privacy, the Postal Service is consistently ranked as the most trusted federal entity, and was recently identified as the fourth most trusted company in the United States.[21] The public's trust in the Postal Service could go a long way when it comes to serving customers looking for new financial solutions, as trust has been identified as a critical factor in successfully implementing financial services.[22]

In addition, the Postal Service has extensive experience in the financial services market through current and past products. By offering these products and services, the Postal Service has accumulated essential institutional experience with financial transactions.

Current Products and Services

The Postal Service has played a longstanding role in providing domestic and international money orders. The Postal Service is actually the leader in the U.S. domestic paper money order market, with an approximately 70 percent market share.[23] This is a lucrative business line and demonstrates that the Postal Service already has a direct connection to the underserved, who purchased 109 million money orders in fiscal year (FY) 2012. Those sales generated $166.3 million in revenue and incurred attributable costs of just $110.5 million.[24] The market is gradually shrinking, however, in competition with electronic money transfer alternatives.[25] In addition to domestic money

[18] Ponemon Institute, *Most Trusted Retail Banks for Privacy,* October 10, 2013, http://www.ponemon.org/local/upload/file/2013%20MTC%20Banking%20Briefing%20V2.pdf, p. 5.
[19] Dennis Jacobe, Gallup, *Americans' Confidence in Banks Up for First Time in Years,* June 13, 2013, http://www.gallup.com/poll/163073/americans-confidence-banks-first-time-years.aspx.
[20] Aytm, *United States Postal Service Brand Survey,* April 21, 2012, https://aytm.com/surveys/167290/stat/7a700df2ff4221ec54cc4e2049f01b7f#charts/chart=pie,color=0.
[21] Ponemon Institute, *2012 Most Trusted Companies for Privacy*, January 28, 2013, http://www.ponemon.org/local/upload/file/2012%20MTC%20Report%20FINAL.pdf.
[22] Alexandre Berthaud and Gisela Davico, *Global Panorama on Postal Financial Inclusion: Business Models and Key Issues*, UPU, March 2013, http://www.upu.int/fileadmin/documentsFiles/activities/financialInclusion/publicationGlobalPanoramaFinancialInclusionEn.pdf, p. 7.
[23] U.S. Postal Service Office of Inspector General (OIG), *Digital Currency: Opportunities for the Postal Service,* RARC-WP-12-001, October 3, 2011, http://www.uspsoig.gov/sites/default/files/document-library-files/2013/RARC-WP-12-001.pdf, p. 31.
[24] U.S. Postal Service, "Public Cost and Revenue Analysis, Fiscal Year 2012," http://about.usps.com/who-we-are/financials/cost-revenue-analysis-reports/fy2012.pdf, pp. 2, 5.
[25] Fiscal year revenues were $191.1 million in 2009, $183.2 million in 2010, and $172.7 million in 2011. U.S. Postal Service, "Public Cost and Revenue Analysis, Fiscal Years 2009 to 2011," available at http://about.usps.com/who-we-are/financials/welcome.htm.

orders, the Postal Service also sells international money orders, which can be cashed at post offices in 29 countries.[26]

While its domestic and international money orders are currently paper-based, the Postal Service does offer electronic money transfers to nine Latin American countries through the Dinero Seguro® (Spanish for "sure money") service.[27] This type of service is also known as an international remittance. For relatively small fees, customers at nearly 3,000 participating U.S. Post Offices can use the service to electronically transfer funds to participating countries.[28]

Since 2011, the Postal Service has sold prepaid debit cards in the form of open-loop American Express gift cards as part of a market test.[29] Most Post Offices that sell greeting cards also sell the gift cards, which come in various denominations and can be spent at any merchant that accepts American Express. After an initial one-time purchase charge, the cards have no additional fees for purchasers or recipients. The Postal Service has extended the market test past the initial 2-year period, and expanded the scope of the test to include the sale of closed-loop gift cards for major national retailers like Amazon, Barnes & Noble, Subway, and Macy's.[30]

Postal Savings System

In addition to its current offerings, the Postal Service has offered other products and services in the past. For example, from 1911 to 1967, the Postal Savings System gave people the opportunity to make savings deposits at designated Post Offices nationwide. The system hit its peak in 1947 with nearly $3.4 billion in savings deposits from more than 4 million customers using more than 8,100 postal units. The system was discontinued in 1967 after a long decline in usage.[31] Interestingly, the system was extraordinarily popular with immigrants in the early 20th century. For more information on the Postal Savings System, please see Appendix A.

Public Purpose

By offering non-bank financial services, the Postal Service could fulfill an essential public purpose: increasing the level of financial inclusion in the United States and expanding the number of alternatives for all consumers. Promoting the financial health of all citizens and meeting the needs of the unbanked are longstanding federal

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[26] U.S. Postal Service, *USPS.com*: "Learn About Domestic & International Money Orders," https://www.usps.com/shop/money-orders.htm.
[27] For a list of participating countries, see https://www.usps.com/shop/wire-money-internationally.htm.
[28] U.S. Postal Service, "Send Money Home Securely with 'Dinero Seguro,'" March 20, 2013, http://about.usps.com/news/state-releases/ma/2013/ct-ma_2013_0320.htm.
[29] Open-loop cards are endorsed by an electronic payment network such as Visa or MasterCard, and are usable for in-store or online payments everywhere the network is accepted. Closed-loop cards are limited to a specific merchant. For more information on the Postal Service's gift cards, please see U.S. Postal Service, "Gift Cards Market Test Launch," 2011, http://about.usps.com/postal-bulletin/2011/pb22313/html/info_005.htm.
[30] "Order Granting Extension of Gift Card Market Test," Postal Regulatory Commission Order No.1781, July 19, 2013, http://www.prc.gov/Docs/87/87368/Order_1781.pdf, and David Rubin, Postal Regulatory Commission data collection report for docket No. MT2011-2, October 18, 2013, http://www.prc.gov/Docs/88/88034/Data%20Coll%20Rpt%20FY13%20Q3-4%20Final.pdf.
[31] U.S. Postal Service, *Postal Savings System*, July 2008, http://about.usps.com/who-we-are/postal-history/postal-savings-system.pdf.

priorities.[32] Postal financial services could assist underserved families in making steps toward the mainstream financial system, possibly building up savings, and eventually embracing offerings from traditional retail banks. Moreover, postal financial services would fit well with the Postal Service's founding mission to serve citizens and support the growth of commerce.[33]

Revenue Opportunity

Financial services are the single biggest driver of revenue for posts around the world, after letter mail.[34] Declining mail volume has led many posts to find new ways to diversify their income, and financial services have been an even greater source of new money than parcel delivery and logistics, accounting for an average of 14.5 percent of revenue for postal organizations in industrialized countries in 2012.[35] A nationwide network of Post Offices that serve as highly valuable retail space further boosts the potential for financial services revenue.

