

The PayNet Deposit Program: Check Cashier-Credit Union Partnerships And the Point of Banking Machine

Executive Summary

The PayNet Deposit program is a partnership among check cashers and credit unions in the New York City metropolitan area that provides credit union members with access to their accounts through check cashing locations. The program is a prime example of the type of innovative partnership that has the potential to work to the benefit of both company and consumer to increase access to financial services among underbanked populations. This report outlines the key aspects of the PayNet Deposit program, including history, partners, economics and technology of the program, and lessons for expansion.

The PayNet Deposit program enables credit union members to make withdrawals, deposits, and transfers directly into their credit union accounts through point of banking (POB) machines in check cashing locations. The program, in development stages for the better part of a decade, has been operational in some form in New York City for three years. The POB machine is a bank transaction terminal with a human interface or a “manned ATM.” In contrast to ATM transactions, in which the system does not really know if the customer put money in the deposit envelope, with POB, the customer hands the money over the counter and the check cashier employee is able to verify the deposit. Moreover, in contrast to point of sale (POS) terminals, the POB platform includes interchange fees and requires bank sponsorship. Perhaps most importantly, the POB platform enables a differentiation between deposits sent through as “checks” (with holds on the funds) and deposits sent through as “cash” (with immediate liquidity of funds).

Overall, the goal of this program is to capitalize on the similarities between the financial needs of check cashing and credit union customers to bring them extended service and convenience. PayNet Deposit combines the transactional model of check cashers with credit unions’ account-based model to give consumers access to a broader set of services, at convenient locations and with affordable prices. Credit unions and other small financial institutions are looking for ways to provide service to members without the hard costs of building new branches or the administrative issues associated with shared branching. Credit unions in particular have financial and regulatory incentives to reach out to unbanked and lower-income consumers, and the POB provides one innovative way to do that. It is important to note that though there is nothing that specifically prohibits banks from joining the program, credit unions are currently the only active partners.

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Through POB, credit union members gain access to a large number of locations to engage in financial transactions. Consumers benefit from the program, as the POB machine allows immediate liquidity of funds if checks are deposited as cash,¹ and consumers can separate funds into different accounts (checking versus saving, for instance) right at the POB terminal. In addition to providing immediate liquidity of funds, the PayNet Deposit program allows consumers who generally cash their paychecks and walk away with cash with a convenient way to save money and earn interest on funds. In turn, credit unions can expand their membership base through increased “locations,” and check cashers reap fee income from the interchange and surcharge fees levied on transactions.

Transaction levels through the PayNet Deposit program are fairly small at this point, though the number of transactions has increased steadily since the beginning of the pilot. One participating credit union is nearing 1,000 deposits a month, a 214% increase over two years, while another participating credit union is using the program to attract new members. Organizers of the PayNet Deposit program are interested in seeing the program expand into other geographies outside of New York. While there is potential for the program to move to scale, challenges remain.

¹ With POB, the customer hands the money over the counter and the check casher employee is able to verify the deposit. PayNet Deposit incorporates technology that enables a differentiation between deposits sent through as “checks” (with holds on the funds) and deposits sent through as “cash” (with immediate liquidity of funds).

Part I: The PayNet Deposit Model

What is POB?

The PayNet Deposit program enables members of participating credit unions to make withdrawals, deposits, and transfers directly into their credit union accounts through point of banking (POB) machines in check cashing locations. The POB machine is a bank transaction terminal with a human interface or a “manned ATM.” The POB might be described as a cross between a POS and ATM machine. It is like an ATM in terms of processing, and it includes interchange fees, but it looks and feels like a point of sale (POS) terminal. The POB is a PIN-based machine that gives customers access to their bank accounts, as opposed to just making purchases via POS. Unlike ATM transactions, in which the system does not really know if the customer put money in the deposit envelope, with POB, the customer hands the money over the counter and the check casher employee is able to verify the deposit. The POB platform enables a differentiation between deposits sent through as “checks” (with holds on the funds) and deposits sent through as “cash” (with immediate liquidity of funds). Moreover, the POB platform requires bank sponsorship. Also, in this system, financial institutions pay interchange fees to check cashers.

Overall, the goal of this program is to capitalize on the similarities between the financial needs of check cashing and credit union customers to bring them extended service and convenience. PayNet Deposit combines the transactional model of check cashers with credit unions’ account-based model to give consumers access to a broader set of services at convenient locations with affordable prices. Currently, there are about 110 POB machines in the New York metro area that are set up to process transactions through the PayNet Deposit program.

In this pilot, innovative partnerships have developed among check cashers and credit unions. The program, in development stages for the better part of a decade, has been operational in New York City in some form for three years. Two credit unions, Bethex Federal Credit Union and Actors Federal Credit Union, are actively enrolled; several others are in the process of enrolling. Four check cashing chains (including Rite Check and Pay-O-Matic, with almost 100 stores combined offering the service), in addition to several independent check cashers, currently offer this service in New York City. In 2002, a Joint Industry Committee of check cashers, credit unions, and other partners began to meet on a regular basis to consider expansion of the program and further develop the program’s infrastructure.

