commonwealth

Building Financial Security Through Integrated Financial Solutions: Combining Savings and Credit

Introduction

Too many people in the U.S. lack financial security. Too many people are financially vulnerable. At Commonwealth, we believe that financial security is essential for people to pursue their full potential. We are committed to building solutions that make people more financially secure.

"What might be possible if we combined multiple financial functions—specifically saving and borrowing—into one financial solution?"

We have found that the best tools to build financial security are customer-informed, even customer co-created. They are designed specifically to meet the needs of people who are experiencing financial vulnerability, rather than being a workaround of existing financial products. They address the challenges of managing uncertainty and risk, managing debt, building savings and developing financial capability – rather than exacerbating them. They are safe, transparent, and affordable, as defined by the people who will use them. And they are well designed, incorporating insights from behavioral economics and behavioral design.

Today these principles are challenging us to think more holistically about how financial products are designed. Retail financial products and services have traditionally focused on single financial behaviors—saving or borrowing or budgeting—however, in our experience, people's financial lives are more deeply interconnected than these products suggest: income impacts expenses; expenses impact savings; savings impacts borrowing; borrowing impacts expenses; and uncertainty impacts everything. Products that fail to acknowledge these interdependencies optimize one financial function at the expense of the whole.

This insight has catalyzed a new line of thinking for our work. What might be possible if we combined multiple financial functions—specifically saving and borrowing—into one financial solution? Might this combination better equip people to solve their financial challenges? Might this solution make more intuitive sense to potential end users because it reflects how they actually manage their money?

This paper makes the case for integrated solutions, details existing examples of the concept, and describes future product ideas that highlight additional ways to integrate savings and credit for the benefit of consumers. Our goal is to inform and inspire innovators, and to invite partners to work with Commonwealth to advance these ideas.

While too many people in the US lack financial security — and this comes at a significant cost to individuals and society — the pervasiveness of financial vulnerability also creates a market opportunity for new ideas. We invite financial services leaders, designers, community advocates, policymakers and entrepreneurs to work with us to explore this new terrain and unlock its potential.

The Need for Integrated Financial Solutions

Financial products and services have traditionally been designed and marketed around financial functions—borrow, save, pay or transact, invest, insure—and typically a single financial function. Savings and investment products focus on providing security and growth for excess cash. Credit products kick in when cash is short and to enable large purchases—such as a home, college education, or vehicle. Financial institutions have been organized around these functions, as have entire industries: investment managers, credit rating agencies, and mortgage brokers, to name a few.

While these single-focus solutions have served many Americans well, they reflect the structures and competencies of financial service providers. They do not necessarily match the way people experience their financial lives. This is especially true for those who live on tight incomes and face considerable volatility, with little in reserve. For these people, a dental emergency, car repair or child-related expense may spell disaster. They may miss a shift due to illness, or discover their new manager has assigned them fewer regular work hours. When such life events happen, addressing a pressing need may require several hundred dollars to make an essential purchase, or to pay an overdue bill. Often, this need occurs in a stressful, time-pressured context. To someone under pressure and with an acute need, the choices offered by the financial system often seem tone deaf to their reality. *Would you like a credit card? A home equity loan? To open a savings account?* Or when the financial system is attuned to their reality, it may be through high cost alternative financial services: *Get cash now! Payday loans here!*

"Customers shouldn't have to think like providers of financial services."

Customers shouldn't have to think like providers of financial services. They should be able to lead their lives, and turn to well-crafted solutions that address their needs as they arise. Ideally, people could reach for one solution when a need arises, and trust that the tool they grab will activate whatever financial functions are necessary to address their need. For instance, imagine:

- A person facing an unexpected expense could reach for a single solution that would draw on savings or enable a line of credit as needed.

- An ill worker who is covered by a High Deductible Health Care plan (HDHCP) could go to the doctor, confident she can pay for it either by drawing on HSA savings or through affordable credit, as needed.

- A person with a "thin file" or "no file" seeking to make a major purchase (such as an appliance or a vehicle) could rely on one solution that would both facilitate the purchase and help build her credit history.

- A person with modest retirement savings could turn to one solution when a financial need or crisis arrives, trusting the solution will help guide them to know when a retirement savings withdrawal or loan is wise and when borrowing from another source makes more sense.

Integrated financial solutions that align with people's financial lives hold much promise for financial service providers . Companies that design and deliver products that truly meet their customers' needs—as their customers experience them—stand out in a crowded financial services marketplace. Integrated financial solutions that enable customers to stabilize their financial lives can create satisfied, loyal customers with significant lifetime value. In addition, in some cases, lower margin products can be bundled with higher margin offerings, creating a more profitable, less risky product for providers. Small balance savings products, for instance, are rarely moneymakers. Bundled with a line of credit, however, the economics of savings products improves.

"Integrated financial solutions that align with people's financial lives hold much promise for financial service providers."

Combining Savings & Credit

As part of our discovery process, we surveyed the financial landscape in search of financial solutions that integrate savings and credit, and found several. These innovations span the development spectrum from concept to design to in-market. Many of these solutions are designed to meet the needs of people who are experiencing financial vulnerability, and several of them address one or more of the consumer challenges that Commonwealth has identified as being essential to building financial security[1]. While some solutions are designed for delivery through financial institutions, others are designed for use in non-traditional contexts, including healthcare and education, reflecting a growing understanding of the range of factors that contribute to financial vulnerability in America. Multiple stakeholders have put forth solutions—financial institutions, direct-service providers, employers, and local governments—illustrating the range of interested players and the cross-sector nature of the challenges.

We have organized our findings by theme—savings and credit to manage risk, credit that builds savings, and savings that enhance credit. High-level descriptions of several solutions follow. A comprehensive list of integrated solutions and more detailed descriptions can be found in the Appendix.

