Systemic Barriers to Banking the Unbanked

Since founding the Bank On movement in 2006, the San Francisco Office of Financial Empowerment (OFE) has found persistent disparities in banking access due to structural flaws in the financial system. This brief outlines four major systemic barriers to banking — distrust of mainstream financial institutions, ChexSystems records, debt in collections and asset limits — as well as opportunities to remove these barriers and increase banking access.

Treasurer José Cisneros and the Office of Financial Empowerment (OFE) launched the groundbreaking Bank On San Francisco program over ten years ago after realizing that many residents of San Francisco did not have access to safe and affordable bank accounts and instead relied on costly fringe financial products, such as payday lenders and check cashers. The program had strong success initially with unbanked rates dropping from 15-20 percent in 2005 to 5 percent in 2017. However, the rates of unbanked clients remain persistently high for certain populations. In our Smart Money Coaching program that provides one-on-one financial coaching to low-income residents, 42 percent of Black clients enter the program unbanked compared to 32 percent of the overall Smart Money Coaching client population.

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Having a bank account is the door to the financial mainstream and greater economic stability. Living without a bank account is expensive as clients are forced to use fringe financial services, such as check cashing services, money orders and payday loans. A recent unbanked Smart Money Coaching client relied on friends and check cashers to cash his paychecks for the past two years before being successfully connected to a safe and affordable bank account. Such practices are common and costly: one analysis found that the average family earning $25,000 per year could spend about $2,400 or ten percent of their income on financial transactions, including fees for prepaid cards and money transfers. Once someone has a bank account, they can access other financial products and services that can help them build wealth and achieve upward economic mobility. Yet, financial coaches who work with Smart Money Coaching consistently report that banking is the hardest outcome for clients to achieve. After ten years of doing this work, why is that still the case?

The financial system is not designed to serve low-income consumers, and is rife with systemic racism that harms Black Indigenous People of Color (BIPOC) communities. Many of the financial challenges our clients experience stem from structural flaws embedded in the financial system that strip families of wealth and keep them in a cycle of poverty. In order to support clients' access to safe and affordable banking, OFE realized it was critical to understand these systemic barriers to help individual clients navigate the current financial system and simultaneously advocate for progressive policy reforms. Through programming and research, OFE has identified four systemic barriers to banking that our Office is committed to addressing. These systemic barriers include distrust of mainstream financial institutions, ChexSystems records, debt in collections, and asset limits. This short report will briefly describe each of the barriers and then describe OFE's current work to improve access to banking for low-income consumers.

Systemic Barriers to Banking

Distrust of Mainstream Financial Institutions

The first crucial barrier to banking is that many people, and in particular low-income people and people of color, understandably distrust mainstream financial institutions due to their history of predatory and discriminatory policies and practices which have harmed these communities. These policies have barred communities of color from accessing the financial mainstream and building wealth and resulted in two separate and vastly unequal financial systems (often referred to as the 'dual financial system'). Discrimination in the financial system is persistent, and includes redlining – the systemic denial of loans and insurance to communities of color by the federal government and private companies — the predatory products that led to the 2008 financial crisis, current disparities in mortgage lending, banking deserts, and outright discrimination in services at branches. These practices deny consumers access to the financial mainstream, drive them to expensive fringe financial services and strip wealth from communities of color, resulting in a racial wealth gap where white families have an average net worth ten times that of Black families. Given these structural issues, it is no surprise that the Federal Deposit Insurance Corporation (FDIC) finds almost one-third of unbanked consumers don't trust banks.

Smart Money Coaches can help clients with previous bad experiences with banks reenter the financial mainstream: one client explained,

> **My coach helped me re-open my checking account with a bank I was with for over 13 years but had been closed because I couldn't afford to pay the bank fees through the pandemic.**
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> - *Ardelia, a Transitional Age Youth served by Smart Money Coaching*

ChexSystems

According to the National Consumer Law Center (NCLC) and Cities for Financial Empowerment (CFE), over 80 percent of banks and credit unions screen new and existing customers through consumer reporting account screening agencies like ChexSystems to determine their eligibility for an account. ChexSystems tracks consumers' checking and savings account history and generates individual records that include activities such as bounced checks, overdrafts, unpaid negative balances, involuntary account closures and suspected fraud, among others. Negative ChexSystems records, like account abuse and suspected fraud, can remain on someone's report for up to five years. When consumers with negative records in ChexSystems apply to open a bank account, they are frequently denied, with limited information about the reasons why and have limited ability to contest this denial. The process is entirely opaque: banks don't publish their policies on ChexSystems records, and most consumers don't know what ChexSystems is, are not aware that they have a record or what the implications of this record is. Until very recently, consumers could only receive reports by mail. It appears that ChexSystems recently added an option for consumers to view their reports online, though this has not been widely publicized. The reports are written in legal jargon, making them difficult to understand, and the dispute process can be difficult even with the assistance of a coach.

