

Government Use of the Payment Card System

Federal Reserve Bank of Philadelphia

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Consumer side: Three legged stool

- Education
- Access
- Consumer Protection

Behavioral Economics

- Information vs understanding
- Intention vs. behavior
- Predictable biases
 - Misperception
 - Misforecasting
 - Myopia
 - Decisional conflict
 - Mental accounting
 - Attention constraints
- Context & Institutions
 - Defaults
 - Behavior
 - Planning

- See Barr, Mullainathan & Shafir (2009)

Education core competencies

Core concept	Knowledge	Action/behavior
Earning	Gross versus net pay	Understand your paycheck.
	Benefits and taxes	Learn about potential benefits and taxes.
	Education is important	Invest in your future.
Spending	The difference between needs and wants	Develop a spending plan.
		Track spending habits.
		Live within your means.
		Understand the social and environmental impacts of your spending decisions.
Saving	Saved money grows	Start saving early.
		Pay yourself first.
	Know about transactional accounts (checking)	Understand and establish a relationship with the financial system.
	Know about financial assets (savings accounts, bonds, stocks, mutual funds).	Comparison shop.
	How to meet long-term goals and grow your wealth	Balance risk and return.
		Save for retirement, child's education, and other needs.
		Plan for long-term goals.
		Track savings and monitor what you own.
Borrowing	If you borrow now, you pay back more later. The cost of borrowing is based on how risky the lender thinks you are (credit score).	Avoid high cost borrowing, plan, understand, and shop around.
		Understand how information in your credit score affects borrowing.
		Plan and meet your payment obligations.
		Track borrowing habits.
		Analyze renting versus owning a home.

Treasury Federal Register release 2010

Core concept	Knowledge	Action/behavior
Protect	Act now to protect yourself from potential catastrophe later.	Choose appropriate insurance.
	Identity theft/fraud/scams	Build up an emergency fund.
		Shop around.
		Protect your identity.
		Avoid fraud and scams.
		Review your credit report.

Technology and Consumer Choice

| From Barr, Dokko & Feit (2011)

Table 4. Relative importance of purchase card attributes indicate that female, African American, unbanked respondents weigh lost card protection and monthly fees similarly in choosing purchase cards, while banked and higher-income, male respondents find monthly fees substantially more important than any other attribute.¹⁸

	Relative Attribute Importance		
	(1) female black \$20K income age 40 unbanked low-income tract	(2) female black \$20K income age 40 banked moderate-income tract	(3) male not black \$50K income age 40 banked moderate-income tract
Requirements	9%	6%	2%
Card Type	17%	8%	11%
Lost Card Protection	24%	19%	11%
Deposits	6%	13%	25%
Savings	7%	9%	3%
Bill Payment	6%	3%	3%
Get Cash	1%	4%	2%
Cash Access Fees	7%	2%	6%
Monthly Fees	23%	35%	36%

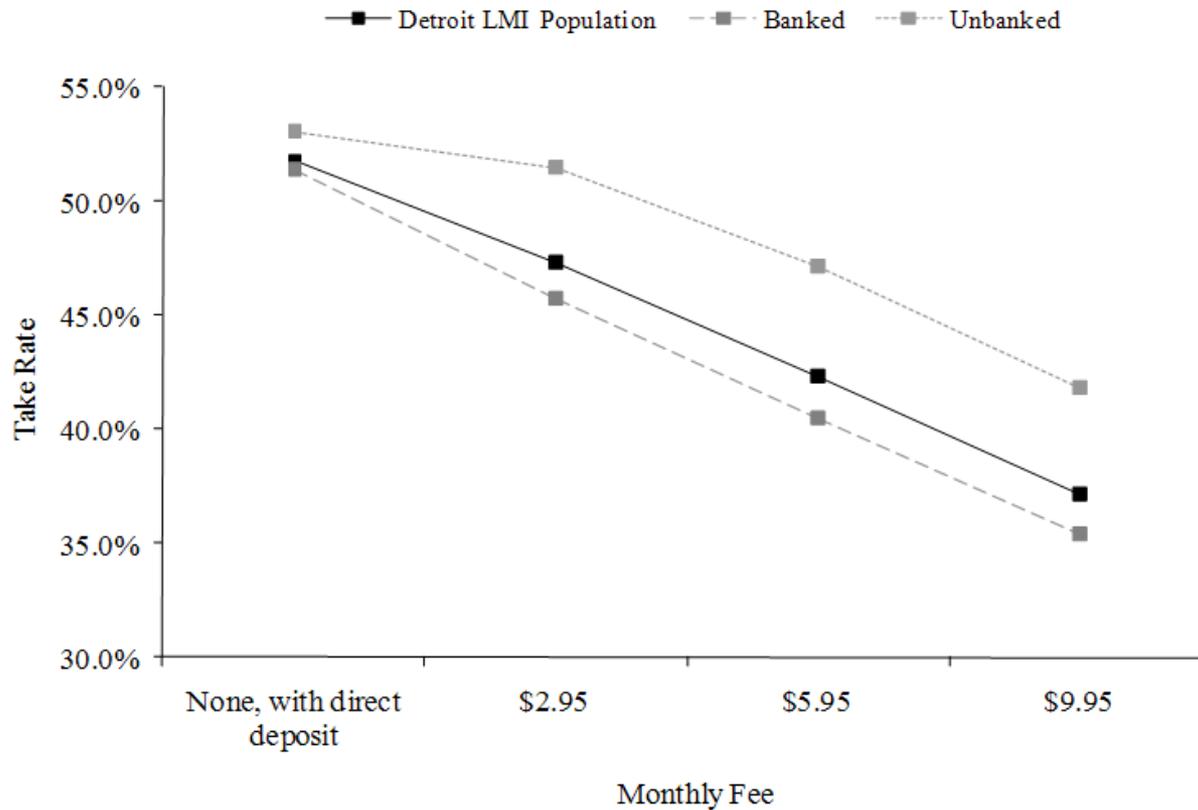
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Table 5. Alternative Payment Card Designs and Take-Rates