Savings and Credit to Manage Risk

Many people who are financially vulnerable are experienced and savvy risk managers, practiced at identifying the least unpredictable or most forgiving personal finance choices. But they do not always have the right tools to enable them to make informed decisions, or they are compelled to make choices that other people do not face. Integrated tools that combine savings and credit mechanisms, working capital accounts, data, and automation can build users' capacity to weather risk and volatility. Imagine an integrated financial solution that tracks cash inflows and outflows of an account over time, and can automatically shift excess funds into savings during flush times, and automatically draws down credit during lean times. Might this type of offering enable people to better manage the risk of uncertain cash flows? Could a secondary benefit of the solution be a reduced need for costly alternative financial services? And might this in turn reduce the amount of financial penalty fees and interest paid, which could free up significant cash that can be saved? And might this financial cushion reduce people's need for future borrowing and strengthen their resilience for unanticipated emergencies?

> *"Imagine an integrated financial solution that tracks cash inflows and outflows of an account over time, and automatically shift excess funds into savings during flush times, and automatically draws down credit during lean times"*

Ideas 42 and Oliver Wyman recently introduced a product concept quite similar to this, which they coined the *Financial Stabilizer*[2]. The solution integrates spending, savings and credit so that expenses can be paid on time, using an optimal blend of savings and credit. How does it work? The Financial Stabilizer separates cash inflows into separate spending buckets: one for bills, one for savings, and one for discretionary spending. It also offers short-term affordable credit to cover any shortfall—these moneys are automatically repaid from future deposits. Should an emergency take place, customers are able to draw down funds from their discretionary spending pot; automatic repayments on withdrawals help to maintain a savings cushion. The amount of credit extended is likely to decrease over time as customers build up a savings cushion. This product is yet to be launched. Its designers estimate that the Financial Stabilizer would save low and middle-income customers an average of $500 in financial services annually and could increase bank profitability by $120 per LMI customer, amounting to over $1billion in profit potential for a large bank.

1. These are supporting consumers: to manage uncertainty and risk, to manage debt, to build a life-long savings habit, and to build financial capability.
2. http://www.ideas42.org/wp-content/uploads/2015/11/Reimagining-Financial-Inclusion-Final-Web-1.pdf

Even helps its customers smooth out volatile earnings by offering Pay Protection[3]. Pay Protection ensures that *Even* customers have consistent inflows every payday. When inflows are less than the average amount that a customer makes, Pay Protection automatically deposits extra money into that customer's account to make up the difference. *Even* doesn't charge interest on the money it deposits. This money is repaid from the next paycheck that is above average, so customers maintain an average inflow of cash in every pay period. If paychecks are lower or higher than average for three consecutive pay periods, the app will automatically adjust. Pay Protection is often provided as a benefit from employers. If users lose their job, *Even* will pause their account until they begin receiving paychecks again.

Credit that Builds Savings

Saving money is hard, but it is essential for building financial security. Credit that builds savings enables borrowers to turn their debt repayment behavior into asset-building behavior. These solutions build upon existing behavior, recognizing that it takes less motivation and energy to continue a behavior than to begin a new one. The integrated nature of these solutions enables borrowers to address their need for a loan, fulfill their debt obligations, and build savings, so that they move from a reactive to a prepared position. Examples of credit that builds savings follow.

In 2007, the "Working Bridges" employer collaborative in partnership with NorthCounty Federal Credit Union created the *Employer Sponsored Small Dollar Loan (ESSDL)* as a way to address the increased number of employees requesting pay advances and/or quitting their jobs to gain access to their retirement funds. The *ESSDL* has proved to be a low-cost, highly valued employee benefit that enables employees to access needed funds, build or repair credit, reduce their dependency on high-cost alternative financial services, and save. One Working Bridges employer reported that *ESSDL* led a to 22 percent decrease in employee turnover; another credited the program with a 23 percent drop in turnover and a decrease in unscheduled time off from 4.3 percent to 2 percent[4].

"Credit that builds savings enables borrowers to turn their debt repayment behavior into asset-building behavior."

Here is how it works. The *ESSDL* is sponsored by employers, but underwritten by local credit unions. Employers verify that an employee is in good standing and has been employed by them for at least 6 months, and in many cases, alert lenders if an employee's work status has changed. The lending institution determines a borrower's creditworthiness based on the borrower's ability to pay, rather than on his or her credit score. Loans are repaid through payroll deduction and positive repayment is reported monthly to credit bureaus. The savings feature kicks in when the loan is repaid; payroll deductions continue and funds are placed in the employee's savings account on an opt-out basis.

Innovations for Poverty Action has created a similar savings feature, *Pay Yourself Back*, which can be added on to any loan. They are extending this innovation to borrowers in over 20 countries in Asia, Africa, and Latin America[5].

Rather than waiting until a loan is repaid to initiate savings, *Borrow and Save* loans have a required savings component. Savings are established at the onset of the loan, with 25- 50 percent of the proceeds from the loan. These funds are frozen in an account and accrue interest until the loan has been paid in full and the savings are released to the borrower. *Borrow and Save* loans range from 90 days to 12 months and are structured as installment loans without balloon payments to facilitate repayment. Savings serve as collateral for the loan reducing the risk for the underwriter. *Borrow and Save* enables borrowers to get the cash they need, build savings, improve their credit score, and break the cycle of payday loan rollovers.

The State Employee Credit Union's *Salary Advance Loan* program takes a similar approach, requiring borrowers to put money aside for savings throughout the life of the loan. The overall balance in the savings account determines required deposits and access to these funds is restricted in the absence of loan officer approval. This loan also offers incentives to encourage additional savings, including an interest rate discount on the loan after the balance in the associated cash account reaches a certain level[6].