Postal financial services are the single best opportunity for new revenue.

New products and services generally take a while to develop, but startup and implementation pains could be minimized by forming partnerships with private sector organizations in the financial services industry.[36]

The Postal Service Could Offer a Variety of Non-Bank Financial Services

The underserved are looking for new financial products and services. Banks and other institutions are looking for partners with unique assets and capabilities. By offering a suite of non-bank financial services, the Postal Service could help give both groups what they are looking for. Utilizing public-private partnerships, a financial services platform offered by the Postal Service could serve as a critical physical link for customers in every community, providing a bridge to 21st century electronic transactions. The 2006 Postal Accountability and Enhancement Act (PAEA) generally prohibits the Postal Service from offering new nonpostal services.[37] However, given that the Postal Service is already providing money orders and other types of non-bank financial services, it could explore additional options within its existing authority.

[32] Some examples include the Federal Deposit Insurance Act of 1950, the 1968 Consumer Credit Protection Act, the 1977 Community Reinvestment Act, the Credit CARD Act of 2009, and the 2010 Dodd-Frank Wall Street Reform & Consumer Protection Act.
[33] USPS OIG, *Meeting America's Emerging Communications Needs*, RARC-WP-12-009, April 27, 2012, https://www.uspsoig.gov/sites/default/files/document-library-files/2013/rarc-wp-12-009.pdf, p. 12.
[34] UPU, *Development Strategies for the Postal Sector: An Economic Perspective,* 2013, p. 28.
[35] Ibid.; Consumer Postal Council, *Universal Postal Service in Major Economies*, November 2013, http://www.postalconsumers.org/uploads/1/Universal_Postal_Service_Nov_13_Final_02_DS.pdf, p. i; and UPU, *Development of Postal Services in 2012,* October 2013, http://www.upu.int/fileadmin/documentsFiles/resources/postalStatistics/results2012PostalStatisticsEn.pdf, p. 22.
[36] For information on public-private partnerships, see U.S. Postal Service Office of Inspector General, *Public-Private Partnerships: Best Practices and Opportunities for the Postal Service*, RARC-WP-13-011, June 24, 2013, http://www.uspsoig.gov/sites/default/files/document-library-files/2013/rarc-wp-13-011.pdf.
[37] 39 U.S.C § 404(e)(2).

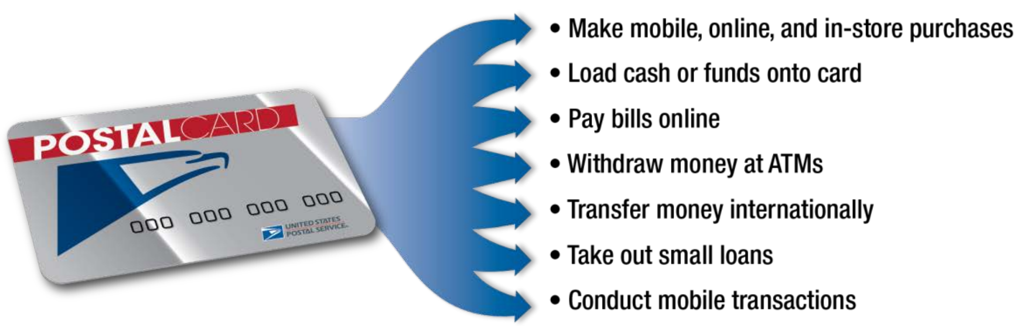
Postal financial services largely fall into three basic categories: payment services, ways to encourage savings, and credit services. Examples of services the Postal Service could offer in each category are discussed below. For information on additional potential services, please see Appendix B.

Payment Services

Payment services are likely the products with the lowest barriers to entry for the Postal Service, as they are the most similar to what the organization already offers. They generally do not require a major capital investment, and are full of opportunities to partner with banks. These payment services might include electronic money orders, bill payments, facilitating e-commerce payments, and other services.

A cornerstone of this product line could be a Postal Service branded open-loop reloadable prepaid card, perhaps called the Postal Card (see Figure 5).[38] Users could load cash or their paychecks onto the card, and then use it to withdraw cash, pay bills, and send or receive international remittances. With the development of highly secure identity verification systems and partnerships with government at the local, state, and federal levels, the cards also could send or receive tax payments and refunds, as well as handle other government-to-citizen or citizen-to-government payments. Such a product would not only help reduce the government costs associated with cash and check payments, it also would help fulfill the goal of bringing the underserved into the mainstream financial fold. The funds on Postal Cards could be covered by the FDIC insurance of a partner bank.

Figure 5: Postal Card as Linchpin to Financial Offerings



For the dwindling number of consumers with paper checks, the Postal Service could offer basic check cashing services, with the option to put the money on a Postal Card.[39] Post Offices also could be equipped with automated teller machines (ATMs) where customers can withdraw or add money to their cards. The Postal Card also could be

[38] For more information on Postal Service payment cards, as well as related payment services and digital currencies, see USPS OIG, *Digital Currency: Opportunities for the Postal Service*, RARC-WP-12-001, October 3, 2011, and USPS OIG, *The USPS Global Card: A Conceptual Analysis of a Smart Card Platform*, RARC-WP-12-006, February 13, 2012.
[39] Federal Reserve System, *The 2010 Federal Reserve Payments Study - Noncash Payment Trends in the United States: 2006 – 2009*, 2011, http://www.frbservices.org/files/communications/pdf/research/2010_payments_study.pdf, p. 11.

tied to a major surcharge-free ATM network, which would allow customers to withdraw cash from tens of thousands of ATMs nationwide without paying a fee.

In addition, the Postal Service could integrate online and mobile technologies with the payment services. People could log into their online Postal Service prepaid card account to check balances, transfer funds, pay bills, and so on. A smartphone app could allow customers to load paper checks onto their card by taking a picture of the checks with their phone, just like they can at most major banks.

Reloadable prepaid cards are soaring in popularity with the underserved, who like the convenience the cards provide.[40] Consumers used prepaid cards for $9.2 billion in purchases in 2012, up 56 percent from 2009.[41] However, the prepaid card market is highly fragmented, with many large and small players offering cards with a range of features. Many cards come with high fees that can sting unsavvy consumers. There is room in the marketplace for the Postal Service to offer a more transparent, affordable option that is tied to a ubiquitous physical distribution network of Post Offices, likely in partnership with banks.

Products to Encourage Savings

As part of its suite of products, the Postal Service could partner with a bank to offer an interest-bearing savings feature on the Postal Card, which would encourage the underserved to build up a reserve for emergencies or to save for big purchases, such as a home or car. The Postal Service also could incentivize customers to divert a small portion of each paycheck into a savings vehicle tied to their card.

