

**Policy level response to financial exclusion in developed economies:
lessons for developing countries**

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Introduction

There is both widespread and mounting concern about access to banking services across most developed nations – in Europe and North America as well as Australasia. This has been stimulated mainly by debates around social inclusion and the profitability (and hence social responsibility) of banks and fuelled by a near universal contraction in the number of bank branches. Perversely, it is a problem that emerges only when the majority of people have a bank account. In such circumstances, lacking a transaction account is costly and reinforces social exclusion.

Although levels of banking exclusion vary across the developed world, it is the same groups of people who are affected: people who either live on low incomes or have a history of bad debt. There is no single cause and although refusal by banks to open accounts is a problem it is by no means the main cause in many countries. Instead a range of factors act to deter or prevent some people from opening and using a bank account for their day-to-day money management. These include identity requirements, terms and conditions, charges, physical access problems and psychological barriers.

Solutions to combat banking exclusion are just as widespread. The most common response has been the introduction of voluntary charters or codes of practice, developed by the banks themselves, through their trade associations. Some countries have enacted legislation defining the right of access to basic banking services.

This study was commissioned by the Department for International Development to provide a brief overview of the policy-level response to financial exclusion in a number of developed economies and to draw from this lessons that could be applied in those countries that have less developed banking systems.

The study has drawn on detailed case studies of Australia, Belgium, Canada, France, Great Britain and the United States including

- A brief overview of the banking sector (including regulatory mechanisms and levels of concentration of the banking sector);
- An overview of the main characteristics of banking exclusion (levels of exclusion, characteristics of the unbanked and their geographical concentration);
- Details of policy responses to banking exclusion that have been implemented by regulatory authorities, government departments and the banks themselves and the impact that these have had on service provision and widened access.

In addition, information was collected on policy responses in a range of other developed countries, including Germany, New Zealand, Portugal and Sweden, as well as South Africa, which has an active programme to bring disadvantaged groups into banking.

The first part of this report comprises an overview of the situation across these countries, beginning with an account of the extent and nature of banking exclusion, followed by an analysis of its causes and concluding with an account of the various policy responses to

tackle the problem. Part 2 includes the detailed country reports of the six countries studied in depth.

The extent and nature of banking exclusion

The number of people with bank accounts has risen steeply over the past 30 years, so that basic transactional banking services are widely regarded as being essential to managing personal and household finances. This means that the minority of people left behind face considerable cost and inconvenience by managing their money entirely in cash (Caskey, 1997; Ekos, 1998; Kempson and Whyley, 1998; Kempson et al, 2000; Konsumentverket, 2000; Morris and Phillips, 1999; Ramsay, 2001).

In the industrialised countries studied, between one per cent and 17 per cent of adults lack a bank account of any kind. The exact proportion varies between countries, reflecting the level of inequality that exists, the make-up of the banking sector and variations in requirements to have wages and/or social security benefits and pensions paid directly into an account. The extent to which individual countries have had political initiatives to combat financial exclusion also plays a part.

Countries with low levels of income inequality (measured by Gini coefficients for equivalent disposable income¹) tend to have lower levels of financial exclusion, while the highest levels of exclusion are to be found in the least equal ones. In Sweden, for example, just under two per cent of adults did not have an account in 2000 and in Germany the figure was about three per cent (CSR Europe, 2001). Further up the scale of inequality, four per cent of adults in Canada and five per cent of adults in Belgium lacked an account as did nine per cent in the UK and in the US (CSR Europe, 2001; Ekos, 1998; Eurobarometer, 2000; Family Resources Survey 2001/02; Federal Reserve, 2001). Countries with the highest levels of inequality, also have the highest levels of banking exclusion. In Portugal, for example, about 17 per cent of the adult population had no account of any kind in 2000 (Eurobarometer, 2000). Typically around half of those without an account have never had one (CSR Europe, 2001; Kempson and Whyley, 1998).

Account-holding tends to be higher in countries like Germany and France where local savings banks and/or the post office are important players in the provision of banking services. Similarly, very few adults lack an account in countries such as Australia where payment of social security benefits and pensions has been made directly into bank accounts for a number of years.

The figures quoted above relate to the ownership of a bank account of any kind. More detailed investigations in Britain have found that as many people only have access to very limited banking services (a simple savings account with no cash machine card or bill-payment facilities) as lack an account of any kind and that as many people have an account that they hardly use as lack one altogether (Kempson et al, 2000). Likewise

¹ Income after taxes and taking account of the size of the household

there is concern in other countries that there may be a group of people who are ‘under-banked’ – that is people who have an account but make little use of it. Such concerns have been expressed in Australia, for example, where many people in receipt of welfare payments have the money paid into a simple pass-book account.

There is also a growing awareness that people are becoming excluded from banking services because they lack access to banking facilities that are widespread in the rest of society. In France the key problem is not having access to cheques, which are by far the most common form of payment. In Sweden, where internet banking is very well developed, people without access to a computer face growing difficulties and costs in making payment transfers.

Who are the banking excluded?

Regardless of the level of exclusion, it is quite clear that some groups of people are at much greater risk than others. Especially vulnerable are people living on low incomes, especially if they are not in employment and living on social security payments from the state. Typically those on the lowest incomes are twice as likely to be without a bank account as the average (ACEF-Centre, 1996; Collard et al, 1996; Daniel and Simon 2001; Ekos, 1998; Hogarth and Donnell, 1999; Institut fur Finanzdienstleistungen, 2000; Kempson and Whyley 1998; Kempson and Whyley 2001; Kempson et al, 2000; Morris and Phillips, 1999; Test Achats, 2001)).

People from low-income indigenous and ethnic minority communities have very low levels of engagement with banking (Buckland et al, 2003 Hogarth and Donnell, 1999; Kempson and Whyley, 1998; Kempson et al, 2000; Westbury, 2002).

Also at risk of exclusion are people with a history of bad debt, who often have their accounts closed if they fail to reduce their overdraft and then find it difficult to open another one. Indeed this is one of the major causes of exclusion in countries such as Sweden and Germany, where there is near universal access to banking (Gallou and Le Queau, 1999; Institut fur Finanzdienstleistungen, 2000; Kempson and Whyley 1998; Kempson 2000; Konsumentverket 2000).

Age and geographical location have also been identified as important factors in identifying those at risk of banking exclusion. The very young and very old are more likely to be unbanked than the general population, as are people living in rural communities (Connolly and Hajaj, 2001; Kempson and Whyley 2001; Kempson and Whyley, 1998;)

Alternative providers

Experience shows that where there are considerable numbers of un- or under-banked people, cheque cashers and remittance agents tend to fill the void. Concern is mounting in Australia, Britain, the United States and Canada, about the very high charges paid by un-banked consumers who use such fringe banking services (Argent 2002, Westbury 2002, Ekos, 1998; Kempson and Whyley, 1998; Morris and Phillips, 1999; Ramsay, 2001).

The causes of banking exclusion

There seem to be six explanations for financial exclusion, although the precise balance between these may vary somewhat from country to country. Obstacles such as identity requirements, the terms and conditions of bank accounts, levels of bank charges, physical access problems brought about by bank branch closures and psychological and cultural barriers are all important. The way government social security benefits and pensions are paid also plays a part in exclusion as does refusal by banks.

Refusal by banks

In every country covered by this review, a minority of people who lack an account have been refused one by the banks. These are mainly people who have a history of bad debt, although this is by no means always the case. Research in Belgium (Bayot, 2002; Test Achats, 2001), the UK (Collard et al, 2001; Kempson and Whyley, 1998; Kempson et al, 2000) the US (Belsy and Calder, 2004; Caskey, 1997; Kempson et al, 2000) and Canada (Department of Finance, Canada, 1998) have all shown that people with low incomes are also either refused an account outright or advised to go to another bank. This particularly affects people who are dependent on social security payments for their income.

Mystery shopping undertaken for the Task Force on the Future of the Canadian Services Sector showed that refusals continued to be a problem even after a voluntary agreement had been reached with the banks that should have solved the problem (Department of Finance, Canada, 1998). A similar situation was found in France, despite a new law strengthening the right of access to a bank account. Indeed people on low incomes faced difficulties opening an account even when they were assisted by charitable or consumer organisations (Bloch, 2000).

There is also evidence showing that people who have been refused seldom appeal against the decision, even when they have the legal right to do so (Bloch, 2000).

Identity requirements

In countries without a compulsory identity card, many people on low incomes and homeless people and refugees, in particular, find it very difficult to supply the types of proof of identity required by banks to open an account (Collard et al, 2001; Connolly and Hajaj, 2001; Department of Finance, Canada, 1998; Kempson et al, 2000). This has been exacerbated by steps taken by governments and the banking industry to combat money laundering and terrorism. Banks now routinely require both proof of home address and photographic identification before they open a bank account, with passports and driving licences being the most widely accepted. People without either of these often face real difficulties finding alternatives that banks are confident will be acceptable to regulators. The UK Financial Services Authority has recently fined two of the main high street banks for failing to make adequate identity checks.

Terms and conditions

A range of different types of terms and conditions deter or prevent people with low incomes from opening an account. The nature of these barriers differs between countries although there are clearly similarities between them.

In France, Canada, the USA and Australia, attention has been drawn to the minimum balances that are required for an account to be opened. In many cases, these opening balances are beyond the budgets of people on low incomes (Caskey 1997; CLCV, 1999; Department of Finance, Canada, 1998; Kempson et al, 2000).

A second area where obstacles occur is the conditions relating to the use of the accounts. In Belgium, for example, accounts have been closed by banks because customers either use them too little or withdraw the money in the account too soon after it has been deposited (Collard et al, 1996). In other countries, banks impose charges if a minimum balance is not maintained (see below). While in Britain one of the major causes of bank exclusion has been the fact that conventional current accounts have no safeguards against unintentional overdrawing. People on low incomes frequently find that their account can become overdrawn by a small sum of money for a few days simply because cheques take too long to clear or electronic transfers out of the account do not take place on the expected day. This results in unauthorised overdrafts, bounced cheques and failed direct debits. As a consequence customers face high charges that may be up to half a week's income for a single person living on government social security payments. Many of the people who had closed bank accounts said that this was the main reason why they had done so (Collard et al, 2001; Kempson and Whyley, 1998; Kempson et al, 2000). Similar problems occur in the United States (Kempson et al, 2000) and Australia (Connolly and Hajaj, 2001; Hajaj, 2002).

