

# Alternatives to Alternative Financial Services

By: Austin Wendling  
and Crispin Alemnka

The average unbanked consumer, which is over 7% of the population in the United States, faces annual fees of \$198.83 for check cashing and money order services charged by alternative financial services. The aim of this research project is to identify the various ways consumers can save money by avoiding alternative financial services, and instead use other financial products that are more beneficial. The research team will identify the various ways consumers can save money by comparing the costs of alternative financial services and the cheaper services provided by banks and personal loan companies. The team will also physically map out low- to moderate-income communities and determine how alternative financial services draw the customers in by concentrating their locations around these specific communities.

*Alternative financial services* is a term used to describe the array of financial services offered by providers that operate outside of federally-insured banks. Some products that these services provide include check-cashing outlets, money transmitters, car title lenders, payday loan stores, pawn shops, refund anticipation loans, and rent-to-own stores. Financial Service Centers of America (FiSCA) is the national trade association that represents nonbank financial service centers, which states that more than 13,000 nonbank financial service companies operate nationwide. FiSCA estimates that financial service centers process more than 200 million checks per year with a face value of \$27.6 billion per year. Amscot and Ace Cash Express, with about 1,700 stores each, are the largest check-cashing companies. While these alternative financial service providers offer convenient services and easy access to cash, their services often carry high costs, limiting a low-income family's ability to accumulate assets and establish a credit history.

Alternative financial services are mostly set up in low-income communities, usually with high traffic and a concentration of payday, title loan, and check cashing outlets so customers often feel like they have more options. Also, financial alternatives draw in consumers by airing radio ads. By locating these businesses within walking distance of low- to moderate-income (LMI) communities, the availability to the majority of their customers increases exponentially. Along with the vital location of business, there are certain factors that explain why people use products from these alternative financial services. These factors include, but are not limited to: they are not bound by the requirement for an existing banking relationship; 25% of

consumers distrust products with hidden rates/fees; these services are readily accessible and flexible in their operating hours; and they provide loans and various products to those with poor or no credit history. These services also place their locations in close relation to bus stops.