One of the major components of POB services that makes the program useful for consumers is the liquidity of funds. Lower-income people often need to access funds as soon as possible. Consumers might patronize check cashing locations rather than banks precisely for this reason; the need to access funds immediately has more value than saving money spent on check cashing fees. At first, POB software could not distinguish between cash and check deposits, and all deposits went through as checks and came with

a four to five day hold.² Credit union processing systems could not understand this distinction at first either. But after a few years of network certification issues with the POB platform, in 2003, credit union processors were able to change their networks and enable checks to be deposited as cash, allowing immediate liquidity of funds.³ In addition to providing immediate liquidity of funds, the PayNet Deposit program allows consumers who generally cash their paychecks and walk away with cash with a convenient way to save money and earn interest on funds.

Background and History

PayNet Deposit is the result of a long history of banking and regulatory innovations. For years, New York check cashers were the primary distribution channel for public benefits. In the early 1990s, as federal benefits began to be distributed through ATM networks via electronic benefits transfer (EBT), partnerships began to form between the NYCE network⁴ and check cashers. The POB platform, created originally by NYCE, offered a new way for check cashers to dispense these benefits and still garner a fee. At the beginning of the POB program, check cashers facilitating EBT transactions would receive both interchange fees from the network as well as surcharges from customers. Check cashers in New York therefore made an investment in the POB platform as opposed to the POS platform, which did not offer interchange income. Check cashers also preferred POB for processing EBT transactions as the platform distinguished them from grocery stores and other merchants with POS capabilities. Consumers who wished to buy merchandise could use POS machines, while consumers who wished to access bank accounts directly had to use POB. So check cashers gained access to a whole new market of banking customers through the new technology.

However, Citibank, the contractor selected by the state of New York to distribute benefits, decided during contract negotiations not to pay interchange on EBT transactions if firms also surcharged customers to access benefits. Thus, check cashers had to choose between a \$1.50 surcharge fee or a \$0.38 interchange fee in order to process benefits through POB. This meant that the interchange benefit that POB provided over POS was lost. At the time, POB machines were more expensive than POS machines. Also, customers could punch in numbers to make PIN-based transactions with POS machines, whereas customers had to physically swipe cards to make POB transactions. Check cashers maintain that this made it less convenient for some benefits recipients to process

² Within each POB transaction, there is a message stream or packet of information that is sent from the terminal and ultimately ends up at the credit union. Credit union processors, including the credit union COOP system, did not initially have the capability of dealing with long message streams that included a code to differentiate between checks and cash deposits.

³ In order to deposit checks as cash, the PayNet Deposit program stipulates that a customer must actually deposit at least 20% of the check; only 80% of the deposit, less the 0.5% or 1% check cashing fee, is available immediately as cash. This rule was adopted to circumvent attempts to receive the discounted check cashing fee of 0.5% or 1% without making a substantive deposit into a credit union account. Thus, the reduced fee is an incentive to use the service to make deposits.

⁴ Following the huge success of Citibank's ATM network in the New York area, a network formed for other banks' ATMs called the New York Center for Interchange or NYCE. NYCE, recently acquired by Metavante, is the only ATM network that supports POB. Metavante claims that NYCE's current interchange rate and switch fee structure will remain in place; the impact that this switch will have on the PayNet Deposit platform has not been determined.

transactions using POB. It became more lucrative for public benefits to be processed through POS terminals than through POB terminals and POBs began to fall out of favor in 1993, as they were too expensive to justify.

By 1995, Rite Check Cashing was the only check cashing chain in New York that still used the POB system, as the company saw the new market of bank account customers as very promising. The program offered the potential to significantly expand access to financial services for currently underserved consumers in a way that was profitable for check cashers. However, the continuance of the POB program faced numerous obstacles. NYCE was the original processor for POB; several of the POB processors that followed failed, which led NYCE to once again take over as processor. LYNK, a national provider of electronic payment, cash dispensing, and e-commerce services and products based in Atlanta, eventually stepped in and created the current processing infrastructure for POB, which is cheaper and more akin to POS. LYNK has been the exclusive back-end processor for PayNet Deposit transactions for three years (following NYCE), and today, check cashers must sign up for POB processing through LYNK.

The pilot was able to take off in part because it relied on a system that was already in place—the PayNet Payroll system. PayNet, a network operated by the Financial Services Center of New York (FSCNY), is the culmination of New York check cashers' attempts to develop a joint venture wherein various check cashers might be seen as one entity. This cooperative agreement between check cashers and banks enables check cashers to cash payroll checks from some banks' large clients. Check cashing is free to the customer; the bank pays the check cashing fee. Moreover, the PayNet model allows for industry-wide pricing for third parties and for consolidation of invoicing for those parties. Financial institutions pay a set fee, receive one invoice, and have a single point of contact through the PayNet program, regardless of how many check cashers are involved.