Thirdly, people on low incomes, or with a history of bad debt, are offered accounts that either have very limited facilities or have facilities that are inappropriate to the needs of someone living on a low income. In France for example, prior to the Government Decree of 2001 (discussed in the section on *Policy responses to banking exclusion*, below) people under 'banking interdiction' because they had a history of bad debt had a right to an account that could receive deposits but no more. In some cases, they could not even gain access to a cash machine card (Gallou and Le Queau, 1999). Mystery shopping by the Confederation de la Consommation du Logement et du Cadre de Vie showed that people with low incomes were often refused a cash machine card outright, or they were offered one for which a fee was charged or which could only be used at a limited number of cash machines (CLCV, 1999).

Finally, in Canada, there is a particular problem with 'holds on funds', where people with only small balances on their account have government cheques that they have deposited put on hold for a week or more before the funds are released to their account (Department of Finance, Canada, 1998; Ekos, 1998; Ramsay, 2000).

Bank charges

Just like terms and condition, levels of bank charges deter customers with low incomes from using transaction accounts. This is a significant problem in almost all the countries studied, with the exception of Britain, where transactional banking is free as long as the account has sufficient funds to cover the transactions made.

As noted above, the costs of inadvertently over-drawing, bounced cheques and failed direct debits are a major deterrent to people on low incomes using a bank account to manage their day-to-day finances (Collard et al, 2001; Connolly and Hajaj, 2001; Hajaj, 2002; Kempson and Whyley, 1998; Kempson et al, 2000).

There is, however, a range of other charges that have a disproportionate effect on people with low incomes. These include:

- Fees for failing to maintain a minimum balance in an account;
- Higher fees for over-the-counter transactions, which tend to be used most by people on low incomes;
- Monthly lump sum fees, which discriminate against those who make few transactions;
- High fees if the number of free transactions is exceeded.

(Connolly and Hajaj, 2001; Ekos, 1998; Department of Finance, Canada, 1999; Hajaj, 2002; Ramsay, 2000).

As discussed below initiatives to combat financial exclusion in Australia, Belgium and Canada have focused on providing low cost bank accounts.

Physical access problems caused by bank branch closures

Increased competition and the economics of international banking have led to programmes of bank branch closures across most developed countries. Technological developments (cash machines and telephone and internet banking in particular) have accelerated this trend. Moreover, it is clear that these closures tend to hit poor urban neighbourhoods and small rural communities quite disproportionately (Bloch, 2000; Connolly and Hajaj, 2001; Department of Finance, Canada, 1998; Kempson et al, 2000).

There is evidence that lack of physical access to a bank branch greatly increases the psychological barriers from banking (Kempson and Whyley, 1999). Interestingly though research conducted both in the USA and the UK shows that being unable to access a bank branch is not one of the main reasons given by people who are unbanked for lacking an account (Collard et al, 2001; Kempson and Whyley, 1998; Kempson and Whyley 1999; Power Financial Corporation, 2003).

Psychological and cultural barriers

Research has shown that many people on low incomes feel quite disengaged from banking. The types of barriers noted above fuel their belief that banks are not really interested in the needs of people like them and that the services offered are not appropriate to their needs (Collard et al, 1996; Collard et al, 2001; Ekos, 1998; Kempson et al 2000).

As a consequence, in many countries (and especially those with higher levels of banking exclusion) self-exclusion by people on low incomes is far more important than direct exclusion by banks refusing to open accounts.

Psychological and cultural barriers impede the use of banking services in the indigenous populations in Australia and Canada (Westbury, 2002; Buckland et al, 2003). In Britain the Pakistani and Bangladeshi communities face religious barriers to banking, because transaction accounts that can be overdrawn (even if inadvertently) are haram (forbidden) under Islamic law (Collard et al, 2001; Kempson and Whyley, 1998; Office of Fair Trading 1999b).

Social security payments

In some countries – Sweden, Germany and Australia, for example – all government social security payments have been paid directly into a bank account for some time. It is, therefore, hardly surprising to find that these countries tend to have the lowest proportions of people without a bank account.

In others – such as the UK, USA and Canada – payments have not been made in this way until very recently. In fact, research in the UK showed that being in receipt of social security was strongly associated with people being unbanked. Indeed statistical modelling showed that it has an effect net of household income, family circumstances and other factors known to influence the likelihood of having an account (Kempson and Whyley, 1998; Kempson and Whyley, 1999). Concerns about financial exclusion, coupled with a desire to reduce the costs of social security administration have encouraged the UK government, US federal and state governments and Canadian provincial governments to move towards making electronic transfer the normal method of payment for all social security benefits.

Policy responses to banking exclusion

Although financial exclusion has only received widespread attention in recent years, in some countries people have had a legal right to a deposit account for some considerable time. In Sweden, for example, banks are not allowed to refuse to open a savings or deposit account under section 2 of the Banking Business Act of 1987. In France, article 58 of the Banking Act of 24th January 1984 first recognised the principle of the right to a bank account. The USA federal government introduced the Community Reinvestment Act in 1997, partly in response to a concern about bank branch closures in low-income neighbourhoods. Under this legislation, which has been modified several times subsequently, federal bank regulatory agencies rate banks on their efforts and effectiveness at serving low-income communities. The main criterion is mortgage loans but regulators also consider the extent to which banks make deposit accounts available. The regulatory agencies can take a bank's rating into account when considering its request for a regulatory ruling, such as permission to merge with another bank. There is no direct sanction for banks that receive unsatisfactory ratings, but since the late 1980s

the vast majority of banks have made efforts to ensure that they receive a "satisfactory" or "outstanding" CRA rating (Kempson et al, 2000).

This early legislation was, however, only designed to ensure access to a deposit account. It did not go further and spell out the nature of the banking services that should be offered. Developments in this area have only really occurred over the latter half of the 1990s and have generally resulted from a wider concern about social exclusion. The majority of initiatives have been in place for fewer than five years and many have been introduced in the past year. It is, therefore, too early to say to what extent they will overcome banking exclusion or whether a voluntary charter is adequate or needs legislation to ensure that banks comply. Such evidence as we have gives grounds for cautious optimism but shows that the situation needs careful monitoring to ensure that the gains are maintained.

Voluntary charters and codes of practice

Voluntary charters and codes of practice, developed by the banks themselves through their trade associations to make provision for 'life-line' or 'basic' bank accounts, are the most common response to financial exclusion. In many cases, these developments have been prompted and encouraged by governments concerned to increase social inclusion.

The earliest of these voluntary charters was introduced in France in 1992. Developed by the French Banker's Association it committed banks to opening an affordable account with facilities such as a cash card, free access to a cash machine network, bank statements and a negotiable number of cheques.

In Belgium, a voluntary code of practice was introduced in July 1997 by the Belgian Bankers Association (ABB/BVV) following a report commissioned by the Ministry for Economic Affairs. This code provides for basic banking services for people on modest incomes who lack a bank account. At a minimum this 'call deposit account' offers three basic types of transaction: money transfers, deposits and withdrawals and bank statements – although individual banks may opt to offer other services if they wish. Up to three transactions a month can be made at a cost of less than 10 Euros per year. Some banks permit withdrawals using a cash card at a cash machine. All transactions are real-time and any taking the account into overdraft are stopped.

In Germany, despite a number of attempts to introduce a legal entitlement to a current account that did not carry an overdraft facility, a voluntary code was introduced by the German Bankers Association in 1996. This makes provision for an 'Everyman' current account, offering basic banking transactions but without an overdraft facility. Individual banks have different interpretations of the 'Everyman' account. The extent to which this voluntary code has reduced banking exclusion is disputed. On the one hand, figures submitted by the banking industry to the Bundestag show that between June 1996 and June 2000 more than 800,000 'Everyman' accounts had been opened – an increase of 350 per cent. Consumer representatives, however, question these figures. In particular, they claim that the majority of people opening these accounts are young people and not those on low incomes (Institut für Finanzdienstleistungen, 2000).

Access to basic banking in the UK and Australia has been achieved through voluntary arrangements with banks, but has not involved formal charters. In both countries, there is a more general Banking Code, which includes a commitment to telling people about basic bank accounts, but does not set down the features such accounts should offer.

In Britain, the incoming Labour government set up a series of policy action teams in 1998 to investigate different aspects of social exclusion. One of these related specifically to financial services, which investigated the extent and causes of banking exclusion as well as the possible solutions. The report of this policy action team puts forward a blueprint for a 'basic bank account'. This is an account offering a full range of banking facilities but differing from conventional current accounts in two key respects. It cannot be overdrawn and so all transactions are real time and it has a cash card for withdrawing money from cash machines but no cheque book. Ideally, it would also have a linked bill-payment account, into which agreed regular amounts could be paid from the current account and set towards a range of household bills (HM Treasury, 1999). The design of this account was based on the needs identified in detailed research with people on low incomes (Kempson and Whyley, 1999). The report of the policy action team also set a time limit of a year within which all banks would be expected to make such accounts available. This was reinforced both by a government-commission on competition in the UK banking industry (Cruickshank, 2000) and the Treasury (Britain's finance ministry) which set a deadline by which these accounts should be available. All banks complied with this deadline. To tackle the issue of access, the Treasury also required the largest banks to make their basic bank accounts usable through local post offices and sixteen now do so. Anyone holding a basic bank account with one of these banks can use their post office for basic transactional banking services. These developments are reflected in the Banking Code, which requires banks to tell customers about their basic bank account if it is suitable for their needs.

Following the Prices and Surveillance Authority's 1995 banking inquiry Australian banks provided the Treasurer with undertakings to provide basic accounts. Unfortunately they did not honour this commitment when the government changed after the 1996 election and the matter was not pursued by the incoming government (Connolly and Hajaj 2001). Competition and the growing emphasis on corporate social responsibility have, however, led a number of banks to look at ways of providing low-cost banking services to people on low incomes, although this has been constrained by competition law.