3. https://even.com/faq
4."Employee Sponsored Small Dollar Loan Tool-Kit, revised December 2013, filene.org/assets/files-brains/Employer_Sponsored_SDL_Toolkit_Dec_2013.pdf.
5. http://www.poverty-action.org/
6. https://www.ncsecu.org/PersonalLoans/SalaryAdvance.html

For people hoping to establish or improve their credit, *Credit Builder Loans* offer a low barrier means to build credit whilst investing in savings for the future. Here's how they work. Borrowers take a loan upfront, which must be deposited in a savings account or CD for a predetermined time period and cannot be accessed until the loan is fully repaid. These funds act as collateral for the loan. Each month, consumers make a payment towards the loan that includes principal and interest. Payment history on the loan is reported to the credit agencies, providing data to establish or repair a credit history. At the end of loan term, the borrower has paid back the loan in full, built credit, and has savings in the form of the lump sum that has been invested in a savings account or CD.

Many banks and credit unions offer secured credit builder loans. The Local Initiatives Support Coalition (LISC) offers a unique credit builder loan program called *Twin Accounts*™. Participants are issued a 1-year $300 loan, the proceeds of which are placed into a master savings account. Participants then make 12 monthly repayments of $26.24, which LISC matches, as the payments are made on time. This payment history is reported to credit agencies. Clients with a zero credit score usually achieve a FICO credit score of 676 within six months. At the end of the loan term, participants who successfully made 12 on-time payments have $300 in savings and $300 in matched funds, and improved credit. LISC limits the use of matched funds to the opening of a secured credit card. Another example is Self Lender, a digital credit building community that offers potential borrowers personalized credit score tracking, credit monitoring, access to financial tools, and the opportunity to apply for a credit builder account.

Savings that Improve Credit

What can people do to improve their credit score? A person's credit score does not capture her overall financial picture, as traditional scores do not take into consideration important factors such as whether a person is employed, has adequate cash flow to cover expenses, or has any liquid assets. Rather, credit scores predict future loan repayment behavior based solely on a person's past performance with credit. So how can savings improve credit? As the products cited below demonstrate, savings can be pooled among a group to offer zero-interest loans to members of the group. Savings can also be used to decrease underwriting risk to lenders that look beyond traditional credit scores to assess creditworthiness.

> *"A person's credit score does not capture her overall financial picture."*

RateRewards is an unsecured loan product that incorporates Adaptive Risk Pricing technology, which automatically adjusts the interest paid on a loan in real-time as a borrower's risk profile changes. Borrowers are empowered to take actions every month that will improve their creditworthiness. These behaviors include increasing savings, among others (e.g., reducing debt, making on time payments, and using a debit card instead of a credit card). Undertaking each of these activities earns a monthly reward that can reduce a borrower's interest expense by up to 50 percent. *RateRewards* is offered by Ascend, a data-driven consumer finance company that is committed to "developing fairer ways to price less than perfect borrowers." In their words, "We believe that credit scores are not very good at predicting what kind of a borrower you will be in the future, and that you deserve a chance to prove that you're better than your credit score indicates[7]."

Mission Asset Fund's (MAF) *Lending Circles* have proven to be a highly successful way for people to access funds, build savings, and improve their credit. They offer an alternative to banks for people who lack a credit

7. https://www.ascendloan.com/#howitworks history or who are not familiar or are uncomfortable with traditional banking environments. Would-be participants complete an online financial training class offered by MAF before joining a *Lending Circle*. Next, six to ten people come together to form a Circle. Participants join with personal goals for the money they will borrow from the group, but the Circle decides together how much it wants to be able to lend to members of the group and therefore how much each participant must agree to contribute each month— contributions range from $50 to $200. Everyone in a *Lending Circle* makes the same payment each month and the pooled money is given to a different participant in the *Lending Circle* every month until everyone has had a chance. For example, a ten-person Circle could agree that each member will pay $100 a month for 10 months so that each member of the group could receive a one-time lump sum of $1,000. MAF provides this payment history to credit bureaus for all participants. The social component of circles keeps users committed to payment obligations (the group absorbs any losses); the loan distribution schedule encourages consistent budgeting and saving behavior; and reporting payment behavior to credit bureaus or lending partners enables members to build a credit history. A 2013 MAF study found that the average person in the control group increased their outstanding debt by almost $3,000, whereas the average person in the Circle decreased their outstanding debt by over $1,000.

Commonwealth Ideas

Challenged by our commitment to build financial solutions that address the needs of financially vulnerable people, and inspired by the variety of integrated solutions that are in development or in the marketplace, we have developed additional ideas that range from early concepts to more fully fleshed out designs. Some of these potential solutions are designed for delivery through financial institutions; others are designed for employer or educational channels. All of them are designed to enable people to act on their own behalf to build their financial security.

Savings and Credit to Reduce Risk

Health Line

Challenge: How might we design an integrated financial solution that enables enrollees in High Deductible Health Care Plans to pay for medical expenses they incur before they have saved ample funds to meet their deductible?

Background: High Deductible Healthcare Plans (HDHCPs) are one of the fastest growing forms of health insurance in the US. According to the Kaiser Family Foundation, 29% of workers with employer-sponsored coverage are enrolled in some form of a HDHCP with Health Savings Account, up from 17% in 2011.

These plans offer lower premiums than traditional health insurance but are offset by large deductibles. These deductibles can be significant financial outlays for enrollees. As of March 2015, nearly 90 percent of enrollees with ACA marketplace-purchased HDHPs had average deductibles of over $2,500; some were as high as $5,300. Recognizing that people may need to save money to satisfy these higher deductibles, HDHCPs are often, though not always, paired with tax-advantaged savings vehicles known as Health Savings Accounts (HSAs). Enrollees can make contributions to their HSA with pre-tax dollars deducted directly from their wages.

HDHCPs can work well for people who are healthy, unlikely to require expensive medical care during the coverage period, and able to fully fund their deductible over the course of the year. But HDHPs create significant challenges for people who are financially vulnerable or who have chronic medical conditions or poor health, as the plans essentially leave enrollees without healthcare coverage until their deductible has been met. Faced with potential medical expenses, insufficient cash to cover a deductible, and a fair amount of confusion about what services are covered under the plans, many HDHCP enrollees choose to forego or delay medical care. Unfortunately, this often results in more serious health conditions and higher cost of care. A recent study conducted by the Employee Benefits Research Institute found that HDHCPs were associated with increased emergency room visits and inpatient hospital admissions for lower-income enrollees.