Many Americans do not have enough money saved to help them through a crisis. In fact, only half of American adults have readily available savings to cover their expenses for 3 months or longer. Twenty-seven percent of American adults have no emergency savings whatsoever.[42] This widespread lack of savings leaves many people highly vulnerable.

Research shows that the underserved tend to have significantly less savings than the fully banked. However, this is largely due to a lack of disposable income among the underserved, whose regular monthly expenses essentially account for their entire paycheck. In fact, 25 percent of adults who work full-time do not make enough money to meet the basic needs of their families.[43] Through less expensive financial products and a savings feature linked to the Postal Card, the Postal Service could help bring

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[40] See Bretton Woods, Inc., *Analysis of Branded General Purpose Reloadable Prepaid Cards, Basic Checking Accounts and Check Cashing, February 2012*; Robert M. Hunt, et. al., for the Federal Reserve Bank of Philadelphia; CFSI, *Consumers' Use of Prepaid Cards: A Transaction-Based Analysis,* August 2012; Mercator Advisory Group, U.S. Prepaid Cards Market Forecasts, 2012-2015, October 2012; and FDIC *2011 National Survey of Unbanked and Underbanked Households*, p. 35.

[41] Federal Reserve System, *The 2013 Federal Reserve Payments Study*, December 19, 2013, http://www.frbservices.org/files/communications/pdf/research/2013_payments_study_summary.pdf, p. 12.

[42] Bankrate, *June 2013 Financial Security Index Charts,* http://www.bankrate.com/finance/consumer-index/financial-security-charts-0613.aspx.

[43] CFPB, *Empowering Low Income and Economically Vulnerable Consumers*, November 2013, http://files.consumerfinance.gov/f/201311_cfpb_report_empowering-economically-vulnerable-consumers.pdf, p. 39.

significant financial stability to millions of Americans, allowing them to pay their bills and avoid eviction, foreclosure, and other socially and economically expensive ills. This, in turn, would help the underserved improve their credit, so that they could one day join the ranks of the fully banked by moving to a traditional savings or checking account.

Credit Services

Generally, banks do not make small personal loans — even to highly creditworthy borrowers. That is because small loans cost about as much to underwrite and service as larger loans, but bring in a fraction of the revenue. So when someone needs a few hundred dollars to pay for an unexpected expense, they instead turn to credit cards. However, the underserved (and especially the unbanked) often cannot get credit cards because they have bad or nonexistent credit histories, which make them a high credit risk under typical underwriting models.

An affordable loan from the Postal Service could save American families from having to depend on costly services like payday loans.

Without access to traditional credit, the underserved often turn to alternative lenders, which charge high interest rates, fees, or both in part to compensate for the riskiness of their borrowers, who are more likely to default on their loans.[44] Generally, payday lenders require borrowers to have a checking account. This leaves the unbanked with even fewer options for credit, forcing them to go to pawnshops or even loan sharks.[45]

In this landscape with scant affordable lending options for the underserved, the Postal Service has a tremendous opportunity to offer small loans that could save borrowers a lot of money — billions of dollars when aggregated across all potential users — which they could spend on more productive things like rent, groceries, utilities, and mortgage and student loan payments. This would, in turn, help the overall economy.

Here is a purely hypothetical example of how a “Postal Loan” could work. Postal Loans would be available to people who have their paychecks directly loaded onto their Postal Service prepaid card (this also could be for government payments, such as Social Security or disability benefits) and have received at least two straight payments. For those whose employers do not offer electronic transfer, they could be eligible for a loan if they load at least two consecutive paychecks onto a Postal Service prepaid card.[46]

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[44] The Consumer Financial Protection Bureau (CFPB) has begun to issue regulations affecting alternative financial services. For more information, see http://www.consumerfinance.gov/regulations/. See also Congressional Research Service, *The Consumer Financial Protection Bureau (CFPB): A Legal Analysis, 2012,* and *A Brief Overview of Actions Taken by the Consumer Financial Protection Bureau (CFPB) in Its First Year, 2012*.

[45] A loan shark is “a moneylender who charges extremely high rates of interest, typically under illegal conditions.” See http://www.oxforddictionaries.com/us/definition/american_english/loan-shark.

[46] Ideally, front line Postal Service employees would collect and verify borrowers’ information and identities, but would not make credit decisions. Such decisions would be made by a computer model and overseen by financial experts.

People could borrow up to 50 percent of their gross paycheck. For a person who earns $18,000 per year and gets paid twice a month, that is $375. Every borrower could be required to pay a minimum of 5 percent of their gross pay from each paycheck until the loan is paid off. In this scenario, that would be $38 from each paycheck.[47] The Postal Service would automatically withhold loan payments from borrowers' paychecks before putting the difference on their Postal Card. If the Postal Service charged a $25 upfront loan fee and a 25 percent interest rate, the borrower would pay off the loan in 5 ½ months, paying a total of $48 in interest and fees across the life of the loan.[48]

Figure 6: Payday vs. Postal Loans

A PAYDAY LOAN ALTERNATIVE

The average payday loan of $375 costs consumers an average of $520 over the life of the loan. A postal loan for the same amount could cost just $48, leaving already cash-strapped borrowers with more money in their pockets to pay other bills and lift themselves up by their own bootstraps.

	Payday	Postal
Loan amount	$375	$375
Average months to repay	4.5	5.5
Average bi-monthly payment	$99	$38
Total interest and fees	$520	$48
Effective annual interest rate*	391%	28%

*Formula used to translate payday fees into an annual interest rate: (Interest & Fees / Loan Amount) / (Loan Days / 365) * 100.

Source: Pew Charitable Trusts, Safe Small-Dollar Loans Research Project, 2013.

That is less than a tenth of the fees charged for a typical payday loan of the same size (see Figure 6).[49] That single loan from the Postal Service could effectively put $472 back into a consumer's pocket, which he or she could then use on more economically productive expenses. If even one-tenth of the 12 million Americans who take out a payday loan each year got this hypothetical Postal Loan instead, they could collectively save more than half a billion dollars a year in fees and interest.[50] And that is to say nothing of the benefits Postal Loans could bring to the 10 million unbanked U.S. households which cannot even get payday loans.

Postal Loans could save Americans hundreds of millions of dollars each year, money they currently spend on paying high fees and interest.