In 2002, the Australian Bankers' Association made an application to the Australian Competition and Consumer Commission on behalf of ten member retail banks (Australian Competition and Consumer Commission, 2002). This proposed a generic basic account with the following minimum features: no account keeping fees; no minimum balance to open the account; no minimum monthly balance requirements; unlimited deposits free of charge; and six non-deposit transactions (including three over-the-counter cash withdrawals) free of charge each month. Consumer groups submitted evidence against the proposal as some banks already offered basic accounts with better features than those being proposed and they feared that these features would be scaled

back. The ACCC accepted these arguments and therefore rejected the proposal as anti-competitive. They invited the ABA to propose an improved generic account, but members have decided not to pursue this but to continue to develop their own accounts. Despite this set-back all four major banks now offer basic bank accounts, some of which go way beyond the original generic account proposals.

Despite these encouraging voluntary developments, there is evidence that basic accounts are not always promoted to people who might benefit from them most (Confederation de la Consommation, du Logement et du Cadre de Vie, 1999; Banking Code Standards Board, 2002; Financial Services Consumer Panel, 2002; National Association of Citizens Advice Bureaux, 2002; Test Achats, 2001). As a result, in Britain, the Code provisions relating to basic bank accounts are to be strengthened in the 2005 edition. At the time of writing there are also press reports indicating that the Government may intervene to ensure the promotion of basic bank accounts by banks. An alternative response, favoured by France and Belgium, has been to look to the law to enforce previously voluntary charters (see below).

Legislation

Three of the countries studied in detail have introduced legislation that both gives a universal right to a bank account and, more importantly spells out the precise nature of the banking services that must be provided.

In France, the law on exclusion (98-657) of 29 July 1998 reiterated the right to an account first set out in the 1984 law, and strengthened it with a right to basic banking services. It also simplified the process of exercising the right to an account. This means that any person with French nationality has the right to open an account at any private or public bank and, if refused, they can apply to the Banque de France for it to designate a bank that should open an account. The 1998 law also made provision for a decree defining the basic banking services to which such people should have a right, as well as the tariff conditions for those services. This decree was issued on 17 January 2001 and sets out a right to a simple transactional account with a cash card for use at cash machines but no overdraft facility. Although similar in most respects to developments in other countries the type of account described in this decree was met with some dismay by consumer organisations.

In Belgium, a basic banking bill was introduced on 18th July, 2001 and became enacted on 24th March 2003 with implementation from 1st October, 2003. This law applies to all banks and aims to enforce the principles of the charter by the imposition of sanctions if these principles are not applied. It does, however, go beyond the provisions in the earlier charter, setting out further minimum standards for basic bank accounts, including a ceiling on charges and a minimum number of free face-to-face transactions. It requires banks to contribute to a compensation fund, which is managed by the National Bank of Belgium, to compensate financial institutions that open more than their 'share' of basic accounts. In addition, statistics on the number of basic bank accounts opened must be communicated to the National Bank of Belgium.

Developments in the United States have been more fragmented – reflecting the banking system itself. In 2002 President Clinton proposed that the federal government enact legislation encouraging banks to create "First Accounts" with very low minimum balance requirements and low fees, for people without deposit accounts. By 2002, just seven states had turned the idea of low cost banking into law; the Federal Government had not.

In many ways, the policy response in Canada combines the best of developments in other countries. The federal government set up a task force on the future of the Canadian financial services sector, which published its report in 1998. In 1999, the government responded with a report (Department of Finance, Canada, 1999) setting out 57 reform measures, which were then included in legislation put before Parliament. Bill C-8 was enacted in June, 2001 and includes new rules designed to tackle banking exclusion. These include rules requiring all banks to provide accounts without minimum opening balances to all Canadians, regardless of employment or credit history, with minimum identification requirements. Significantly, though, the Act also includes rules allowing the Government to make regulations regarding the provision of low-cost accounts. The banks were given an opportunity to address this issue voluntarily before regulations were introduced. Eight banks have signed a Memorandum of Understanding with the Government pledging to offer low-cost accounts to their customers.

Lessons that can be learnt from these experiences

When the vast majority of people are making full use of banking provision, reliance on cash transactions becomes both difficult and expensive. This is a major problem for the people who are excluded in highly banked nations. Furthermore, one of the consequences of not providing adequate access to banking services for everyone includes the proliferation of high cost alternative providers, such as cheque cashing services and remittance agents. It is therefore important to look at ways of encouraging universal access to banking.

Levels of banking inclusion inevitably rise in response to both increasing prosperity and declining income inequalities. There are, however, a number of barriers that can stand in the way of achieving banking for all. As discussed above, these include: features of bank accounts (including terms and conditions and charges); the way that applicants are screened and vetted; physical access problems and cultural and psychological barriers. It is possible to identify ways in which these barriers can be minimised. This would include ensuring the availability of simple accounts that are both appropriate and affordable for people on low incomes; maximising the advantages of technology to provide appropriate access; encouraging take-up of the banking services available, and involving not-for-profit organisations such as post offices.

There is a need for low-cost no-frills accounts

The increase in the breadth and complexity of banking services has undoubtedly contributed to banking exclusion in highly-banked countries. Simple products, on the other hand, help ensure access to people on low incomes whose needs tend to be more

basic. All the countries studied in depth for this report have needed to reinvent simple bank accounts to achieve banking inclusion. Such accounts, typically, do not have an overdraft facility and have addressed both terms and conditions and charging structures that act as barriers to use by people on low incomes.

Applicants need a good credit score to open a current account with an overdraft facility, whereas a simple account with no overdraft facility can be offered regardless of an applicant's income or previous credit history. In any case, all the evidence suggests that people on low-incomes would prefer to have an account that cannot be overdrawn inadvertently as this gives them greater control over their finances.

People on low incomes can be prevented from opening an account by conditions such as requiring a minimum balance to open an account and/or a minimum number of transactions to keep it open. Simple 'no frills' accounts can overcome these problems.

Moreover, charging structures often impact hardest on people who have low incomes and/or only need to make a small number of transactions. This would include fees for failing to maintain a minimum balance and monthly lump sum fees regardless of levels of use. Simple accounts typically relate charges solely to levels of use.

Developments in technology offer solutions and risks

Technological advances have made it much cheaper for banks to conduct business electronically. In many highly-banked countries, however, this has tended to reinforce banking exclusion as poor peoples needs have not been considered and they have been left reliant on traditional banking facilities, such as pass books and face-to-face transactions in branches, which are costly to provide and therefore, in decline.

Solutions to banking exclusion have involved using developments in technology to contain costs and allow wider geographical access while ensuring that people on low-incomes retain the financial control which underlies their preference for traditional banking services.

Arguably one of the most important developments is real-time banking. Real-time banking can be used to prevent unauthorised (and often unintended) over-drawing and allows customers to be in full control of their account. With this facility credit checks become less important, and even young people can have access to electronic payment methods, so building confidence in the system at an early age. It also replaces costly paper-based transactions with ones using plastic cards and electronic funds transfer. Some, but not all, highly banked countries have created a banking infrastructure that utilises real-time banking for all accounts. Countries that developed real-time accounts only for people on low-incomes have created a system that has restricted access. In Britain, for example, basic bank accounts have Solo or Electron cards, which can be used at all ATMs, but not at all retail units as some lack the equipment needed to check accounts on-line in real-time. As the number of people with these accounts increases, so too do signs outside petrol stations and small retailers saying that they do not accept payment by Solo or Electron cards.

At the same time, it is important that technological developments do not create new forms of exclusion. There is a real danger of this happening in countries (such as Sweden) where internet banking is fast becoming the norm.

There is a need to encourage the use of banks

Access to appropriate and affordable banking is only part of the problem. In some apparently very highly-banked countries, a number of people with a bank account are nonetheless making very little use of the services on offer; they are described as being under-banked. These people share many of the characteristics as those who are unbanked in other countries.

Low utilisation of banking facilities can result from policies aimed at improving the percentage of people with an account without addressing the underlying reasons for them being unbanked. For example, a number of countries took the decision that wages and/or all state benefits and pensions would be paid into a bank account before addressing the need for accounts that were appropriate to the needs of people on low-incomes. Whilst this can have the desired effect of encouraging people to open an account, they often withdraw all their income as soon as it is received and continue to operate a cash budget.

Even where appropriate accounts are on offer, if banks are seen as being predominantly for the better-off, people on low-incomes will be reluctant to use them. Experience shows that there is a need to promote the use of banking services as well as increase access to them.

Not-for-profit organisations can have an important role to play

Levels of banking exclusion tend to be lower where not-for-profit organisations, such as post offices, play a role in delivering banking services. This is partly because, compared with banks, they have a much larger network of outlets and partly because poor people see them as more user-friendly. This could involve the post office offering banking services itself (as in France) or acting as a local agent for the banks (as in the UK).

It is, however, important that such not-for-profit organisations are fully integrated into the systems for electronic transfer of funds used by banks. Without this, people using the banking services they offer will still remain on the margins of the banking system

Achieving universal access to banking

In an ideal world, competitive pressures would ensure that the banking needs of all people are met. Experience shows, however, that some intervention may be needed to ensure that appropriate provision is made for people on low incomes. Among the six countries we have studied in detail this has been achieved in a range of ways.

Least successful is legislation conferring the right to a bank account, without ensuring that appropriate accounts are available. Instead, most countries have relied on pressure being applied to banks to recognise their corporate social responsibility and provide access to transactional banking to all through the development of appropriate products.

This has been achieved in a number of ways – through ‘voluntary agreement’, as in Britain; through legislation as in Belgium, where a voluntary charter did not work; and, in Canada, a mix of the two, with legislation underpinning a voluntary agreement.

It is difficult to say which of these three approaches is the most appropriate as, in large part, it depends on the culture and legal system of the country concerned. In Britain, self-regulation through voluntary codes of practice is commonplace; in Belgium or France it is not. Moreover, experience suggests that careful monitoring of compliance is more important than whether self-regulation or legislation has been used. Least successful is relying on consumers themselves to seek redress. There needs to be an independent body monitoring the extent to which banks have genuinely removed barriers to access and both developed an appropriate account and promoted it to the people who might benefit.

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Australia

Overview of the Australian banking sector

Australian Government figures indicate that there are 53 authorised banks in Australia, of which 39 are foreign-owned and 14 are domestic (Australian Prudential Regulation Authority, 2002). 19 institutions account for over 90 per cent of the banking sectors assets (Reserve Bank of Australia Bulletin April, 2003). The “Big Four” domestic banks are ANZ Bank, Commonwealth Bank of Australia (CBA), National Australia Bank (NAB) and Westpac Banking Corporation.