More than 500 check cashing locations offer the PayNet Payroll program in New York State; 110 of these locations have since added deposit transactions to their systems. Having the PayNet Payroll network in place helped make the business case for PayNet Deposit for check cashers, as the partners involved had already invested in the cooperative structure before deposits were added to the system. Moreover, financial institutions were aware that they would be able to enroll in PayNet Deposit through a single point of contact, and that the program would incorporate standard fees and policies.

Chart 1: Chronology of PayNet Deposit Program

September 1995	New York State Banking Department (NYSBD) Superintendent Neil Levin encourages check cashing industry to form joint enterprise and common cause with credit union industry
September 1997	First meeting between Check Cashing Association of New York (CCANY) and Bethex Federal Credit Union (Joe Coleman and Joy Cousminer)
October 1997	Pilot program description developed by CCANY and Bethex
February 1998	NYSBD receives first draft of POB operations manual
July 1998	NCUA denies insurance for program, as check cashers are not employees of credit union
December 2000	After several drafts of operations manual are submitted and meetings take place, NCUA approves the program
February 2001	Test POB machine with pin pad for deposits received and software tested
February 2001	NYSBD approves pilot
March 2001	POB-based deposit at Bethex successfully processed
April 2001	Unofficial start of pilot at a Bronx Rite Check location
August 2001	POB processing switches from NYCE to LYNK
October 2001	Official launch of credit union/check casher partnership and ribbon cutting ceremony
May 2002	Actors Federal Credit Union joins program
June 2002	Formation of Joint Industry Committee (JIC) to define standardized program and enlarge pilot
July 2002	Meeting with NYCE at which it was discovered that cash and check deposits could be differentiated at point of entry.
September 2003	Check cashers begin accepting check deposits and allowing consumers to deposit checks as cash, enabling immediate liquidity of funds
November 2003	Outreach to new credit unions begins

Partnership between Rite Check and Bethex Federal Credit Union

One of the most unique features of the POB PayNet Deposit program is the history of the partnership between Rite Check Cashing, with 11 locations in the Bronx and Manhattan, and Bethex Federal Credit Union, a Bronx-based community development credit union with approximately \$8 million in assets and 10,150 members. Bethex has two full service branches and also operates part-time teller windows in a church, senior citizens center and an animal hospital. Bethex’s membership includes significant numbers of low to moderate income Haitian, African-American, Caribbean, Asian, Russian, South American, and Mexican individuals. Of Bethex’ members, 60% are on welfare, Supplemental Security Income, Social Security, or other federal benefits and 40% are employed but generally do not have direct deposit of payroll.⁵

⁵ For more information on the Rite Check-Bethex partnership, see: *RETAIL FINANCIAL SERVICES INITIATIVE: A Report on Innovative Products and Services for Low Income and Unbanked Customers* by Lisa Richter and Christopher Tan. 2002.

Like other depositories, credit unions work on an account-based model but, especially in the case of small credit unions, often have difficulty reaching scale and providing full functionality. On the other hand, check cashers have a distribution network that sells transactions, and they provide liquidity, access and service to consumers. Check cashers usually have a well-developed infrastructure, including security, insurance, and renovated locations. These factors lead to possibilities for partnership.

As Chart 1 shows, Rite Check's and Bethex' efforts to form a partnership began in 1995 when the New York State Banking Superintendent at the time, Neil Levin, pointed out the similarities among check cashing and credit union customers in a speech to the New York State Check Cashers Association.⁶ It was at this time that Rite Check's CEO, Joe Coleman, began to think about ways to partner with credit unions, and conversations began with Joy Cousminer, CEO of Bethex Federal Credit Union on collaboration possibilities.

In the mid-1990s, Bethex, which has a very small advertising budget, began to realize the potential to gain new members by capitalizing on the customers who were already using check cashers. The credit union wanted to find a way to successfully reach out to those customers. Bethex also saw that check cashers provide great convenience for members, as they are open late hours and have multiple locations. Cousminer believed that working with check cashers could enable the credit union to better its goal of providing low-income families with affordable banking services.⁷

The advent of the POB machine was, according to both Cousminer and Coleman, a serendipitous event that fed off of earlier ideas on how to work together. In 1997, the partners began to see that the POB machine might offer possibilities for check cashers to engage credit union customers in a way that would allow for deposit-taking. Cousminer felt that the PayNet Deposit program would provide a way for Bethex to offer services to its members at multiple locations and ultimately gain new members by expanding its geographic base and serving a larger field of membership. Over the course of several months, a Rite Check-Bethex joint proposal was drafted and a pilot program description developed. In 1998, after much discussion and skepticism, the New York State Banking Department gave permission for the partnership to proceed.