What happens if a Postal Loan borrower stops making payments on her loan? After diligent follow-up, the Postal Service could potentially utilize the Treasury

[47] Studies show that most payday borrowers can afford to pay no more than 5 percent of their income toward debt payments and still have enough money left over to cover their expenses. For more information, see Pew Charitable Trusts' Safe Small-Dollar Loans Research Project.
[48] Based on two paychecks a month. When including fees, the effective annual interest rate would be 28 percent, using the payday lending method of interest calculation. While this is a higher rate than a traditional consumer loan, it is significantly lower than virtually all other options available to those who do not qualify for traditional credit. However, the rate reflects the inherent challenges in dealing with a high-risk segment of consumers. This interest rate is hypothetical and only intended to serve as an illustrative example. The Postal Service would need to ensure that rates and other conditions for loans or advances comply with all applicable laws and regulations.
[49] Pew Charitable Trusts, *Payday Lending in America: Who Borrows, Where They Borrow, and Why,* p. 4.
[50] Ibid.

Department's offset program, which allows federal agencies to collect debts from the tax refunds of debtors.[51] Because a high proportion of the "working poor" get tax refunds — including many people who would be prospective Postal Loan borrowers — this collateral could serve as a built-in insurance policy that would significantly reduce the risk that Postal Loans would go unpaid.[52] While testing, experimentation, and review would be required, this potential risk reduction could allow the Postal Service to offer loans to otherwise high-risk borrowers at affordable rates.

There is a wide range of consumers who need access to small-dollar credit, and the Postal Loan could strongly appeal to these different types of borrowers. For example, people whose income varies throughout the year, consumers with no other avenues to credit, families with unexpected expenses, and others. In addition, because of the unique strengths and capabilities of the Postal Service, the Postal Loan would likely meet key criteria for being a high quality loan, such as affordability, transparency, fair pricing, a structure that does not depend on repeat borrowing, and helping customers to build up their credit.[53]

To help fund credit products, the Postal Service could rely on partnerships with banks or other institutions, which could hold Postal Loans on their books.

Postal Financial Services Would Have Clear Benefits

Were the Postal Service to expand its financial services offerings, there would be three key beneficiaries: the American public (especially the underserved), the financial services community, and the Postal Service itself.

Benefits for the Public

For the most vulnerable Americans — including many of the underserved — the difference between making it and not is a small amount of money. Among the 1.1 million people who filed for personal bankruptcy in 2012, their median average income of $2,743 a month was just $26 less than their median average monthly expenses.[54] Put another way, these people were just $26 a month away from making ends meet.

On average, Americans who fell into bankruptcy in 2012 were only $26 a month away from staying afloat.

[51] Specific details about participation and implementation would need to be resolved.
[52] While the data are a bit murky (agencies report the numbers in somewhat different ways), it appears that the vast majority of the working poor file federal tax returns. Using the wage percentile benchmarks for 820 occupations listed in the Bureau of Labor Statistics' May 2012 Occupational Employment Statistics survey, we calculate that there are about 32 million employees, or about 25 percent of wage earners, who earn less than $25,000 per year. Internal Revenue Service (IRS) data show that, among those reporting less than $25,000 a year in income, about 70 million people filed a tax return in 2011. This includes people who did not earn a "wage," but who still filed a return. Of this group, 82 percent of filers got a refund averaging $1,562, according to the IRS.
[53] Nicholas Bianchi and Rob Levy, Center for Financial Services Innovation, *Know Your Borrower: The Four Need Cases of Small-Dollar Credit Consumers*, December 2013, http://www.cfsinnovation.com/CFSI_KnowYourBorrower.pdf p. 6.
[54] Administrative Office of the United States Courts, *2012 Report of Statistics Required by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 2013, http://www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BAPCPA/2012/BAPCPA-report.pdf, p. 44.

As mentioned above, the Postal Loan product outlined in this paper could, by itself, save the average payday loan borrower more than $100 a month in fees and interest. With this kind of cost savings, users of postal financial services would have much more financial security. If this helped decrease personal bankruptcies by just 5 percent, it would not only help more than 50,000 people a year avoid the lasting stigma and financial effects of bankruptcy, it also would potentially keep some $10 billion a year in loans and other debts from being dragged through bankruptcy court, where much of it would be canceled at tremendous expense to creditors (most of whom are financial institutions).[55] That would be good for American families, for banks, and for the entire country.

Because the underserved tend to spend nearly every penny they make, any money they save by using Postal Service financial products would immediately go back into the economy. They would spend it on groceries, gasoline, utilities, medical bills, and entertainment. Businesses small and large would benefit.

Benefits for the Financial Services Community

To be clear, the Postal Service should not aim to take customers away from mainstream banks and credit unions. To the contrary, the mainstream financial services community would be a beneficiary of a successful suite of postal financial services and products for three key reasons: partnerships, payments, and new customers. Moreover, the target market for postal financial services consists of people who are not currently a major focus of banks. In fact, cooperating with trusted nonfinancial entities helps financial institutions reach more low-income consumers.[56]

Partnerships: The Postal Service would rely on the financial sector to provide the back-end for some of these services, including providing Postal Cards, setting up and managing web and mobile access, servicing the accounts and loans, and possibly funding and holding the loans on their balance sheets. This could add up to substantial new revenue for the Postal Service's financial institution partners.

Postal financial services could result in millions of new customers and tremendous revenue for banks that partner with the Postal Service.

Payments: When people fall off the financial cliff, they typically stop paying many of their bills, including their credit cards, auto loans, and mortgages. If the Postal Service's financial services initiative were to succeed, a key outcome would be that the underserved would stumble far less often. That means they could continue making payments to the bank. For example, Internal Revenue Service figures show that in 2011, individual taxpayers reported $6.7 billion in canceled debt from foreclosure, repossessions, and the like.[57] If just 5 percent of this canceled debt was avoided, it could help lenders save some $335 million a year in

[55] Based on $208 billion in discharged personal bankruptcy debts in 2012. Ibid., p. 28.
[56] CFPB, *Empowering Low Income and Economically Vulnerable Consumers*, p. 32.
[57] IRS Individual Statistical Tables, *Table 2.1 Returns with Itemized Deductions: Sources of Income, Adjustments, Itemized Deductions by Type, Exemptions, and Tax Items, by Size of Adjusted Gross Income, Tax Year 2011,* http://www.irs.gov/file_source/pub/irs-soi/11in21id.xls.

write-offs — not to mention countless other millions of dollars in collection costs and legal and administrative fees.

New customers: Postal financial services could help bring financial stability to many families. As the underserved become more financially stable, they will be in a better position to pay off past debts and clean up their credit histories. As their credit improves, some of them could graduate to fully banked status, qualifying for mainstream checking and savings accounts, credit cards, auto loans, and home mortgages. In short, postal financial services could help create more full-fledged customers for banks.