Banking supervision and regulation

In 1998 Australia saw wide-ranging changes to its financial regulatory structure following the recommendations of the Financial System Inquiry (known as the Wallis Inquiry, 1997). These changes included the establishment of a single prudential regulator, the Australian Prudential Regulation Authority (APRA). APRA is now responsible for banks, credit unions, building societies, insurance companies, friendly societies and superannuation funds. A separate regulator was created to deal with market integrity and consumer protection issues across the financial system - the Australian Securities and Investments Commission (ASIC) (Reserve Bank of Australia, 1998). The Council of Financial Regulators is the co-ordinating body for the main financial regulatory agencies: the APRA, ASIC and the Reserve Bank of Australia (RBA), which chairs the Council and has responsibility for monetary policy and the stability of the financial system².

In addition, the Australian Bankers Association has produced a Banking Code, with provisions that go beyond regulation. The second edition of this Code was produced in 2003. At present, only around half of Australian banks are signatories to the Code.

Overview of the main characteristics of banking exclusion in Australia

The Australian social security system relies heavily on direct deposit of benefits into a bank account – those without an account make special arrangements with their local Centrelink provider for the payment of benefit. This means that the prevalence of unbanked adults is much lower than in other developed nations. A survey (of adult financial literacy) conducted in 2002-2003 found that just three per cent of adults in Australia lacked an ‘everyday’ banking account (ANZ Banking Group 2003). There is, however, growing concern about people being ‘under-banked’ – that is people who hold an account but make little use of it and operate a cash budget.

Despite the wide access to banking there are clusters of excluded people – most particularly in the indigenous communities.

² (see www.rba.gov.au)

Reasons for banking exclusion

There seem to be three main reasons for banking exclusion in Australia: limited physical access; bank charges and proof of identity.

In 1998 the National Farmers Federation in Australia estimated that 600 rural communities were without access to financial providers. It has been estimated that there were about 2,000 bank branch closures (28 per cent of the total) between 1993 and 2001, which disproportionately occurred in low-income urban areas and remote rural communities (Connolly and Hajaj, 2001).

Elderly people face particular difficulties with access, especially if they live on low incomes or have mobility problems which make physical contact with banks difficult (Connolly and Hajaj, 2001). The indigenous population also faces access difficulties, due to disproportionately low incomes and living in remote communities. In towns, such as Alice Springs, poor security is an additional issue. Lack of banking facilities for these indigenous communities can result in a “feast and famine cycle” because poor, unbanked families have no means of accessing funds/credit between welfare cheques (Westbury, 2002).

Affordability has, however, been the main barrier to banking in Australia. This has been described as the ‘bank fee poverty trap’, and occurs because banks are pricing in a way that will dissuade potential applicants with low incomes from becoming customers. Fees are imposed if customers fail to keep a minimum balance in their account, and both fees and minimum amounts regularly increase. High charges are incurred for temporary overdrafts, bounced cheques (both paid out and in) and failed direct debits (Connolly and Hajaj, 2001, Hajaj, 2002). A report by the Reserve Bank of Australia in 2003 noted that whilst banks offered fee waivers for students, disabled customers, pensioners and rural customers unable to access an ATM, this was not always the case for other customers with low balances who made non electronic transactions. These people were paying considerably more in fees and charges in 2003 than they had been in the mid 1990s.

Proof of identity is also a problem for some Australians and immigrants. Identification requirements come under the Financial Transactions Reporting Act 1988. The requirements are based on a “100 points” test. It is difficult to reach the required 100 points without a driving licence or passport, both of which are costly and not held by many people on low incomes.

The gap in banking provision has resulted in the emergence of money lenders and cheque cashers. Money lenders offering loans of 62 days or less are exempt from State consumer credit laws that impose a curb on loan fees (Argent, 2002). Alternative providers are a particular concern in North Australia where almost 38 per cent of welfare recipients were still receiving payment by cheque in 1999. An estimated 90 per cent of these are indigenous people, some of whom are resorting to cashing their cheques using a variety of non-regulated services (Westbury, 2002).

Policy responses to banking exclusion

Following the Prices and Surveillance Authority's 1995 banking inquiry the banks provided the Treasurer with undertakings to provide basic accounts. Unfortunately they did not honour this commitment when the government changed after the 1996 election. The incoming government took no steps to ensure that banks implemented their undertakings as they believed that technological advancements and competition would be sufficient to ensure that banks reached out to more of the population (Connolly and Hajaj, 2001).

At first it was argued that it was not viable to provide fee-free banking services in Australia (Connolly and Hajaj, 2001). Despite this, there are indications that competition and the growing emphasis on corporate social responsibility have led a number of banks to look at ways of providing low-cost banking services to people on low incomes. This has, however, been constrained by Competition law.

In 2002, the Australian Bankers' Association made an application for a generic basic account to the Australian Competition and Consumer Commission on behalf of ten member retail banks (Australian Competition and Consumer Commission, 2002). This proposed a set of minimum standards for a basic bank account that would be offered by the ten banks. These included the following features: no account keeping fees; no minimum balance to open the account; no minimum monthly balance requirements; unlimited deposits free of charge; and six non-deposit transactions (including three over-the-counter cash withdrawals) free of charge each month. The ACCC rejected the proposal, which they considered anti-competitive as the four largest banks already offered basic accounts with better features than those being proposed for the generic account. There was a fear that the generic account would become the industry norm. The ABA was invited to propose an improved generic account, but members have decided not to pursue this but to continue to develop their own accounts.

All four major banks now offer basic bank accounts. ANZ and National Australia Bank both provide very generous basic bank accounts at no cost to people who qualify for Government benefits. The ANZ account offers an unlimited number of free transactions each month, although it does not allow the use of other bank's ATMs. There is no minimum monthly balance and no account servicing fee. The National Australia Bank offers a National Concession Card Account which has no monthly service fees. With this account customers are entitled to a monthly rebate of \$40 (transactions are priced according to channel and then totalled at the end of the month). Commonwealth Bank and Westpac also provide basic accounts.

Moreover, the revised ABA Code of Practice now includes a clause requiring bank staff to give information about suitable accounts to low-income customers, if they tell the bank about their circumstances or it becomes apparent that they are in receipt of social security payments. It also commits the industry to providing rural and remote areas with face to face banking services even after a branch is closed, through alternative means such as franchising or in store provision.

The ABA is considering ways of improving access to banking for the elderly. They have implemented a programme called Self Service Banking and Older Australians in which a bank representative demonstrates how to use ATMs, EFTPOS, telephone and internet banking. For communities faced with the loss of their bank branch, the banking industry has also undertaken to adopt a minimum uniform standard for rural and remote branch closures (except in unusual circumstances, banks will give three months written notice to customers before closing any rural or remote branch) and to consult with local communities on the trends in the delivery of banking services so that they may consider developments that may affect the way they will be able to access banking services in their area (Australian Bankers' Association, 2003b).

The Australian Government has committed A\$70 million, funded by a partial sale of Telstra (a communications provider), to provide banking and other transaction services to communities without banking facilities. The provision, known as the Rural Transaction Centre programme (RTC), is aimed at smaller rural communities and towns. Facilities can be set up in existing stores and post offices or in stand-alone centres, and run by communities or local councils. In addition, rural communities that might not be eligible for the RTC programme can apply for funding to install EPOS equipment in post offices as a result of a cooperative venture between the federal government and Australia Post. The EPOS equipment offers deposit and withdrawal facilities as well as other options such as bill payment through 70 financial institutions.

The Rural Transaction Centre programme was integrated into the Australian Government's new Regional Partnerships programme in July 2003. It is intended that this will allow a straight forward, single application process for communities to apply for all Australian Government funding support for regional development projects. Communities will also be offered support throughout the application, development and establishment of an RTC through the Regional Partnership programme (Department of Transport and Regional Services).

It is not intended that RTCs will duplicate existing services, nor will they provide new services already planned by other organisations. Despite this the programme has been criticised for causing banks to pull out of some communities. It has also been suggested that some rural communities see the RTC as no more than a way of replacing old (Telstra) services and with new ones (Connolly and Hajaj, 2001). Notwithstanding these criticisms, to date over 100 communities have RTC facilities, and many more have successfully applied for funding to be provided in the near future (Department of Transport and Regional Services).

Access to banking has also been improved by other providers. The CBA operates an instore banking service within Woolworths which claims to offer competitive interest rates, no account keeping fees and unlimited free electronic withdrawals per month in all Woolworths/Safeway stores. Other banks have a presence in other chains across Australia (see Argent, 2002). Community banking is also flourishing in parts of Australia, supported by Bendigo Bank. Bendigo Bank offers to conduct viability studies and then provides infrastructure, training and support if a community can show that a viable

Community Bank can be established. There are over 100 Community Bank branches open, including two in Tasmania. Last year Community Banks opened their 250,000th account.

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Belgium

Overview of the Belgian banking sector

The Belgian banking system has seen some major changes in the last 12 years, as a result of mergers and takeovers and the conversion of special status financial institutions into limited companies. Between 1995 and 2002, the number of Belgian domiciled banks fell from 105 to 65 as a result of the wave of mergers and acquisitions. Between 1997 and 2002, the share of the five largest banks by total assets – Fortis, Dexia, KBC and ING and Artesia - increased from 54 per cent to 82 per cent.

In addition, the post office delivers banking services (bank accounts, savings products) through la Banque de la Poste, a 50/50 joint venture with Fortis in which La Poste acts mainly as a distributor through its agents. La Poste acts *de facto* as a bank for the poor. Consequently, it holds 11 per cent of bank accounts but only one per cent of account balances.

The government makes extensive use of cash transfer services offered by La Poste for the payment of social security benefits. These operations are managed by La Poste Financière, a division within La Poste parent company. Until recently, La Poste was the only institution which had, by law and through its management contract, to open an account to any applicant over the age of 12.

Banking supervision and regulation

Since 1993, distinctions in the legal status and supervisory framework between commercial banks, savings banks and public credit institutions have disappeared. Most public and special status credit institutions have been privatised.

