

# Check-Cashing Outlets in the U.S. Financial System

By John P. Caskey

**I**n the current debate over banking reform, some policymakers and consumer advocates have expressed concern that many lower-income Americans have lost access to basic payment services provided by banks. Reports of branch closings and increased service charges have led to proposals that banks be required to provide basic banking services to all consumers.

Most discussions of this issue are incomplete, however, because they overlook existing alternatives to banks for those who cannot or choose not to use banks to meet their payments needs. This article examines the role of check-cashing outlets (CCOs), a principal alternative to banks for many low and moderate-income consumers.<sup>1</sup> Despite evidence of rapid growth over the past decade, relatively little is known about the check-cashing industry. Understanding who uses CCOs and why provides new insight into the costs of payment services and adds a new dimension to the debate over basic banking services.

The first section of the article provides an overview of the check-cashing industry, including its services, fees, structure, and recent growth. The second section examines who uses CCOs and why, and offers possible explanations for recent growth. The final section addresses the regulation of CCOs and their possible role in providing basic banking services to low-income consumers.

## *An Overview of the Check-Cashing Industry*

The check-cashing industry began in the 1930s as a response to banking problems during the Depression and to changes in employer payment practices. CCOs originally specialized in cashing payroll checks but over the years have evolved to provide a

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variety of payments services. Largely unregulated, the check-cashing industry has grown rapidly in the past decade, expanding beyond its traditional base in urban areas.

### *Services provided by CCOs*

Nonfinancial businesses have cashed consumers' checks for many decades. Traditionally, this role was filled by bars, grocery stores, or other businesses that would cash third-party checks for regular customers or for customers making purchases. Such establishments rarely charged an explicit fee for cashing checks. The cost of the service was covered by the additional sales it generated.<sup>2</sup>

It is difficult to establish exactly when firms began to specialize in check-cashing and to levy a fee for the service. Most evidence suggests that CCOs evolved from other businesses that cashed checks on the side. CCOs apparently first appeared in Chicago and New York in the 1930s and spread to other large urban areas.

Most accounts cite widespread banking problems and changing employer payment practices as the principal factors motivating the early development of CCOs. For example, in Chicago, specialized check-cashing firms arose to provide payments services during the banking crisis of the 1930s (Illinois Department of Financial Institutions 1980). In addition, CCOs were stimulated by firms converting from cash payrolls to payroll checks during the 1930s and 1940s (Wolf).

The core business of a contemporary CCO is cashing checks for a fee. The fee is intended to provide the check-casher a profit after covering expenses, which include the cost of maintaining a storefront and insurance and personnel costs. Moreover, because the check-casher advances funds on checks that must subsequently be cleared through the banking system, CCOs incur interest expenses on the funds

advanced. And, CCOs run the risk that some cashed checks will be uncollectible because of insufficient funds or fraud.<sup>3</sup>

Because of the risks associated with advancing money on checks, many outlets cash only customers' payroll or government entitlement checks. Some CCOs also cash personal checks but typically charge a higher fee for this service to cover the higher risk that the check will bounce. Many CCOs cash personal checks only after they have confirmed with the bank it is drawn on that there are sufficient funds.

In some states, CCOs make "payday" loans. They do this by cashing a customer's personal check, which is sometimes postdated, and agreeing to hold it until the customer's payday. Since this amounts to making an unsecured loan, check-cashers generally charge much higher fees for this service. It is generally offered only to customers with stable employment records who have maintained bank accounts in good standing for several months.<sup>4</sup>

While most CCOs derive most of their revenue from check-cashing fees, almost all CCOs do more than just cash checks.<sup>5</sup> They typically offer a range of financial and nonfinancial services—they may sell money orders, make wire transfers of cash, and handle telephone and utility bill payments. In some states, they sell lottery tickets and public transportation passes, offer income-tax preparation services, and distribute welfare payments and food stamps. In addition, many sell cigarettes and candy or buy and sell gold jewelry.