Benefits for the Postal Service

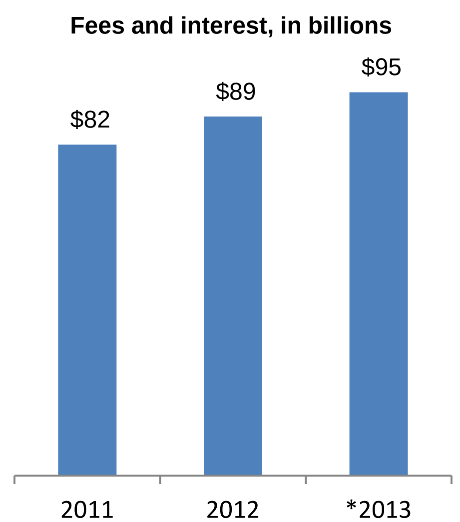
Financial services are hugely profitable for postal organizations around the world. Whether using a fully chartered "postal bank" or partnering with private institutions, postal financial services account for a major portion of postal profits and revenue in many countries. For more on the financial services offerings of foreign posts, please see Appendix C.

To get a ballpark figure, one can look at revenues in terms of the size of the alternative financial services market in the United States. If 10 percent of the $89 billion spent on alternative financial services was instead spent at the Postal Service, it could bring in $8.9 billion a year. That amount would be in line with the results seen by other industrialized countries. In 2012, postal financial services made up an average of 14.5 percent of their total revenue. For the U.S. Postal Service, that percentage would translate to $9.5 billion in additional revenue.[58] In addition, the alternative financial services market is expected to continue growing in the coming years, and is "ripe for innovation."[59]

Figure 7: The Growth of the Underserved Market

A GROWING MARKET

The underserved paid $89 billion in financial fees and interest in 2012, and projections suggest the market may have topped $95 billion in 2013. As the market grows, it represents an ever-greater opportunity for the Postal Service.



*Projected

Source: CFSI 2012 Financially Underserved Market Size Study.

As an alternative to high-level estimates for an overall suite of financial services, one can look at potential revenue through estimates of what individual products or services could bring in. Consider prepaid cards, for example. The fees they generate can vary widely, depending on a customer's particular habits. A study by the Pew Charitable Trusts

[58] Based on 2012 operating revenue of $65.2 billion, http://www.prc.gov/Docs/85/85646/2012_USPS_%20FORM_10K_FINAL.pdf.

[59] Eva Wolkowitz, "2012 Financially Underserved Market Size Study," CFSI landing page, December 2013, http://www.cfsinnovation.com/content/2012-financially-underserved-market-sizing-study.

showed that inexperienced consumers, who make heavy use of prepaid card services without regard for fees, spend a median of $32.60 a month on prepaid card fees, including monthly service charges, ATMs, retail purchases, and other fees. Consumers who take more care to avoid fees can pay significantly less.[60] The Postal Card could come with fewer and lower fees than others, bringing in an average of, perhaps, $15 a month in fee revenue per consumer. At that rate, if 10 percent of the 68 million underserved Americans used the Postal Card, the card alone would bring in $1.2 billion a year in revenue.

Financial services also could help maintain the viability of the Postal Service's retail network.

Strategic Considerations for the Postal Service

In order to expand its presence in the financial services market, the Postal Service needs a solid strategy, based, in part, on some of the lessons learned from international posts, the banking industry, and others. We offer here some considerations for the Postal Service on how it could lay the groundwork for an effective suite of postal financial services. This work is not in any way intended to be a business plan, which would be necessary for the Postal Service to closely examine the potential costs, revenue, and other details for any new services. The Postal Service also should consider creating a dedicated group — perhaps consisting of experienced financial sector executives — to research, implement, and manage financial products and services.

Timing is a Critical Factor

The Postal Service should carefully consider the timing with which it introduces any new postal financial services. Some types of products or services may require relatively lengthy development and rollout periods. However, a quick victory or two could help garner stakeholder support for implementing additional postal financial services.

Electronic payment products like Postal Cards might be a wise entry point, and would expand upon existing services like paper money orders. These types of services could immediately result in increased foot traffic and new revenue. And to the extent that these services are expansions of existing offerings, the changes required within the Postal Service would be minimal compared to more complex financial services. Moreover, these services could build off the Postal Service's current network and infrastructure.

Pilot tests in targeted areas could prove the value of postal financial services. A quick victory or two could help gain support for additional services in the future.

[60] Pew Charitable Trusts, *Loaded with Uncertainty: Are Prepaid Cards a Smart Alternative to Checking Accounts?*, September 2012, http://www.pewstates.org/uploadedFiles/PCS_Assets/2012/Prepaid_Checking_report.pdf, pp. 18-20.

It may be best for the Postal Service to introduce products through pilot programs or market tests in a small number of Post Offices in select geographic areas. If the new services are successful in these limited tests, the Postal Service could expand the offering to include additional Post Offices and locations. Some products might have ready-made target audiences in certain locations, such as areas with large immigrant communities.

Consider Partnerships with the Private Sector

The Postal Service could create a “win-win” situation by partnering with banks and other organizations to provide financial products and services to new customers. Postal financial services could complement the current offerings from banks by helping banks reach customers in new geographic areas, by offering products to customers who were not previously a main focus of banks, and by helping some customers transition to traditional savings or checking accounts. Moreover, a partnership would highlight what each partner brings to the table. The Postal Service offers trust, a vast physical network, and other critical assets. Banks offer reliability, expertise, and competence when it comes to financial transactions. They also could provide valuable knowledge that could help the Postal Service structure new offerings. The end results could be new services for customers, more revenue for banks, and an easier way for the Postal Service to expand its presence in the financial services market. In addition, the right partners could bring much needed startup cash to the table as part of the deal, overcoming the Postal Service’s current funding limitations.

To start, the Postal Service should identify which financial products and services would best be offered through partnerships. Some partnerships might be most effective if they included multiple banks or other institutions. Different products will likely call for different partners as well, based on the needs of the potential customers and the service gap the partners are trying to fill. One important note of caution: the Postal Service should be very mindful to ensure that no partnership damages its reputation. The level of trust the Postal Service has earned from the public is an unmatched asset, and one that should not be jeopardized.

Identify and Understand Key Customers

Although some financial products and services offered by the Postal Service could appeal to segments of the broader market, most of these offerings would be especially attractive to the underserved. As discussed above, the underserved have a wide range of needs and characteristics. Understanding the varying needs of different customers will be crucial for postal financial services to succeed. For example, some services may appeal to young consumers or those who are not native English speakers. As such, marketing toward these consumers should be designed so that it addresses their specific needs and clearly signals that the Postal Service and its partners are listening to what these consumers want. The FDIC’s surveys of banks on their efforts to reach the underserved could provide useful tips on how best to serve specific customer segments.[61] In addition, many alternative financial services providers have been highly

[61] See http://www.fdic.gov/unbankedsurveys/.

successful in reaching underserved markets, and their success stories could provide useful lessons.