The partners worked on an operations manual and negotiated specifics with the credit union regulator, the National Credit Union Administration (NCUA). In 2000, under the supervision of Norman D'Amours, NCUA approved the program. The PayNet Deposit POB pilot between Rite Check and Bethex became operational in early 2001. The following year, a Joint Industry Committee of check cashers, credit unions, NYCE, LYNK, JP Morgan Chase Bank and others was formed and members began to meet on a regular basis to build the infrastructure needed to expand the program beyond Rite Check and Bethex.

⁶ The New York State Banking Department regulates check cashers that are licensed in New York.

⁷ Bethex's complete mission statement can be found at www.bethexfcu.org/mission.htm.

Program Sign-Up, Management and Marketing

Financial institutions undergo a relatively straightforward procedure in order to enroll in PayNet Deposit – simply joining the NYCE network. In contrast, check cashers go through several steps in order to offer PayNet Deposit. First, if they are not already members of the association, check cashers in New York must join the Financial Service Centers of New York (FSCNY). Then, they sign an agreement stating they will abide by the rules governing the PayNet network. Check cashers must then apply to JP Morgan Chase for sponsorship into the PayNet Deposit program.⁸ At the time of this writing, JP Morgan Chase is the sole sponsoring bank of PayNet Deposit. Thus, Chase must approve all new check cashers into the program. If Chase decides to sponsor the check casher, Chase arranges for the check casher to join the NYCE network. At that point the check casher works with LYNK to develop a processing agreement.

One major issue with PayNet Deposit is the determination of who is responsible for procedures involving returned deposits; this is a main reason that JP Morgan Chase is so integral to the program. If a customer deposits a bad check, it bounces in the settlement account held by Chase. Check cashers and credit unions have responsibilities related to identifying and handling adjustments, but ultimately, JP Morgan Chase is responsible for funds held in settlement accounts if significant problems arise.

The check cashing firms engaged in the program are actively seeking additional credit union partners. Once financial institutions sign up for the program, the PayNet network of check cashers provides marketing materials for credit unions to offer to members to inform them of the program. Check cashers also place stickers and signs in their windows to advertise acceptance of PayNet Deposit. Financial institutions are ultimately responsible for marketing the program to their customers, although coordination between credit unions and check cashers is important. For example, Bethex is looking for ways to utilize the POB partnership as a way to increase credit union membership by partnering with Rite Check and other check cashers to turn walk-in check cashing customers into credit union members. Rite Check has included information about Bethex in videos showcasing Bethex product offerings in Rite Check stores. The company also provides posters advertising Bethex and membership opportunities. Further, Bethex staff make site visits and train Rite Check staff to answer questions that enable check cashing employees to process customers' requests for Bethex membership and selected credit union services. Actors has a regular newsletter in which it includes information about the program; the credit union has also done a direct mailing on POB and included information on the program along with customers' receipts.

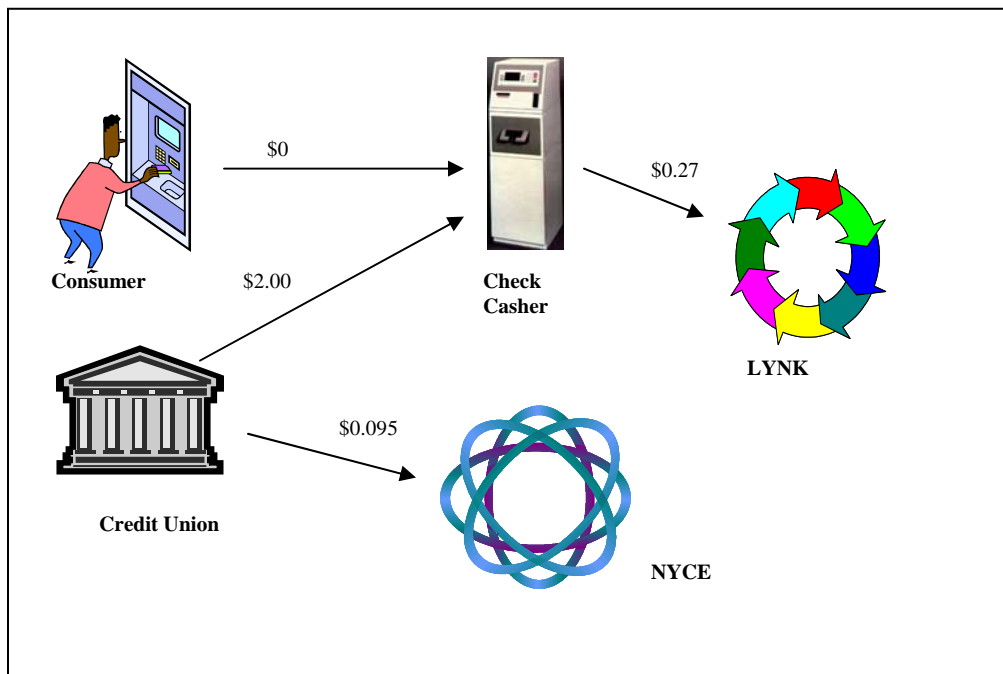
⁸ In contrast to POS systems, the PayNet Deposit POB platform requires a sponsoring bank, as check cashers are not normally deposit-takers. JP Morgan Chase Bank maintains the settlement accounts for all POB transactions and is liable for all deposits collected by sponsored check cashers. Currently, all check cashers that wish to enter into this program must go through JP Morgan Chase for approval. Chase requires check cashers that wish to enter the program to fulfill three criteria. Check cashers must: 1.) Be members in good standing of the Financial Service Centers of New York association; 2.) Have locations in New York State; and 3) Be licensed New York State check cashers. If these conditions are not met, it could take into 2005 or beyond for new check cashing partners to join the program. If the conditions are met, the bank states that check cashers can join the program within one week. Moreover, if check cashers do not currently bank with JP Morgan Chase, they also must submit financials for audit.