### *Fees charged by CCOs*

CCO fees for cashing checks are usually expressed as a percentage of the face value of the check. In most states, check-cashers can charge whatever the market will bear; however, seven states currently set ceilings on check-cashing fees (Table 1).<sup>6</sup> As shown in the table,

Table 1

**Maximum Check-Cashing Fees in Regulated States**

(Rates are a percentage of the face value of the check)

<u>State</u>	<u>Legal ceiling rate</u>
Connecticut	2% for non-public aid checks and 1.0% for state public aid checks. (Ceiling fees set in 1990.)
Delaware	1% or \$4.00, whichever is greater. (Ceiling fee set in 1989. The previous ceiling rate was 0.5% or \$0.25.)
Georgia	The larger of \$5.00 or 3% for public aid checks, 10% for personal checks, and 5% for all other checks (payroll). (Ceiling fees set in 1990.)
Illinois	1.2% plus \$0.90. (Ceiling fee set in 1986. The previous ceiling rate was 1.1% plus \$0.75.)
Minnesota	2.5% for public aid checks above \$500 (5% for a first-time customer), no limit on personal checks but the rate must be filed with the state Commerce Department and be "reasonable," 3.0% on all other checks (6% for a first-time customer). (Ceiling fees set in 1991.)
New Jersey	1% for in-state checks and 1.5% for out-of-state checks or \$0.50, whichever is greater. (Ceiling fees set in 1979. The previous ceiling rates were 0.75% on in-state checks and 1.0% on out-of-state checks, or \$0.35.)
New York	0.9% or \$0.50, whichever is greater. (Ceiling fee set in 1988. The previous ceiling rate was 0.75%.)

Source: State regulatory agencies.

the maximum permissible fee sometimes varies, depending on whether the check is drawn on an in-state or an out-of-state bank or is a government entitlement, payroll, or personal check. The different ceilings on fees across categories reflect the different speeds with which checks clear, different default risks, and the desire to limit the fees that public aid recipients pay for cashing their entitlement checks.

Outside of these seven states, commercial check-cashing fees vary widely. In 1989, the Consumer Federation of America (CFA) conducted a survey of the fees levied at check-cashing outlets in 20 major cities across the

United States (Table 2). This survey suggests that CCOs charge roughly similar fees for payroll and government support checks.<sup>7</sup> For both types of checks, fees range from about 1.0 percent to 3.0 percent of the face value of the check, with an average rate of about 1.75 percent.<sup>8</sup>

About a third of the check-cashing outlets contacted by the CFA were willing to cash personal checks. Not surprisingly, given the default risk, they charge far more for this service. In the survey group, fees ranged from 1.66 percent to 20 percent of the face value of the check and averaged 7.7 percent.<sup>9</sup>

Table 2

**National Check-Cashing Fees**

<u>Service</u>	<u>Minimum charge</u>	<u>Maximum charge</u>	<u>Average</u>
Payroll checks	.9%	3.0%	1.74%
Government checks	.9%	3.25%	1.73%
Personal checks	1.66%	20%	7.7%
Money orders (\$50)	\$.19	\$.99	\$.55

Source: Consumer Federation of America (1989).

CCOs also levy fees for the other financial services they provide, such as selling money orders or making wire transfers. These services are largely used to pay bills by customers who do not have checkable bank deposits. The data suggest that many CCOs set low prices on these services. For example, the CFA survey found that the average charge for a \$50 money order was \$0.55, and many CCOs charged a flat fee independently of the size of the money order. This compares favorably to the \$0.75 charged by the U.S. postal system for money orders up to \$700.<sup>10</sup>

**Structure of the industry**

An examination of the structure of the check-cashing industry indicates commercial check-cashing is a relatively large industry, dominated mainly by local owner-operators. Historically, CCOs have been regulated extensively in only a few states. However, this picture is changing as national chains begin to develop and as more states consider regulating CCOs.

CCOs are currently regulated in only eight states. Seven states set ceilings on check-

cashing fees and require that CCOs be licensed and abide by other regulations. These regulations generally require check-cashers to post their fees in a prominent location in the outlet and to provide customers with receipts. Often, the regulations require the CCO owner to meet a minimum bonding or capital requirement. Some states prohibit newly opened outlets from locating within a specified distance of existing CCOs. All states specify record-keeping requirements for the firms, and several of the states require check-cashers to report large sales of money orders or large wire transfers. This is to prevent check-cashing firms from being used in a money laundering process. Typically, the state banking department is responsible for issuing licenses and enforcing the regulations.