What is Health Line? Health Line is an employer-sponsored salary advance that enables employees enrolled in HDHCPs to augment the savings in their HSA to cover medical expenses incurred before their deductible has been fully met. Accelerating HSA contributions enables employees to get the medical care and prescriptions they need without incurring medical debt and experiencing its consequences.

Offering *Health Line* to employees can foster employee loyalty, improve worker health, focus, and productivity, and increase job satisfaction, all factors associated with higher retention, reduced absenteeism, and positive referrals. *Health Line* should only be offered to employees that understand their financial obligations under their HDHCP and can readily meet the financial responsibilities.

How Health Line Works. Employees commit to making regular contributions to their HSA (or another dedicated savings vehicle, if they do not have access to an HSA) through direct deductions from their wages. If at any point an employee's medical bills exceed the amount of money they have put aside in their HSA, they can draw upon their *Health Line* to cover their expenses. *Health Line* preserves the tax-advantages of the HSA, if employees save in an HSA, as the advance is still considered pre-tax income. Loan repayments are automatically deducted from the employee's future paychecks according to a pre-agreed repayment plan with his or her employer. Employer risk is mitigated by the limited value of the line of credit, repayment directly from payroll deductions, and a single dedicated use (health expenses) for *Health Line* advances.

How Health Line Builds Financial Security. Health Line enables employees enrolled in HDHCPs to pay for the medical care they need before they have fully met their deductible. It enables employees to avoid late payments on their medical bills, which can have an adverse impact on their credit rating—medical debt is an often-cited reason for why people end up using alternative financial services such as small dollar loans. Medical debt is responsible for more collections than credit cards and is the #1 cause of personal bankruptcy in the US.

Community College Cash

Challenge: How might we design an integrated financial solution to enable community college students to solve the primary financial challenges that often delay or impede their ability to complete their education on time?

Background: Forty-five percent of undergraduate students in the US attend community colleges. The open postsecondary education offered by these colleges builds workforce development skills in students earning their Associate's degree and prepares students who are committed to earning a Bachelor's degree to successfully transfer to and succeed in four-year colleges. Generally speaking, community colleges offer a lower cost alternative to public and private four-year colleges. The average tuition at community colleges is less than half of the average tuition and fees at a public four-year institution and 1/10th of the tuition and fees at private four-year institutions. However, financial aid packages can impact the relative cost-effectiveness of four-year colleges, as can the additional 1½-2 years that it takes students who begin in community colleges to complete their Bachelor's degree.

Community colleges struggle with student persistence and completion rates. According to a 2015 report published by the National Student Clearinghouse (NSC), just 39.1percent of the students who started at a community college completed a program either at the starting institution or a different institution within 6 years. (This number jumps to 57 percent for full-time students.) National efforts are under way to improve retention rates; six national community college organizations have committed to producing "50 percent more students with high quality degrees and certificates by 2020, while preserving access and quality." Factors that adversely affect community college completion rates include, but are not limited to, part-time status, lack of clear academic and career goals, the effectiveness of academic advising, and financial challenges. Amongst these challenges, financial issues—such as mismatches between cash inflows and outflows or stress from debt—are a pervasive and overriding theme undermining college completion.

What is Community College Cash? Commonwealth and Opportunity Fund collaborated on the design of *Community College Cash (CCC)*. CCC integrates savings and credit to enable students to better "pace" their cash inflows and outflows throughout the semester. Student surveys reveal that the timing of Pell Grants disbursements, one of the largest sources of cash for community college students, is often not aligned with students' expenses. Typically, Pell grants are disbursed between weeks 3-5 of the semester, which presents a significant cash flow challenge for students who may need to purchase books, technology, and supplies at the beginning of the semester. Student surveys further suggest that cash often runs low or is completely depleted before the end of the semester. CCC enables students to better match their cash inflows and outflows across a given semester. This financial stability can reduce students' stress, increase their ability to focus on school, and prevent drop out.

How does CCC work? CCC combines a flexible loan to cover upfront school-related expenses with a savings vehicle in which funds for late semester use could be kept. CCC's loan has a 0 percent interest rate for the first 2 months; the expectation is that the loan will be repaid in full when a student's Pell Grant money is disbursed later in the term. The amount of the loan is directly correlated with the number of courses in which a student is enrolled for a given semester. (Secondary incentives for repaying the loan on time include eligibility for matched savings and a 10 percent interest rate on the loan balance after 2 months.)

Students will have the option of directing a portion of their Pell Grant proceeds into a savings account, earmarked for use at the end of the semester. To encourage ongoing saving, students will be eligible for up to 6 small-dollar matches for savings deposits of $25 or more over the course of 6 months. Students are eligible for additional cash incentives ($100 each) for undertaking the following designated behaviors: repaying their CCC loan on time, completing their FAFSA application on time, completing an academic plan with their advisor, and declaring their major by the end of the semester.

How CCC Builds Financial Security: CCC helps students stabilize their finances by better matching cash inflows and outflows across a given semester. This financial stability reduces students' stress, increases their ability to focus on school, and prevents drop out. In addition to building persistence, CCC develops students' financial capability by offering them first-hand experience with budgeting, borrowing, repaying debt, saving, financial goal setting and planning, and cash flow management.

Save to Raise

Challenge: How might we combine savings and credit to enable people to improve their credit scores?

Background: Traditional credit measures do not take important factors into consideration such as whether a person is employed, has any savings, or has ample cash flow to cover expenses. Credit scores focus on a person's past performance with credit to predict likelihood of future repayment. Since savings are not captured in traditional credit scores, one of the most effective ways to use savings to improve a credit score is to direct some portion of these funds to paying down outstanding debt.

