Bridging the divide digest: Positioning purpose and profit through financial inclusion

Regulatory developments in the financial services industry (FSI) on financial inclusion

Leading off

Financial inclusion has become increasingly important in the face of societal adversity. Time and again, the global and domestic economic challenges demonstrate that the need for financial inclusion is growing, and the time for action is now. With the global economy showing signs of instability, it is crucial for individuals—especially those from disadvantaged communities—to have access to financial services and resources that can help them weather an economic downturn. In a recession, having access to these services can mean the difference between financial stability and economic hardship, making financial inclusion a critical component of economic resilience and recovery.

For industry leaders, this presents an opportunity to understand the landscape, to identify the opportunities, and to make progress on the financial inclusion front. For regulators and policymakers, the global scenario is leading to increased action from their end to nudge the industry toward financial inclusion.

Continuing from our December 2022 issue, we bring forward six of the latest developments in the industry regarding how exclusion and inequality continue to impact underserved markets, and how regulators are coming up with different ways to help further the cause for financial inclusion.

Remarks at the Banking on Financial Inclusion Conference[1]

In recognition of Black History Month, Vice Chair for Supervision Michael S. Barr discussed financial inclusion during the Banking on Financial Inclusion Conference. Barr focused on using available tools to address discrimination in lending and supporting communities and development of products to address consumer needs. He further added that along with using tools as a measure, creating awareness among individuals for such issues is also equally important.

According to Vice Chair Barr, there are three drivers to disparity particularly for Black households: discrimination in lending, the legacy of the racial wealth gap, and disparities in access.

Discrimination in lending: Research has suggested that although progress has been made in addressing racial discrimination, there still exists significant and troubling disparities in lending for Black individuals and businesses. The Federal Reserve System's small business credit survey has highlighted that Black-owned businesses reported more significant credit access challenges including feeling discouraged from applying for credit or other loans.

Racial wealth gap legacy: This is one of the major factors compounding the challenges of financial discrimination. Lower levels of wealth historically have made it difficult for people of color to finance down payments for homes, education, and small businesses. The low levels of wealth also exacerbated difficulties for many Black families when it comes time to manage emergencies and related expenses.

Disparity in access: The Federal Deposit Insurance Corporation's (FDIC) most recent annual[2] survey of the unbanked and underbanked found that the unbanked rate for Black households was 11.3%, compared to just 2.1% for White households. The unbanked rate for Black households in Mississippi was more than double the national average for Black households—23.2%.

Barr then offered three ways to help address these issues:

Pursuing eradicating discrimination through regulation: The civil rights movement brought about changes in public opinion and in law, but discrimination in housing and lending became illegal in 1968 and 1974, respectively, through passage of the Fair Housing Act and the Equal Credit Opportunity Act. Congress has also passed laws, such as the Community Reinvestment Act in 1977. According to Barr, banks should actively analyze their own data using artificial intelligence or other algorithmic systems to identify areas where racial disparities occur, identify discriminatory practices, and make more informed lending decisions.

Supporting vibrant communities: Community Development Financial Institutions (DFIs) and Minority Depository Institutions (MDIs) are critical in the sense that they deliver financial products to places and people often left behind by other financial institutions. Compared to other banks, MDIs originate a greater share of mortgages to minority borrowers and borrowers who live in lower- and middle-income segments. Large banks also have a key part to play; many large financial institutions initiated or expanded special purpose credit programs, many of which provide mortgage assistance to benefit Black and Hispanic communities.

Responsive products: Income disruption and unexpected expenses are more common in low and moderate income (LMI) households, and quick access to a fair interest-rate loan products do make a difference. Similarly, updating rules on check clearance, so that consumers and small businesses still receive checks and have access to their funds, is necessary. Finally, strong consumer protections are needed so that consumers do not have to worry about making payments in a safe way.