Because only a few states regulate the commercial check-cashing business, it is impossible to know exactly how many check-cashing firms are currently operating. However, across the United States there were 4,289 yellow-page listings of check-cashing firms in early 1991. This count is a lower-bound estimate of the total number of commercial check-cashing outlets

nationally. In six of the eight states that require CCOs to be licensed, for example, the yellow-page count closely approximates the number of licenses outstanding. However, the yellow-page count understates the number of licensed outlets in New York by about 20 percent and by almost 50 percent in Georgia.

Given the sparse information on the industry, any estimate of the size of the industry in dollar terms is subject to a large margin of error. However, a conservative estimate indicates that the industry cashed about 150 million checks in 1990 with a combined face value of \$45 billion. From this activity, the check-cashing industry earned approximately \$790 million in fees.<sup>11</sup>

The vast majority of CCOs across the country appear to be owned by local independent operators, many of whom own three to ten outlets in a given area. There is evidence, however, that large national chains are developing. For example, one check-cashing company owns over 100 stores in the Northeast and is publicly traded on the over-the-counter stock market. And some check-cashing franchise operations have grown rapidly in the past few years. Recently, Western Union, which has provided money-wiring services to many check-cashers, announced plans to develop a national network of check-cashing outlets (*Wall Street Journal*).

### ***The growth and location of the check-cashing industry***

Data on the check-cashing industry are sparse but nevertheless indicate that the industry is growing rapidly. Moreover, the evidence suggests that the industry is beginning to expand beyond its traditional concentration in lower-income urban areas.

In interviews, check-cashers who have been in the business many years said that the

industry grew slowly until the early or mid-1980s and then expanded rapidly. Unfortunately, there is not sufficient data to confirm this view.<sup>12</sup> However, American Business Information (ABI), a firm that tracks yellow-page listings of businesses, reported 4,289 listings of check-cashing (or currency exchange) outlets nationally in July of 1991. In 1987, the earliest year it provided data, ABI reported just 2,151 national listings. Thus, in four years, the industry appears to have doubled, a phenomenal growth rate.

Existing CCOs are disproportionately located in major urban areas, generally in low and moderate-income neighborhoods. For example, in eight states fewer than 10 percent of the CCOs are located in cities of less than 100,000.<sup>13</sup> The Illinois Department of Financial Institutions (1980, p. 107) reported that of 624 licensed check-cashers in the state in 1985, 90 percent were located in the Chicago area. And, a study for the New York State Banking Department found that 69 percent of all check-cashing outlets in New York City in 1990 were located in low-income census tracts (Kemlage and Renshaw).

The evidence suggests that the recent growth in CCOs has been uneven, with especially rapid growth outside of the few major urban areas where check-cashing establishments have long existed. For example, yellow-page listings from late 1988 to early 1991 show growth rates for Illinois, New Jersey, and New York of below 20 percent. Over that same period of time, the number of listed check-cashers grew by 85 percent in Florida, 195 percent in Georgia, 96 percent in Missouri, 293 percent in North Carolina, 80 percent in Texas, and 87 percent in Washington.

In states with early and well-developed check-cashing industries, recent growth has occurred mainly outside of the traditional inner-city areas. For example, the Illinois Department of Financial Institutions (1989, p. 5) reported

that from 1985 to 1989, 108 new check-cashing licenses were granted but only 13 of these were for locations in Chicago; 75 were for locations in the Chicago suburbs and the remaining 20 were for downstate locations.

### ***Explaining the Use and Growth of CCOs***

Understanding the reasons behind the recent growth of check-cashing firms requires knowledge of who uses them and why. This section compares the cost and types of services offered by banks and CCOs, presents recent survey evidence on usage of CCOs, and examines factors behind their recent growth.