Until the end of 2003, banking and credit institutions were supervised by the Banking and Finance Commission (BFC), which was legally autonomous from the National Bank of Belgium (NBB) but had to consult them before publishing regulations concerning solvency and liquidity. A single regulator, la Commission Bancaire, Financière et des Assurances covering banking, insurance and investment took on this function on 1st January 2004.

Overview of the main characteristics of banking exclusion in Belgium

According to the Eurobarometer Survey, five per cent of people in Belgium lack a current account, giro account or something similar (Eurobarometer, 2000).

A study commissioned by the Ministry of Economic Affairs in 2002 estimated that out of an adult population of around 8.5 million, between 40,000 and 80,000 people lacked a bank account (Bayot, 2002) and that the number had increased since 1996. The figure of 40,000 includes only people on unemployment and invalidity benefits who do not have their benefits paid into a bank account. The larger figure of 80,000 was arrived at by

adjusting this figure using the results of survey of consumer representatives and the number of benefits paid by postal order (chèques circulaires). They also found that social security agencies were making fewer payments in cash, alternative payment methods were under threat and prohibitive charges were levied on chèques circulaires (Bayot, 2002). They concluded that the consequences of not having a bank account were becoming more serious.

Typically, people who lack bank accounts are on a low income: 45 per cent have incomes of less than 620€ per month, and 85 per cent less than 868€. There is a high concentration among the young and the unbanked often suffer from multiple deprivation: low educational attainment, on minimum income or unemployed. Legal immigrants are over-represented (illegal immigrants do not qualify by law) (Bayot, 2002).

Reasons for banking exclusion

In Belgium, concern about access to basic banking services has arisen mainly since 1993, partly because before that date price controls ensured free or quasi-free bank accounts and transaction services and partly because of the rapid changes which took place after the 1993 banking deregulation law.

Much of the debate on banking exclusion has focused on people being denied access to an account. In 1994, the national report on poverty indicated that *'Poor people have a right to banking services; abuses must be avoided but it is a practice among certain banks to refuse to open a bank accounts for those on the minimum income (minimex)'* (Rapport National du Gouvernement sur la Pauvreté, 1994).

Following this, in 1996, the Ministry for Economic Affairs commissioned a study of banking exclusion from the Centre Coopératif de la Consommation. The research concluded that banking exclusion was growing and that people who were unemployed or living on the minimum income were being refused access to a bank account or having their existing accounts closed. This drew on evidence from social workers employed in social aid centres (CPAS, or Centres Publics D'Aide Sociale) (Centre Coopératif de la Consommation 1996).

Policy responses to banking exclusion in Belgium

On 20th December 1996, following publication of the report commissioned by the Ministry for Economic Affairs, banks signed a charter on basic banking services which committed them to provide a basic bank account without overdraft facilities to people who lack a transaction account. These accounts have to offer credit transfers, direct debits, deposit and withdrawal facilities to those without another transaction accounts. The bank can choose to add a debit card but bundling of additional products is not allowed. Such accounts cannot require a compulsory initial deposit or the maintenance of a minimum balance; other charges must not exceed standard bank charges. Bank statements must also be made available through ATMs, but not necessarily in paper form. Banks can refuse to open a basic bank account if the applicant is an existing customer who has a previous history of default, or for reasons of fraud and money laundering, but

must tell them why their application was refused. They cannot, however, turn down an application from someone with a poor credit history if they are not an existing customer of theirs. Appeals can be made to banking ombudsman.

On request from the Conseil de la Consommation – a consensual organisation associating all stakeholders: industries, trade unions and consumers - the Belgian Banking Association carried out a survey of how their members were applying the Charter. With only 25 cases brought to the ombudsman (all settled) and no negative reports from CPAS and other charities working with vulnerable individuals, the Commission considered on 8th December 1999 that the voluntary charter produced the desired effects (Conseil de la Consommation, 2003).

Furthermore, pricing for the basic banking service was reported to be below €10 per year. La Poste provides the service free of charge. Cash withdrawals from the bank's private ATM network are also free of charge. Debit cards (sometimes equipped with proton) are available for a fee of between €12 and €20 a year.

They did, however, identify problems related to the use of chèques circulaires, a payment form used by social security organisations for emergency situations. The reports showed that banks were becoming less willing to accept these and/or were increasing the charges for doing so. A second major problem is that social security and alimony payments, which cannot be seized, become seizable as soon as they are paid into an account. The Conseil recommended a new evaluation by the end of 2000, involving the CPAS, the relevant charities, the banks and the ombudsman.

Consumer associations expressed reservations about the optimism of the assessment made in this report and did not sign up to the recommendations. And concern continued to be expressed by a wide range of bodies about limited access to banking for people on low incomes. In May 2001, FGTB, a trade union, issued a press release stating that two of the main banks were breaching the charter. They maintained that ING was requiring unemployed customers to maintain a minimum balance of €25 in their accounts. They also alleged that Fortis had set up a special unit aimed at identifying and closing unprofitable bank accounts in underprivileged urban districts Fortis denied this but admitted that they had pilot experiments in ten branches aimed at redirecting unprofitable clients towards Banque de La Poste.

In April 2001, Test Achats, the consumer test association, organised a small mystery shopping survey undertaken by people who lacked a bank account who were either unemployed, or on the minimum income. It also checked with the management of each bank, that it was committed to the Charter. The survey produced damning results for the banks: out of 29 applications to open a bank account, 13 were accepted and 16 turned down. Most people were refused because of their low income. In some cases people were unable to open an account because they were unable either to meet the minimum initial deposit requirement or to maintain the required minimum balance in the account. In other cases, staff refused to open an account because people did not meet internal rules

for account-opening. The publication of the study caused an outcry in the Belgian press (Test Achats, 2001).

The Ministry of Economic Affairs decided to commission a further study which was undertaken by the Réseau de Financement Alternatif de Namur (Bayot, 2002). This found that the Banking Charter was having little or no effect in overcoming financial exclusion. As already noted, the number of people who were judged to be un-banked was estimated to have increased. In a postal survey of social aid organisations, 60 per cent of respondents had clients who had experienced banking exclusion. The most common problem was the refusal to open a bank account, followed by refusal to carry out operations at the bank counter, refusal of a debit card and the closure of an account. The main reasons for these refusals related to potential insolvency (low income, debt or a past history of unauthorized overdrafts); lack of a permanent address; not having a regular income paid into the account; and refusal by the applicant to carry out transactions other than face-to-face. In 70 per cent of cases, the problem was overcome - mainly by applying to another bank.

Further to this study, the Conseil National de la Consommation produced its second Opinion on 28th March 2002 (Conseil de la Consommation, 2002b). This Opinion was used almost word-for-word in the basic banking bill which was introduced on 18th July 2001 and became enacted on 24th March 2003 with implementation from 1st October 2003. This law applies to all banks and aims to enforce the principles of the charter by the imposition of sanctions if these principles are not applied. It does, however, go beyond the provisions in the earlier charter in a number of ways:

- It imposes a 12€ a year ceiling on charges for managing the account and related authorised payments; whereas the charter permitted standard bank charges.
- The number of free face-to-face transactions a year has been fixed by Royal decree at 36 for accounts with a debit card; or 72 if no debit card is provided.
- The banks must offer a face-to-face service and cannot force basic banking clients to use ATM services.
- Banks must contribute to a compensation fund, which is managed by the National Bank of Belgium, to compensate financial institutions that open more than their 'share' of basic accounts. This compensation is based on the difference between the standard cost of the account and the €12 ceiling. The method of calculating the 'share' of each bank has not yet been indicated by Royal decree, which prevents the creation of the fund for the time being.
- Disputes about basic banking services will not be referred to the banking ombudsman, but to an independent dedicated extra-judiciary litigation service comprising representatives of banks and consumers.
- Banks must give unsuccessful applicants the reasons for refusal in writing.
- Statistics on the number of basic bank accounts opened must be communicated to the National Bank of Belgium.

A bill is being prepared (to be passed at the earliest in Spring 2004 and implemented a year later) which will forbid the seizure of all social security and alimony payments transferred into bank accounts. This bill follows the Opinion of the Conseil de la

Consumption on the subject (Conseil de la Consommation, 2002). It is the responsibility of the issuer to identify these payments through a special code.

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Canada

Overview of the Canadian banking sector

The Canadian banking sector is dominated by six big players, the Royal Bank of Canada, TD Bank Financial Group (including Canada Trust), Canadian Imperial Bank of Commerce, The Bank of Nova Scotia, Bank of Montreal and National Bank of Canada. (Department of Finance, Canada 2002). The remainder of the banking sector is made up of many thousands of smaller financial institutions. The largest of these include nine smaller domestic banks, 33 foreign bank subsidiaries and 21 branches of foreign banks (Canadian Bankers Association (CBA), 2003a). Other providers of banking services include both Federal Government agencies, such as the Business Development Bank of Canada and Farm Credit Canada, and Provincial Government savings agencies, such as Alberta Treasury Branches and Investissement Quebec.

Credit unions or “caisse populaires” are important providers of financial services in Canada, particularly in small towns. They are often the only financial institution available in a community, particularly in the province of Quebec, where they were first introduced in 1900. They compete directly with chartered banks; indeed in British Columbia some even rival banks in size.

Banking supervision and regulation

The Office of the Superintendent of Financial Institutions (OSFI), established in 1987, is the primary regulator of federally chartered financial institutions and federally administered pension plans, reporting to the Minister of Finance. OSFI is responsible for the supervision and regulation of all banks, and all federally incorporated or registered trust and loan companies, insurance companies, cooperative credit associations, fraternal benefit societies and pension plans³. OSFI has powers to monitor the financial condition of federally regulated financial institutions, but not the authority to dictate how these institutions conduct their day-to-day affairs with their customers. Consequently, in 2001 a new independent government body was created by the federal government, the Financial Consumer Agency of Canada (FCAC). The FCAC is responsible for enforcing (financial) consumer protection laws, and as such is responsible for the supervision of all federally regulated financial institutions, including banks. It also aims to inform and educate consumers about their rights and responsibilities. 2002 saw the introduction of the Ombudsman for Banking Services and Investments (OBSI), an independent organisation to investigate complaints against banks and other financial providers operating in Canada.