Monitor and Respond to Emerging Trends

The market is changing rapidly and the Postal Service should keep an eye on key trends to ensure that it positions itself effectively to meet a variety of potential future scenarios. Depending on the outcomes of these trends, the Postal Service could either be well positioned or scrambling to catch up.

Cashless Economy and Mobile Banking

The United States is moving toward a cashless economy. A 2012 Rasmussen Reports poll confirmed Americans' dwindling reliance on physical currency: 43 percent had gone a full week without paying for anything with cash or coins.[62] A suite of financial services and products would help the Postal Service to meet the needs of customers in this increasingly cashless economy and allow it to adapt in a rapidly evolving market.

We are living in an increasingly cashless economy. The Postal Service can help the underserved function in this new landscape.

Even with the rush to adopt cashless payment options, one big question remains: what will happen to the underserved in this cashless economy? People without access to payment cards cannot participate in e-commerce or other aspects of the digital economy. Many of the underserved — especially those who are unbanked — prefer or are confined to using cash for nearly all of their transactions. For these consumers, the Postal Service could provide easy and convenient ways for them to convert their cash to digital currency or other electronic payment methods. And it is not just the underserved who are sticking to cash; some young Americans choose to use cash because they want to avoid taking on debt.[63] In addition, many businesses have stopped even accepting credit cards after banks increased the fees associated with processing transactions.[64] These large increases in fees may be especially challenging in struggling communities, where businesses may have difficulty passing the costs along to their customers.

Related to the rise of a cashless economy is the growth of mobile banking, which is fueled by the spread of smartphones. According to Federal Reserve research, 59 percent of the unbanked and 90 percent of the underbanked have a mobile phone, roughly half of which are smartphones. Moreover, 49 percent of underbanked consumers reported using mobile banking in the past 12 months.[65]

[62] Sarah Todd, "*Got Cash? Not for Long.,*" *American Institute for Economic Research*, June 14, 2012, https://www.aier.org/article/7672-got-cash-not-long.
[63] Rachel Sapin, "Credit-shy: Younger generation is more likely to stick to a cash-only policy," *Denver Post,* August 26, 2013, http://www.denverpost.com/styleheadlines/ci_23929523/credit-shy-younger-generation-stick-cash-only-policy.
[64] David Lazarus, "Some merchants stop taking credit cards because of high fees," *Los Angeles Times*, July 1, 2011, http://articles.latimes.com/print/2011/jul/01/business/la-fi-lazarus-20110701.
[65] Board of Governors of the Federal Reserve System, *Consumers and Mobile Financial Services 2013*, March 2013, http://www.federalreserve.gov/econresdata/consumers-and-mobile-financial-services-report-201303.pdf, p. 2.

Adapting to New Financial Regulations

New regulations could alter the financial services landscape and potentially lead to an increase in the number of customers looking for new solutions. The 2010 Dodd–Frank Wall Street Reform and Consumer Protection Act was seen as the most far-reaching piece of legislation in the financial sector since 1933's Glass–Steagall Act. However, only about half of the hundreds of provisions required under Dodd-Frank have taken effect.[66] One of the completed results of Dodd-Frank is the establishment of the Consumer Financial Protection Bureau (CFPB). Among other things, the CFPB has regulatory authority over many non-bank financial institutions, such as payday lenders. These institutions were not previously subject to such federal regulatory control.

These regulatory developments could affect the Postal Service in at least two ways. First, they could directly affect existing and potential financial products and services offered by the Postal Service. Second, there could be a role for the Postal Service to play in helping banks and other institutions to comply with regulations. For example, the Postal Service might explore whether banks that partner with it could earn credit toward fulfilling their requirements under the 1977 Community Reinvestment Act to meet the credit needs of the communities where they operate.[67] This might be especially helpful for community or local institutions that have fewer resources to dedicate to ensuring compliance with new and changing regulations.

The UPU International Financial System Might Offer Advantages

Another possible way for the Postal Service to expand its financial services offerings could be joining the International Financial System (IFS) of the Universal Postal Union (UPU). The IFS is a software application developed by the UPU for the secure and expedient electronic transfer of international and domestic money orders. It supports a variety of fund transfer services, including cash and account-based money orders, and urgent wire transfers. Currently, the IFS network includes postal operators in at least 60 countries.[68] By using this platform, global posts can avoid developing their own system for such payments, which could result in shorter implementation time and lower costs.

The UPU's International Financial System could be an effective and low-cost way for the Postal Service to offer new electronic money transfers.

There is a huge market opportunity for secure international money transfers in the United States: migrant remittance outflows in the United States grew

[66] U.S. Government Accountability Office, *Financial Regulatory Reform: Regulators Have Faced Challenges Finalizing Key Reforms and Unaddressed Areas Pose Potential Risks,* Report to Congressional Addressees No. GAO-13-195, January 2013, http://www.gao.gov/assets/660/651401.pdf, p. 5.
[67] Federal Reserve, About the Community Reinvestment Act, http://www.federalreserve.gov/communitydev/cra_about.htm.
[68] UPU, Electronic Money Order, http://www.ptc.upu.int/ps/ifs.shtml, and Bishar A. Hussein, Director General for the UPU, "Opening address to the Postal financial services conference, Paris, France," February 28, 2013 http://actualites.upu.int/actualites/discours/upu-la-poste-conference/. According to UPU officials we spoke with, the UPU is currently working on integrating additional features able to support mobile and e-commerce payments. Personal communications, July through October 2013.

from $35 billion in 2000 to more than $51 billion in 2012.[69] The IFS could provide the opportunity for the Postal Service to offer new channels for international money transfers — beyond just paper money orders and the Dinero Seguro service — and expand the geographical reach of its money transfers. In addition, the IFS could provide a safer and faster digital alternative to domestic and international paper money orders, without requiring the Postal Service to be responsible for the back-end operations. There is a growing need for ways to send money abroad, and the Postal Service could play a much bigger role in helping to fulfill that need.

As with any new endeavor, there are implementation considerations. The Postal Service would need to make sure that the IFS complies with all necessary laws and regulations, and that the service could be offered profitably without slowing down transactions. Even though the Postal Service has previously looked into the IFS and decided not to implement it, times have changed. A fresh look may be in order. Among the many reasons, the IFS might help the Postal Service to serve a quickly growing population in the United States: foreign-born individuals.[70] Between 2000 and 2011, the foreign-born population grew from 31.1 million to 40.4 million.[71] The Postal Service's participation in the IFS could be valuable as this number continues to grow.