What is Save to Raise? Save to Raise (StR) is a digital decision-making tool that enables people to improve their credit score by directing a portion of their savings to pay down outstanding debt. It clarifies for people the "cost" of the choice of saving versus paying down debt in terms of their credit score, so that they can consider if they wish to trade savings for greater access to and lower cost for credit. When future windfalls are likely coming, it enables people to consider in advance how to allocate these cash inflows, including in a way that will improve one's credit score.

How StR Works: StR considers a person's credit score in light of the total amount of outstanding debt that they have, the terms of the debt, and their savings. StR's algorithms continuously assess whether it might be advantageous for the user to direct a portion of their savings to pay off existing debt, based on pre-agreed-upon liquidity parameters, including when likely windfalls may be approaching (e.g., tax refunds). This integrated solution alerts customers when the time for action is approaching. Simple and engaging graphics illustrate trade-offs and how various options may improve a credit score over time. Debt payments can be flexible; they can be one-time or regularly scheduled transfers from savings, and can continue until the outstanding debt is paid down to a certain level or entirely paid off.

How StR Improves Financial Security: StR helps build financial security by enabling people to improve their credit scores. Whether a heavy or light lift is needed, improvements can enable borrowers to shift from subprime rates to prime rates. This shift can reduce their borrowing costs, improve their "bankability" by traditional financial institutions, ease their ability to rent housing, and improve their prospects in the job market. StR ensures that users designate their liquidity requirements and respects these requirements when crafting its recommendations. The net effect of StR is that users end up building a savings cushion, paying off debt, and increasing their credit score.

Savings Jar Challenge

Challenge: How might we create an integrated financial solution that enables people to realize their dreams of owning a home, obtaining a degree, or starting a small business?

Background: Many Americans aspire to improve their lives by purchasing a home or car, going back to school, or starting a small business. Often these dreams go unrealized because people do not have the cash needed for a down payment on a loan. Saving is hard but many people on tight budgets can and do put money aside. Having very specific goals in mind for savings efforts makes it easier. According to a 2016 America Saves Week survey, 84 percent of those with savings goals reported that they spent less than their income, compared to 45 percent of those without savings goals[8].

What is the Savings Jar Challenge? The *Savings Jar Challenge* is a savings program designed to help those with thin or no credit files build an ample down payment for an affordable long-term loan.

How the Savings Jar Challenge Works: The *Savings Jar Challenge* couples goal-based savings with a credit incentive. Participants identify a set of short-term savings goals and one long-term financial goal that will require a long-term loan. Drawing upon the simplicity of savings jar practices, participants are given a set of small "jars" (virtual accounts) into which they can allocate savings. Reminders are texted throughout the savings period to keep participants on track with their savings goals. After demonstrating consistent savings behavior and reaching specific savings goal milestones, participants unlock access to longer-term credit. In essence, the *Savings Jar Challenge* is a preview of the long-term loan payment experience that provides borrowers with the chance to accumulate a down payment and demonstrate to prospective lenders their creditworthiness through a regular payment pattern.

How the Savings Jar Challenge Builds Financial Security: The *Savings Jar Challenge* provides people with thin or no credit files a savings vehicle to demonstrate loan repayment behavior to prospective borrowers through savings, to accumulate a necessary down payment for a loan to enable a longer-term goal, and to gain access to a safe and affordable longer term loan.

Mobile Pay Back Catalyst

Challenge: How might we use mobile payment apps to enable college graduates with student loans to repay their loans faster and put some money aside for savings?

Background: Student debt is ubiquitous among young people and many have difficulty paying back their student loans with entry-level salaries. Citizens Bank's Millennial Graduates Debt study found that college graduates aged 35 and under with student loans spend just under one fifth of their current salaries on loan repayments[9]. This same group expects to be paying off their student loans well into their forties. Not all college graduates are as aware of the state of their student loan debt: 45 percent of survey respondents didn't know what percentage of their salary went to paying off student loans; 37 percent were unaware of the interest rate on their loans, and 15 percent were unaware of what they owe[10]. The Department of Education reports that 43% of borrowers who hold federal student loans are either behind on their payments or simply not making them at all[11].

8. http://www.americasavesweek.org/less-than-half-of-u-s-households-report-good-savings-progress-according-to-9th-annual-america-saves-week-survey/
9. http://investor.citizensbank.com/about-us/newsroom/latest-news/2016/2016-04-07-140336028.aspx
10. http://www.forbes.com/sites/jmaureenhenderson/2016/04/07/the-scary-truth-about-millennials-and-student-loan-debt/#7641c10bb8ae
11. http://www.wsj.com/articles/more-than-40-of-student-borrowers-arent-making-payments-1459971348

Millennials have embraced financial technology—41 percent of Millennials report having made purchases with their smartphones and 56 percent have adopted mobile payment services[12] such as Venmo, PayPal, or PopMoney. Such technologies are gaining traction and influence; Venmo handled $7.5 billion in transactions in 2015, and in January 2016, it had its first $1 billion month. How can we leverage the heavy adoption of mobile payments systems to help Millennials develop healthy savings and debt repayment behavior?

What is the Mobile Pay Back Catalyst? Mobile Pay Back Catalyst (MPBC) is a mobile payment app add-on that would promote savings and debt repayment within the payment experience.

How the MPBC Works: Each time a user makes a spending payment, the MBPC asks users in fun and clever ways if they would also like to send a payment to their savings account and/or to their student loan provider. MPBC offers users positive reinforcement for every payment made to a savings account or student loan, quantifying the lifetime savings of early or additional payments, and users have the chance to socialize their payments with new finance-related emoticons and images. The idea is to transform debt repayment from a private matter into a social norm and public virtue, much as Venmo has transformed person-to-person payments from a transaction into a social, fun experience.

"The idea is to transform debt repayment from a private matter into a social norm and public virtue."