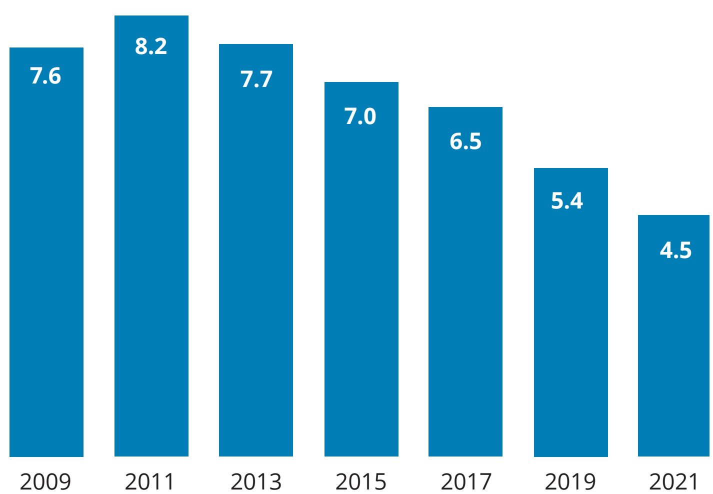
Regulators may also need to engage in areas such as cash flow underwriting and alternative data, new credit models, and other technologies that hold out the promise to increase access and reduce bias in credit intermediation.

2021 FDIC National Survey of Unbanked and Underbanked Households[3]

On November 14, 2022, the FDIC released the results of its biennially conducted "National Survey of Unbanked and Underbanked Households," covering bank account ownership; use of prepaid cards and nonbank online payment services; use of nonbank money orders, check cashing, and money transfer services; and use of bank and nonbank credit.

An estimated 4.5% of US households were "unbanked" in 2021—the lowest since the survey began in 2009. The unbanked rate fell 0.9 percentage points, corresponding to an increase of approximately 1.2 million banked households.

Figure 1. Household unbanked rate, 2009–2021 (%)

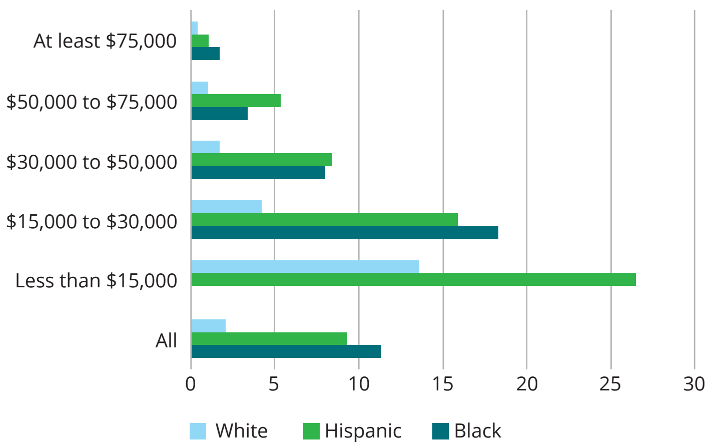


Source: FDIC, "2021 FDIC National Survey of Unbanked and Underbanked Households."

Consistent with the results of previous surveys, unbanked rates varied considerably across the US population. For example, unbanked rates were higher among lower-income households, less educated households, Black households, Hispanic households, working-age households with a disability, and single-mother households.

Differences in unbanked rates between Black and White households and between Hispanic and White households in 2021 were present at every income level. For example, among households with income between $30,000 and $50,000, 8.0% of Black households and 8.4% of Hispanic households were unbanked, compared with 1.7% of White households.

Figure 2. Unbanked rates by income level and race and ethnicity, 2021 (%)



Source: FDIC, "2021 FDIC National Survey of Unbanked and Underbanked Households."

