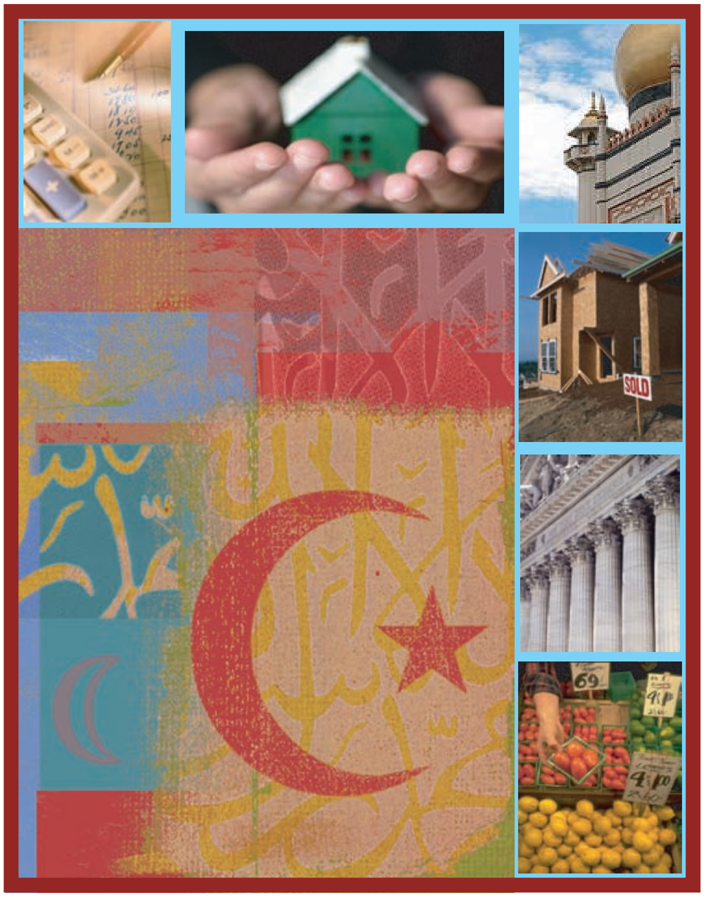
Profitwise
News and Views

Published by the Consumer and Community Affairs Division

February 2006

Islamic Finance: Meeting Financial Needs with Faith Based Products



Index

Around the Seventh District *Page 1*

Foreclosure Alternatives: A Case for Preserving Homeownership *Page 2*

CFED's Assets and Opportunity Scorecard Highlights National Inconsistencies in Financial Security *Page 6*

Islamic Finance: Meeting Financial Needs with Faith Based Products *Page 8*

First Accounts: A U.S. Treasury Department Program to Expand Access to Financial Institutions *Page 15*

Sustainable Rural Development: The Role of Strategic Visioning, MAPPING the Future of Your Community Program, IIRA, WIU *Page 20*

Landmark Payday Loan Act in Illinois *Page 23*

Calendar of Events *Page 25*

FEDERAL RESERVE BANK
OF CHICAGO

Profitwise
News and Views

Profitwise News and Views welcomes story ideas, suggestions, and letters from bankers, community organizations, and other subscribers. It is mailed (either electronically or via U.S. mail) at no charge to state member banks, financial holding companies, bank holding companies, government agencies, nonprofit organizations, academics, and community economic development professionals. You may subscribe by writing to:

Profitwise News and Views
Consumer and Community Affairs Division
Federal Reserve Bank of Chicago
230 S. LaSalle Street
Chicago, IL 60604-1413
or
CCA-PUBS@chi.frb.org

The material in *Profitwise News and Views* is not necessarily endorsed by, and does not necessarily represent views of the Board of Governors of the Federal Reserve System or the Federal Reserve Bank of Chicago.

Advisor
Alicia Williams

Managing Editor
Michael V. Berry

Assistant Editor
Kathleen Toledano

Compliance Editor
Steven W. Kuehl

Economic Research Editor
Robin Newberger

Economic Development Editor
Harry Pestine

Contributing Editor
Jeremiah Boyle

Production Associates
Mary Jo Cannistra
Jennifer Cornman

Announcement: Opportunity for Educators

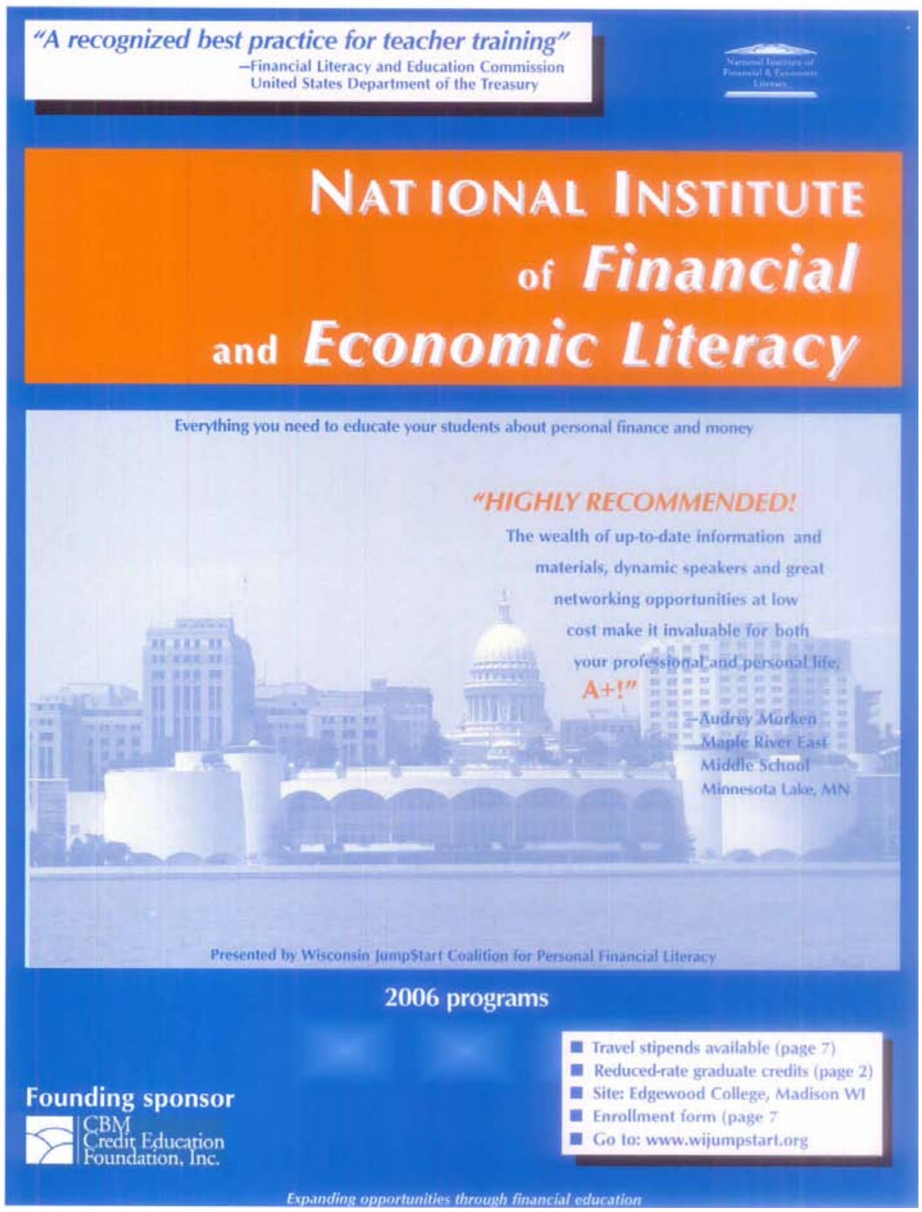
2006 National Institute of Financial and Economic Literacy
Edgewood College, Madison, WI

Who Should Attend:

Teachers of personal finance, family and consumer sciences, social studies, economics, math, business, and others who want to acquire the ability to teach money management and personal finance.

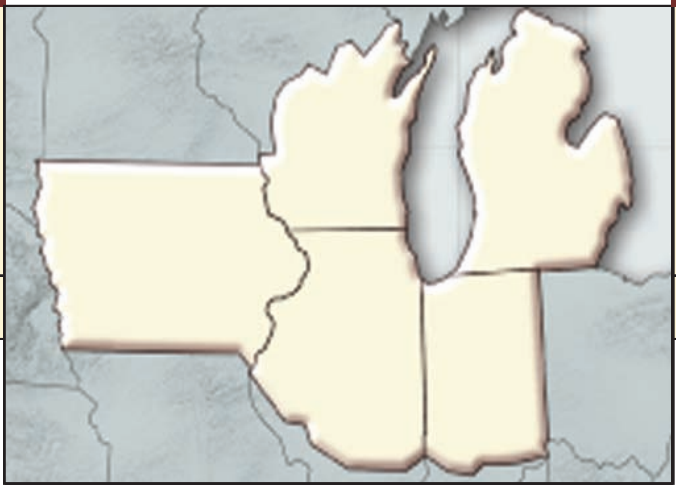
Superintendents, directors, administrators, and principals of high schools, middle schools, and grade schools, and other financial counselors and technical college faculty.

For more information, visit www.wijumpstart.org.



Visit the Web site of the Federal Reserve Bank of Chicago at:

chicagofed.org



Around the Seventh District

Illinois

Illinois State Asset-building Initiatives
As a means to address poverty in the state, the Federal Reserve Bank of Chicago has facilitated the growing asset building movement in Illinois, including co-sponsoring policy conferences with the Sargent Shriver National Center on Poverty Law and CFED.

The Illinois Asset Building Group (IABG) is a group of organizations dedicated to helping people build and preserve financial assets. As a priority, IABG will pursue state-wide children's accounts and other asset building policy initiatives.

For additional information, contact Dory Rand at (312) 368-2007 or Gina Guillemette at (773) 336-6083.

Indiana

Community Groups Fight Foreclosures in Indianapolis' Center Township
Preventing mortgage foreclosures is the focus of the new Saving Homes in Center Township Legal Project, a collaborative community project being launched by Indiana Legal Services (ILS), the Organization for a New Eastside (ONE), Momentive, the Southeast Neighborhood Development Corporation (SEND), the Martindale-Brightwood Community Development Corporation, and the United Northwest Area Development Corporation. The project is designed to help eligible homeowners (not investors) who are seniors or low-income persons, and who face the threat of foreclosure, to stay in their homes or to mitigate financial losses.

Persons seeking legal advice or representation through the Saving Homes in Center Township Legal Project are urged to contact the following Project partners: ILS - (317) 631-9410, x 250; Momentive - (317) 266-1300; SEND - (317) 634-5079; ONE - (317) 917-8922; Martindale Brightwood CDC - (317) 924-8042; United Northwest CDC - (317) 924-0199.

Iowa

Altoona, Iowa: Site for Business Continuity Center
LightEdge Solutions and LBC Technology plan to construct a business continuity center in Altoona, which will withstand most types of disasters and be equipped with electric power generation, auxiliary communications, and other free-standing systems. The $10 million facility will have 30,011 sq. ft. and 288 work stations to allow contracting businesses a base of operations if their normal business place is rendered inoperable. The board of the Iowa Department of Economic Development awarded $100,000 in CEBA (Community Economic Betterment Account) funds and HQJC (High Quality Job Creation) tax benefits to the project, which is near the Interstate 80/1st Avenue interchange in Altoona.