Despite the recent changes to the supervision of the banking sector, the regulation of financial institutions remains complex, and is described by the Canadian Bankers Association as a “patchwork quilt approach” split as it is between federal and provisional control. Provincial governments are, for example, still responsible for the supervision of

³ See The Office of the Superintendent of Financial Institutions website:

<http://www.osfi-bsif.gc.ca/eng/about/index.asp>

credit unions, securities dealers, mutual fund dealers, finance companies and cheque cashing outlets.

Also, in contrast to Britain and Australia, Canada does not have an overall Banking Code setting standards that go beyond regulatory requirements. There are, however, five codes of practice that cover specific areas of banking such as debit card services and electronic banking.

Overview of the main characteristics of banking exclusion in Canada

The most recent figures show that between three and four per cent of Canadian adults over the age of 18 do not have a bank account of any kind (ACEF-Centre, 1996; Ekos, 1998). This figure is much higher among low earners (less than \$25,000CAD a year) at eight to ten per cent (Ekos, 1998; Morris and Phillips, 1999; Environics 2000). It also appears that many of the unbanked are Native Canadians (Buckland et al, 2003).

Reasons for banking exclusion

Reasons cited for the number of adults without a bank account include the difficulty and cost of supplying the right kind of personal identification, providers refusing to open an account for certain people, the requirement for minimum deposits, 'holds on funds' for people depositing government cheques into accounts with small balances, bank charges, and branch closures (Department of Finance, Canada, 1998; Ekos, 1998; Ramsay, 2000).

The underlying reasons for disengagement given above are not always the reasons stated by poor people when asked. In research interviews most of those that lacked an account said it was because they did not want or need one, or they disliked banks (Ekos, 1998). Indeed attitudinal and cultural factors were considered a major hurdle to the take-up of accounts by the Task Force on the Future of the Canadian Financial Services Sector (Department of Finance, Canada, 1998).

In 2002 the Department of Finance reported that there were over 8000 bank branches in Canada. However, branch closures are of particular concern with over 2,000 bank branches closed between 1990 and 2003(Power Financial Corporation, 2003). This is a particular problem in rural and low-income urban areas, for example Power Financial Corporation quote estimates indicating that 45 per cent of the bank branches in rural Canada have been closed (Financial Post 2000). The closures are especially problematic for the elderly (Department of Finance, Canada, 1998).

Some adults without access to regular banking facilities gravitate towards "alternative banking" facilities such as cheque-cashing firms, which have become more prevalent in areas that have lost bank branches. For example Money Mart, a cheque-cashing service targeting low-income Canadians, has added 85 units between 1999 and 2003(Power Financial Corporation, 2003). Typical fees for cashing a \$100CAD cheque are around \$5CAD (flat fees of \$2CAD plus 3% of face value) (Ekos, 1998; Morris and Phillips, 1999; Ramsay, 2001)

Policy responses to banking exclusion

In 1998 the Task Force on the Future of the Canadian Financial Services Sector published its report 'Change, Challenge, Opportunity'. The following year the Federal Government responded with a report⁴ setting out 57 reform measures including providing banking services to all adults and ensuring that these services are well promoted. Bill C-8 was enacted in June 2001⁵. The *Access to Basic Banking Services Regulations* took effect on September 30th 2003.

The Financial Consumer Agency of Canada (FCAC) is responsible for enforcing the above regulations, which attempt to widen access by making the rules for obtaining a basic personal bank account clear and straightforward. For example, a bank now can not refuse to open a basic personal account just because the applicant has no job, is or has been bankrupt or is not depositing money into the account. Importantly, a bank must also cash most Government of Canada cheques for non-customers at no charge. The issue of rural banking has also been addressed in the regulations. Banks must give four months notice of branch closures, and six months notice where they are the only branch for 10 kilometres, in order for communities to be consulted and make alternative arrangements.

Banks were given the opportunity to address the issue of the unbanked voluntarily before the introduction of regulations. Eight banks signed a Memorandum of Understanding (76) (MOU76) with the Government pledging to offer low-cost accounts to their customers. These accounts charge fees ranging from a monthly charge of \$2.95CAD to \$4.00CAD (the maximum allowed) with between 8 and 15 free transactions. The banks have recently renewed their commitment to this approach in an attempt to "ensure that all Canadians have access to affordable banking services" (FCAC, 2003a). A 2003 nationwide mystery shopping exercise has provided evidence about the compliance with these voluntary codes. The research indicated that information about low fee accounts was available in almost 85 per cent of the 1642 bank branches visited across Canada that had signed up to MOU76. Almost all banks visited (95 per cent) agreed to cash a cheque for free (FCAC, 2003b).

There have also been local attempts to provide banking facilities for disenfranchised communities, but as the following example indicates, success is far from guaranteed. In response to the closing of unprofitable branches in downtown East Vancouver the provincial government of British Columbia set up Four Corners Community Savings bank in 1994. It served 3500 customers, 95 per cent of whom were income assisted. (Times Colonist, 2003). This provision was, however, controversial because the financial support required to run Four Corners was not offered to other providers and the plan was not discussed fully with the local community, many of whom wanted to establish a credit union (Canadian Community Reinvestment Coalition, 1997). In December 2003 the Competition Minister in British Columbia announced that Four Corners would be closed

⁴ 'Reforming Canada's Financial services sector: a framework for the future'

⁵ 'An Act to establish the Financial Consumer Agency of Canada and to amend certain other Acts relating to financial institutions 2001' (77).

as the \$600,000CAD annual contribution required from the province was “not sustainable.”

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France

Overview of the French banking sector

Retail banking in France is provided through commercial banks, co-operative/mutual banks, and saving banks (caisses d'épargne) and regulated by the Bank of France. The financial services division of the Post Office also offers accounts, on which it can grant limited overdraft facilities on bank accounts but does not yet have fully-fledged credit institution status. A proposal to create a full-fledged postal bank was being debated in Parliament in the spring of 2004 and seems likely to be adopted.

Despite this diversity of provision, banking provision has become concentrated in a relatively small number of institutions and the number of banks has halved over the last twenty years. Seven banking groups dominate the French system: Crédit Agricole/Crédit Lyonnais, BNP-Paribas, Caisses d'Épargne, Société Générale, CCF-HSBC, Banques Populaires and Crédit Mutuel/CIC. The top ten banking groups now control more than 85 per cent of the total retail banking business in France.

The past two decades have seen substantial changes in the French banking system. The 1984 Banking Act initiated a process of re-regulation by placing all banks, whatever their status, under the same set of rules and effectively ended the traditional distinctions in the services provided by the different types of banks. Further restructuring occurred in the late 1990s, and resulted in extensive changes in ownership. In 1999, the savings banks assumed the status of co-operative banks and in 2002 mutual banks became members of the French Banking Association (Fédération Bancaire Française or FBF).

National tax exempt national savings schemes - "livrets A and bleus", delivered through the networks of savings banks, the Post Office and Crédit Mutuel still remain from the previous regulated era.

Overview of the main characteristics of banking exclusion in France

During the gradual transfer to paying salaries into bank accounts in the 1970s, banks competed for market share without much consideration for profitability. In 2002, just 1 per cent of households had a no bank account of any kind, although the less well-off clients were heavily concentrated in savings banks and La Poste (BIS 2003). Figures from the Ministry of Finances show that about 4 per cent of adults in France did not have a transaction account in 2000 (Bloch et al 2000); the Eurobaromètre survey put it a little lower at 3 per cent (Eurobarometer 2000).

Despite this widespread access to banking, a survey undertaken by CREDOC for the Bank of France found a substantial number of people on low incomes who were 'under-banked'. Only 54 per cent of those living on benefits had a cheque book and just 40 per cent had a bank card – compared with 96 per cent and 79 per cent in the total population (Daniel and Simon, 2001). Not having a cheque book and a banker's card in France

constitutes a stigma. Conversely, 45 per cent of those on social security had cash withdrawal cards compared with 25 per cent for the whole population. Poor people were also more likely to use branch-based services - 44 per cent visited their bank or post office branch several times a month compared with 32 per cent for the whole population. It should be noted in this context that France is the only European country in which cash is not the preferred means of payment (18 per cent versus 49 per cent for the EU); cheques remain the main method of payment (40 per cent compared with an EU average of 10 per cent) (Eurobarometer 2000).

Cheques are the preferred method of payment in France because banks abide by the “ni-ni” rule according to which transaction accounts may not be remunerated, nor can any charges be made for cheques. However, a major shock is expected to the current reliance on cheques as a result of an imminent European Court of Justice ruling. This is likely to make the non-remuneration of transaction accounts illegal for competitive reasons, in which case not charging of cheques will become unsustainable for French banks. The European Court judgement, together with the change in status of the French Post Office, will lead to a major shake-up of the French payment systems and will impact on access to basic banking services.

Policy responses to banking exclusion

There are a number of reasons why account-holding in France is so high.

The payment of salaries into accounts, prompted by the Government and implemented through national industry labour agreements, undoubtedly led to a greater involvement with financial services.

Secondly, savings banks and banking services offered by La Poste have traditionally been used by a wide cross-section of the public and are used extensively by people on low incomes. Since their transformation into co-operative undertakings through the 25th June 1999 law, savings banks have been formally entrusted with a duty to fight exclusion, to protect savings, to finance social housing through Livret A and to create employment. The Livret A is the only financial product in France to have a pass book. It is also free, does not have a limit on over-the-counter withdrawals, and is tax-free. Almost every French resident holds a Livret A or Livret Bleu (similar but provided by Crédit Mutuel), but it is within La Poste clientele, where the poorest customers are concentrated, that the Livret comes into its own. According to research carried out in 1997, 36 per cent of family allowances, 20 per cent of retirement pensions and 12 per cent of unemployment benefits are paid to this type of account (Larcher, 1997). Even homeless people can open such an account. About 6 millions livrets A with La Poste have less than £100 in their balance.

Thirdly, the 1984 Banking Act⁶ made access to a bank account a legal right (article 58), so that people refused one can apply to the Bank of France, which will nominate an institution to provide the bank account. This right was limited to opening a bank account

⁶ Loi bancaire n.84-46 du 24.1984

and access to cash transactions at the counter; it did not include cashless payments such as cheques. In 2000, only 8,500 people used this procedure, which is almost certainly only a minority of those eligible to do so. Few people who are refused an account are aware of their right, not to mention how to exercise it, and most would naturally turn to using a Livret A or an account with La Poste instead.