Conclusion

Underserved Americans need financial services that work for them, especially in today's tough economy. The Postal Service is in an excellent and, in some ways, unmatched position to meet these citizens' needs. A suite of non-bank financial services offered through the Postal Service — available online, through mobile devices, and at Post Offices in every community — could greatly benefit families everywhere. Postal financial services could help American families to save money through avoiding exorbitant fees and interest. This would make it easier for these families to pay their bills on time, build up a more comfortable level of savings, and spend their money in better ways — which would benefit the economy overall. And someday, many of these same families might be able to open a traditional bank savings or checking account. In addition, as shown by postal organizations all across the globe, moving into financial services has been the best way for posts to shore up their retail networks and find new revenue. As the Postal Service continues to look for new ways to serve the citizens of the 21st century, non-bank financial services may be the "killer app" for diversifying its revenue base.

[69] World Bank, *Migrant Remittance Outflows,* 2013, http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1288990760745/RemittanceData_Outflows_Oct2013.xls.
[70] The Bureau of Labor Statistics defines foreign-born persons as "persons who reside in the United States but who were born outside the country or one of its outlying areas to parents who were not U.S. citizens. The foreign born include legally-admitted immigrants, refugees, temporary residents such as students and temporary workers, and undocumented immigrants." For more information, see http://www.bls.gov/news.release/pdf/forbrn.pdf.
[71] Pew Hispanic Center, *Statistical Portrait of the Foreign-Born Population in the United States, 2011,* 2013, http://www.pewhispanic.org/files/2013/01/PHC-2011-FB-Stat-Profiles.xlsx.

Appendix A The Postal Savings System

The History of the Postal Savings System

The Post Office Department offered savings accounts for decades, from the early 20th century until the late 1960s. The system found a niche among immigrant populations and provided readily available access to basic financial products for all Americans. However, interest waned over the decades of its operation, eventually leading Congress to discontinue the program.

Origins and Design

From 1911 to 1967, the Postal Savings System gave people the opportunity to make savings deposits at designated Post Offices nationwide. In establishing the system, Congress intended to encourage people to save their money in banks rather than under their mattresses, bring in savings from immigrants who may have used post offices for savings in their native counties, provide for a safe place for individuals to deposit their money, and create a deposits system that was more convenient for the public. Initial banking industry opposition to the system turned into support when bankers realized that the system was successfully drawing in a lot of money that used to be stored away in cookie jars and other hidden places.[72]

To minimize competition with banks, deposits were limited to $500 and the interest rate to 2 percent. Deposited funds were to be funneled to local banks, which would pay a 2.25 percent interest rate for the money — considerably less than the 3.5 percent that most banks were paying for deposits at that time, and lower than the interest paid to depositors by any other post in the world.[73] Because banks would use the postal deposits to fund loans to local consumers and businesses, the economic benefits of those deposits stayed with local communities. Banks found they had little reason to oppose an institution providing them a source of cheap money, so not much controversy surrounded increases in deposit limits to $1,000 in 1916 and $2,500 in 1918. The 2 percent interest rate for depositors was never changed, but the 2.25 percent rate paid by banks to the Postal Savings System was raised to 2.5 percent in 1934.[74]

Growth and Decline

Throughout the decades of its operation, the Postal Savings System had its ups and downs in popularity. Deposits grew slowly for the first 20 years, and throughout that period never amounted to more than 1 percent of the total amount in savings and time accounts in the banking system. The situation changed in the 1930s, when many banks failed during the Great Depression, and the Postal Savings System was perceived as

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[72] U.S. Postal Service, *Postal Savings System*.
[73] Patricia Hagan Kuwayama, "Postal Banking in the United States and Japan: A Comparative Analysis," *Monetary and Economic Studies,* May, 2000, http://www.imes.boj.or.jp/research/papers/english/me18-1-3.pdf, p. 78. For example, the United Kingdom paid 2.5 percent; Canada, Austria, and Hungary paid 3 percent; and Japan paid 4.2 percent in tax-free interest, although in general interest rates were higher in the United States than in any of these countries. E.W. Kemmerer, "The United States Postal Savings Bank," *Political Science Quarterly,* vol. 26, no.3, September, 1911, p. 485.
[74] Patricia Hagan Kuwayama, "Postal Banking in the United States and Japan: A Comparative Analysis," p. 78.

uniquely safe and reliable before the government established bank deposit insurance. A second surge in deposits came in the 1940s, when the 2 percent interest paid by the postal system to depositors was higher than the rates banks were paying.[75] The system hit its peak in 1947 with nearly $3.4 billion in savings deposits from more than 4 million customers using more than 8,100 postal units.[76]

Usage of the Postal Savings System dropped over the next couple of decades due to several factors, including increased interest rates from traditional retail banks for savings deposits. As explained in the Postal Service's official history: "after the war, banks raised their interest rates and began offering the same governmental guarantee as the Postal Savings System. In addition, United States savings bonds gave higher interest rates. Deposits in the Postal Savings System declined, dropping to $416 million by 1964."[77] The Postal Savings System ended on July 1, 1967.[78]

Who Used It?

One particularly interesting fact about the Postal Savings System was its popularity among recent immigrants to the United States during the early 20th century. These immigrants embraced the system much more than non-immigrants. For example, in 1915, fully 71.8 percent of the total deposits in the system belonged to foreign-born immigrants, even though they were only 14.3 percent of the overall U.S. population.[79] The statistics are particularly stark when considered on a per capita basis. For example, Americans overall held an average of just 23 cents each in postal deposits in 1915, while Greek immigrants had an average of $11.70 and Russian immigrants (who held a fifth of all postal deposits) had an average of $7.85 each.[80] One reason immigrants from southern and eastern Europe were partial to the Postal Savings System was the well–publicized problems of informal "immigrant banks" that depended on cultural ties but often proved dishonest.[81]

[75] Ibid., p. 82.
[76] U.S. Postal Service, *Postal Savings System.*
[77] U.S. Postal Service, *The United States Postal Service: An American History 1775-2006*, November 2012, https://about.usps.com/publications/pub100.pdf, p. 29.
[78] Ibid.
[79] Patricia Hagan Kuwayama, "Postal Banking in the United States and Japan: A Comparative Analysis," p. 80.
[80] Ibid.
[81] Ibid., pp. 80-81.

Appendix B Examples of Postal Financial Services

The following table provides examples of postal financial services that might be considered by the Postal Service and its stakeholders.