Michigan

Payday Lending Regulation Takes First Step
In November of 2005, Governor Granholm signed into law the Deferred Presentment Service Transaction Act. Under the new act, deferred presentment service providers, which are commonly known as "payday lenders," shall not engage in the business of providing deferred presentment service transactions after June 1, 2006, without a license. License applications will be available on Michigan's Office of Financial and Insurance Services' Web site on February 1, and payday lenders will have until March 31 to submit applications.

For more information, check the Department's Web site at www.michigan.gov/cis/0,1607,7-154-10555-133330--,00.html.

Wisconsin

Feasibility Study Report Released
The State Association of Wisconsin Nonprofits Project recently released its Feasibility Study Report. The Report concluded that:

"The nonprofit sector is clearly a powerful player in the state of Wisconsin. The most recent available data on Wisconsin's nonprofits illustrates the significant role this sector plays. . .It is time to define a strong collective voice, develop a collaborative vision and plan of action that builds on the strengths and effectiveness of Wisconsin nonprofits as a catalyst for Wisconsin's future."

To view the complete Feasibility Study Report, visit http://epic.cuir.uwm.edu/NONPROFIT/research/feasibility.php. To view the results of the nonprofit capacity-building survey, visit http://epic.cuir.uwm.edu/NONPRIOFIT/research/capacity.php. You can contact the report's authors at j.stormer@hotmail.com or fisherhl@uwec.edu.

Foreclosure Alternatives: A Case for Preserving Homeownership

By Desiree Hatcher

Residential foreclosures have become a growing concern in the lending industry. GMAC-RFC (Residential Funding Corporation), America's largest private issuer of mortgage-backed securities and a leading warehouse lender, estimates that it loses over $50,000 per foreclosed home. According to the U.S. Census Bureau's statistical abstracts, the number of nonfarm mortgage loans in foreclosure at year-end 2003 (the latest year for which information is available) was over 500,000. This translates into $25 billion in foreclosure cost for lenders.

Of course, lenders are just one stakeholder in the foreclosure process. What are the total costs associated with foreclosing on a home? Who is responsible for paying these costs? Are there alternatives to the foreclosure process? And if so, what are the advantages of using those alternatives?

The Cost of Foreclosure – Who Pays?

The impacts of mortgage foreclosures are widespread and costly not only for homeowners, but for lenders, servicers, insurers, cities, and neighborhoods. What follows is a description of the cost to each of these stakeholders.

Homeowners: Some of foreclosure's effects on homeowners are readily apparent, while others are just as severe but less well known:

- Loss of a stable, secure place to live.
- Loss of equity in the property.
- A damaged credit rating. Poor credit resulting from foreclosure often becomes a barrier to obtaining rental housing or purchasing another home.
- Potentially higher costs to replace lost housing.
- Possible tax consequences. For tax purposes, foreclosure is treated like a sale; any principal balance and accrued interest forgiven are treated as income for the former owner. The amount of gain or loss is determined just as if the property had been sold for cash equal to the face amount of the debt.

Private and public lenders: A public lender is any entity that uses government funding (public funds) to make loans. This includes cities such as Minneapolis and St. Paul, that have mortgage lending departments, or any nonprofit organization that uses government funding to make mortgage loans. For public lenders, major foreclosure losses are absorbed by loan servicers and mortgage insurers.

Insurance protects most private lenders from major foreclosure losses but does not cover certain types of expenses — for example, those related to holding and maintaining the property. A private lender is any entity not using government funding to make loans, including banks, credit unions, and thrifts. Greater losses are faced by private lenders that originate mortgage loans under their own affordable homeownership programs. These loans, which do not meet conventional underwriting criteria, are held in lenders' portfolios. For the lender, foreclosure means absorbing the full loss for outstanding principal, accrued interest, legal fees, costs of holding and maintaining the property, and real estate broker fees, less any amount recovered through the sale of the property.

Loan servicers: For loan servicers, the income stream from servicing fees stops when borrowers halt payments.

Mortgage insurers: The cost of foreclosure for mortgage insurers is the amounts paid for claims as either insurers in government mortgage programs (FHA, VA) or insurers of conventional mortgage loans. The amount of loss equals the outstanding principal and all the expenses incurred, less the proceeds from the sale of the house.

Cities: Cities do not incur large direct losses from foreclosures, but they do suffer significant — and costly — consequences. Foreclosed properties often deteriorate and lose value, eventually requiring restoration or demolition. If a house is beyond repair, the city absorbs the cost of demolishing it. If the house is vacant, the city also loses tax revenue. Additional costs include administrative expenses involved in rehabbing or demolition, health and building department expenses for property checks, health and safety violations, and condemnation.

Neighborhoods: Boarded-up houses and empty lots affect property values and marketability throughout a neighborhood. Houses in the vicinity of a boarded-up house can decrease in value. Even beyond the immediate area, foreclosed properties affect the "comparables" used in appraisals. Boarded-up properties also increase the likelihood of vandalism and other criminal activity.

Alternatives to Foreclosure

There are workout options available to lenders to help borrowers keep their home. However, some lenders do not inform borrowers that alternatives are available, in part because not all lenders are fully aware of alternatives to foreclosure. What follows is an overview of foreclosure alternatives. It should be noted that these options work best when the loan is only one or two payments behind. Borrowers delinquent beyond two payments severely limit their options.

For Temporary Setbacks

Reinstatement: Accepting the total amount of back interest and principal owed by a specific date. This option is often combined with forbearance.

Forbearance: Reducing or suspending payments for a short period, after which another option is agreed upon to bring the loan current. A forbearance option is often combined with a reinstatement, when it is known that the borrower will have enough money to bring the account current at a specific time in the future. The money might come from a bonus, investment, insurance settlement, or a tax refund.

Repayment Plan: With a repayment plan, the bank agrees to add, for example, half the amount of the first missed payment onto each of the next subsequent two payments. These plans provide some relief for borrowers with short-term financial problems, such as expensive car repairs that make it too difficult to pay the mortgage in a given month.

For Long-term or Permanent Set Backs

Mortgage Modification: If the borrower can make the payments on the loan, but does not have enough money to bring the account current or cannot afford the total amount of the current payment, a change to one or more of the original loan terms may make the payments more affordable. The loan terms could be changed in one or more of the following ways:

- Adding the missed payments to the outstanding loan balance;
- Changing the interest rate, including making an adjustable rate into a fixed rate;
- Extending the repayment term.

Short Refinance: Forgive some of the debt and refinance the rest into a new loan, usually resulting in lower financial loss to lender than foreclosing.

Claim Advance: If the mortgage is insured, the borrower may qualify for an interest-free loan from the insurer to bring the account current. Full repayment of this loan may be delayed for several years.

For Older Homeowners

Reverse Mortgage: Reverse mortgages allow older homeowners (with little or no outstanding mortgage debt) to convert the equity in their homes to cash while retaining ownership. With a regular mortgage, the borrower makes monthly payments to the lender. But with a reverse mortgage, the borrower receives money from the lender and generally does not have to repay it for as long as they live in the home. In return, the lender holds some — or all — of the home's equity. For more information on reverse mortgages, go to www.ftc.gov.

If Keeping the Home is Not an Option

Sale: If the borrower can no longer afford to repay the mortgage, the lender agrees to give the borrower (or their agent) a specific amount of time to find a purchaser and pay off the total amount owed.

Pre-foreclosure Sale or Short Payoff: If a property's net sales proceeds do not cover the loan in full, the lender may accept less than the full amount owed. Though the lender takes a loss on the sale, the additional cost of foreclosing on the property is avoided.

Assumption: Allow a qualified buyer to assume the mortgage, even if the original loan documents state that it is non-assumable.

Deed-in-lieu: Agree to allow the borrower to voluntarily surrender the property and forgive the debt. This option may not be available if other liens such as judgments of other creditors, second mortgages, and IRS or state tax liens exist.

Note: both a short sale and a deed-in-lieu damage the borrower's credit rating less than a foreclosure as they reflect efforts by the borrower to come to terms with the lender. But the short sale is less damaging than a deed-in-lieu, because it indicates recognition by the lender that the event was caused by factors outside of the borrower's control.

Is Foreclosure Prevention Effective?

A national study released July 2004 by Freddie Mac Deputy Chief Economist Amy Crews Cutts and George Washington University Professor Richard Green found that home retention workouts, such as repayment plans and loan modifications, are very effective at keeping borrowers in their homes. The study found that repayment plans lower the probability of home loss by 80 percent among all borrowers and by 68 percent among low- to moderate-income borrowers. Repayment plans appear to work well, regardless of the income level of the homeowner. For more detailed information, this study can be found at www.freddiemac.com/corporate/reports.

Is Foreclosure Prevention Cost Effective?

Do mortgage foreclosure prevention programs save public and private dollars? In 1995, the Family Housing Fund undertook an evaluation of the cost-effectiveness of the Mortgage Foreclosure Prevention Program (MFPP). MFPP was established in Minneapolis and St. Paul in 1991 to provide counseling and, in some cases, financial assistance to help low- and moderate-income homeowners avert foreclosure. Supported by a combination of private and public funding, the program is administered by the Family Housing Fund, and the results compiled in a database maintained by the Amherst H. Wilder Foundation's Research Center.

The study focused on data from two participating Twin Cities agencies: the Northside Residents Redevelopment Council (NRRC) and the St. Paul Housing Information Office (HIO). The study covered the period between July 1991 and March 1995. During this time, over 800 homeowners in the Twin Cities received foreclosure prevention counseling and/or emergency assistance. Total expenditures for the program were $1.6 million.

The average cost of foreclosure prevention in this study was $3,300 ($1.6 million divided by 487 homeowners who had their mortgage reinstated). The cost of foreclosure, on the other hand, was many times higher. The exact amount varies with factors such as interest rates and their effects on refinancing, the strength or weakness of the local real estate market, the type of mortgage insurance (FHA, VA, or private), and whether the property is sold quickly or abandoned, boarded, or demolished. In this study, costs were estimated for two typical scenarios:

- In Scenario 1, a house with an FHA mortgage goes into foreclosure, becomes vacant and boarded up, and is eventually acquired by the city, which rehabilitates it and sells it.
- In Scenario 2, a house financed with a privately insured, conventional mortgage goes into foreclosure, is put on the market, and is sold, recouping some expenses.

The tables below compare the costs of mortgage foreclosure prevention versus the costs of foreclosure to stakeholders under the two scenarios.

Scenario 1		
	Foreclosure Prevention Cost	Foreclosure Cost
Homeowner		$7,200
Lender		$1,500
Servicer		$1,100
FHA-HUD		$26,500
City		$27,000
Neighbors		$10,000
Counseling, Financial Assistance	$3,300	
Average Cost per Household	$3,300	$73,300

Note: Losses listed in Scenario 1 for lenders, servicers, FHA-HUD, and the city represent dollar losses directly related to the foreclosed property, unrecovered rehab subsidies, and lost tax revenues. They do not include administrative cost, such as staffing of servicers' collection departments, public health inspections and condemnation process, the cost of police calls, or city staff time spent coordinating rehabilitation work.

Scenario 2		
	Foreclosure Prevention Cost	Foreclosure Cost
Homeowner		$7,200
Lender		$2,300
Servicer		$1,100
Private Mortgage Insurer		$16,000
Counseling, Financial Assistance	$3,300	
Average Cost per Household	$3,300	$26,600

Note: Losses listed in Scenario 2 for lenders, servicers, and private mortgage insurers represent dollar losses directly related to the foreclosed property. They do not include administrative costs, such as paying for collections or foreclosure staff.