In 1992, French banks signed a charter committing themselves to opening a bank account at an affordable cost with related payment facilities – cash card, free access to cash machine network, distance payment facilities, bank statements, the availability of a banking identity statement and cheques, the number of which can be negotiated with the customer.

The law against exclusion (29th July 1998)⁷ specified that the right to a bank account was to be accompanied by relevant payment instruments (article 137). The right to a transaction account was extended to those who had been banned from using banking services because of past payment incidents – most commonly bounced cheques, although this also includes cases of fraud. In addition, it allowed those who had written a bounced cheque an extra month to correct the matter before the bank could apply a ban on further cheque writing. The law left it to an implementing decree to define the scope, the content and the working of the basic banking services.

In 1999, a consumer association - La Confederation de la Consommation du Logement et du Cadre de Vie or CLCV, carried out the first mystery shopping survey on the conditions which banks apply to low income consumers for the opening of a bank account. Although responses even between branches of the same bank differed, the survey revealed that branch staff never referred to the charter even if the question was raised directly. In most cases, the bank employees genuinely did not know about the charter: no information or training has taken place as there is no formal duty on the bank to inform the customer. The survey underlines a number of practices contrary to the spirit and the letter of the banking charter: demands on minimum deposit on the accounts, bundling practices, unreasonable charging of cash withdrawal cards and, above all, turning down of account opening request in six per cent of the cases (La Confederation de la Consommation du Logement et du Cadre de Vie, 1999).

More recently a consultative committee was formed to discuss banking charges in view of the unavoidable ending to the ‘ni-ni’ agreement. The remit of the committee was to arrive at a consensual solution which would also protect vulnerable individuals and ensure their right to a bank account. As compensation to the ending of the ‘ni-ni’, the powerful consumer associations wanted all bank operations to come within the consumer code. They were also opposed to a ‘stigmatising’ basic banking services, which would be applied only to the poor through a specific product and/or a specific service. The banks turned down these suggestions, arguing that a universal service obligation was an impeachment of their contractual freedom. In the absence of an agreement, the government issued a decree defining the content and scope of the basic banking service

⁷ Loi n.98-657 du 29.7.98 d’orientation relative à la lutte contre les exclusions

(decree n 2001-45 of 17.1.2001)⁸, which is limited to those consumers having recourse to the Bank of France, following the refusal of an account. This basic banking service is offered for free by any designated banking establishment or La Poste. The facilities it offers include: cash withdrawals; two cheques per month; either a real-time debit card or an ATM cash card that does not permit overdrawing; direct debits, and credit transfer facilities.

Finally, the Murcef law of 11th December 2001⁹ regulated the bundling of financial services products as well as bank charges to people on low-income individuals who are banned from writing cheques. In addition, it imposed the principle of price transparency in banking, through contracts between banks and their customers for the management of accounts. It also required a mediation function (ombudsman) to be set up within each bank and at industry level. Consumer satisfaction with transactional banking has significantly improved as a result.

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⁸ Décret n.2001-45 du 17.1.2001 pris en application de la loi n.98-657

⁹ Loi (Murcef) n.2001-1168 portant mesures urgentes de réforme à caractère économique et financier du 11.12.01. This law aims at limiting unfair terms between banks and clients in bank account contracts and establishes banking ombudsmen

Great Britain

Overview of the British banking sector

Retail banking in Britain is dominated by five large banks, four of which are British in origin - Barclays Bank, Royal Bank of Scotland, Lloyds TSB, HBoS - and the fifth, HSBC is an international bank which took over the Midland Bank. Banking in the UK has been subject to a number of mergers and take-overs creating very large organisations that are global players.

Re-regulation of financial services in the 1980s broke down the traditional distinction between banks and building societies. As a consequence of this many building societies moved into retail banking, having previously concentrated on home loans and savings products. Since that time, all but one of the large national building societies (Nationwide) have ended their mutual status and become public companies, traded on the London Stock Exchange. One of these – the Halifax –merged with the Bank of Scotland to form HBoS. Others such as the former Abbey National and Alliance and Leicester building societies are among the larger banks in the UK. Other than Nationwide, the remaining (mutual) building societies are all local in their coverage.

Until 1990, banking services were also offered by the Post Office through the state-owned Girobank, which was originally set up as a part of the European network of 'peoples banks' in 1968. This was sold to Alliance and Leicester and has now ceased to operate as a separate bank.

Banking supervision and regulation

Prudential supervision of banks is the responsibility of the Financial Services Authority (FSA), having been transferred from the Bank of England (the central bank). The FSA, which was created in 1998, supervises and/or regulates most of the financial services sector in the UK. Banking, however, differs from other financial service sectors under the FSA in that it retains a system of self-regulation of conduct of business under the Banking Code. Almost all banks and credit card companies are signatories to the Code.

A wide-ranging review of such codes of practice was set up by HM Treasury in the form of a Banking Services Consumer Codes Review Group. This concluded that the Banking Code worked well and offered consumers protection that could not be achieved through formal regulation (Banking Services Consumer Codes Review Group, 2001). The Banking Code, and the accompanying Guidance for subscribers, is subject to independent review every two years (the current review is in progress). Code compliance is monitored by the independent Banking Code Standards Board.

Overview of the main characteristics of banking exclusion in Britain

The annual *Family Resources Survey* shows that, in 2002-3, 12 per cent of households (and 14 per cent of individuals aged 16 or over) lacked a current (transactional) account with either a bank or building society. Rather fewer (8 per cent of households; 8 per cent of individuals) lacked an account of any kind - that is they had neither a current nor savings or deposit account. The proportion without a current account would appear to have fallen in recent years. In 2000-1 the proportion of households without an account stood at 14 per cent, having remained at this level for a number of years¹⁰.

There is a very strong link between current account-holding and incomes. So, individuals and households lacking a current account are drawn quite disproportionately from those with the lowest incomes, particularly if they are not working (Kempson and Whyley 2001; Kempson and Whyley, 1998; Office of Fair Trading 1999b).

Women are much less likely to have an account in their own name than men, but this is largely explained by their lower incomes and their personal circumstances, not by gender alone. Households headed by women (lone parents and single pensioners in particular) have a low incidence of account-holding (Kempson and Whyley 2001; Kempson, 1994, Office of Fair Trading, 1999a; Office of Fair Trading 1999b).

African Caribbean, Pakistani and Bangladeshi people are disproportionately likely to have no account. And account holding among Pakistani and Bangladeshi women is incredibly low (Kempson and Whyley 2001; Kempson and Whyley, 1998; Office of Fair Trading 1999b).

Account-holding is lowest among people aged under 20 and over 80, but for rather different reasons. In the main, young people have not got round to opening an account, while the very elderly are part of the 'cash-only' generation, who have never had an account (Kempson and Whyley 2001; Kempson and Whyley, 1998).

There are also important differences by housing tenure, with social tenants being much more likely to lack an account than owner occupiers. Finally, there are clear geographical variations in account-holding. Account-holding is lowest in inner city areas and there are strong links to the deprivation of the area in which people live. In other words, people who lack a bank account are fairly concentrated geographically (Kempson and Whyley 2001; Kempson and Whyley, 1998).

Reasons for banking exclusion

Research has identified a number of reasons why people do not have a current account.

Few seem to lack an account because they have been refused one following credit scoring (Kempson and Whyley 1998; Office of Fair Trading 1999a) although there is evidence that people who believe they might be turned do not even bother applying (Burrows, 1999; Collard et al, 2001). There is also clear evidence that legislation to prevent the use

¹⁰ This fall is greater than the margin of error of plus or minus 0.4%

of bank accounts for ‘money laundering’ has had the unintended effect of denying access to banking as many people on low incomes lack the forms of identity (a passport and a driving licence) that are universally accepted by banks and building societies (Burrows, 1999; Collard et al, 2001).

The main explanation seems to be that people on low incomes consider both current accounts and banks inappropriate to people in their circumstances. Unlike most other developed countries, routine transactional banking in Britain is free-of-charge provided the account remains in credit. However, all conventional current accounts in Britain can be overdrawn, even if they do not have an authorised overdraft facility, and the charges of going into unauthorised overdraft can be high, especially when considered against the income of someone who does not work. It is this fear that has, traditionally, deterred many on low incomes from using a current account (see for example, Collard et al, 2001; Kempson and Whyley, 2001; Kempson and Whyley 1999).

There is also widespread mistrust of financial services companies among people who are on the margins of financial services. People living on low incomes often hold a strong belief British banks are not interested in people like them; in contrast they feel more comfortable using building societies and especially post offices (Collard et al, 2001; Kempson and Jones, 2000; Kempson and Whyley 2001; Kempson and Whyley, 1999).

There is considerable evidence that bank branch provision is poorest in low-income communities. Although lack of a nearby branch does not seem to play a direct part in people’s decisions not to have a bank account, it may well fuel their belief that banks are not for them. There is little doubt that the types of people who are especially at risk of financial exclusion – lone parents, people unable to work through long-term sickness or disability, and very elderly people (aged over 80) on low incomes – are also the ones who face most difficulties getting to branch if it is distant. Similarly, they are the ones who are most resistant to automated banking, such as cash machines or ATMs (Kempson and Whyley, 2001; Kempson and Jones, 2000).

Finally, research shows that people whose main source of income is social security benefits or the basic state pension often opt for a cash budget and avoid the use of a bank account because they have, until recently, had the choice not to have this income paid directly into a bank account (Kempson and Whyley, 1998; Kempson and Whyley, 1999).

Policy responses to banking exclusion

The main initiative to bring people into banking has been the development of ‘basic bank accounts’. These are card-based accounts, with no cheque book, where all transactions are checked before acceptance so that the account cannot be overdrawn. Such accounts were designed following research to explore the reasons why people were unbanked (Kempson and Whyley 1998; Kempson and Whyley 1999) and promoted by the HM Treasury *Policy Action Team 14 on Access to Financial Services* (HM Treasury 1999). For the most part, banks developed these new accounts voluntarily, although the

Chancellor of the Exchequer imposed a deadline of October 2001 by which all banks should provide such an account for their customers. All banks met this deadline and many building societies also offer basic bank account. There is, however, considerable evidence that banks are not always drawing these accounts to the attention of people who might benefit from them, despite provisions in the Banking Code to this effect (Banking Code Standards Board, 2002; Financial Services Consumer Panel, 2002; National Association of Citizens Advice Bureaux 2002). The revised Banking Code, due for publication in March 2005 will contain a strengthened commitment to tell customers about basic bank accounts if they are appropriate to their circumstances.