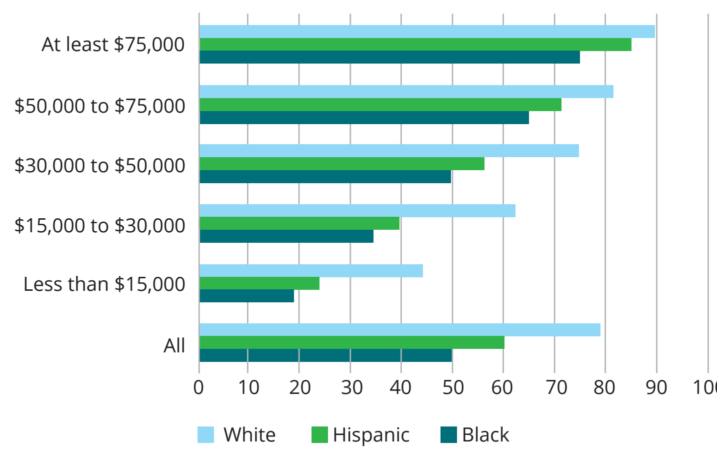
For unbanked households, the top two reasons for not having a bank account were cited as "Don't have enough money to meet minimum balance requirements" and "Don't trust banks" cited by 21.7% and 13.2% unbanked population, respectively.

The survey also mentioned the effects of pandemic-induced economic changes being the reason for opening and closing of bank accounts. Receiving a government benefit payment was cited as the main reason for bank account openings while the main reasons for closing of accounts were losing or quitting a job, being furloughed, having reduced hours, or having a significant loss of income.

Among banked households, use of mobile banking increased sharply (34.0% in 2019 to 43.5% in 2021) and use of a bank teller declined considerably (21.0% in 2019 to 14.9% in 2021) but remained prevalent among certain segments of the population, including lower-income and less educated households. Use of nonbank online payment services was much lower among unbanked households (18.1%) than among banked households (47.7%).

The share of households that had a personal loan or line of credit from a bank (e.g., a bank personal loan) decreased from 10.8% in 2019 to 8.0% in 2021; 2.8% of households had a nonbank personal loan. Differences by race and ethnicity in the likelihood of having a credit card or bank personal loan were present at every income level.

Figure 3. Use of credit card or bank personal loan by income level and race and ethnicity, 2021 (%)



Source: FDIC, "2021 FDIC National Survey of Unbanked and Underbanked Households."

Figure 4. Use of credit by income level, 2021

	Percentage of all households						
	Credit card	Bank personal loan, most recent loan $1,000 or less	Bank personal loan, most recent loan more than $1,000	Nonbank personal loan, most recent loan $1,000 or less	Nonbank personal loan, most recent loan more than $1,000	Rent-to-own service or payday, pawn shop, tax refund anticipation, or auto title loan	No credit
All	71.5	1.3	6.7	0.6	2.2	4.4	25.5
Family income less than $30,000	43.7	1.0	2.4	0.9	1.2	6.9	50.0
Family income at least $30,000	79.8	1.3	8.0	0.5	2.4	3.7	18.2

Source: FDIC, "2021 FDIC National Survey of Unbanked and Underbanked Households."

An estimated 14.1% of US households (approximately 18.7 million) were "underbanked" in 2021, meaning that the household was banked in the past 12 months and used nonbank products such as money orders, rent-to-own services, and payday loans. Underbanked households were less likely to have a credit card and were more likely to have both bank and nonbank personal loans than fully banked households in 2021. For example, 62.4% of underbanked households had a credit card, compared with 76.6% of fully banked households.

Despite economic challenges posed by the pandemic, more consumers became banked and sustained their banking relationship through financial distress. Additionally, household use of some nonbank financial services, such as check cashing and certain consumer credit products, has declined significantly over the past decade. While many banked households appear to use nonbank online payment services to complement banking products, unbanked households may be using them as substitutes for banking or other financial services.