In Scenario 1, the combined losses for all parties were about $73,300 — over 22 times the average cost of prevention. In Scenario 2, the combined losses were about $26,600 — eight times the cost of prevention. These figures were based on average losses experienced by typical homeowners served by the foreclosure prevention program and by lenders, servicers, mortgage insurers, and neighborhoods. The losses calculated for the city were at the lower end of the typical range. Losses to lenders were lower in Scenario 1 than in Scenario 2 because FHA mortgage insurance provides more comprehensive coverage than private mortgage insurance.

In addition, the study yielded the following results regarding the effectiveness of the foreclosure prevention program:

- Of the 800 homeowners serviced during the review period, the two agencies helped 487 (60 percent) homeowners to reinstate their mortgages.
- Of the 487 mortgages reinstated, 432 (89 percent) were FHA, VA, or privately insured. Averted losses to the insurers totaled an estimated $9.6 million.
- After two years, 244 (50 percent) of the homeowners were still current on their mortgages, dropping the averted losses to an estimated $5.4 million. Still, the savings are more than triple the program's cost.

Foreclosure prevention is both impactful and cost effective. The collected losses to the many parties affected by foreclosure are many times the cost of working with the homeowners to prevent foreclosure before it occurs. Furthermore, the benefits of foreclosure prevention increase for lending institutions, mortgage insurers and investors, government at all levels, and homeowners with each home saved.

As indicated previously, workout options work best early in delinquency. However, many people avoid calling their lenders when they have money troubles. Most are embarrassed to discuss money problems with others or believe that if lenders know they are in trouble, they will rush to collection or foreclosure. It is to the lender's advantage to contact the borrower as soon as delinquency begins. Borrowers who don't feel comfortable talking with their lender should immediately contact a HUD-approved housing counseling agency. A counselor will help assess the borrower's financial situation and determine what options are available. A counselor will be familiar with the various workout arrangements and will know what course of action makes the most sense for the borrower, based on their circumstances. In addition, the counselor can call the lender with the borrower or on the borrower's behalf to discuss a workout plan. Also, a counselor will have information on local services, resources, and programs that may provide the borrower with additional financial, legal, medical, or other assistance.

To find out more about HUD-approved housing counseling agencies and their services, call (800) 569-4287 or go to www.hud.gov to look at the list of HUD-approved agencies by state.

References

Crews Cutts, Amy and Richard K. Green. Innovative Servicing Technology: Smart Enough to Keep People in Their Houses? Freddie Mac News Archive, July 2004, www.freddiemac.com/corporate/reports.

Northwest Area Foundation. *Preventing Mortgage Foreclosure – Is it Cost Effective?*, Northwest Report, December 1997, available from the Family Housing Fund at (612) 375-9644 or at www.fhfund.org.

Home Ownership Preservation Enterprise, Foreclosure Prevention, Mission Statement, November 2004.

HUD, *Help for Homeowners Facing the Loss of Their Home, Homes and Communities*, www.hud.gov/offices/hsg/sfh/econ/cfm#4.

FTC. *Reverse Mortgages: Proceed with Care*, Facts for Consumers, www.ftc.gov/bcp/conline/pubs/homes/rms.htm.

U.S. Census Bureau. *Construction and Housing, Statistical Abstracts 2001-2005*, www.census.gov.prod.www/abs/statab.html.

U.S. Census Bureau, *Mortgage Delinquency and Foreclosure Rates, Statistical Abstracts 2001-2005*, www.census.gov/prod/www/abs/statab.html.

Desiree Hatcher *is the community affairs program director for Indiana at the Federal Reserve Bank of Chicago's Consumer and Community Affairs division. Ms. Hatcher provides technical assistance and conducts forums, conferences, seminars, and workshops on community development, fair lending, and consumer banking regulations. Ms. Hatcher has over 15 years experience as an examiner for the Office of Thrift Supervision, the Federal Reserve Bank of Chicago, and the Office of the Comptroller of the Currency, and as a senior internal auditor for a savings and loan. Ms. Hatcher holds a bachelor's degree in finance from the University of Detroit Mercy, and a master's degree in administration from Central Michigan University. Ms. Hatcher is a commissioned examiner and a certified financial services auditor.*

CFED's *Assets and Opportunity Scorecard* Highlights National Inconsistencies in Financial Security

By Andrea Levere

Asset building plays an integral role in alleviating poverty and bolstering financial security for individuals and families. Assets move families beyond living paycheck to paycheck and give them tools to plan for the future. But in order to improve asset building in the future, we first have to determine where we stand today. To do this, CFED, a nonprofit organization that works to promote economic opportunity, has created its most comprehensive tool yet to measure ownership and financial security, the *Assets and Opportunity Scorecard: Financial Security Across the States* (Scorecard). The recently released Scorecard provides a detailed picture of how the states are faring in both performance and policy.

The Scorecard – which can be accessed online at www.cfed.org/go/scorecard – measures the financial security of families in the U.S. by looking beyond just income to the whole picture of building ownership and protecting against financial setbacks. The Scorecard ranks the 50 states and the District of Columbia on 31 performance measures in the areas of financial security, business development, homeownership, health care, and education.

The Scorecard quantifies various aspects of household financial health across the states, and grades related state policies. The data show some alarming discrepancies in net worth between women and men, minorities and whites, and even between average residents of different states.

Among the key findings:

- Nearly one in five American households has zero net worth or is in debt, that is, "owes more than it owns." The ratio is one in three for minority-headed households.
- For every dollar of net worth of a household headed by a male, female-headed households have less than 40 cents.
- The median Massachusetts household net worth (the highest of all states) is three times that of median households in Arizona, Texas, Georgia, West Virginia, and a number of other states.

States were graded from A to F on their performance in building assets. Among the virtues of a highly graded state is high net worth among a large number of residents, low levels of asset poverty and bankruptcies, widespread ownership of small businesses, high homeownership with a low number of foreclosures, a high percentage of residents with health insurance, and high test proficiency from students and advancement into higher education.

The Scorecard also looks at 38 state policies in these areas (as well as tax policy) that can help or hinder citizens' efforts to get ahead. Policies are assessed as either "favorable," "standard," or "substandard," relative to the policies of the other states.

Among these are policies that address predatory lending standards, small business investment, first-time homebuyer assistance, per-pupil spending, and asset-building savings programs.

The top performers on the Scorecard — those states that earned an overall A in performance measures and a favorable rating in policy measures — include Connecticut, Delaware, Vermont, Maine, Minnesota, and Iowa. The state of Iowa is within the Federal Reserve System's Seventh (Chicago Fed) District. The scores earned by the remaining states within the Seventh District boundaries — Illinois, Indiana, Michigan, and Wisconsin — were mixed:

- Illinois earned a D, but received a favorable rating for its asset-building policies;
- Indiana and Michigan earned Cs on overall performance measures, and also garnered substandard policy ratings; and
- Wisconsin returned an overall B, as well as a favorable asset-building policy rating.

Along with the Scorecard, CFED has created a Scorecard Advocacy Center to encourage state-level asset-building and ownership advocates to use the Scorecard as a tool for effecting policy change. CFED has already incorporated state-level advocacy into the roll-out of the 2005 Scorecard by working closely with organizations in the asset-building field. Among these groups are the Chicago-based Sargent Shriver National Center on Poverty Law and the Michigan IDA (individual development account) Partnership.

Asset-building Partnerships

CFED and the Sargent Shriver Center on Poverty Law recently presented Scorecard findings as part of two asset building policy briefings, one at the Federal Reserve Bank of Chicago and another for state legislators in Springfield, IL. The Shriver Center also plans to use the Scorecard as a tool to further its work with the newly formed Illinois Asset Building Group (IABG), of which the Shriver Center is a co-chair. IABG's mission is to foster financial strength, economic development, and family and community stability and well being in Illinois, both today and for future generations.

CFED's working relationship with the Shriver Center predates the Scorecard, as the Shriver Center is also a partner in the CFED-managed Saving for Education, Entrepreneurship, and Downpayment (SEED) Policy and Practice Initiative — a multi-year national initiative to develop, test, and impel matched savings accounts and financial education for children and youth. For SEED, the Shriver Center has partnered with the William M. and Charles H. Mayo Elementary School in Chicago to deliver SEED accounts to students in kindergarten through fourth grade.

Not unlike the Shriver Center, the Michigan IDA Partnership—a collaboration between the Michigan Department of Human Services and the Council of Michigan Foundations—is planning to use the Scorecard to further its efforts through the newly formed Asset Building Coalition (ABC) for Michigan. ABC for Michigan will use the Scorecard to help draw attention to existing policy and create new policy options with the greatest potential to help working poor households build assets and become more financially secure.

Andrea Levere *is president of CFED. Established in 1979 as the Corporation for Enterprise Development, CFED works nationally and internationally to expand economic opportunity. CFED has offices in Washington, DC, Durham, NC, and San Francisco, CA.*

Islamic Finance: Meeting Financial Needs with Faith Based Products

By Shirley Chiu and Robin Newberger

This article explores the demand for and the availability of financial products for Muslims who adhere to religious prohibitions against receiving and paying interest. This is an evolving area of consumer and small business finance, and the goal of this article is to provide an overview of the potential market for Islamic finance, to describe the organizations that currently provide these products, and to highlight some of the challenges of satisfying both religious tenets and government regulations. Two facets of financial products, asset financing, and investments, are addressed. Furthermore, the article identifies three types of organizations that offer Islamic financial products and services: financial entities, nonprofits, and for-profit ventures that sell models of Islamic finance products and consulting services to firms.[1] Drawing largely on interviews with regulators, practitioners, and experts in the field, we find that the few financial entities that offer formal Islamic finance in the United States are often motivated by strong grassroots demand in their local service areas. These entities are often charting new territory in terms of product development and conformity with government regulations. Regulatory issues have not yet been tested on a large scale, and decisions as to whether a bank may offer an Islamic financial product are typically determined on a case by case basis.

What is Islamic Finance?

Islamic finance is fundamentally different from the conventional finance model as it is based on a profit and loss structure (PLS), which requires that a financial institution invest with a client in order to finance their needs, rather than lending money to the client. Because of the inherent risk involved in an investment, the financial institution is entitled to profit from the financial transaction.

In assuring customers that the structure of the advertised Islamic finance products are compliant with Islamic law, financial institutions employ a panel of Islamic scholars, also known as a *Shari'ah* board, to analyze and approve of the product's compliance with *Shari'ah*, or Islamic law. If the *Shari'ah* board approves of the product, it signs a certificate called a *fatwa* designating the product *Shari'ah* compliant, which also serves to assure customers of the product's adherence to Islamic law.