Economics of the Program

The POB machine offers a way for consumers to conduct banking transactions in check cashing locations that provide enhanced convenience of location and hours of operation. Credit unions receive benefits through increased access to membership; check cashers receive fee income and a way to retain underbanked consumers; and consumers receive enhanced convenience and immediate liquidity of funds, while also having access to insured deposits. Understanding the flow of funds among various partners is important to the PayNet Deposit program.

Funds Flow: Per-Transaction Costs for Deposits⁹

This figure demonstrates the funds flow on a per-transaction basis for a credit union member depositing a \$500 check into her credit union account using a POB machine in a check cashing location.



⁹ If a customer chooses to cash the check and then deposit the check as cash and receive cash immediately, the check casher would levy a 0.5% or \$2.50 fee for that service. In this scenario, the consumer would deposit at least \$100, (per PayNet Deposit rules, which require a 20% deposit into an account in order to receive the reduced check cashing fee) into her credit union account; after fees, the consumer would receive \$397.50. Portions of this figure reprinted with permission from Rite Check. 2004.

Credit Unions

Credit unions, perhaps more so than other types of financial institutions, have financial and regulatory incentives to reach out to unbanked and lower-income consumers in order to expand their membership base. The PayNet Deposit program might therefore appeal to credit unions that are seeking to find ways to include more lower-income and unbanked individuals in the ranks of their membership quickly and without significant hard costs. At this point in time, the PayNet Deposit program is most attractive to small credit unions or small community banks that are looking to expand their physical presence but lack the capital to support additional branches or engage in shared branching.

With these benefits come costs. Financial institutions pay \$175 per month to be a part of the NYCE network. If a credit union is already a member, this cost does not change when POB functionality is added. For the PayNet Deposit program, credit unions pay NYCE \$0.095 per transaction for up to 200,000 transactions per month.

Interchange fees are payments made by one party to another to compensate for providing a service to the other party's customers. In the POB system, financial institutions pay the following interchange fees to check cashers.

- a) \$2 per deposit. Financial institutions can choose to charge the customer this fee or subsidize it and absorb part or all of the cost.
- b) \$0.38 per withdrawal.
- c) \$0.25 per balance inquiry.
- d) \$0.25 per transfer.

Thus, the cost to a credit union for a single deposit transaction through the POB platform is about \$2.10. For Actors Federal Credit Union, which has \$85 million in assets, over 15,200 members, and a diverse membership that spans the country, POB is a significant cost savings over shared branching, which is the other option the credit union was considering to expand its geographic base. Because the credit union has only two branches, attracting deposits has always been challenging. Actors President Jeff Rodman estimates that the POB interchange fees are less expensive than the \$2.50 average for authorizations under shared branching. When overhead costs are taken into consideration, shared branching becomes even more expensive, while there is very little overhead with POB. The credit union also views the process of setting up PayNet Deposit as much less complex and bureaucratic than shared branching. Additionally, the cost of a POB deposit is cheaper than processing the same transaction through a teller.

Moreover, building new branches is simply too expensive for small credit unions like Bethex or for larger credit unions like Actors that have a widely-dispersed membership base. Bethex estimates that establishing a new branch costs about \$400,000 and requires three full-time equivalent staff, a large upfront cost that is not feasible for the credit union to absorb.¹⁰

¹⁰ See RETAIL FINANCIAL SERVICES INITIATIVE: *A Report on Innovative Products and Services for Low Income and Unbanked Customers* by Lisa Richter and Christopher Tan. 2002.