How the MPBC Builds Financial Security: The MBPC offers an easy way for Millennials to understand and manage saving and debt repayment, which may otherwise seem intimidating or unfamiliar. MBPC intervenes within the technological environment familiar to the user at the very moment when they are making a financial payment. The app keeps healthy debt and savings habits at the top of mind, ultimately building user's financial capability and establishing a path towards a more secure, debt-free, asset-rich position.

Will You Join Us?

Wrestling with the challenges of financial vulnerability has led us to think more holistically about financial solution design. This paper reflects Commonwealth and the market's earliest efforts at answering the question: What might be possible if we combined multiple financial functions —specifically savings and borrowing—into one financial solution? This paper is also an invitation for you to join us in bringing fresh eyes, a customer-first perspective, and an integrated solution lens to the challenges of financial vulnerability in America. Together, might we be able to develop a new generation of solutions that enable people to build financial security, and as a result, more fully realize their potential?

Special thanks to J.P. Morgan Chase Foundation for supporting this work and to our diverse network of thinkers and doers who have joined with us to explore the potential of integrated financial solutions to solve some of today's most pressing financial challenges.

12. *http://www.paymentsjournal.com/Content/Blogs/Industry_Blog/30315/*

APPENDIX

Borrow and Save

What is it?
Borrow and Save is a small dollar loan with a required savings component.

Who is behind it?
The loan program was initially used by members of the National Federation of Community Development Credit Unions as a way to help their low- and moderate-income customers avoid high-cost borrowing and build savings for emergencies. The Filene Institute conducted a broader pilot over 16 months with a grant from the Ford Foundation.

How does it work?
Through Borrow and Save, users can access small dollar short-term loans within 24 hours without collateral or credit history. Rather, the loans incorporate an asset building component that requires a portion of the loan to go directly into savings.
Borrow and Save loans incentivize additional savings by providing the customer with a savings bonus after the loan is fully repaid. For example, a loan that requires borrowers to set aside $5 a month for a year for savings will match that savings with $60 when the loan is fully repaid.

During the sixteen-month incubator reporting period, credit unions closed 3,100 loans for over $2.9M in lending and $900,000 in savings. The average loan per borrower was $944 and the average savings was $290.

Employee Sponsored Small Dollar Loans

What is it?
Employer Sponsored Small Dollar Loans are emergency loans offered to LMI consumers by employers in partnership with credit unions

Who is behind it?
The NorthCountry Federal Credit Union developed this product and piloted with the Filene Institute.

How does it work?
Employer Sponsored Small Dollar loans are 6-12 month small dollar credit building loans up to $1500 offered to employees through their employers.

Loans are underwritten based on ability to pay and employers pay $300-1500 sponsorship fees per employee. These fees are based on turnover rates used to offset losses. Once the loan is paid, employees have the option to continue making payments into a savings account.

In a United Way/Working Bridges pilot test of over 500 loans, only 4% of loans defaulted. While helpful to the consumer, this product is also beneficial to employer bottom-lines. With this product, consumers are able to deal with emergencies quickly, reducing mental and emotional strain, effectively increasing worker productivity. In a United Way/Working Bridges pilot test of over 500 loans, one workplace reported a 22% deduction in turnover. [1]

Federally insured debit card based bank accounts

What is it?
Federally insured debit card based bank accounts have no check writing, no overdraft, and low and transparent fees.

Who's behind it?
Michael Barr, describes this solution concept in his book, "No Slack: The Financial Lives of Low Income Americans".

How it works?
This no check-writing, no overdraft account would present an affordable banking option to low and middle income consumers. The overdraft restriction would allow consumers to open these accounts without extensive documentation. The lack of check-writing and minimum balance requirements would also these accounts appropriate for those who have had demonstrated difficulty managing checkings accounts in the past. With this debit card, funds would be accessible from ATMs or at the point of sale.
The accounts would grow through an automatic savings plan, tied to bill payment and consumer credit options. Credit options would be offered at reasonable interest rates, and could also include a savings component in which monthly loan payments would include a savings contribution. For example, the accounts could offer a six-month, self-amortizing

[1]https://filene.org/incubator/incubator-project/employer-sponsored-small-dollar-loans
VIDEO:https://vimeo.com/82016948

consumer loan up to $500 that would have automatic repayment via direct debits from the account.

Challenges
Given the relatively low profit margins, uptake by financial institutions may prove challenging. Public policy could further incentivize the financial sector in the form of tax credits for example, which would ultimately make it easier for LMI consumers to access such accounts.[2]

Financial Stabilizer

What is it?
The “Financial Stabilizer” is a solution that integrates spending, savings and credit.

Who’s behind it?
The “Financial Stabilizer” is an idea introduced by Ideas 42 and Oliver Wyman in their “Reimagining Financial Inclusion” publication.

How it works
This product would extend beyond a traditional savings account by separating deposits into savings and discretionary spending pots. It would also provide short-term credit that shrinks as savings grow, and is automatically paid back with deposits. Customers would be able to take money from the discretionary spending pot for sudden liquidity needs, and automatic repayments on withdrawals would help maintain the savings buffer.

Automated mechanisms for building savings and maintaining an affordable credit source could lower credit risk and potential losses, leading up the possibility of more profitable, larger expense lending that presents lower risk for the bank and lower rates for the customers.

Oliver Wyman suggests that because the Financial Stabilizer product could result in lower credit risk consumers, higher customer engagement and retention and ultimately more stable deposits, a large or medium-sized bank could achieve an estimated $1BN lifetime profit potential by offering this product.

[2] Barr, 50.