Although Islamic finance is relatively new to the United States, various interpretations of this concept are widely practiced in other countries. In Egypt, Indonesia, Malaysia, Sudan, and the Gulf States, Islamic banking coexists with conventional banking. In many cases, international banks have established Islamic finance windows, or branches of their bank that specifically offer Islamic finance products and services. In countries such as Iran and Pakistan, Islamic banks are the only type of financial institution. Islamic finance is also offered in Europe by a small number of conventional banks and through the recently established Islamic Bank of Britain. Over the past ten years, the global Islamic finance industry has grown significantly and today has between $200 billion and $300 billion in assets.[2]

A fundamental distinction of an Islamic Bank is the lack of deposit insurance common in conventional banks. The PLS structure permits receipt of money by depositors where deposits invested have incurred a profit, but they must incur losses in situations where deposit investments incur losses to comply with *Shari'ah*. Deposit insurance defeats the purpose of PLS because the depositor does not incur any risk. This very fundamental aspect of an Islamic bank runs contrary to the standards of western banking regulations. In fact, rather than overcome this hurdle, the Islamic Bank of Britain's *Shari'ah* board, finding in the end that this was the only remaining obstacle faced, allowed for the deposit insurance as long as customers were made aware that deposit insurance was not *Shari'ah* compliant.

The U.S. does not currently have an Islamic bank. Prior to 1997, no bank in the U.S. offered formally structured

Islamic financing that was both publicly approved by a U.S. regulatory agency, and approved by a board of Islamic scholars. In the late 1990s the New York branch of the United Bank of Kuwait (now closed) paved the way for financial institutions that currently offer Islamic financial products. In 1997 and 1999, the Office of the Comptroller of the Currency issued two interpretive letters permitting a New York branch of the United Bank of Kuwait to offer its Islamic home financing products to Muslim customers. The interpretive letters have since been the premise for determination by certain regulatory agencies whether an Islamic finance product is compliant with U.S. banking regulation and can be offered by a financial institution.

Demand for Islamic Finance Products

The U.S. State Department notes that Islam is one of the fastest growing religions in the U.S. Most of this growth is due to immigrants and descendants of immigrants. Immigrant Muslims are mostly from Iran, Iraq, Somalia, Sudan, Afghanistan, and the former Yugoslavia. In the past few decades, the number of Pakistani and Indian Muslims living in the U.S. has also grown significantly. More recently, the number of Muslims from Indonesia and Malaysia has been increasing.

These demographic trends are useful for estimating the demand for Islamic finance in the U.S. According to the U.S. State Department, there is no official count of Muslims in the United States. The analysis here draws on data from a number of sources, including the *American Religious Identification Survey* by the City University of New York; the Department of Homeland Security; the U.S. Census Bureau's *Current Population Survey*, March Supplement; and the U.S. State Department. The *Current Population Survey* (CPS) shows 2.1 million people in the U.S. who emigrated from countries where Islam is the dominant religion or are children of such emigrants.[3] This value is close to the 2.2 million Muslims identified by the *American Religious Identification Survey*.[4] Some leaders of the Islamic community put the number of Muslims living in the U.S. as high as 9 million. According to data from the Department of Homeland Security, Muslims made up about 4 percent of new immigrants in 1990 and 7 percent of new immigrants in 2000, representing about 72,000 new arrivals that year. Between 1995 and 2003, the percentage of immigrants in the United States who came from a country where Islam was the majority religion increased from 10 percent to 14 percent.

In addition to immigrants and their descendent children, nonimmigrant Muslims are comprised mostly of African Americans and are estimated to make up more than one quarter of the U.S. Muslim population.[5]

Another factor in estimating potential demand is degree of religious observance. Experts identify three distinct levels of observance in the Muslim community. The first level comprises the most observant Muslims who do not use conventional financing. This group represents the core market for Islamic financing arrangements. The second level currently uses conventional financing, but might switch to Islamic financing if it were available. This group often consists of U.S.-born children of immigrants, rather than the immigrant parents themselves. The final level comprises the least observant Muslims, who currently use conventional financing, and would likely continue to use it even if a religiously compliant alternative were available.

Although mosque affiliation does not necessarily imply a demand for Islamic finance, financial institutions assume that mosque attendees would form the basis of their Islamic market and have concentrated their outreach efforts on this population. Several surveys collect information on membership at mosques to provide a greater understanding of the Muslim presence in the U.S.[6] In 2001, there were 1,368 mosques in the U.S. The states with the greatest number by rank were California, New York, New Jersey, Michigan, Pennsylvania, Texas, Ohio, Illinois, and Florida. Between 1986 and 2001, California, New York, New Jersey, Michigan, and Pennsylvania experienced the greatest growth in the number of mosques. Of the 2.2 million self-identified Muslims living in the United States, 62 percent are members of a mosque. Between 1990 and 2001, the number of self-identifying Muslims increased by 50 percent.

Another way to think about demand for financial products is in terms of the socio-demographic status of Muslims in the United States. National data sets show that immigrants from predominantly Muslim countries, and the children of these immigrants, have relatively high levels of education and income. An estimated 46 percent of Muslims have at least a college degree, compared with 23 percent and 25 percent of all immigrants and natives, respectively. Similarly, Muslim immigrants and their descendents have median incomes closer to natives than to those of immigrants overall. So too, the Muslim population has the highest proportion of young adults under the age of 30 as compared to any other religious group.

Islamic Financial Transactions

U.S. financial institutions that offer Islamic finance products typically offer *Murabaha*, *Ijara*, and *Musharaka* financing for purchasing homes, cars, and small businesses. In a typical *Murabaha* transaction, the financial institution acts as an agent and purchases a good requested by a customer; the financial institution, in turn, sells the good to the customer at the acquisition cost plus the profit over a stated period of installments. If the customer defaults, they are only liable to the financial institution for the contracted sale price. The key requirement of *Murabaha* is that the financial institution must own the good before transferring it to the customer. The financial institution justifies its profit based on the risk it assumes from buying the asset.

The *Ijara* is a leasing agreement where the financial institution purchases an asset and leases it to the customer. The financial institution, or a subsidiary of the financial institution, owns the asset throughout the lease period and the customer pays the financial institution a rental fee each month during the leasing period. The customer may purchase the asset in its entirety either during or at the end of the lease period, but is not required to do so. The typical *Ijara* asset financing models offered in the U.S. are lease-to-own in nature. Until the buyout is consummated, the investor is the owner of the asset and is responsible for any taxes and risks associated with the ownership.

The *Musharaka* is a declining balance or shared equity purchase. Typically, the financial institution provides a percentage of the capital needed by its customer in a business undertaking, with the understanding that the financial institution and customer will proportionately share in profits and losses in accordance with a formula agreed upon before the transaction is consummated. In the case of home financing, the homebuyer makes monthly payments to the investor such that each month less of the total payment goes toward the actual use of the property and more toward building the buyer's equity. The *Musharaka* is a legally binding contract to form a partnership to buy the property. That agreement allows the homebuyer exclusive use of the whole property and extracts a morally binding promise from the buyer to purchase the property from the investor in the future.

A much less common method of Islamic finance in the United States is the *Mudaraba. T*he *Mudaraba* is an agreement between an investor and an agent, where the investor provides capital for the project and the agent invests the funds according to the investors' instructions. The investor provides the capital, entrusting the agent for his expertise and experience. Profits from the investment are shared between the two parties at a predetermined ratio, and losses are borne by the investor.

Islamic Finance Providers in the United States

A small number of entities formally offer Islamic financing products in the United States. Other banks might customize loan products for Muslim customers on an as-needed basis, but do not offer a formal Islamic finance product and book these transactions as traditional loans. We identify seven institutions below that currently advertise formal Islamic finance products and two for-profit organizations that offer models of *Shari'ah* products to entities.[7]

LARIBA and Guidance are finance houses – institutions that offer asset financing, but cannot hold deposits. Established in 1987 by business people who believe in *Shari'ah* compliant financing, LARIBA is the oldest of the organizations listed in Table 1, and is currently owned by members of the American Islamic community. It is based in Pasadena, California, and licensed to sell its *Shari'ah* financing products in 49 states. LARIBA offers a lease-to-purchase model with terms up to 30 years, or a variation of the *Ijara* model to finance homes, automobiles, and medical clinics and equipment. LARIBA also offers leasing with declining equity for construction of single-family homes and finances small business and trade.

Guidance Financial Group also has origins in the Muslim community and has been offering products since April 2002. Guidance is based in Virginia, and currently licensed to sell its products in 18 states. The organization offers home financing through its declining balance co-ownership program, or a variation of the *Musharaka*. In addition to offering home financing products, Guidance is currently looking to securitize its home financing contracts so that they are *Shari'ah* compliant for purchase by Islamic investors.

Devon Bank in Chicago and University Bank in Ann Arbor, Michigan are privately owned community banks. Their involvement in Islamic finance has developed largely as a result of their locations in multi-ethnic neighborhoods with high concentrations of Muslims. Devon Bank offers its products both inside and outside of Illinois. It offers Islamic home, construction, and small business financing. Home financing is offered through either the *Murabaha* or *Ijara* model. Devon Bank offers commercial *Murabaha* and *Ijara* transactions for real estate acquisitions to business customers.

University Bank started offering Islamic finance products in July 2003 when brokers and real estate agents made them aware of this niche market. In an effort to expand its Islamic home finance business nationwide, University Bank in December 2005 created a subsidiary, University Islamic Financial Corporation, to focus solely on selling its line of Islamic home finance products, profit sharing deposit accounts, and shares of Islamic mutual funds. University Islamic Financial Corporation uses home financing and deposit product patents from SHAPE Financial Corp. It currently offers the *Ijara* home-lease financing model and interest-free deposit accounts. The money from these deposit accounts is invested in the bank's *Ijara* home financing contracts, and in return, the deposits receive a net yield calculated from profit-sharing in the home-lease financing products.

HSBC, the only large bank offering Islamic home financing and other *Shari'ah*-compliant products in the United States, focuses its Islamic finance activity in

Table 1: Islamic Finance Providers

Name of institution	Location	Type of institution	Islamic financial products offered
LARIBA Finance House	Pasadena, CA	Finance house	Home, auto, and business financing
Guidance Financial Group	Reston, VA	Finance house	Home financing
Devon Bank	Chicago, IL	Bank	Home and business financing
University Bank	Ann Arbor, MI	Bank	Interest-free deposit accounts, home financing
HSBC	New York, NY	Bank	Home financing, interest-free checking accounts, credit/ debit card
Neighborhood Development Center	Minneapolis/St. Paul, MN	Nonprofit	Small business financing and training
World Relief	Nashville, TN	Nonprofit	Small business financing
SHAPE Financial Corp.	West Falls Church, VA	For-profit wholesaler/ consultant	Home financing, savings accounts, and consulting services
Reba Free	Minneapolis/St. Paul, MN	For-profit wholesaler/ consultant	Small business financing models, and consulting services

the state of New York. Since 1996, HSBC has offered Islamic finance products and services in offices in its global Islamic services division overseas in the UK, Saudi Arabia, Malaysia, Bangladesh, Indonesia, Singapore, and Brunei. In the United States, HSBC offers *Shari'ah* home financing, deposit accounts, and credit cards. HSBC utilizes an *Ijara* lease-to-own home finance model. The deposits from interest-free deposit accounts are invested as capital for the *Shari'ah*-compliant home financing products. The specified percentage of the profit collected from the home financing models is then distributed at a specific rate across the deposit accounts. The money in the interest-free accounts is segregated from investment in "interest-based" funds.

Home financing is the most important source of business for each of these institutions. Each tends to serve socioeconomically diverse customer bases, although some recognize particularly strong growth potential among Muslims in professional occupations.

In contrast, the Neighborhood Development Center and World Relief are nonprofit, small-volume lenders that offer Islamic small business financing mainly to Somali refugees in Minneapolis/St. Paul, Minnesota, and Nashville, Tennessee, respectively. While these states do not have large Muslim populations overall, the nonprofit organizations serve communities with large concentrations of Muslim refugees.