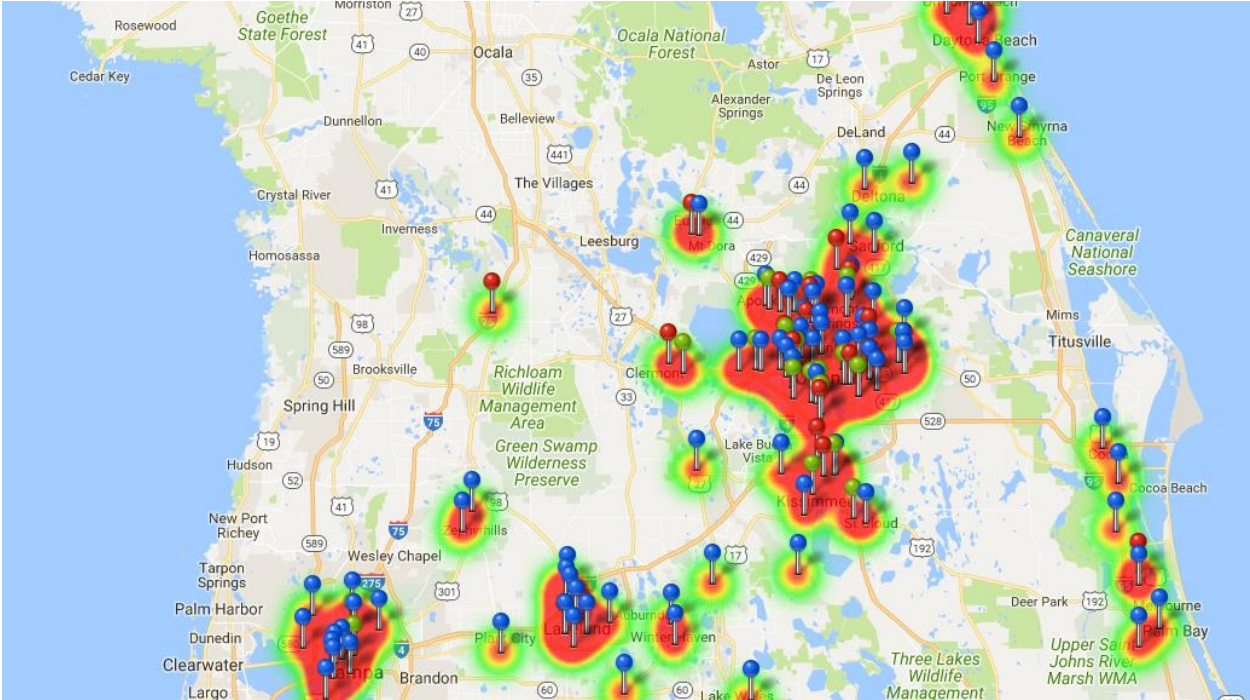
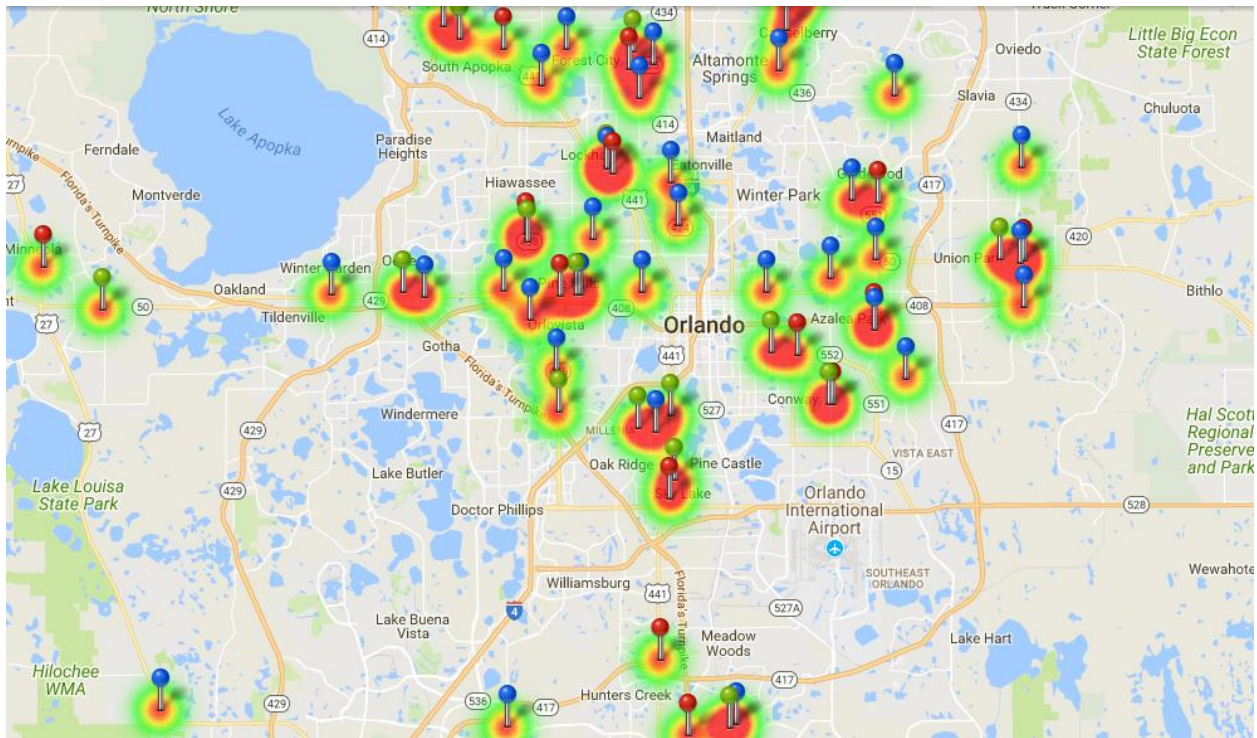


Figure 1: This heat map visually represents and reinforces the technique that alterative financial services concentrate their locations around high traffic areas and big cities. The blue markers indicate all of the Amscot locations throughout Central Florida, the green markers indicate the Ace Cash Express locations, and the red markers indicate the Advance America locations. You can clearly see that the majority of all three companies' locations are centered near larger metropolitan areas such as Orlando, Tampa and Lakeland.



*Figure 2: This image is a closer look that only shows Orlando, not all of Central Florida. It is clear to see that there is a much higher concentration of alternative financial services around Pine Hills and Oak Ridge as compared to Windermere and Doctor Phillips. This is not a coincidence, as both Pine Hills and Oak Ridge are considered LMI communities.*

People often tend to prefer using these alternative financial services for various reasons, such as the lack of trust people may have with their money in a bank. People are often misled by false advertising such as “Free money orders” and even by attractive marketing strategies such as TV commercials. Alternative financial services could also be more convenient for most people since they are located “right around the corner.” This would be more appealing to a consumer rather than driving to the bank or credit union, which may be further in distance from where they reside. One of the most prominent reasons why individuals use alternative financial services deals with their credit score. Because these companies do not check an individual’s credit history or require a certain credit score, someone with a low score or no credit history at all can still qualify for the same short-term loans as everyone else who uses these services. Many individuals need to wake up and realize that these alternative financial services are not as kind as they seem. Even with

great customer service and easy accessibility, they are taking advantage of LMI (low- to moderate-income) families because they're not informed on how these companies truly operate and function.

Below are the various services and fees that alternative financial services provide:

#### Check Cashing

- These services charge a per-check fee. Checks include payroll, personal, and government checks.
- Fees are usually 2% to 3% of check amount for payroll and government checks, and as high as 15% for personal checks.