Consumers

Though PayNet Deposit offers significant benefits in convenience and liquidity of funds, there are costs to consumers as well. Under this system, there is no cost for customers who deposit cash only or who deposit checks without cashing them. However, if the customer is cashing a check and depositing some or all of the proceeds of the check as cash, check cashers levy a surcharge of 0.5% of the total for checks up to \$1,000, a discount over the standard 1.5% check cashing fee.¹¹ For example, if a customer wishes to cash a \$500 check and then deposit \$100 into her credit union account, she will pay a fee of \$2.50 and receive a total of \$397.50 in cash from the check casher. The \$100 deposit will be noted in the system as cash, thus providing the customer with immediate liquidity. If a credit union member uses the POB machine to make a withdrawal from a credit union account, there is a flat fee of \$1.50 per withdrawal.

Check Cashers

When POB machines were first being used to process federal benefits, they were very expensive to maintain. POB machines used to cost check cashers \$85 per month plus \$0.25 per transaction, compared to \$15 per month for POS machines. Today, POBs are much more affordable. This fact makes the program more attractive for expansion. Check cashers are already serving the unbanked market; this program offers extra service at a fairly minimal cost.

LYNK has been the exclusive processor and terminal driver of the program for three years. Check cashers must sign up for POB processing through LYNK, which charges check cashers \$15 per month per machine for terminal driving and network access service and \$10 per month for the POB support desk. LYNK receives \$0.18 for each withdrawal, transfer or inquiry generated through POB from check cashers, and \$0.27 per deposit. Check cashers can purchase POB machines, which are basic Verifone models, for about \$1,000. Check cashers must also purchase a dedicated phone line for each POB terminal and maintain that line.

Thus, a check casher might pay an average of \$1,000 upfront to buy the POB machine, \$250 per year to JP Morgan Chase for sponsorship,¹² and \$25 for monthly fees to LYNK.. These costs are fairly minimal in comparison to the interchange fees paid by credit unions. Notwithstanding the one-time cost of the machine, Rite Check estimates that a check casher needs to process about 20 transactions a month per POB machine to break even.

¹¹ The fee increases to 1% for checks between \$1,000 and \$6,000, which is the limit for a single check.

¹² Check cashers that are not current customers of JP Morgan Chase pay higher sponsorship fees of \$500.

Part II: Results, Lessons and Issues for Replication

Program Results

Transaction levels through the PayNet Deposit program are fairly small at this point, though the number of transactions has increased steadily since the beginning of the pilot. Bethex Federal Credit Union, the smaller of the two credit unions in the pilot, noted 127 deposits through this program in the month of June 2004. It is important to note that Bethex does not see this program as the only way to increase transactions among members; rather, it is one way to offer increased convenience and service for members. Bethex has succeeded in attracting 167 new members since 2003 out of the PayNet Deposit program. These members have approximately \$18,000 in savings at Bethex and have also taken out 24 consumer loans worth about \$16,000 from the credit union. Actors Federal Credit Union documented 919 deposits in June 2004 through POB, compared to 794 in June of 2003 and 293 in June of 2002—a 214% increase over two years.

According to Rite Check, a total of \$62,230.27 was deposited into eight Rite Check locations through POB terminals in June of 2004. Credit union members deposited roughly 40% of these funds as cash with immediate liquidity of funds; the remaining deposits came through POB terminals as checks with 4-5 day holds. Between March and August of 2004, credit union members deposited about \$386,000 in these eight RiteCheck locations, with the average 40% deposited as cash remaining consistent in the time period. Rite Check estimates that they receive 70 POB deposits per month at all locations. The vast majority of these transactions occur at three of Rite Check's locations, in areas where Bethex's members are most heavily concentrated. In addition, several credit unions are considering joining the program, and there are currently over 110 check cashing locations that utilize the PayNet Deposit program.

Key Lessons

1. The fact that credit unions and check cashers have found common ground and are working together to serve consumers is an innovative lesson. Credit unions and other small financial institutions are looking for ways to provide service to members without the hard costs of building new branches or the administrative issues associated with shared branching. The POB provides one innovative way to offer such services. As credit unions are now allowed to expand their fields of membership to include lower-income geographies, strategies are needed to enable lower-income consumers to access credit union services in areas where physical branch presence might be lacking.
2. The partners have found it challenging to market the program. Small credit unions often have little to no budget for marketing purposes. Larger institutions with staff time and money to actively market the program might see more success. For example, Actors Federal Credit Union, which is very small in comparison to many banks and large mainstream credit unions but is nonetheless significantly larger than Bethex, has a marketing staff person who can concentrate on sending mailings and

- developing other advertising for the program. Those involved in PayNet Deposit attribute Actors' larger transaction volume through POB in part to the credit union's marketing capabilities. To date, there are no large institutions involved that might be used as a point of comparison to these two credit unions. Mainstream credit unions and possibly community banks are being recruited for the program. On the other hand, larger credit unions and banks must wade through additional bureaucracy, and financial institutions with significant branch networks are less likely to see the utility of the PayNet Deposit program.
3. Staff training has also been a challenge. Actors Federal Credit Union might see 1,000 transactions per month occurring at over 100 locations. This averages out to about 10 transactions per location per month; however, the credit union estimates that the majority of transactions occur at a few locations. With frequent staff turnover and few POB transactions at many locations, check cashing staff might be unfamiliar with the POB infrastructure and procedures.