Since 2001, the Neighborhood Development Center (NDC) has partnered with Reba Free, an organization which develops *Shari'ah* approved Islamic financing products, to finance small business entrepreneurs. Most of the NDC's customers are Muslim, particularly Somali refugees, but the program is open to anyone who is looking for an alternative method of financing. NDC offers a buy/sell agreement, which is very similar to that of a traditional *Murabaha* agreement, where NDC purchases the asset and resells it to the client at a predetermined profit rate. NDC also offers a royalties agreement that is similar to the traditional *Musharaka* agreement, in that both the client and the NDC put a certain percentage of capital towards the asset.

World Relief offers micro-financing to Nashville refugees with small businesses. Funding comes from the Office of Refugee Resettlement in the U.S. Department of Health and Human Services. In addition to offering Islamic business financing through a *Murabaha* model, World Relief also provides technical assistance and training.

In addition to these entities, SHAPE Financial Corp. and Reba Free are for profit ventures founded by experts in Islamic finance that supply pre-designed *Shari'ah*-

approved products and consultations to financial institutions. SHAPE offers asset financing and deposit account products to institutions in the United States, Canada, Singapore, and Lebanon. Reba Free offers small business finance products and consulting services within the Minneapolis/St. Paul, Minnesota metropolitan area.

Islamic Investment Products

Another set of institutions that offer financial products for Muslims in the U.S. is asset management companies. The main companies are Assad Asset Management, Allied Asset Advisors, and Saturna Capital's Amana Income and Amana Growth funds.

Most have their own *Shari'ah* board that oversees the portfolio to ensure compliance. Compliance relates both to a purification standard that ensures money is not invested in non-*Shari'ah* compliant businesses, and to a speculative uncertainty standard that ensures the fund is not using financial derivatives or debt products. Globally, 95 percent of investment funds perform their own investment research with their own *Shari'ah* boards. In the U.S., as an alternative to conducting their own investment research, investors and fund managers can purchase a license to the Dow Jones Islamic Index (DJII), an Islamic equity benchmark index comprised of companies that have already been *Shari'ah* approved. The DJII screens out non-*Shari'ah* businesses, which include producers of alcohol- and pork-related products, providers of conventional financing (banks, insurance, etc.), and providers of entertainment services.[8] The DJII then evaluates financial risk by excluding remaining companies with unacceptable financial ratios.

To date, demand for Islamic investment products in the U.S. has been small compared to that for home financing. The U.S. Islamic investment market is estimated to be $112 million.[9] While that number is only a fraction of the total assets of all mutual funds, U.S. based Islamic investment firms have recorded strong annual growth since their creation in the late 1990s. An often cited reason for the smaller demand in the U.S. is that the investment portfolios of Islamic investments focus on returns for the short run, which results in portfolios more liquid and volatile than the conventional long-term retirement portfolios typical of this group. The main challenges to the Islamic investment industry include a lack of understanding by investors as to the particular function of *Shari'ah* funds, high fees, and limited distribution channels.

Debt Investment Products on the Horizon

Within the last four years, tradable Islamic bonds or *sukuk*, have made their way into investment portfolios and mutual funds, particularly outside of the U.S. Governments in Bahrain and Malaysia spearheaded sovereign project financing with *Shari'ah*-compliant transactions and securitized these contracts in the form of *sukuk*. To date, the primary issuers of *sukuk* are government sovereigns or sub-sovereigns, mainly Malaysia, Bahrain, Qatar, Dubai, Germany (Region of Saxony), and Pakistan, as well as a small number of corporate entities and the Islamic Development Bank, an international financial institution. *Sukuks* are the fastest growing form of Islamic financing worldwide. In the last two years alone, the global *sukuk* market amassed about $5 billion. Fifty percent or more of *sukuk* investors are in the Middle and Far East, while another 30 to 40 percent are in Europe. The largest investors are mostly nonbank financial institutions and private investors. In the United States, investments in the *sukuk* market have been limited but growing. Because it is the only type of bond product that is *Shari'ah*-compliant, investors are hard pressed to relinquish *sukuk*, resulting in little liquidity in the overall *sukuk* market.

Challenges Facing the Industry

Organizations that offer Islamic finance in the United States face two principal challenges. One is offering products that conform not only to Islamic religious doctrine, but also to state and federal regulation. For example, the National Bank Act of 1864 prohibits banks from the purchase, holding of legal title, or possession of real estate to secure any debts to it for a period exceeding five years. This would seem to prohibit many Islamic home finance products. However, in two interpretive letters, Numbers 806 and 867, the Office of the Comptroller of the Currency (OCC) concluded that particular versions of *Ijara* and *Murabaha* transactions can be considered exceptions to the prohibitions of the National Bank Act if they meet the standards for functional equivalence to conventional asset financing. The specific standards that must be satisfied are that: 1) the underwriting standard used in these models must incur the same risks as that of a conventional loan; 2) the risk incurred by the bank if a customer defaults on payments must be the same as that of a conventional loan; and 3) the risk from the bank's holding of legal title to the property must be the same as that of a bank providing a conventional loan. In their application of these standards to United Bank of Kuwait's *Ijara* and *Murabaha* models, the OCC determined that the risks incurred by the bank in offering these models are equivalent to those of a conventional loan. The OCC specified that the standards set forth in the two interpretive letters, including the detailed structure of the particular *Ijara* and *Murabaha* models, must be strictly observed in order to receive approval. At this time, no other agency rulings have been made.

The second challenge involves the added costs of offering products that have little precedent in the United States. Some of these costs stem from research required to develop new methods of financing; designing and producing new financial documents to accompany the products; consultations with religious and regulatory experts; and the training of staff in different home purchase procedures. Additionally, banks face the "typical" initial set-up costs related to financial transactions, regulatory capital, and compliance costs from offering new products. Islamic small business products offered by nonprofit institutions tend to generate lower costs than home financing products because they raise fewer regulatory issues. Often the additional costs associated with Islamic finance are passed on to the Islamic banking customer.

The treatment of certain real estate transactions within individual states can also result in higher costs of Islamic finance products. For example, a bank in New York that offered a regulatory and *Shari'ah*-approved *Ijara* model found that its lease to purchase nature resulted in double real estate transfer taxes under the New York real estate code – once during the initial transfer from the original seller to the bank, and again when the property is transferred to the lessee at the end of the lease term. However, this double-taxation does not occur with the *Murabaha* when there is both a transfer and acquisition of property during the same transaction.

A further cost relates to limited opportunities for selling Islamic financial products in the secondary market. To date, three of the institutions that formally offer Islamic finance products have sold their specialized "mortgages" to Freddie Mac. Fannie Mae is looking to establish a similar program by creating standardized documentation for financial institutions that are looking to sell Islamic home finance transactions in a secondary market. In order for Freddie Mac and Fannie Mae to give their appraisal to financial institutions, the transactions must fall within the scope of their charter and meet the standard requirements of qualified conventional loans.

Opportunities for selling assets to private secondary market purchasers in the U.S. are few. According to bankers, traditional bondholders are unfamiliar with the underlying structure and risks of these transactions. Some of the purveyors of Islamic finance have sought to build more complex financial products that would be marketable to Islamic investors domestically and internationally. Guidance Financial Group's motivation to enter the Islamic finance market was to be the first in the industry to build financial instruments from Islamic home financing contracts that would allow Islamic investors to invest in mortgage-backed securities. Meanwhile, religious experts are still debating whether all models of Islamic financing can be sold on the secondary market. *Shari'ah* law permits a bank to sell a note only if it represents an interest in the property by the bank. At present, only the *Ijara* model is structured this way. The approval of such products by religious authorities is likely to affect their appeal to Islamic investors.

Conclusion

Islamic finance is thriving at a small, local level, where interest from Muslim communities has prompted financial institutions to offer products that comply with state and federal regulations, as well as with *Shari'ah* law. In efforts to expand their customer base, many of these financial institutions are also licensed to offer *Shari'ah*-compliant home financing in states outside of that which they are located. As a result, religiously observant Muslim families who previously thought they were unable to purchase a home are now able to become homeowners. Islamic finance is sometimes better understood by banks and finance houses that have developed and marketed the Islamic finance products than by regulators whose approval they need. However, regulatory agencies are interested in building their knowledge in this area. For example, the U.S. Treasury currently hosts an in-house Islamic scholar, so that its staff can better understand the issues as part of an international effort to design a regulatory framework for Islamic finance.

Although the Islamic finance industry has grown in the U.S., there are many questions that remain unanswered. One question is the scope of national demand for Islamic finance. This may be a less pressing concern for individual banks that are responding to abundant demand in specific areas. Another question for financial institutions is how strictly Islamic finance products have to adhere to *Shari'ah* principles before a Muslim individual will become a new customer or switch from conventional to Islamic finance products. Islamic scholars would argue that even the most *Shari'ah*-compliant products in the United States have their limitations. This raises the concern for U.S. financial institutions to determine to what extent their customer base is religiously conservative before deciding to proceed with creating *Shari'ah*-compliant products. Finally, a key issue for regulators involves understanding the risks associated with Islamic finance products. Currently, both banks and their regulators assess risk according to the "functional equivalent" standard established by the OCC. Federal and state regulatory agencies have stated their intention to hold regional discussions with financial institutions aimed at developing regulatory standards that take into account the institutional and systemic risks of Islamic financial products.

Notes

1 Financial entities denotes primarily those entities that sell products for personal financing.

2 Under Secretary of the Treasury John B. Taylor's keynote address at the Forum on Islamic Finance at Harvard University, May 8, 2004.

3 In the CPS data, we define Muslims as those who were born in a country where Islam is the major religion or have a parent from such a country. These countries are defined as those where more than 50 percent of the people are Muslim according to the CIA World Fact Book.

4 The American Religious Identification Survey asks Americans to identify their religious affiliation. It finds between 2.2 million and 2.8 million Muslims in the United States, including African–American Muslims.

5 Council on American-Islamic Relations (CAIR).

6 City University of New York, American Religious Identification Survey; Hartford Seminary's Hartford Institute for Religious Research, as reported by the U.S. State Department.

7 Information is collected from interviews with officers of each of these organizations and from each of the organization's financial literature.

8 Tobacco manufacturers and defense and weapons makers, although not strictly forbidden for investment under Islamic law, are also excluded from the index.

9 Conversation with Monem A. Salem, Director of Islamic Investing, Saturna Capital, March 19, 2005.

Shirley Chiu *is an associate economist in the Consumer and Community Affairs (CCA) department at the Federal Reserve Bank of Chicago. She conducts statistical analyses to support economic research projects by CCA's Consumer Issues Research unit, and has co-authored several articles for the Chicago Fed Letter, a Federal Reserve Bank of Chicago publication. Ms. Chiu holds a B.A. in economics from the University of Chicago.*

Robin Newberger *is a business economist in the Consumer Issues Research unit of the Federal Reserve Bank of Chicago. Ms. Newberger holds a B.A. from Columbia University and a master's in public policy from the John F. Kennedy School of Government at Harvard University. Ms. Newberger holds a Chartered Financial Analyst designation.*

First Accounts: A U.S. Treasury Department Program to Expand Access to Financial Institutions

Program Study by the Center for Impact Research, the University of Chicago Graduate School of Business, the Center for Economic Progress, and ShoreBank

By David Marzahl, O.S. Owen, Steve Neumann, and Joshua Harriman

Introduction

In 2002, there were almost 56 million individuals in the U.S. who did not have either a savings or checking account at a bank or other traditional financial institution.[1] Additionally, over 83 percent of families without a bank account earn under $25,000.[2] These families often use alternative financial services, including check cashing, payday loans, refund anticipation loans, and others, that provide convenience at high cost. A 2004 report estimated that these alternative financial services handled 280 million transactions, generating $78 billion in fee revenue.[3] As a result, "unbanked" low-income workers who can least afford to pay more for basic services often do. They pay to cash checks, are subject to higher interest rates on credit, and pay higher fees and interest rates for consumer loans, auto loans, and home mortgages.[4] This article describes First Accounts, a program designed to provide better financial alternatives for the "unbanked," and highlights some insights from research on the Chicago-based First Accounts program.