### ***Comparing banks and CCOs***

Since both banks and CCOs provide basic payments services, a key question is why consumers use CCOs rather than banks. One possible explanation is that CCOs are cheaper than banks. Or, perhaps CCOs are more convenient than banks or provide a type of service that banks are unable or unwilling to provide.<sup>14</sup>

The information on fees presented earlier can help provide an estimate of the cost to a household of meeting its payment needs through a CCO. For example, assume a family cashes its paychecks or government entitlement checks at a check-cashing firm charging a 1.5 percent fee and buys six money orders a month at an average price of \$0.50 per money order. In this situation, a family with a \$10,000 yearly income (about 75 percent of the 1990 official poverty level for a family of four) would spend \$186 annually on basic financial transactions. Since check-cashing fees are a fixed percentage of the value of a check, a family with higher income would pay more. Thus, in this example a family with \$24,000 annual income would spend \$396 annually for financial services.<sup>15</sup>

The cost of obtaining similar services from a bank would be somewhat less, according to a 1990 national survey of bank fees by the Consumer Federation of America (1990). In estimating the cost of a checking account based on its survey data, the CFA assumed that a family maintains an average balance of under \$400 in the account and that the account balance falls below \$200 only once a month. In addition, the CFA assumed the family writes ten checks, makes four ATM withdrawals, and two deposits monthly and, over the year, the family bounces two checks and deposits one check that fails to clear. Based on this behavioral pattern, the CFA estimated that a family would pay \$107.96 a year to maintain a noninterest-bearing checking account and would pay \$111.39 a year to maintain an interest-bearing NOW account.

Regardless of the type of account maintained, it appears a family would save significant out-of-pocket costs by conducting its financial transactions through a bank rather than a CCO.<sup>16</sup> Because the fees for cashing checks at a CCO are assessed as a percentage of the face value of the check, the difference can be small for very low-income households. For example, a family earning \$10,000 a year would save only about \$80 annually by using a checking account rather than a CCO, while a family earning \$24,000 a year would save almost \$300. However, the very poorest households may be least able to afford the additional cost.

Two explanations account for the success of the check-cashing industry in the face of this cost disadvantage. One explanation is that out-of-pocket expenses do not measure the full cost of using a financial institution. Convenience, quality, and type of service also matter. In these aspects, CCOs may have an advantage for many consumers since most CCOs have much longer opening hours than do banks and are located more conveniently for some consumers. Also, CCOs may be faster with the range of simple

financial transactions in which they specialize.

Another explanation for the success of CCOs is that bank services do not fully substitute for CCO services. Most important, while CCOs are willing to assume the risk that a check they cash will bounce, banks generally will not. Most banks require a consumer to maintain a deposit account in order to cash checks, even government checks with a negligible default risk.<sup>17</sup> For depositors, most banks require the customer either maintain sufficient funds in an account to cover the check or wait a few days for the check to clear. If the check fails to clear and the bank has cashed the check for a customer with sufficient funds to cover it, the customer's account is docked for the amount of the check. Moreover, many banks charge the customer for the bank's cost of handling a "returned" deposit.

Because of these differences in check-cashing policy, consumers without bank accounts may be forced to take their business to CCOs. Moreover, even if they maintain a bank account, consumers may not be able to cash a paycheck or government assistance check because the amount exceeds their account balance. Although these consumers could save money by depositing their check in a bank and waiting for it to clear, they may prefer to pay a fee to have the cash immediately.

### ***Evidence on CCO use***

Surveys of who uses commercial check-cashing firms and why they choose to do so suggest that most customers are either low-income to lower-middle income workers cashing payroll checks or recipients of government transfer payments. Relative to the population as a whole, a disproportionate percentage of CCO customers are young, nonwhite, and do not have bank accounts. Limited access to banking services and the convenience of CCOs appear to be

the most important factors governing their use.

This profile of CCO customers is drawn from two recent surveys. One, a survey by the Consumers Banking Association (CBA), focused on consumers cashing paychecks. A second survey, conducted by the New Jersey Department of the Public Advocate, concentrated on those cashing public assistance and social security checks.<sup>18</sup>

The CBA survey found that CCO customers were younger and poorer than the general population and more likely to be a racial minority. Thirty-seven percent of respondents were between the ages of 18 and 30, and 29 percent reported a household income of less than \$15,000 a year. The median reported household income in the survey was \$20,400 as compared with a 1985 national median family income of \$28,906. While 33 percent of respondents were white, 47 percent were black and 18 percent hispanic.