Issues for Replication and Expansion

The partners in this program, particularly the check cashers and LYNK, which receive significant monetary benefits from POB, are very interested in seeing the program expand into states beyond New York. Check cashers in Illinois and Florida have expressed interest in joining the pilot. However, some challenges must be overcome in order for this to become a reality. For example, if a financial institution is for some reason unable or unwilling to join NYCE, that fact poses a problem for expansion at this point in the program. NYCE, which is a national network, is currently the only ATM network that supports POB. Because firms need to join the NYCE network to offer POB services, there might be geographic restraints related to this aspect of the program. Perhaps in the future, other ATM networks will support similar programs and this barrier will disappear.

Another issue involves the availability of a network of check cashers like the PayNet Payroll system. This pilot was able to take off in part because it relied on a system that was the culmination of New York check cashers' attempts to develop a joint venture wherein various check cashers might be seen as one entity. The PayNet model allows for industry-wide pricing for third parties and for consolidation of invoicing for those parties. Having the PayNet Payroll network in place helped make the business case for PayNet Deposit for check cashers, as the partners involved had already invested in the cooperative structure before deposits were added to the system. Moreover, financial institutions were aware that they would be able to enroll in PayNet Deposit through a single point of contact, and that the program would incorporate standard fees and policies. This factor could become relevant for expansion to markets that do not currently have this type of cooperative agreement, as PayNet is currently available in only three states: New York, New Jersey, and Connecticut.

Moreover, the PayNet Deposit program could be challenged in moving to national scale if JP Morgan Chase does not agree to sponsor the program outside of New York State or if the bank decides to discontinue program sponsorship. At the time of this writing, Chase is the only bank sponsoring check cashers into the program. If the bank pulls out or

decides not to geographically expand the program, the partners involved would need to find another sponsoring bank in order for the pilot to be replicated elsewhere. Because of the responsibility for funds held by the sponsoring bank, it might be challenging to find an institution that is willing to take on this risk.

PayNet Deposit programs might be more effective in markets that already regulate check cashing services. In a regulated environment, check cashers often have more reputable “bank-like” images than they do in non-regulated states. Because New York has relatively strong check cashing regulations, check cashers are already heavily scrutinized and audited. Because check cashers in New York are used to complying with rules created by New York regulators, the check cashers involved claim that it is easier to comply with the POB platform requirements than if no other regulations existed. In turn, financial institutions are more likely to view regulated check cashers as reputable partners. One issue that might arise is that in some states, check cashers also provide payday loans (this is not the case in New York). Federal bank regulators have issued advisories warning against relationships between banks and payday lenders. This issue needs to be examined if national banks and others attempt to replicate PayNet Deposit.

Check cashers in the program have been reaching out to additional credit unions to encourage membership in the program. Take-up has been slow up to this point, perhaps because the program is new and credit unions are unaware of it, but also perhaps because of reputation issues that go along with partnering with check cashing firms. Though credit unions are currently the only financial institutions utilizing the PayNet Deposit platform, banks could also benefit from participation. However, the regulatory landscape is less certain. For instance, federal bank regulators have issued advisories covering third party contracts, branching and deposit taking, general compliance, and reputation and money laundering risks that banks may encounter when conducting business with check cashing companies.

Staffing issues also affect expansion. There is no one staff person, at the check casher or credit union level, dedicated solely to the PayNet Deposit program and its replication. The parties involved, who have championed the program for so long, are ready to see the pilot “leave home” and be taken up by an outside representative so the program’s founders can return their focus to other lines of business.

Additionally, profitability is an issue for expansion. Though costs for the check cashers remain limited, the financial institutions have fairly substantial costs per transaction. However, for the credit unions involved, the cost is still lower than building up a branch network or engaging in shared branching. As more credit unions join the program, each institution will need to weigh for itself the costs and benefits.

Conclusion

The PayNet Deposit model serves to meet lower-income consumers “where they are” as they go about their financial business. In addition to providing immediate liquidity of funds, the PayNet Deposit program allows consumers who generally cash their paychecks and walk away with cash with a convenient way to save money and earn interest on funds. Credit union members get additional services and convenience, while the

possibility of credit unions gaining additional members, and unbanked consumers becoming part of the financial mainstream, increases by using check cashing locations as a conduit into that mainstream. An immense amount of a few key individuals' and firms' time and effort went into the vision of the project, enabling the program to become significantly simpler for future entrants than it was at the inception. The partners worked through many of the most complicated issues that arose, paving the way for others to follow. However, obstacles to expansion remain. New entrants still need to navigate regulatory, marketing, and technological issues. The involvement of new ATM networks, sponsoring banks, and partner financial institutions is also an issue for expansion. At the same time, a clearer picture of the profitability of this program, especially for the financial institution involved, is important in order to garner interest in significant expansion. But the PayNet Deposit pilot program offers an insightful look into making a business case for expanding financial services for underbanked consumers in a way that benefits all sides—in this case, the consumer, credit union, and check casher.