Other notable regulatory developments

Brown, Casey, and colleagues introduce bill to ensure a fair banking system[4]

Industrial loan companies (ILCs) are state-chartered banking institutions whose holding companies are not subject to consolidated supervision by the Federal Reserve, as all other bank holding companies are, due to a loophole in the Bank Holding Company Act. Nonbank commercial companies that seek to operate like banks through an ILC raise systemic financial stability, competition, and consumer protection concerns. The result is that ILCs owned by tech companies have a leg-up on traditional banks with regulatory safeguards.

Senator Sherrod Brown, chair of the Senate Committee on Banking, Housing, and Urban Affairs, along with Senators Bob Casey and Chris Van Hollen, introduced the Close the Shadow Banking Loophole Act[5] legislation to require companies that own an ILC to be subject to the same rules and consumer protections as traditional banks.

FINRA creates Industry Diversity Advisory Committee[6]

On November 9, 2022, the Financial Industry Regulatory Authority (FINRA) announced establishment of a 13-member Industry Diversity Advisory Committee representing industry professionals, diversity practitioners, and academics. The committee will be focusing on collaborating with other securities industry organizations to strengthen diversity, equity, and inclusion (DEI) across the industry and identify the impact of FINRA rule proposals and initiatives.

FINRA now has 13 advisory committees that provide feedback on rule proposals, regulatory initiatives, and industry issues. The established advisory committee structure is a key component of the self-regulatory model, as it helps FINRA ensure rules and activities reflect the diverse business models of firms and the complexity of today's securities markets.

FINRA has taken significant steps to enhance diversity and inclusion in its advisory committees. It introduced term limits in May 2021, which aims to promote diversity by creating more opportunities for underrepresented groups to participate. Furthermore, FINRA and its Board of Governors conduct annual reviews of each committee to ensure that members have the appropriate expertise and represent a diverse range of geographic locations, business models, and sizes. This approach enables FINRA to consider diversity holistically and ensures that each committee reflects a wide range of perspectives.

FINRA Foundation partners with Girl Scouts of the USA to launch new financial empowerment programming[7]

November 1, 2022, FINRA Investor Education Foundation (FINRA Foundation) announced partnership with Girl Scouts of the USA (GSUSA) to launch new financial education programs and resources to meet the needs of girls and their families in underserved communities. The FINRA Foundation is committed to making financial education more accessible to underserved communities. FINRA Foundation would work with the GSUSA program design team to develop financial activities including the development of a Financial Empowerment Playbook designed to aid Girl Scouts in the development of council-run single or multiday events leveraging Financial Literacy, Entrepreneurship, and Cookie Business badges to teach 1.7 million girls spread across Atlanta, Chicago, Dallas, Los Angeles, New Orleans, Philadelphia, Rockville/Washington, DC, and Southeast Florida (Boca Raton) key financial literacy and money management concepts.

Treasury promotes small business growth and entrepreneurship and announces New Markets Tax Credit awards to revitalize low-income and distressed communities

On October 11, 2022, the US Department of the Treasury announced the approval of 11 additional state (Alaska, Idaho, Iowa, Massachusetts, Minnesota, Missouri, Nebraska, Nevada, New Mexico, Ohio, and Utah) plans for up to $1 billion in funding under the State Small Business Credit Initiative (SSBCI).[8] Treasury has now announced the approval of 31 state plans for approximately $4.8 billion in SSBCI funding.

The American Rescue Plan reauthorized and expanded[8] SSBCI, which was originally established in 2010 and was highly successful in increasing access to capital for small businesses and entrepreneurs. The new SSBCI builds on this successful model by providing nearly $10 billion to states, the District of Columbia, territories, and tribal governments to increase access to capital and promote entrepreneurship, especially in traditionally underserved communities as they emerge from the pandemic.