Challenges
Regulatory considerations may impact the ability to advance such a product. For example, one of the biggest challenges is around the inability to mandate autopay for loans under Regulation E and disclosure requirements under Regulation Z. [3]

LISC Twin Accounts

What is it?
LISC Twin Accounts™ is a program which helps low- to moderate-income individuals build credit and save money at the same time

Who is behind it?
LISC offers Twin Accounts through its network of Financial Opportunity Centers (FOCs) through its financial partner, Justine Petersen Housing & Reinvestment Corporation, based in St. Louis, MO. The Twin Accounts product is now available in five states: Illinois, Michigan, Minnesota, Ohio and Texas

How does it work?
Twin account participants are issued a 1-year $300 loan that is locked into a Justine Petersen's master savings account. Proceeds from the loan are deposited into a sub account for each participant. Participants then make $26.24 monthly repayments. LISC matches each monthly payment – dollar for dollar – as long as it gets to Justine Petersen on time. At the end of the loan term, participants who make 12 on-time payments have $300 in savings and $300 in match funds, and improved credit.

LISC limits the use of match funds to one option: the opening of a secured credit card.

To be eligible, individuals must 1) want to build credit, 2) have sufficient net income to cover the $26.24 monthly loan payment, 3) have few, if any, active credit cards or lines of credit; and 4) have either no credit score or a low credit score at program entry. Participants must work with a LISC-supported financial counselor who is also a certified credit-building counselor* at a participating Financial Opportunity Centers.

Clients who are "unscored" at program entry typically generate a FICO credit score of 676 within six months (if all six payments are made on time). More importantly, among the 220 participants in the program to date, 82 percent have paid off the loan in full. Two thirds have made all of their payments on time.[4]

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[3] "Reimagining Financial Inclusion", p47.
[4] http://www.lisc-chicago.org/news/2561

Mission Asset Fund Lending Circles

What is it?
Formalizing rotating savings and credit associations, Mission Asset Lending Circles provide an opportunity for consumers to access zero-interest loans, while building credit.

Who is behind it?
The program is offered at MAF's office in San Francisco or through MAF's nonprofit partner providers across the country. Mission Asset Fund's 2011 study of over 600 participants found that clients felt nonprofit organizations, specifically those who offer in-house financial services, were ideal for the implementation of lending circles. Because clients felt that nonprofit organizations were concerned about their wellbeing, clients felt enough trust in the organizations to participate.

How does it work?
After completing an online financial training class, consumers can join a six to ten person group and decide on the amount of the monthly loan. For example, ten participants may decide on a loan amount of $1000. Then, each participant makes the same monthly payment of $100, which Mission Asset Fund reports to the credit bureaus. The loan rotates each month to a different participant. In the first month, one participant receives $1000 and each month after that a different borrower will receive the loan, until everyone in the Lending Circle has gotten a chance.

In Mission Asset Fund's 2013 study, following the recession, the average person in the control group increased their outstanding debt by almost $3,000, whereas the average person in the treatment group decreased their outstanding debt by over $1,000. Credit reporting allow participants to build credit to access fair credit in the long-term- Participants access 3 new lines of credit after participating in a circle.[5]

Challenges
Lending circle success is dependent on social connections. In order to successfully execute, a level of trust between participants and the agency offering the program must exist. Moreover, the upfront capital to sustain these programs may be difficult for some organizations. In Mission Asset Fund's 2013 study, they reported that the nonprofits not continuing the program mentioned limited resources or a perceived difficulty in generating funds as factors in their decision. Fundraising efforts to is lending circles require buy-in from

[5] http://missionassetfund.org/wp-content/uploads/Repli-short-web-FINAL.pdf)

leadership which hard to achieve for some, given the newness of the program and the uncertain funding stream.[6]

M-Shwari

What is it?

M-Shwari is a low-barrier, savings-and-loan product.

Who is behind it?

M-Shwari made possible through a partnership between Safaricom, M-PESA, Kenyan mobile money transfer service, and the Commercial Bank of Africa.

How does it work?

Through a mobile phone, M-PESA consumers can open an account in as little as thirty seconds and apply for a loan without any previous banking history. M-Shwari uses an algorithm based on a customer's Safaricom phone and M-PESA usage history to assess credit-worthiness, assign credit limits, and lend to new applicants. Customers are able to instantly check their loan limit and receive a loan in seconds if approved. M-Shwari offers an opportunity to save money in digital money wallets, paying quarterly interest from 2 percent to 5 percent, based on the average daily balance in the account. These rates are well above the 1.5 percent weighted average reported by the Central Bank in the Kenyan banking sector and do not require a minimum balance to obtain.[7]

Challenges

Although M-Shwari offers an interest rate that is high by Kenya banking standards, customers did not mention interest received from savings as a key benefit. Instead, the main appeal appears to be that customers can save for short-term needs while also increasing access to credit in the future. A 2014 Financial Inclusion Insights survey found that the most common biggest reason customers deposit into M-Shwari is to increase their loan limit.[8] How might we increase consumers appeal to leveraging interest for long-term savings and expand the use cases of M-Shwari beyond the management of short-term cash flow?

[6] http://missionassetfund.org/lending-circles-evaluation-released/
[7] https://www.cgap.org/sites/default/files/Forum-How-M-Shwari-Works-Apr-2015.pdf
[8] FII M-Shwari Survey in Kenya, May 2014, N=594

Pay Yourself Back

What is it?
Pay Yourself Back is a product add-on to any loan type encourages consumers to keep making regular payments (or a portion of it) to themselves after the loan is paid off.

Who is behind it?
Innovations for Poverty Action developed the product and piloted it during a 17-month reporting period with the Filene Institute.

How does it work?
Users pre-commit to building savings after paying off a new or existing loan. With Pay Yourself Back, borrower deposits are automatically transferred to a savings account after a loan is fully paid. Consumers can choose the size of their automated savings.

Challenges/Gaps
Pilot programs saw uptake of 5-15%.

P9 Loan

What is it?
P9 is a savings and loan service designed to help low income consumers manage liquidity in the face of low and irregular incomes.

Who is behind it?
Founded in 2007, P9 is run by Shohoz Shonchoy, the rural version of SafeSave, in Hrishipara, central Bangladesh.