The First Accounts Model – Introducing Banking Services to the "Unbanked"

The First Accounts program was an initiative of the U.S. Department of Treasury to expand access to traditional financial institutions for the "unbanked." The program partnered community organizations with financial institutions to provide low- or no-cost checking and savings accounts. A key element of First Accounts was a commitment to financial education.

From 2002 through 2004, the Chicago-based Center for Economic Progress (the Center) was one of fifteen community organizations nationwide to participate in First Accounts. The Center increased economic opportunities for low-income families, children, and individuals by improving access to public, private, and nonprofit programs and services. It was in this spirit that the Center led the Chicago First Accounts program. The Center partnered with Volunteer Accounting Service Team of Michigan and the Consumer Federation of America to implement the program in Detroit as well. First Accounts helped previously "unbanked" consumers open 1,428 bank accounts in Chicago and Detroit, exceeding the initial program target of 1,000 new accounts.

In Chicago, the Center partnered in First Accounts with ShoreBank to provide checking and savings accounts with no monthly fees or minimum balances. Community organizations provided the Center access to over 1,470 previously "unbanked" participants who attended a total of 183 financial education workshops as an entry point to the program. The curricula, developed with the National Consumer Law Center, focused on using accounts effectively, personal budgeting and financial goal setting.

The Center also used free tax preparation services provided by its Tax Counseling Project as another channel to First Accounts. Participants were able to immediately open a savings account and use it for fast direct deposit of their income tax refund, sometimes avoiding more than $100 in check cashing fees. Roughly 26 percent of First Accounts were opened this way. These accounts were opened with deposits significantly higher than the remaining 74 percent of accounts opened by participants who had attended financial education workshops. Total First Accounts program opening deposits were approximately $657,000.

Studies show the importance of financial literacy in making sound financial decisions.[5] For example, the 2002 American Dream Demonstration (ADD) project, which evaluated 14 individual development accounts programs, revealed that financial education had a very significant impact on the savings rates of program participants, and that the higher education participants received (up to eight hours), the better their savings rate.[6] A study evaluating the effectiveness of the Money2000 education program also found significant behavior changes in program participants.[7]

Research on the Chicago First Accounts Program

Two studies have examined the Chicago First Accounts program. Dr. Marianne Bertrand of the University of Chicago Graduate School of Business led a general phone survey of 201 program participants, examined bank data on program participants, and investigated the effect of various program-related and demographic factors on some key measures of program success. Additionally, Dr. Lise McKean of the Center for Impact Research (CIR) led a team in conducting in-depth face-to-face interviews with 77 program participants to examine their financial habits, experiences, and attitudes related to banking, asset building, and managing household finances. Full research reports are available through the Center for Economic Progress Web site, at www.centerforprogress.org. On the national level, ABT Associates, Inc. is conducting a survey of all U.S. Treasury First Accounts grantees, examining program implementation, operations, and outcomes.

Demographics of Chicago First Accounts Program Participants

The participants of the Chicago First Accounts program were nearly 70 percent female, with an average age of 37 at the time of survey. The average household size was 3.3. This population also faces many financial challenges: 70 percent of participants have a high school education or less, 43 percent were unemployed at the time of program entry, and only 33 percent of were employed full time. Thirty-eight percent reported household income of less than $1,000 per month.[8]

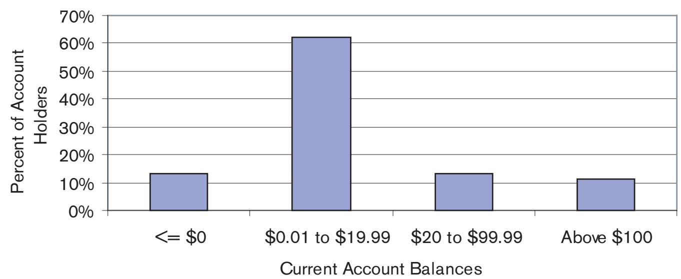
Key Findings from Chicago First Accounts

1. "Unbanked" people want to and can save money.

The overwhelmingly positive response to the Chicago First Accounts program shows that "unbanked" people want to save money. When surveyed, participants "talked about the importance of saving and their efforts to save, with the belief that it is empowering to do so regardless of the amount."[9] They overwhelmingly reported three reasons for attending a First Accounts workshop — desire to manage their money more effectively, desire to learn how to manage a bank account, and desire to open an account. More than 90 percent of workshop participants responded very positively when surveyed about their experience.[10]

In the period studied, 1,428 accounts were opened; 65 percent of these were savings accounts. Participants also maintained their accounts — 87 percent of First Accounts were still open at the end of the period, and over 89 percent of savings accounts carried a balance. At the time of the survey, the average savings account balance was $134.92.[11] Sixty-one percent of survey respondents had saved at least $10 the previous month,[12] compared to just 42 percent who reported having saved anything in the month prior to entering First Accounts. Although a majority of the accounts had low balances, these participants still enjoyed the benefits of having an account: direct deposit of paychecks, ease of saving, free access to cash, FDIC-insured deposits, and the ability to build credit history and maintain a relationship with a bank.

Figure 1: First Accounts Savings Balances November 2004



2. First Accounts program led to dramatic reduction in use of check cashing.

Alternative financial services providers are a growing phenomenon in Chicago and across the nation. The number of individuals that use check cashings services nationally is now estimated at around 10 million per year,[13] and they paid $8 billion in fees. Non-bank check-cashing establishments in the United States doubled between 1996 and 2001, and there are over 520 in the Chicago area alone.[14] Typical fees charged in Illinois to cash a check are 1.4 percent to 1.85 percent the face value of the check,[15] adding up to $300 or more per year for some low-income families who primarily use check-cashing services.

About 72 percent of First Accounts participants used check cashing an average of 3.8 times a month prior to attending the financial education workshops and opening their accounts.[16] Only 18 percent of those surveyed who opened an account are still using check cashing, and even those who chose not to open accounts reported a significant drop in its use.[17] Participants that continue to use check cashing do so because of hours and locations, services available, not having to wait for checks to clear, and convenience of combining finance related tasks in one trip.[18]

Figure 2: First Accounts Participants Using Check Cashers

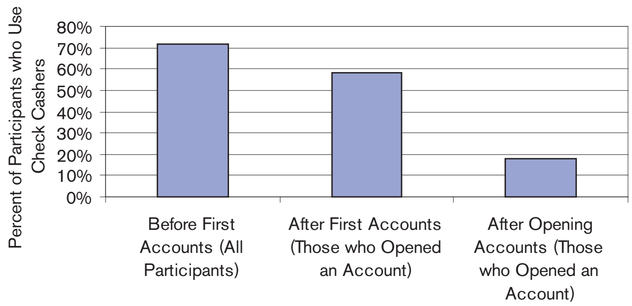
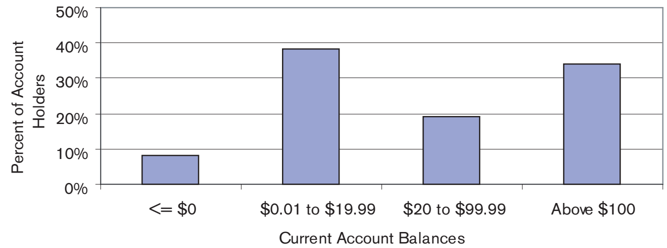


Figure 3: First Accounts Checking Balances November 2004



3. First Accounts made significant impact in financial behavior.

Surveys of program participants and examination of one month of ShoreBank account data show significant account usage and impact on financial behavior. Of those individuals surveyed by CIR, 88.6 percent said that the checking account changed the way they managed their finances.[19] They reported it helped them to:

- Become more aware of their money and their expenses,
- Keep money in the bank (i.e., save more),
- Track their money better,
- Reduce impulse buying,
- Pay bills more conveniently, and
- Reduce the need for money orders.

Overall, 24 percent of First Account holders use direct deposit, 78 percent have an ATM card, and 18 percent use electronic funds transfers (such as automated bill payments). All account holders averaged 2.4 visits to the bank each month. Program participants also deposited a monthly average of $743.98. ATM cards were used an average 6.3 times a month as a debit card and 3.1 times a month at an ATM.[20]

According to ShoreBank, 92 percent of current checking accounts had positive balances in the month surveyed. Over 53 percent of these accounts maintained a balance of at least $20, and 34 percent had a balance of $100 or more. Thirty-seven percent of checking account holders had at least one direct deposit per month. Over 51 percent of those with a checking account wrote at least one check in a six-week period, with 28 percent writing at least three checks. For some participants, the checking accounts imposed heavy fees when the account balances were overdrawn. Seventeen percent of First Account checking accounts had fees over $50 in one month, primarily as a result of insufficient funds in the account, with 35.7 percent of all checking account holders having at least one returned check in the previous six weeks.[21]

Recommendations Based on First Accounts

The First Accounts program demonstrates that many “unbanked” households, including low-income families, want and need quality financial education and good vehicles for saving money and conducting other basic financial transactions at reasonable cost. Initiatives like First Accounts are needed to combat the rising tide of high-cost alternative financial service providers. The experience of First Accounts programs can help bankers, policymakers and community organizations to better serve potential customers who are currently “unbanked,” or who currently have relatively low levels of income.

Understanding the needs of “unbanked” consumers is crucial to serving them. As shown above, alternative financial services collect $78 billion in fees; often from those who can least afford it, for services that in many cases could be provided at lower cost by banks. Customers of alternative financial services often have a bank account, or have had one in the past. First Accounts participants reporting the following drawbacks regarding the traditional banking industry: the wait for cash necessitated by the check clearing process, fees, and overdraft problems. Providing more convenient service, encouraging direct deposit, and utilizing technology to immediately cash checks, or at least reduce the time to make funds available from deposited paper checks, will go a long way toward meeting the financial needs of low-income families and the “unbanked.”

New and better financial products are also needed to better serve the “unbanked.” Savings accounts with low minimum balance requirements better meet the typical short-term savings goals and low average balances of low-income consumers. As technology brings down the cost to banks of holding accounts and processing transactions, affordable savings accounts should become more and more available. Additionally, the rise of stored value cards, which have the potential to be tied to savings products, can increase the savings options for all consumers. Although the traditional checking product offered by the Chicago First Accounts program worked well for many participants, it did not adequately meet the needs of a significant number of others. Checking accounts that minimize the risk of overdraft and the resulting fees, while still allowing users to pay bills and meet other basic financial needs, can provide a solid alternative to those for whom a traditional checking account may not be the right fit. By building a relationship based on understanding the customer's needs, bankers can help to steer consumers toward products that are the best individual fit and create a lasting relationship with this underserved population.