Access to basic bank accounts does, however, seem to be improving (Banking Code Standards Board, 2003) and their impact can already be seen in statistics on current account-holding. As we note above, the *Family Resources Survey* shows a statistically significant fall in the proportion of households lacking a current account between 2000-01 and 2002-03 - the period during which basic bank accounts were being introduced. Particularly large falls occurred among unemployed people (10 per cent), single female pensioners (6 per cent) lone parents (4 per cent) and households with only a part-time worker (4 per cent), all of which were statistically significant.

The second initiative to promote integration into banking services has been the decision to pay all social security benefits and state pensions into a bank account. This transfer to automated credit transfer began in 2003 and will be completed in two years. In preparation for this transfer, the Government held discussions with banks and the Post Office as a result of which basic bank account-holders with any of the 16 main banks can now use their local post office to undertake routine banking transactions. In addition, the Post Office has, itself, developed a very limited-function account. Known as the Post Office card Account, this is a card-based account into which state benefits and pensions (but no other source of income) can be paid. Users can then draw money out of the account as and when they need it. In other words, it operates like an 'electronic purse' or stored value card. Early indications are that take-up of these Post Office accounts by benefit recipients has been relatively high.

In the 2004 Budget Report, the Government has said that it will work in partnership with both the financial services sector and community bodies to achieve 'dramatic reductions' in the numbers of people without a current account and without an account of any kind (HM Treasury, 2004).

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United States

Overview of the US banking sector

Compared with the other countries covered in detail in this report, banking provision in the United States is more fragmented with many thousands of small local banks rather than a few clear market leaders at a national level. Moreover, commercial banks, savings banks, savings and loans, and credit unions all provide transaction and savings accounts to the public. There have however been two important and inter-linked trends in the American banking sector in recent years: the development of inter-state banking and a decline in the number of independent banking organisations. In 1994 the Riegle-Neal Interstate Banking and Branching Efficiency Act permitted banks to operate across state borders through merger, thus moving away from the tradition of local banks. Through mergers and acquisitions the number of banks in the United States fell from 14,000 in 1985 to about 8,300 at the end of 2000. The number of independent banking organisations fell from about 11,000 to less than 7,000 (Bassett and Brady, 2001). Yet despite this restructuring, in 2002, Citicorp, JP Morgan Chase, Bank of America, Wachovia and Wells Fargo, the five largest companies, accounted for just 35 per cent of the total market value (Euromonitor, 2003).

Banking supervision and regulation

Banking supervision is complex, with the type of charter held by a bank determining its primary supervisor. For nationally chartered banks the primary supervisor is the Office of the Comptroller of the Currency. State chartered banks that are members of the Federal Reserve System are supervised by the Federal Reserve and their state; those not members of the federal Reserve System are supervised by the Federal Deposit Insurance Corporation and their state. In addition The Office of Thrift Supervision¹¹ (OTS) is the primary regulator of all federally chartered and many state-chartered thrift institutions, which include savings banks and savings and loan associations. OTS was established as a bureau of the U.S. Department of the Treasury on August 9, 1989, and has four regional offices located in Jersey City, Atlanta, Dallas, and San Francisco. OTS is funded by assessments and fees levied on the institutions it regulates.

Overview of the main characteristics of banking exclusion in the United States

In 2001, 9.1 per cent of American households were without transaction accounts, a drop of only half a per cent since data was collected in 1998 (Aizcorbe et al, 2003). Of the families in the lowest income quintile in 2001 only 62.5 per cent had a transaction account (Federal Reserve, 2001). Immigrants are also more likely to lack a basic account; 54 per cent of Mexican immigrants are unbanked and overall around 32 per cent of foreign born households do not have access to mainstream banking (Federal Reserve Bank of Chicago, 2004). Most unbanked adults are under the age of 35, but adults over 75 with low incomes

¹¹ See <http://www.ots.treas.gov/>

also make up a significant proportion of the American unbanked (Aizcorbe et al, 2003; Weissbourd, 2002).

Reasons for banking exclusion

There seem to be two main explanations for the low penetration of accounts in the United States: problems of access and charges.

Access to transaction accounts can be difficult for consumers without a good credit history. The most widely used credit database is ChexSystem, and an entry on this system is seen by many banks as sufficient reason to refuse to open an account (Belsky and Calder, 2004). According to credit consultants, 9 million people in America are listed on ChexSystems, a clearing house used to identify those customers with banking problems in the past. It has records of 19 million accounts closed “with cause”. These people have to wait five years before banks using the ChexSystem will consider them as customers and an estimated 85 per cent of banks use the system¹².

The cost of banking prevents people with very low incomes from opening an account, as even apparently low cost accounts can have prohibitively high additional costs such as unauthorised overdrafts or cheque return fees (Hogarth and O’Donnell, 1999).

People dissuaded from using banks often turn to alternative providers for essential services such as cashing pay or benefit cheques. Dunham (2002) found that 73 per cent of the unbanked incurred some costs cashing cheques and buying money orders. Significantly, however, 83 per cent of the unbanked paid less per year on these services than the revenues a bank would require to provide them with a basic account (estimated at \$100 per year). They were able to cash cheques in banks or stores at very little cost. Indeed, Dunham’s report concluded that many of the unbanked may have been choosing to use other providers as a means of economising because of high account costs, rather than through lack of choice per se.

For those who are not able to access low cost alternatives to banks, activities such as cashing pay cheques require the payment of considerable fees to an alternative provider, such as a grocery store or commercial cheque-cashing outlets that typically charge two to four per cent of the face value to cash pay cheques and government support cheques. A lower-income household, receiving \$16,000 a year and regularly using a fee-charging cheque casher might easily spend as much as \$400 on such services over the course of a year. The US Treasury secretary Lawrence Summers reported in 2000 that the lifetime cost of not having a bank account could be in excess of £15,000 per household (recorded on Treasury website).

Policy responses to banking exclusion

In some countries, consumers find the time period between paying cheques into a bank and being able to draw on that money intolerable. In the US there has been legislation in

¹²See <http://www.carreonandassociates.com/chexsystems.htm>

place since 1987 to prevent banks holding cheques for extended periods. The Expedited Funds Availability Act¹³ (EFA) mandates that funds deposited into a customer's account are made available according to "specified time schedules" which in most instances is the next day (National Consumer Resource Center, 2001).

In 1996, the federal government enacted legislation (Electronic Funds Transfer, 1999) requiring that all federal transfer payments be made electronically by 1999. This initiative began as a cost cutting exercise rather than a way of involving benefit recipients in the banking system – indeed the statistics on account-holding quoted above show that it has apparently done little to bring people into banking. In 1999 the Department of Treasury, realising that some 20 per cent of recipients were unbanked, began to urge federally insured depository institutions to create Electronic Transfer Accounts (ETAs). These accounts must accept electronic transfers from the federal government, have no minimum balance requirement, and permit the account owner to withdraw the funds using an ATM card. The federal government pays banks a one-time setup subsidy of \$12.60 for every account they open¹⁴. Consumers are asked to pay minimal fees of \$3 per month and risk a maximum overdraft fee of \$10, making this account appear to be very similar to a basic bank account. Unfortunately regulation prevents banks from including some essential banking features such as a cheque book or direct debit payments. (Hogarth and O'Donnell, 1999).

A similar scheme to the ETA has been initiated by employers, again in reaction to the high costs of providing paper cheques. An estimated four million payroll cheques are lost or stolen every year, each costing employers an additional \$8 to \$10 a cheque to replace. The new employer scheme deposits pay into an account and provides payroll cards, which allow employees to withdraw funds from cash-points. By the end of 2002 one million families were using payroll cards, and the number is expected to grow. Unfortunately, whilst some cards are backed by various banks and big name companies such as Visa and MasterCard, they are not a full substitute for the full range of services offered by a bank. For example, credit on payroll cards does not earn interest, and they don't have the guaranteed legal protections of debit or credit cards (Smith, 2004).

In 2002, President Clinton proposed that the federal government enact legislation encouraging banks to create "First Accounts" with very low minimum balance requirements and low fees, for people without deposit accounts. By the end of 2002 just seven states had turned the idea of low cost banking into law; the federal government had not. Although bank trade associations fought against the proposed laws, especially at the federal level, they called on banks to offer such accounts voluntarily. The majority of banks claim that they do offer them, but research in New York suggests that they are not being marketed effectively '*... NYPIRG has done surveys where we've found that about one in three of the account representatives in the banks failed to describe the account or tell us about accounts that were available even when we asked point blank.*' (Briers 2000).

¹³ See <http://www.fdic.gov/regulations/laws/rules/6500-3240.html>

¹⁴ See *Finance on the fringe: America's check cashers don't exploit the poor; they serve them* http://www.findarticles.com/cf_dls/m1568/11_33/84246682/p8/article.jhtml?term=

The Community Reinvestment Act (CRA), introduced by the federal government is often cited as a major initiative to combat the issue of unbanked households. In fact, its aim has always been to improve access to credit, although it does have some impact on the availability of bank branches. The CRA is intended to encourage banks to meet the credit needs of lower income households, and incorporates a "service" test for banks based primarily on their efforts and effectiveness at making mortgage loans to lower-income households. The Joint Center for Housing Studies (2002) reported that the CRAs impact on rural areas is minimal, primarily because they tend to be served by small banks that are outside the scrutiny of the CRA process. More positively, however, they do find that lending to black and hispanic Americans is higher within CRA regulated lenders and that there has been a "crowding out" of lenders falling outside the regulatory powers of the CRA in lower income communities.

A further public policy measure seeks not to increase account ownership, but to reduce the cost of turning to alternatives. Advocates for the poor in many states have proposed legislation that would set ceilings on the fees that cheque-cashing outlets can charge. There is no federal law but as of 1999, 14 states had adopted fee ceilings, typically ranging from just over one per cent to three per cent for payroll and government cheques. In several cases the ceilings are higher than the free market rates so the ceilings are not binding.

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