Ideal Design for Detroit LMI Population				
	(1) Detroit LMI Population	(2) Detroit LMI Unbanked	(3) Detroit LMI Banked	
Purchase Card Attributes	Requirements	No credit check	No credit check	No credit check
	Card Type	Debit (ATM) Card	Debit (ATM) Card	MasterCard Prepaid Debit Card
	Lost Card Protection	Federal protection	Federal protection	Federal protection
	Deposits	Direct Deposit	Direct Deposit	Direct Deposit
	Savings	Automatic savings plan	Automatic savings plan	Automatic savings plan
	Bill Payment	Automatic bill payment available	Pay bills in person with card	Automatic bill payment available
	Get Cash	Get cash at participating ATMs and with purchases at stores	Get cash at any ATM, from bank tellers and with purchases at stores	Get cash at participating ATMs and with purchases at stores
	Cash Access Fees	\$1.50 fee for each ATM cash withdrawal	\$1.50 fee for each ATM cash withdrawal	\$1.50 fee for each ATM cash withdrawal
	Monthly Fees	No monthly fees with Direct Deposit of your paycheck	No monthly fees with Direct Deposit of your paycheck	No monthly fees with Direct Deposit of your paycheck
	Estimated Take-Rates	Detroit LMI Population	51.8%	50.4%
Residents of Low Income Census Tracts (stratum 5)		52.8%	51.4%	50.3%
Residents of Moderate Income Census Tracts (stratum 6)		50.8%	49.2%	52.2%
Banked Detroit LMI Population		51.4%	49.2%	52.5%
Unbanked Detroit LMI Population		53.0%	53.3%	47.8%

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Figure 2. Response of take-rates to monthly fees (banked v. unbanked).



Government initiatives

- Go Direct
- Direct Express
- Garnishment rule; prepaid card rule; EFT rule
- State benefit and program cards
- Treasury pilot for tax-time accounts
- FDIC pilot for safe & affordable accounts
- Bank on USA
- CFPB
- Potential impact of Durbin amendment

Behaviorally Informed Regulation

See Barr, Mullainathan & Shafir (2009)

Table 1. The Firm and the Individual

Behavioral Fallibility	Market neutral and/or wants to overcome consumer fallibility	Market exploits consumer fallibility
Consumers misunderstand compounding	Consumers misunderstand compounding in <i>savings</i> → Banks would like to <i>reduce</i> this to increase savings base	Consumers misunderstand compounding in <i>borrowing</i> → Banks would like to <i>exploit</i> this to increase borrowing
Consumers procrastinate	Consumers procrastinate in signing up for EITC → Tax filing companies would like to <i>reduce</i> this so as to increase number of customers	Consumers procrastinate in returning rebates → Retailers would like to <i>exploit</i> this to increase revenues

Behaviorally Informed Regulation

Table 3. Behaviorally Informed Regulation

	Market neutral and/or wants to overcome consumer fallibility	Market exploits consumer fallibility
Rules	<p>Public education on saving</p> <p>Direct deposit/auto-save</p> <p>Licensing</p>	<p>Sticky defaults (opt-out mortgage or credit card)</p> <p>Information <u>debiasing</u> (payoff time and cost for credit cards)</p>
Scoring	<p>Tax incentives for savings vehicles</p> <p>Direct Deposit Tax Refund Accounts</p>	<p>Ex post liability standard for truth in lending</p> <p>Broker duty of care and changing compensation practices (Yield Spread Premiums)</p>

Behaviorally Informed Regulation

- Dodd-Frank Act
 - Mortgage broker regulation: YSPs, ability to pay, ban on steering, required registration
 - Enhanced disclosures, escrow requirements
- CARD Act
 - Debiasing re: fees, minimum payments
 - Enhanced disclosures
 - Opt-in for over-limit transactions
 - Bans on double-cycle billing, late fee traps
- Role of CFPB

Policies to consider

Automaticity

Tax refund accounts

State program enhancements, transitions to work,
saving

Financial stability cards

Consumer protections

Mobile payments infrastructure, rules, stds

Smart disclosure, financial capability

Usage issues: overdraft, atm v pos, call centers

Internalize payments costs and benefits

Conclusion

- Three Legged Stool
 - Education
 - Access
 - Consumer Protection
- Behavioral insights
- Technology
- Innovation
- Government policy