Notes

1 General Accounting Office, "Electronic Transfers: Used by the Federal Payment Recipients Has Increased but Obstacles to Great Participation Remain," 2002.

2 Michael S. Barr, "Banking the Poor: Policies to Bring Low-income Americans into the Financial Mainstream," The Brookings Institution Research Brief, September 2004.

3 Kenneth Temkin and Noah Sawyer, "Analysis of Alternative Financial Service Providers," Fannie Mae Foundation and the Urban Institute, September 2004.

4 "Double Jeopardy: Advocacy Explores the High Cost of Being Poor" Volume 7, Number 1, Winter 2005.

5 Angela C. Lyons and Erik Scherpf, "Moving from Unbanked to Banked: Evidence from the Money Smart Program," Financial Service Review, Volume 13/3, pp215-231, Hogarth, Jeanne M., Beverly, Sondra G., and Marianne Hilgert, "Patterns of Financial Behaviors: Implications for Community Educators and Policy Makers," Discussion Draft, February 2003, Federal Reserve System Community Affairs Research Conference.

6 From the CFED Web site at http://add.cfed.org/training.html, accessed July 13, 2005.

7 O'Neill et al., (2000). "Successful Financial Goal Attainment: Perceived Resources and Obstacles," Financial Counseling and Planning, 11(1), 1-12.

8 Marianne Bertrand, Sendhil Mullainathan and Eldar Shafir, "Evaluation of the First Account Program: Final Report," University of Chicago Graduate School of Business, February 20, 2005, Table 1. Hereafter UCGSB.

9 Lise McKean, Sarah Lessem, and Elizabeth Bax, "Money Management by Low-income Households: Earning, Spending, and Accessing Financial Services," Center for Impact Research, February 2005, p71. Hereafter CIR.

10 UCGSB, Table 3.

11 UCGSB, Table 7.

12 UCGSB, p15.

13 A Survey of Check Cashers in the San Fernando Valley, Valley Economic Development Center, December 2004.

14 Sherrie L.W. Rhine, et al. "The Role of Alternative Financial Service Providers in Serving LMI Neighborhoods," Consumer Issues Research Series, Federal Reserve Bank of Chicago, April 2001.

15 Sherrie L.W. Rhine, et al.

16 From Center for Economic Progress records of First Accounts program workshops. Hereafter CEP.

17 UCGSB, p14.

18 CIR, pp45-47.

19 CIR, p47.

20 UCGSB, Table 7.

21 ShoreBank data on First Accounts provided to M. Bertrand. Data based on November 2004, some variables running over a six-week period.

The Center for Economic Progress would like to thank Dr. Lise McKean of the Center for Impact Research, and Professor Marianne Bertrand of the University of Chicago Graduate School of Business, for their efforts in leading the research of the Chicago First Accounts program. We would also like to thank ShoreBank, and particularly Jim Cobb, for contributing to the research and partnering in First Accounts. Finally, the Center would like to thank the United States Department of Treasury for supporting First Accounts.

David Marzahl *is the executive director of the Center for Economic Progress in Chicago, Illinois. The Center is a statewide and national advocacy and service organization that seeks to increase economic opportunities for low-income families, children and individuals by improving access to public, private and nonprofit programs and services. Prior to joining the Center in 1998, Mr. Marzahl was the founding director of the Illinois Coalition for Immigrant & Refugee Rights, a statewide coalition of organizations promoting the rights of immigrants and refugees. He has worked in the Chicago nonprofit community since 1981 as a community organizer, outreach worker, and activist seeking to advance opportunities for economically and politically disadvantaged persons. Mr. Marzahl has a master's degree in political economy from Northwestern University.*

O.S. Owen *is the director of Financial and Community Education at the Center for Economic Progress, leading the Center's efforts to promote economic self-sufficiency and ensure a future of growth, security, and stability for working families. Mr. Owen has 15 years of experience in delivering financial education, budget, and credit counseling, and is recognized as an expert in helping families to build their financial foundation.*

Steve Neumann *is the Financial Programs Manager at the Center for Economic Progress. In this position, he focuses on optimizing the reach of the Center's Financial and Community Education, leveraging partnerships with community based organizations, government entities, and financial institutions. Mr. Neumann worked for five years in business consulting with Deloitte and Touche LLP prior to joining the Center.*

Joshua Harriman *is an Americorps VISTA volunteer in the Financial and Community Education department at the Center for Economic Progress. He specializes in researching and implementing effective asset-building strategies. He is currently on a leave of absence from American University, where he is completing his doctorate in anthropology.*

Sustainable Rural Development: The Role of Strategic Visioning,
MAPPING the Future of Your Community Program
Illinois Institute for Rural Affairs
Western Illinois University

By Nancy E. Richman, Ph.D.

Rapid and widespread change in the world around us is affecting rural communities in dramatic and often unexpected ways. Leaders and residents of rural communities are continually challenged by the questions of how to nurture their communities through increasingly complex twenty-first century issues, how to lead change that produces the quality of life desired, and how to sustain the effort over time. No longer can rural communities expect that government agencies will provide for their needs, but instead, must look to the people and resources within their communities from which to build their future.

MAPPING the Future of Your Community, a program of the Illinois Institute for Rural Affairs, offers communities an innovative approach to enable positive change and meet these new challenges. The strategic visioning process enables the community to see beyond what exists now to describe its vision for the future, and bring that vision to reality. Through collaboration and consensus building, diverse sectors of the community are brought together to determine what they want the community to be in the future, and by their active participation in the decision-making process, people become empowered and thereby become more able to proactively respond to change.

The MAPPING (Management and Planning Programs Involving Nonmetropolitan Groups) program is a strategic visioning and planning process whereby rural community residents and leaders come together to create a long-range vision for the development of their community and a plan of action for achieving it. The core of the MAPPING program is a series of four visioning sessions. Each session is organized around a central theme: "Where are we now?", "Where do we want to be?", "How are we going to get there?", and "Making it happen and keeping it going!" During the course of this process, participants identify a shared vision of a desirable future, build consensus for high-priority goals for their community, develop a workable action plan, and become organized to address these issues in a town meeting. The town meeting serves to further broaden public participation and input on an evolving plan of action, as well as to mobilize community residents to embrace positive change and become actively involved in the implementation of the action plan.

Created in 1991 with support from the Governors Rural Affairs Council, MAPPING has been supported by the Illinois Department of Commerce and Economic Opportunity since 1995. MAPPING programs have been conducted in 90 communities in 47 counties throughout rural Illinois. Participating communities have ranged in size from as small as ~300 to as large as ~18,000 residents, with the average size MAPPING community of approximately 3,000 residents. MAPPING is conducted either on a community, county, or community-cluster basis.

In the 14 years since the inception of the MAPPING program, we've come to recognize that two elements of the community strategic visioning process are essential to promoting sustainable economic development in rural communities and contribute to community success. These are:

- Building an inclusive leadership coalition among community leaders and residents; and
- Obtaining local commitment and empowering the community to work together effectively across diverse interests, cultures, and socioeconomic classes.

Building a Leadership Coalition

Canton, IL (population: 15,288)

Following their MAPPING the Future program in 1998, the Canton MAPPING participants formed an informal organization, the Canton Community Resources (CCR) Board to implement the MAPPING action plan.

This grassroots coalition began with 16 Board members representing a diverse cross-section of the Canton community. From this broad group of dedicated community residents several sub-committees were formed to tackle goals identified during MAPPING. Since 1998, specific outcomes include: the renovation of a historic opera house, the creation of the Canton Leadership Academy, significant progress in developing a four-lane highway in collaboration with Illinois Department of Transportation, the construction and rehabilitation of several homes, and the formation of the Central Illinois Ag Coalition – a group that has just broken ground for the construction of their new ethanol plant.

Table 1: Percentage of MAPPING Communities Demonstrating Achieved Outcomes* (n=64)

Jobs Created	Beautification Projects	Parks & Recreation	Improved Infrastructure	New Housing	Education Projects	New Festivals/ Events
77%	75%	58%	58%	54%	47%	38%

*Communities were included in this summary if they achieved measurable outcome in the specified domain; projects in progress were not included.

Obtaining Local "Buy-in" and Empowering the Community to Work Together

Elkhart, IL (population: 443)

The Village of Elkhart recognized a need for an overarching plan to guide its future growth and development. Inadequate infrastructure had limited growth in both residential and business sectors. The downtown was badly in need of revitalization and the elementary school was at risk for consolidation. However, preliminary discussions of zoning changes and potential annexations resulted in the community becoming fragmented regarding growth opportunities. Divisions among community residents between the "founding families" and the "newcomer" families further paralyzed progress. By the end of the intensive MAPPING curriculum, the diverse group of community participants had indeed come to agree on a shared direction for their future with action teams formed around identified high-priority goals. Since then, the village has moved ahead aggressively on community development efforts. Several results have been achieved: all downtown storefronts have been filled, including one by an archaeologist who opened a museum, "Under the Prairie," and a bakery/coffee shop that created several jobs; a zoning officer was hired; a new housing subdivision ordinance was developed; and several houses have been built and occupied with new families.

Results from MAPPING community visioning and planning projects during the past decade have been impressive, spanning the scope of economic and community development initiatives. During the fiscal year 2004, an extensive telephone survey was conducted in order to assess the outcomes and impact on rural communities of the MAPPING the Future Program over the past decade. Sixty-four communities participated in the survey. Table 1 presents aggregate results.

In the aggregate, creating jobs was achieved in 77 percent of all MAPPING communities surveyed. Although the approximate number of jobs created as reported by this group of community informants exceeded 4,000, time and resource constraints prevented additional verification of this result.

In addition to aggregate data illustrating long-term end outcomes to which the MAPPING program has contributed, the following example demonstrates the kind of specific community and economic development outcomes that have occurred following the MAPPING program.

Mendota (population: 7,272), LaSalle County

Mendota is one of many communities in which the MAPPING program had demonstrable impact. Key "intermediate outcomes," which local informants attribute directly to their 1998 MAPPING program, have truly set the stage for the achievement of the longer-term outcomes. First, after MAPPING, the city government created a local "Office of Community and Economic Development," and hosted an IIRA Peace Corps Fellow as its first manager. The initial scope of work for this city department consisted of the high-priority goals and strategies from the MAPPING action plan. This action plan was later incorporated into a comprehensive City plan, which forms the core of the current full-time economic development director's focus. Ad hoc MAPPING committees remain involved in community and economic development initiatives in the city.

Additional outcomes since the 1998 MAPPING:

- $1.3 million federal and state funding resulting in the purchase of land and extensive infrastructure improvements to create a local industrial park. The park is almost entirely filled.
- One major industrial employer moved into the city bringing 100 jobs; another significant business expansion is projected to create 125 new jobs.
- Several tax increment financing districts have been created that have successfully sparked development efforts in nine areas of the city. Four entrepreneurs have started businesses creating approximately 15 jobs.
- Strong marketing efforts, including direct mailings, attending targeted conventions, and advertising in site selection magazines have brought new dollars.

- In the near future, Mendota will begin a $1.25 million sewer upgrade to increase the loading capacity, in addition to the $2.5 million water system upgrade currently underway to address high radium content. Another $100,000 water project will connect an industrial user to city water. Finally, a state road construction project will help with traffic flow, adding a traffic light, turning lanes, and widening the road.
- A new housing subdivision has been developed, adding 12-15 homes in the past year. Previous years showed an annual average of about six new homes.
- A new high school opened in January 2004, with an increase in capacity of 200 students.