How does it work?
Saving may often be constrained by a consumer's lack of liquidity, as savings intentions are swept aside by the need to spend. P9 responds to this dilemma by accepting deposits while offering liquidity in the form of zero interest loans.

After paying an account opening fee of 200 taka to cover registration and insurance, consumers receive a loan. One-third of the loan amount is immediately placed in a savings account (the client only receives two-thirds of the loan amount in-hand). Payments are collected physically through collectors. After repaying the full amount, clients are eligible for a new loan at a higher amount. Clients also have the option to "top-up" a loan if additional cash is needed before repaying the loan completely.

The basic product does not pay interest on savings. Savings withdrawals are subject to a five percent fee if withdrawals are made before savings reach a pre-committed threshold of $285. In 2013, P9 added a "P9 Special Savings" option that offers interest, creating a longer-term home for savings accumulated in the basic P9 account. Savings withdrawals are subject to a five percent fee if withdrawals are made before savings reach a pre-committed threshold.

Challenges

Scaling such a product may prove difficult in the United States, as profitability is small relative to other financial products. Mobile Venture Kenya realized that the that mobile money transactions using M-PESA could offer a number of advantages over the field staff model, especially flexible, anytime payments and disbursements and thus launched a mobile version of P9 loans through M-PESA. How might we leverage technology to launch a viable P9 product in the United States?

<u>SALO Advance Loans and Cash Accounts</u>

What is it?

The SALO program is an advance loan opportunity with a required savings component.

Who's behind it?

The State Employees' Credit Union (SECU) offers this program as a low-cost alternative to payday lenders.

How it works

SALO features a $500 maximum credit ceiling for a loan term of 30 days, at a 12% APR. This no fee, low interest loan allows members to borrow up to $500 per month and is also repaid monthly with funds from the members' next paycheck. Borrowers are required to place a small percentage of the loan proceeds in their SALO deposit cash account, which also earns dividends. When the SALO cash account reaches $500, the loan rate drops to 5.50% APR. As savings grow, members can use their accumulated savings in lieu of additional loan advance.

SECU complements the SALO program with financial counseling and education to assist members with long-term financial security.

Secured Credit Builder Loans

What is it?
Secured credit builder loans are small, secured loan that help establish credit history.

Who is behind it?
Secured credit builder loans can be found at banks or Community Development Financial Institutions. Online lenders include Self Lender, a venture-funded financial technology startup founded in 2014.

How does it work?
With secured credit builder loans, the money borrowed must be deposited in a savings account or CD for a predetermined time period and cannot be accessed until the loan is fully repaid. Each month, consumers make a payment towards the loan and interest. Payment history is reported to the federal bureaus. There may be administrative fees. For example, with Self-Lender, there is a $12 administrative fee and interest fee (scenario ex:. in a $550 credit builder account, the CD will pay out at $550.55 interest, but you will have paid $582 in monthly principal/interest)

At the end of loan term, a consumer has built credit, and can collect the loan back. Some institutions such as Self-Lender also pass the interest made on savings back to the customer.

Secured Credit Cards
What is it?
Secured credit cards is a credit card that uses money you place in a security deposit account as collateral.

Who is behind it?
Most of the large credit card issuers offer a secured card, with the largest market share belonging to Bank of America, Wells Fargo, and Capital One. Some small to medium sized providers also offer secured credit cards, including First National Bank of Omaha, many credit unions, and several of the largest prepaid card providers. Among the card networks, Visa represents the majority of all secured cards by a two-to-one margin over MasterCard.[9]

How does it work?
Secured credit cards combine the flexibility of a credit card with a forced savings mechanism in the form of a security deposit. The security deposit enables issuers to offer a credit card to

[9] 2016 CFSI Secured Credit Card Paper

those with thin or poor credit histories. Credit limits equal the value of the security deposit. The security deposit is held by the credit card issuer in a bank account and only used if the consumer fails to pay their outstanding balance. With a self-collateralized safety net, individuals can spend and pay down balances, with little fear of overextending or racking up an unmanageable debt load.

Over time, secured credit account holders may "graduate" to unsecured credit products and financial services from their card issuer. In addition, the use of the secured card is reported to the credit bureaus, helping the consumer to build a credit score that may qualify them for additional financial products at other providers.

Secured credit cards could serve different long-term savings purposes. For example, the Emerald Secured Credit Card by H&R Block can be funded using an existing personal bank account or a tax refund and Refund Anticipation Check if it was prepared by H&R block. The Prosperity SmartSave Card, offered by a national network of credit unions, builds an emergency savings account simultaneous to building credit.

To encourage growing emergency savings, incentives are offered including (1) gifting the child's savings account as the parent sets aside savings into the family emergency savings account; and (2) providing rewards for on-time repayment of credit lines.

<u>Two Grand Plan</u>

What is it?
The Two Grand Plan is a long-term savings account coupled with a semi-share secured micro loan.

Who is behind it?
The Filene i3 team at the Filene Institute developed this concept.

How does it work?
With a goal of at least $2000 in savings, consumers open a savings account that requires direct deposit or a recurring deposit schedule. The program ends when the savings account reaches $2000, at which point the member would have a liquid option for any emergency expenses. The balance can be moved to a money market or certificate of deposit where the member can reap the benefit of earning higher dividends.

The Two Grand Plan also sets up a semi-share secured micro loan to discourage members from withdrawing cash from their Two Grand Plan savings account. The loan amount is equal to double the savings balance or $2000, whichever is less. Until the member reaches $1,000 in savings, the credit union would be granting a 50% secured loan which is why the loan is described as a semi-share secured loan.

Credit unions establish withdrawal rules to discourage any unsubstantiated or frivolous withdrawals and to encourage changes in behavior. Should a member choose to withdraw money outside of these parameters, he or she would not be able to take advantage of the affordable rate loan benefit.

Challenges

Due to the limited gain this opportunity presents credit unions, Filene found it difficult to identify a pilot credit union to test the Two Grand Plan.