On October 28, 2022, Treasurer of the United States Chief Lynn Malerba, joined by US Senators Benjamin L. Cardin and Chris Van Hollen, US Representative Kweisi Mfume, and Community Development Financial Institutions Fund (CDFI Fund) Director Jodie Harris, announced more than $5 billion in New Markets Tax Credit (NMTC) awards nationwide.[9] Speaking at the recently redeveloped Lexington Market, Treasurer Chief Malerba announced the selection of 107 organizations across the country to receive NMTC allocation awards, made through the calendar year 2021 round of the NMTC Program.

Note: This is a brief spotlight on current industry ongoings and not Deloitte's point of view.

Key takeaways

While financial inclusion efforts have increased significantly over recent years, regulators continue to take critical steps to implement a more equitable and resilient financial sector and correct discrimination, increase access to financial services, and promote equality with consumer protection. In this issue, we've noted several aspects of the ongoing wave of regulatory initiatives to address potential inequities including:

- Federal Reserve Board remarks at the Banking on Financial Inclusion Conference – Vice Chair for Supervision Michael S. Barr identified three drivers of financial exclusion for Black households (discrimination in lending, the racial wealth gap legacy, and disparities in access) as well as ways to address these issues by eradicating discrimination through regulation, supporting vibrant communities, and responsive products.
- From the 2021 FDIC National Survey of Unbanked and Underbanked Households, an estimated 4.5% of US households were "unbanked" in 2021—the lowest since the survey began in 2009. The unbanked rate also fell 0.9 percentage points, corresponding to an increase of approximately 1.2 million banked households.
- Senators Brown, Casey, and colleagues introduced the Close the Shadow Banking Loophole Act, which requires companies that own an ILC to be subject to the same rules and consumer protections as traditional banks.
- FINRA announced establishment of a 13-member Industry Diversity Advisory Committee to strengthen DEI across the industry by identifying the impact of FINRA rule proposals and initiatives and advancing its commitment to DEI in the securities industry.
- FINRA Foundation announced partnership with Girl Scouts of the USA to launch new financial education programs and resources to meet the needs of girls and their families in underserved communities.
- The Department of the Treasury announced the approval of 11 additional state plans for up to $1 billion in funding under the SSBCI. It also announced New Markets Tax Credit awards to revitalize low-income and distressed communities.

For Deloitte's perspective on financial inclusion

Please see our ongoing series on financial inclusion and the impact it has on the financial services industry and the broader economy:

- Driving purpose and profit through financial inclusion
- Advancing social and economic goals with global financial inclusion
- Accelerating toward greater financial inclusion
- The Consumer Financial Protection Bureau (CFPB) underscores the application of anti-discrimination law throughout the credit life cycle
- Deloitte Financial Services Industry, Financial Inclusion campaign

Endnotes

1. Michael S. Barr, "Remarks at the 'Banking on Financial Inclusion' Conference," Board of Governors of the Federal Reserve System, February 7, 2023.
2. Federal Deposit Insurance Corporation (FDIC), "2021 FDIC National Survey of Unbanked and Underbanked Households," 2021.
3. Ibid.
4. US Senate Committee on Banking, Housing, and Urban Affairs, "Brown, Casey, colleagues introduce bill to ensure a fair banking system," December 6, 2022.
5. US Senate Committee on Banking, Housing, and Urban Affairs, "Close the Shadow Banking Loophole Act" factsheet, accessed February 20, 2023.
6. Financial Industry Regulatory Authority (FINRA), "FINRA creates Industry Diversity Advisory Committee: New committee highlights FINRA's commitment to improving DEI in the securities industry," news release, November 9, 2022.
7. FINRA, "FINRA Foundation partners with Girl Scouts of the USA to launch new financial empowerment programming," news release, November 1, 2022.
8. US Department of the Treasury (DOT), "Treasury announces eleven additional states to receive up to $1 billion from U.S. Treasury Department to promote small business growth and entrepreneurship through the American Rescue Plan," press release, October 11, 2022.
9. DOT, "Treasury announces $5 billion in New Markets Tax Credit awards to revitalize low-income and distressed communities," press release, October 28, 2022.

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