Table 1: Examples of Postal Financial Services

Service	Description
E-commerce payments	The facilitation of e-commerce payments for the underserved, both domestic and cross-border. These payment methods could include credit cards, direct debit, mobile payments, wire transfers, and other payments.
Bill payments	Bills currently paid in cash at payday loan centers, retailers, and other locations.
Government-to-citizen payments	Payments made by government agencies to the unbanked by means other than direct deposit or prepaid cards.
Closed-loop prepaid cards	Prepaid cards that can only be used at certain locations, such as gift cards for a specific store or group of stores.
Open-loop reloadable prepaid cards	Prepaid cards with a network logo (Visa, MasterCard, American Express, or Discover) and which can be used at any location that accepts that brand. Some of these cards have additional features, such as direct deposits or a link to a savings account.
Mobile financial services	Use of mobile devices as a specific payment mechanism or as a channel of access to bank accounts.
Check cashing	The cashing of underserved customers' checks for a fee.
Savings	Encouraging customers to build up savings, possibly through savings features on prepaid cards.
Identity authentication	Identity authentication services for citizens, businesses, and financial institutions. This could include identity authentication features embedded into a Postal prepaid card, which would increase security and privacy in digital and physical transactions in support of e-commerce growth.*
Financial literacy	Providing information on financial literacy, counseling, education, and other topics for the benefit of underserved consumers.

Source: Decision/Analysis Partners analysis provided to USPS OIG.

*Note: For more information, see U.S. Postal Service Office of Inspector General, *Digital Identity: Opportunities for the Postal Service*, RARC-WP-12-011, http://www.uspsoig.gov/sites/default/files/document-library-files/2013/RARC-WP-12-011.pdf.

Appendix C Lessons Learned from International Posts

Many international posts are already providing financial services, through which they have found new ways to meet customer needs and bring in additional revenue. Although there is no “one size fits all” model for introducing postal financial services, due to differences between countries and posts, there are common success factors and implementation strategies across multiple postal operators. Figure 8 shows the earnings obtained by several industrialized countries through postal financial services.

Figure 8: Financial Services at Foreign Posts

FINANCIAL SERVICES DRIVE EARNINGS AT FOREIGN POSTS

For many posts abroad, financial services account for a large portion of sales and profits.

Country	Financial services earnings
Switzerland	71% of operating profits
New Zealand	70% of profits
Italy	67% of profits
France	36% of pre-tax earnings
United Kingdom	25% of sales

Source: Canadian Centre for Policy Alternatives, *Why Canada Needs Postal Banking*.

International Posts Are Succeeding at Financial Services

In March 2013, the UPU issued a report on the state of postal financial services development around the world (139 countries) and the role of postal operators in financial inclusion.[82] The UPU found that posts are key players in advancing financial inclusion in most of its member countries, second only to banks.[83] In addition, the UPU found that postal operators around the world often use their nationwide infrastructures to help ensure success for postal financial services. These vast footprints allow posts to maintain high volume and easy access for customers. Moreover, foreign posts are often already deeply integrated into community life.[84]

The UPU found that the business models adopted by postal operators for financial services varied widely. They ranged from relatively basic arrangements, like rental of post office space or offering simple transactional services, to more complex arrangements like transforming postal operators into full-fledged postal banks.[85] Many postal operators followed more than one business models, and often retained basic models while progressing to more complex models.

[82] Alexandre Berthaud and Gisela Davico, *Global Panorama on Postal Financial Inclusion: Business Models and Key Issues*.
[83] Ibid., p. 9.
[84] Ibid, p. 7.
[85] Ibid., pp. 9, 83.

The UPU also identified 10 common factors that have been critical to the success of postal financial services across the globe.[86] Table 2 lists these success factors.

Table 2: How Have Posts Made Financial Services Successful?

Success Factor	What Leads to Success?
Network	Does the network reach all across the country, including urban and rural areas? Are the different points in the network well connected?
Staff	Are staff properly trained? Are they computer literate? Do they offer high-quality customer service?
Financial capacity	Does the post have the resources to invest in upgrading its systems and training its staff? Is there enough cash moving through the network to cover financial transactions?
Trust	Does the public trust the post? Does the post earn and maintain this level of trust?
Automation and process integration	Are there processes to guide critical functions, such as how much cash is in post office drawers and how often the cash should be replenished? Does the post have the right information technology?
Willingness to foster financial inclusion	Is there popular support behind using the post as a means to enhance financial inclusion?
Governance between the post and postal financial services	Is there an effective system in place to govern the relationship between the post and its postal financial services? Is it clear whether the postal financial services will be a part of the post or completely independent of the post?
Legal and regulatory framework	Is the post authorized to provide financial services, or to form partnerships with banks? Does the post have access to national payment systems? Can the post issue forms of electronic money?
Marketing	Can the post effectively promote its products and brand? Does it understand its customers' needs?
Flexibility	Does the post offer convenient hours of operation? Can customers get services close to home? Can the post adapt to customers' changing needs?

Source: Alexandre Berthaud and Gisela Davico, *Global Panorama on Postal Financial Inclusion: Business Models and Key Issues*, UPU, March 2013.

Implementation Strategies of International Posts

One of the experts we contracted to research this project has real-life experience in assisting postal operators to implement financial services. That expert also identified success factors for international posts engaged in financial services. He found that one of the posts' main strengths is their ability to reach out to a mass market, including low-income and unbanked consumers. These consumers are typically not served by major

[86] Ibid., p. 10.

banks, and the consumers often feel uncomfortable in the environment of a traditional bank branch. In addition, our expert found that international posts succeed at financial services when they engage in effective marketing campaigns and excel at dealing with consumers from a wide range of cultural backgrounds.

Research has shown that postal financial services have resulted in significant revenues for some international posts, at the same time as revenue from other sources has continued to decline.[87] This can help to maintain the vitality of postal networks. However, implementation is not as easy as flipping a switch. International posts used different implementation strategies to help ensure that their financial services were successful, including the following:

International posts have used their ubiquitous networks and ability to reach many different types of consumers to succeed at financial services.

- Successful financial services complemented the established banking sector, rather than openly competed with it.[88] In part, this has been done by focusing on niches that traditional banks generally do not prioritize.
- A diverse suite of financial services will help bring in additional customers, and can boost the viability of individual products or services that have a natural market but might not be profitable if offered on their own.
- Forming partnerships with established financial institutions lets posts focus and capitalize on their unique strengths, capabilities, and experience.
- While financial products and services may be best managed by a licensed, regulated bank partner, the operations should be overseen by a dedicated unit inside the post.
- Transparency and accountability over fees, processes, and other critical aspects of financial services help posts to make their offerings appeal to customers who might be wary of doing business with some traditional banks.
- The positive reputation and public trust associated with posts are crucial to the success of postal financial services.
- It is essential to understand the various needs of different consumer segments, such as mass market customers versus the underbanked.

[87] Canadian Center for Policy Alternatives, *Why Canada Needs Postal Banking*, p. 10.
[88] Decision/Analysis Partners analysis provided to USPS OIG.

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