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ChexSystems records impact millions of people — one 2005 report (the most recent data found) estimated up to 19 million people have records — and this system disproportionately impacts low-income individuals and communities of color, potentially keeping them from opening bank accounts and accessing financial mainstream. A primary reason consumers end up in ChexSystems is due to repeated overdrafts, indicating that they simply do not have enough income to cover their basic needs. A 2008 working paper by Harvard Business School professors reported that involuntary bank closures — which lead to ChexSystems records — were most frequently found in communities of the U.S. with high Black populations, high rates of households headed by single mothers and low levels of wealth. More recently, an initial OFE analysis of almost thirty Smart Money Coaching clients in San Francisco found that more than one in five unbanked clients had account closures on their ChexSystems report, typically due to repeated or unpaid overdrafts.

Recently one client came to Smart Money Coaching in need of assistance because their bank account had been forcibly closed, and the client was not sure if their options for recourse. The financial coach and client reviewed the client's ChexSystems record and found that the closure was due to the financial institution flagging a payment as suspected fraud despite no wrongdoing on the part of the client. The financial coach helped the client file and resolve a dispute with ChexSystems as well as open a new bank account at Mechanics Bank, a financial institution that has more progressive policies for new customers with negative ChexSystems records.

Debt Collections and Bank Levies

Another systemic barrier to banking is debt in collections. Clients with private and government debt in collections can have money taken directly from their bank accounts by creditors via a bank levy. These bank levies create mistrust between banks and customers. Smart Money Coaching clients have shared that they hold the bank responsible for the levy, not the creditor, and feel that their money will not be protected in future similar situations. It is critical that advocates and financial coaches understand the implications of different types of debt on banking access. For example, some clients may fear garnishment even though the debt they have cannot be levied. Financial coaches should work with clients to understand their debt, explain the impacts of the debt, including potential garnishment or bank levies, help clients negotiate down or pay off the debt, and perform a banking assessment to find banking opportunities that work for clients while they address their outstanding debt. Addressing debt, including debt in collections, is a critical part of the Smart Money Coaching model, because it helps clients increase their financial security today while charting a new path forward.

There are racial disparities in levels of debt and collections. According to Prosperity Now, Black households are more likely to be late paying debts than white households. When they are late paying back their debt, Black and Latinx individuals are more likely to be sued for defaulting on payments than white individuals, according to a ProPublica investigation. In terms of debt owed to the government, OFE's sister program, The Financial Justice Project, has shown again and again how government fines and fees can result in crushing debt that disproportionately harms low-income communities of color. According to the Urban Institute, 22 percent of San Franciscans overall had delinquent debt and that number increases to over 30 percent of residents in Bayview-Hunters Point and Treasure Island, both neighborhoods with significant Black, low-income populations.

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Asset Limits

The final structural barrier to banking that OFE identified are asset limits. Many clients explain that they are concerned that having a bank account could jeopardize the public benefits that they depend on to survive in one of the most expensive cities in the United States. Most public benefits programs — such as the Supplemental Nutrition Assistance Program (SNAP) and Temporary Assistance for Needy Families (TANF) — have strict eligibility requirements around familial assets and require recipients to document and recertify their assets on a frequent basis to retain eligibility. If recipients have more than a certain amount of assets – for example, $2,000 for Medi-Cal – they will lose their benefits for having too much money. The fear of losing benefits because of their savings keeps many families from opening bank accounts at all. For example, Research from Urban Institute finds that asset limits keep families from saving and opening bank accounts because they are worried these accounts might make them ineligible for public benefits. In this way, asset limits can disincentive and penalize families from saving ultimately and paradoxically keeping families from becoming financially stable so they can exit systems of poverty.

Solutions to Improve Access to Banking

Now that OFE has identified these barriers, we are committed to doing more to address them to ensure that low-income communities and people of color have equal access to the financial mainstream. One of OFE's foundational beliefs is that access to a bank account is the door, the first step, to the mainstream financial system and achieving greater economic stability.