#### Payday Lender

- These services offer small cash advances, usually between \$100 and \$300 with a term of usually 2 weeks.
- A bank account, steady job, and no history of writing bad checks are required since payday loans are originated with a personal check as collateral.
- The fee could be 15% to 17% for a two-week loan.
- If the loan is rolled over, there can be an effective APR of 400% or more.

#### Pawnshop

- A loan is issued with pledged collateral.
- The average loan is \$70, which represents roughly 50% of the collateral resale value.
- Average monthly fee is 1.5% to 30%, which is a 18% to 360% APR.

#### Rent-to-Own Shops

- Consumer goods are provided through installment payments.
- Effective prices are 2 to 3 times retail price.

### Auto Title Lender

- Single-payment loans are provided, usually with 30-day terms secured by an auto title.
- Typical loans are for 25% of the collateral value.
- Interest rates are 1.5% to 25% monthly, which is 18 to 300% APR.

### Money Order

- A paper document, similar to a check, which is used for making payments.
- Checks at a bank are free for an account holder.
- Retail locations charge \$1.00 to \$5.00 per money order, while financial institutions will charge up to \$10.00.

### Buy-Here-Pay-Here Car Lots

- Dealerships extend credit to consumers with little to no credit history in order to purchase a car.
- Interest rates tend to be between 20% and 30%.

Along with nonbank financial companies, some well-known companies are also offering these alternative financial products. For example, PayPal is partnering with other bank partners behind the scenes to offer debit cards connected to their PayPal accounts. PayPal is also adding a new feature for consumers to have the ability to direct deposit checks and other services. PayPal profits by charging fees in their banking service such as ATM withdraw fees, and 1% of any check deposited via photo from your mobile smartphone. PayPal is targeting younger consumers, including millennials, because of the appeal to the mobile apps in which these services use.

Florida House Bill 857, approved in 2018 and effective in 2019, was a bill to lower restrictions on deferred presentment transactions (pay-day loans). Amscot and Advance America reached out to influential members and leaders in LMI socioeconomic areas all over Florida in order to entice them to lobby in support for the bill. The majority of these leaders were leaders in various churches, such as

pastors. These two alternative financial companies enticed them by giving these churches huge sums of money in the form of donations. After gaining support, Amscot and Advance America flew these church leaders up to Tallahassee via first class. After all of the lobbying that took place, only 9 out of 115 legislative officials voted against the bill. This demonstrates and exemplifies the dirty and nasty strategies these companies use in order promote the alternative financial services industry.

After taking a look at the various products that alternative financial services offer, consider facts and statistics about alternative services that banks, credit unions, and personal loan companies are currently offering. Account holders at banks and credit unions are able to acquire free checks, which are essentially what money orders are, except without the added fee. Interest rates on loans can vary from 3.00% up to 13.00%, depending on the client's credit score, the term, and the current economic condition. There are certain banks and credit unions that offer small dollar loans for those in a financial crisis with a poor credit score. Research concludes that there are approximately 224 banks and 21 credit unions across the state that offer loans for the same amount as alternative financial services.

The Federal Deposit Insurance Corporation (FDIC) developed a two-year small dollar loan pilot program to encourage individuals to acquire relationships with traditional banks. The qualifications for these small dollar loans include: less than \$2,500.00, an APR of 36.00% or less, and a 90-day term or longer.

Personal loan companies also have services that can take the place of small dollar loans. Oportun Loans offers loans with a principal of \$300-\$800 and a term of 6-24 months. The Director of Public Affairs at Oportun, Alejandra Velazquez, informed the researchers that most banks do not offer loans in this space because they do not find it profitable. These personal loan companies use formulas to determine whether someone is credit-worthy even when they don't have a credit score. More financial companies should be encouraged to develop programs such as the FDIC did and offer smaller loans to those who cannot afford the time and money that a larger loan may require.

Because these alternative financial services are so prominent and available in LMI areas, more effective solutions are needed to help community members avoid using these services. The simplest, yet best

solution to this is simply to educate individuals about the techniques these services use and exactly what fees and rates they are charging. On the assumption that people want to save money and use money in the most efficient way possible, if the general public acquires even a basic knowledge of these services, then people will be more inclined to think about the end result when using these services. This end result consumers can avoid would be paying up to 300% interest rates, having exponentially higher fees, and less security when compared to banks, credit unions, and personal loan companies.

The research team is composed of two Florida Prosperity Partnership (FPP) *Bright Minds, Fresh Ideas* interns who are developing a better way to educate the public on the alternatives to alternative financial services. Both of them have seen and experienced the downfalls and negative outcomes of using these alternative financial services by seeing friends and family go through financial struggles. From going into debt and not being able to pay the overwhelming interest, to becoming dependent on small dollar loans, they have seen it all and it affects numerous people in their communities. Due to this, the motive is to better prepare and equip individuals without a previous education on this topic, with an initial understanding to where they can save money and stress in the future by using other products rather than paying high interest fees. The hope is that whoever reads this can take away strategies and remember prominent details that they can carry with them for the rest of their life, and can aid their decision-making when considering alternative financial services.



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