The MAPPING program helps to provide pertinent data, to create opportunities for public dialogue resulting in enhanced local decision-making, and to build capacities. Clearly, economic development in some areas may have occurred with or without outside intervention. Nevertheless, in the years following MAPPING programs, we have documented numerous businesses that have been started, new homes that have been built, additional children enrolled in rural schools, parks and green spaces that have been created, services for seniors that have improved, industry that has been retained or expanded, new commercial districts that have been formed, and health clinics that have opened. We are continually inspired by the many rural leaders and citizen volunteers who have come together across the state of Illinois to take responsibility for the future of their communities.

Nancy E. Richman *joined the Illinois Institute for Rural Affairs (IIRA) in January 2001. Ms. Richman manages the MAPPING: the Future of Your Community program, a unit of the Illinois Institute for Rural Affairs at Western Illinois University. She is responsible for developing and implementing a strategic visioning and planning process in which local residents of rural communities create a long-range vision for their community, and a plan of action for achieving it. Ms. Richman manages the Rural Community Development Initiative, a program providing financial and technical assistance to assist MAPPING communities in implementing their community action plans. She has a Ph.D. in Clinical Psychology from Boston University. For additional information, contact Nancy E. Richman, Ph.D. at (309) 298-2648 or via e-mail at ne-richman@wiu.edu.*

Landmark Payday Loan Act in Illinois

By Harry Pestine

On June 9, 2005, Governor Rod R. Blagojevich signed a landmark Payday Loan Reform Act that for the first time will regulate the payday loan industry in Illinois and strengthen protection to consumers, especially working families and members of the military against predatory and abusive practices. The Act became effective in December 2005.

"Payday loans are supposed to help working people cover unexpected costs and emergencies. They're not supposed to break their bank accounts. We needed to do something about this, and we have achieved it," said Gov. Blagojevich upon signing the law during a ceremony at the Sargent Shriver National Center on Poverty Law. The Governor was joined by elected officials, legislators, advocate organizations, and individuals who have been the victims of abusive loans.

A payday loan is a short-term, very high-interest debt secured by a borrower's post-dated check. Payday loans become a problem when consumers cannot repay and instead renew the loan. Many consumers take out additional loans to pay the fees on their original payday loan. This extends the cycle of debt further, with no resources for recovery periods or optional repayment plans.

Currently, there are 995 payday or other short-term lenders in Illinois, a 23 percent increase from 2004. According to industry figures, the average annual percentage rate for short-term loans is 595 percent, and the average amount of a short-term loan is $380. According to the Illinois Department of Financial and Professional Regulation, in 2004 lenders made 1.4 million payday loans, which generated $1.3 billion in receivables.

"We can now protect working families from abusive lenders, very high interest rates, and endless debt. This law also helps members of the military. Lenders are no longer able to garnish their pay, collect when a member of the armed forces is in a combat zone, or contact their commanding officer," added the Governor.

"For too long, payday loan operators took advantage of the most vulnerable consumers, including members of the military," said Lt. Gov. Pat Quinn. "This legislation curbs the spiral of debt so many Illinois residents have experienced due to predatory lenders."

The Payday Loan Reform Act provides consumer protections by restricting payday lending in several ways:

- Limits the interest that can be charged for each loan to $15.50 per $100;
- Sets a cap on total loan amounts to $1,000 or 25 percent of a customer's monthly salary, whichever is less;
- Prevents borrowers from having more than two loans at a time;
- Provides that payday borrowers cannot have payday loans for more than 45 days. Once they have reached the 45-day limit they must have at least a seven-day loan free period.
- Creates a new 56-day repayment period with no additional interest charges for borrowers who have trouble repaying their loans;
- Protects borrowers from facing criminal prosecution for unpaid loans, and from paying attorneys fees and court costs; and
- Extends special protections to members of the military, including a ban on garnishing wages, deferral of collections for deployed personnel, and a prohibition on contacting a borrower's commanding officer.

In order to enforce these rules there will be a new state database that lenders will use to view the applicant's payday loan record. If a new loan violates the rules, the payday lender will not receive authorization to issue it. Borrowers will also receive information – in English and Spanish – that outlines their rights and responsibilities before taking a loan.

"Payday loans are a temporary product that put me in a permanent bind. This law will help make sure other borrowers can keep these short-term loans, short term," said Jodie Ackerman who, along with her 9-year old daughter, joined Gov. Blagojevich at the event. Ms. Ackerman is a working single mother who needed extra money to pay her bills, and ended up thousands of dollars in debt from taking out payday loans at interest rates over 700 percent. At one point, she had three outstanding loans and needed a fourth just to make payments on her other loans. Currently, she still has two outstanding payday loans.

The Monsignor John Egan Campaign for Payday Loan Reform was started by the late Msgr. Egan in 1999, after hearing the story of one his parishioners who was victimized by a payday loan. Msgr. Egan convened a group of religious leaders, consumer advocates, public interest organizations and social service groups to form the Campaign for Payday Loan Reform, renamed after Egan following his death in May of 2001. Leaders of the coalition include Citizen Action/Illinois, The Woodstock Institute, Metropolitan Family Services, and Sargent Shriver National Center on Poverty Law.

Sen. Lightford, who worked on the legislation for five years, said the Payday Loan Reform Act "is the first step to protect consumers. Payday loans can cause people's lives to go into a tailspin because of the constant cycle of debt that the borrower can never repay."

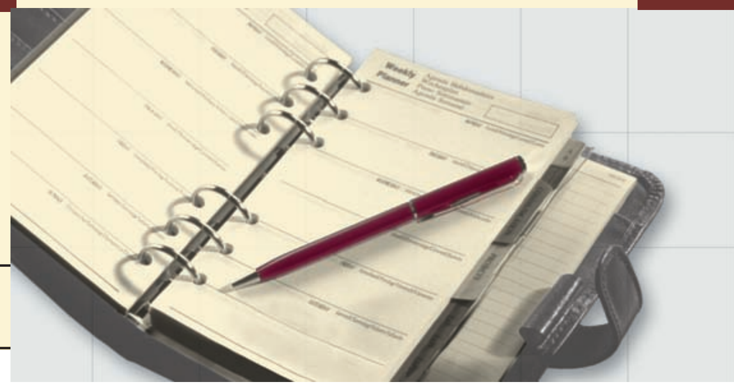
The Illinois Department of Financial and Professional Regulation will license payday lenders and enforce the new Payday Loan Reform Act. "Payday lending is one of the fastest growing types of consumer credit in Illinois…. This bill ensures that borrowers receive the protection they deserve," said Illinois Secretary of Financial and Professional Regulation Fernando Grillo.

The Payday Loan Reform Act, which was introduced in the State Legislature as HB 1100, passed the House of Representatives unanimously and the Senate near unanimously.

For additional information, contact Citizen's Action-Illinois at (312) 427-2114, www.citizenaction-il.org, The Woodstock Institute at (312) 427-8070, www.woodstockinst.org, or Sargent Shriver National Center on Poverty Law at (312) 263-3830, www.povertylaw.org/index.cfm.

Harry Pestine *is the community affairs program director for Illinois at the Federal Reserve Bank of Chicago's Consumer and Community Affairs division. A community and economic development specialist, and the economic development editor for Profitwise News and Views, Mr. Pestine serves on numerous task forces and is a member of the Consul General of Mexico's New Alliance Task Force. Mr. Pestine has been an instructor at the Neighborhood Reinvestment Institute and the National Small Stores Institute. Mr. Pestine has a bachelor of science degree in economics from the University of Illinois.*

Calendar of Events



The Impact of Local Predatory Laws on the Flow of Subprime Credit

St. Louis, MO
March 16, 2006
Starting with North Carolina in 1999, states and other local governments have enacted laws to curb predatory lending in the subprime mortgage market. A new report from the Federal Reserve Bank of St. Louis takes a look at these laws and how they affect the flow of credit in the subprime mortgage market. The report will be presented at this meeting, and a panel of experts will lead a discussion on the topic.

The deadline for registration is March 13, 2006. Register at www.stlouisfed.org/ExternalCFForms/ComForms/LocalLaws.cfm, or contact Cynthia Davis at (314) 444-8761.

2006 National Community Reinvestment Conference

Las Vegas, NV
March 19-22, 2006
Hosted by the Federal Reserve Bank of San Francisco, the Office of Thrift Supervision, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, the conference will feature sessions covering CRA examination training, innovations in community development investing, comprehensive approaches to community development, and the National Community Development Lending School.

For more information, visit www.frbsf.org/news/events/index.html, or contact Lauren Mercado-Briosos at (415) 974-2765.

Reinventing America's Older Communities

Philadelphia, PA
April 5-7, 2006
A national conference on the latest thinking, strategies, and successes in creating vibrant communities. Community developers, planners, government leaders, bankers, researchers, and funders will examine key issues involving schools, the arts, parks, brownfields, displacement, foreclosures, community organizing, eminent domain, waterfront development, and other subjects.

For more information, visit http://www.philadelphiafed.org/cca/conferences.html.

Affordable Housing and Child Care: The Nuts and Bolts of Successful Development

San Francisco, CA – February 6-7, 2006
Sacramento, CA – February 9-10, 2006
New York, NY – March 14-15, 2006
San Diego, CA – April 24-25, 2006
Los Angeles, CA – April 27-28, 2006
The training institutes consist of four sequential two-day modules designed specifically for housing developers who are considering child care operators as development partners and tenants in their projects.

For more information, visit www.liifund.org/programs/childcare/abcd/abcd_devassistance_training.htm.

Call for Papers – Closing the Wealth Gap: Building Assets Among Low-Income Households

Phoenix, AZ
September 19-21, 2006
The Community Affairs Officers of the Federal Reserve System and CFED invite you to submit papers for a policy research forum. The research forum will be held in conjunction with the CFED 2006 Assets Learning Conference. Submission deadline: March 30, 2006.

The Program Committee welcomes research papers and policy studies related to asset- and wealth-building topics, such as the role of tax policy in asset accumulation, housing and wealth, innovations in asset building products and programs, and cost/benefit analyses of asset-building policies.

For more details on all topic areas and submission guidelines, visit www.frbsf.org/community/resources/callforpapers.pdf.

Call for Papers – Financing Community Development: Learning from the Past, Looking to the Future

Washington, DC
March 29-30, 2007
The Community Affairs Officers of the Federal Reserve System are jointly sponsoring their fifth biennial research conference on March 29-30, 2007 to encourage objective research into the factors governing the availability of credit and capital to individuals and businesses within this changing financial services environment.

For more information, visit www.chicagofed.org/cedric/files/2007_call_for_papers.pdf.

FEDERAL RESERVE BANK
OF CHICAGO
Consumer and Community Affairs Division

P.O. BOX 834
CHICAGO, IL 60690-0834

PRESORTED
STANDARD
U.S. POSTAGE PAID
CHICAGO, IL
PERMIT NO. 1942

RETURN SERVICE REQUESTED

Attention:
Executive Officers
Board of Directors
CRA Officer
Community Lender
Community Representative

Profitwise News and Views is published
by the Consumer and Community Affairs
Division of the Federal Reserve Bank
of Chicago
230 S. LaSalle Street
Chicago, IL 60604-1413