Our current work is focused on addressing the outlined barriers via the four following tactics:

Targeted Coaching to Gather Data and Stories

The core mission of Smart Money Coaching is to empower clients to navigate the current financial system so that they can make informed decisions and improve their financial lives. OFE is first and foremost focused on serving populations that are farthest from the financial mainstream and seeks to advocate for more equitable access to financial products and services that will enable this population to build their financial capability. With Smart Money Coaching, OFE targets communities most likely to experience systemic banking barriers, including transitional age youth experiencing homelessness, residents in subsidized public housing developments, and clients in Human Service Agency's Welfare-to-Work program. OFE is acutely aware that no amount of financial coaching will solve the systemic structural barriers that our clients face, including not just barriers to banking but also unstable jobs, high cost of living (especially housing) and insufficient income. However, by gathering information and stories from our clients' lived experiences, OFE can build a detailed picture about these systemic barriers and begin the hard work to advocate for broader reforms.

> **As a coaching manager, I have seen the ways that financial coaching and support can make a difference in people's lives, particularly for those who are farthest from the financial mainstream. The daily work that we do at BALANCE is so crucial to improving individual outcomes, but this work alone is not enough because we know broad scale reform is needed. We are grateful to have OFE's support in pursuing systemic change – from creating a solution process for clients with ChexSystems records, to clarifying California's new policies regarding asset limits for CalWORKS, to most recently supporting clients to trouble shoot issues with the IRS Economic Impact Payment non-filer tool. I've been working for Smart Money Coaching for almost three years and every day brings new challenges. I appreciate OFE's work as a partner to help us meet emerging needs of our clients and fight for systemic change.**
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> *– Aqil Algere, financial coaching manager*

ChexAdvisor & ChexSystems Resolution Process

To address clients' ChexSystems records, OFE recently partnered with the Credit Builders Alliance to allow Smart Money Coaching service providers to use their new ChexAdvisor Educational Report. Rather than waiting for a copy to arrive via mail, coaches now have real-time access to their clients ChexSystems reports online via the ChexAdvisor tool. To address these records, OFE created a ChexSystems records resolution process and workflow for the Smart Money Coaching program so that clients understand why they have a record and their options for resolving and disputing their records so they can open a bank account. Through the Bank On program, OFE plans to continue to advocate for banks to offer more second chance accounts and to be more transparent about their policies and procedures around ChexSystems records.

Promoting Innovative Financial Products

OFE is also promoting innovative financial products for clients struggling with these systemic barriers who might not currently be good candidates for a traditional bank account. For example, Smart Money Coaching recently partnered with Community Financial Resources (CFR) to offer their consumer-friendly Focus Visa Prepaid Debit to clients. This card is available without any ChexSystems review or credit check. Beyond the CFR prepaid card, OFE is researching other financial products and services, including innovations from the financial technology sphere, that are accessible to clients with negative ChexSystems records. Though these products do not address root causes, they can help clients increase their financial capability and support and put them on a path to the financial mainstream.

Advocacy

Lastly and most crucially, OFE is engaged in advocacy at the local, state and federal level to address these systemic barriers to banking to ensure that all San Franciscans have access to the financial mainstream. This advocacy includes calls for greater transparency and access to ChexSystems records and requirements that banks publicize their policies around customers with negative ChexSystems records. For debt in collection, OFE supports local, state and federal policies to improve debt collection rules and oversight for both government-issued and private debt, including limiting the amount of money that can be garnished or levied, promoting ability-to-pay standards and eliminating collections for vulnerable populations (for example, those re-entering after serving time in jail or prison). In October 2019, Governor Newsom signed SB 616 into law, which prevents debt collectors from levying all of the funds in an individual's bank account and protects the last $1,724 in an account (the minimum a family of four in California needs to survive each month according to the California Department of Social Services, adjusted annually). However, these limitations do not apply to certain debts, including child and spousal support debt and debt owed to the government. On asset limits, last year California increased the asset limits for CalWorks recipients from $2,250 to $10,000. More reform has been proposed with State Senator Scott Wiener leading the movement to eliminate asset limits entirely for CalWorks, most recently with SB 268. While all these reforms are impactful, OFE believes that further protections are needed for families, and our office is committed to working closely with our partners to advocate for better policies around collections, asset limits and ChexSystems.

Safe and affordable accounts through Bank On San Francisco are ineffective if our most vulnerable communities cannot access these accounts due the systemic banking barriers. To be serious about reducing the unbanked rates for low-income communities, policymakers and advocates must move beyond simplistic, individualistic narratives and must tackle these systemic barriers head-on. Addressing these issues will require a combination of data collection, financial innovation, and legislative advocacy, and ultimately it will require all parties to come together to reimagine a financial system that is accessible for everyone. Anything less fails to meet the demands of the moment.