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Appendix: Description of Important Actors

Key Partners:

In order for PayNet Deposit to work, several diverse institutions must remain dedicated to the program. These include, but for the future are not limited to, the following groups, all of which are represented in the Joint Industry Committee that meets on a regular basis to strategize around the program:

- Check Cashers: Rite Check Cashing (nine stores currently offering PayNet Deposit), Pay-O-Matic (over eighty stores currently offering PayNet Deposit) and other check cashers: Check cashers must sign an agreement stating they will abide by the rules for the PayNet Deposit program (such as set fees and check cashing percentages). These firms then buy POB machines, install them in their stores, and enable check cashing and deposit functions at their retail locations for financial institution customers. In order to join the program, these firms must first join the NYCE network and pass criteria set forth by the sponsoring bank, JP Morgan Chase. Check cashier employees manually review each POB transaction. Check cashers are responsible for reporting adjustments for returned deposited items.
- Credit Unions: Bethex Federal Credit Union and Actors Federal Credit Union: These credit unions have joined the program to increase convenience and access to financial services for their members. Bethex has approximately \$8 million in assets and 10,150 members, while Actors has approximately \$85 million in assets and 15,200 members. In order to join the program, financial institutions must join the NYCE network and make sure that their processing systems support POB functionality. Financial institutions should not have to change processors to join the program, but the processor might have to adjust its systems, which can be a time-consuming process. Other credit unions are considering joining the program as well.
- Financial Service Centers of New York (FSCNY): FSCNY, formerly named Check Cashers Association of New York (CCANY), is the largest association of community cash access outlets in New York. FSCNY was integral to the development of the POB system; the PayNet network was created by the association in 1994.
- JP Morgan Chase: JP Morgan Chase is based in New York City and is one of the largest banks in the U.S; the bank is the sponsoring bank for check cashers that wish to provide PayNet Deposit transactions. The PayNet Deposit POB platform requires a sponsoring bank, as check cashers are not normally deposit-takers. Chase maintains the settlement accounts for all POB transactions and is liable for the funds if deposits are returned.¹³ Currently, all check cashers that wish to enter into this program must therefore go through Chase for approval.

¹³ Check cashers pay dues to FSCNY of \$1,200 per year per location and between \$250-500 per year to Chase for sponsorship per chain.

- **LYNK**: A national provider of electronic payment, cash dispensing, and e-commerce services and products based in Atlanta, LYNK is the processor and terminal driver of the program and is in charge of handling adjustments. LYNK has been the exclusive back-end processor for PayNet Deposit transactions for three years. Check cashers must sign up for POB processing through LYNK. LYNK charges check cashers \$15 per month per machine for terminal driving and network access service. LYNK also charges \$10 per month for the POB support desk. LYNK receives \$0.18 for each withdrawal, transfer or inquiry generated through POB, and \$0.27 per deposit.
- **NYCE**: NYCE Corporation operates the NYCE Network, which provides thousands of financial institutions, retailers and independent ATM deployers with shared network services for automated teller machines (ATMs), PIN debit point-of-sale, point-of-banking services, EBT, gateway services, account-to-account, and direct debit applications.¹⁴ NYCE is currently the only ATM network that supports POB. NYCE originally designed the POB platform to allow cardholders to perform limited banking transactions at non-bank locations. In order to be included in the PayNet Deposit program, both the financial institution and check casher must join NYCE's network. Once the financial institution is a member of NYCE, it must inform the network that it would like its deposits taken by PayNet.
- **Regulatory Agencies**: The State of New York Banking Department and the National Credit Union Administration (NCUA) had historically important roles in the development of the PayNet Deposit Program. New York State banking regulators had to approve the rates, rules, and other aspects of PayNet Deposit before the program could be operational. The program also required NCUA's approval to ensure the issuance of insurance to cover deposits taken by non-credit union employees (check cashers) on behalf of credit union members.

¹⁴ <http://www.nyce.net>

The Center for Financial Services Innovation (CFSI), an initiative of ShoreBank Advisory Services with support from The Ford Foundation, was founded in 2004 to encourage the development of asset-building opportunities that create value for both customers and companies. CFSI provides funding and resources, enables partnerships, and develops and distributes authoritative information on how to respond to the needs of the underbanked profitably and responsibly. We assist pioneering institutions and organizations both large and small to serve underbanked consumers across the economic, geographic and cultural spectrum. Banks, credit unions, technology vendors, alternative service providers, consumer advocates, and policy makers all can find support here to forge the new relationships, products, and strategies that will transform industry practice, and people's lives. For more on CFSI, go to www.cfsinnovation.com.



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