The survey found that customers' reasons for using a CCO revolved around their access to bank services. Two-thirds of customers surveyed had deposit accounts at banks or other financial institutions. Only 13 percent of these customers used CCOs regularly, citing convenience and ready access to cash. In contrast, the one-third of CCO customers without bank accounts made more regular use of CCOs. For those customers, lack of funds to maintain bank minimum balances and high bank service charges were cited as the main reasons for use of CCOs.<sup>19</sup>

The study by the New Jersey Department of the Public Advocate provides a somewhat different portrait of the customer base of the check-cashing industry because it focuses on those cashing public assistance and social security checks.<sup>20</sup> The Department interviewed 750 recipients of government transfer payments. In contrast to the CBA survey, 92 percent of those interviewed said that they did not

have a bank account. Fifty-seven percent were cashing Aid to Families with Dependent Children (AFDC) checks. Another 20 percent, were cashing social security checks, and the rest were cashing unemployment benefits, veterans assistance, or state disability checks.

In the New Jersey survey, 79 percent of those interviewed stated that they never go to a bank to cash their government checks and, of these, 61 percent said they only go to CCOs. When asked why they were using a CCO to cash their government check, respondents cited lack of access to bank services and the convenience of CCOs.

### ***Factors behind CCO growth***

Knowledge of who uses CCOs and why is important for understanding the rapid growth in the industry during the 1980s. Changes in the economic situation of households may have led to an increased demand for check-cashing services. At the same time, regulatory changes may have increased the cost of banking services.

One factor contributing to the growth of CCOs may have been the strong growth in payroll employment following the 1982 recession. From 1983 to 1989, total civilian employment increased 16 percent (*Economic Report of the President*). Unlike the economic expansions of the 1960s and 1970s, however, employment growth in the 1980s was accompanied by a fall in employees' real incomes. For example, average weekly earnings of private sector, non-agricultural, industrial workers fell from \$408 in 1978 to \$346 in 1990.<sup>21</sup> Because the customer base of CCOs is disproportionately low-wage and moderate-wage workers, lower real incomes may have contributed to the demand for CCO services.

More generally, the 1980s saw a fall in the standard of living for many low-income families. From 1979 to 1988, the mean real

family income of families in the lowest income quintile fell 5.4 percent (Bradbury, p.26). And, the number of families falling below the poverty line rose from 24.5 million in 1978 to 31.9 million in 1989 (*Economic Report of the President*). To the extent that poorer families had increased difficulty in accumulating financial savings to maintain bank balances, they may have had an increased incentive to use CCOs.

The 1980s also saw changes in the cost and supply of banking services. In 1980, the federal government enacted the Depository Institutions Deregulation and Monetary Control Act. Among other things, this act began a phaseout of ceilings on the interest rates banks could pay on deposits. The Act also required the Federal Reserve System to begin charging banks for a number of services it had previously provided for free.

Another factor was a change in the attitude of bank regulators at the federal and state levels toward competition among banks. Prior to 1980, regulators often looked unfavorably on a proposed branch that would be located in a community already well-served by other bank branches. However, after 1980, in an atmosphere much more favorable to free-market competition, regulators began to consider the increased competition provided by an additional community bank to be a positive factor in approving new bank branch applications (Spong).

Following these changes, banking became a much more competitive business. Banks reacted by pricing services based on the costs of providing those services. Thus, they began to charge for accounts with high transactions volume and small balances, significantly raising the cost of using banks for many low and moderate-income consumers (U.S. GAO). Bankers also reacted to the increased competition by closing branches in unprofitable or marginally profitable areas, which were often



low-income areas, and opening branches in the more desirable, higher-income areas already served by other banks.<sup>22</sup> Combined, these changes worked to make banks both more expensive and less convenient for many low-income and moderate-income consumers, and likely contributed to a growing demand for commercial check-cashers' services.

Finally, the rapid growth in the check-cashing industry in the 1980s may have been stimulated by an increased awareness of the market potential of the millions of Americans who do not regularly use the banking system for their financial transactions. Beginning in the mid-1980s, journalists, academics, and policy analysts began to write about bank closings in low-income neighborhoods and the large number of households not using banks.<sup>23</sup> These reports may have captured the imagination of entrepreneurs and fed the expansion of nonconventional financial institutions serving those whose needs were poorly met by banks.

### ***Public Policy Issues***

Recognizing that CCOs are playing a more important role in the U.S. financial system raises a number of public policy issues concerning CCOs and the delivery of affordable financial services to low-income households. This section considers the trade-offs in regulating CCOs and the role they could play in the financial system.

### ***Regulation of CCOs***

Bank closings in low-income communities, increases in bank fees on small deposit accounts, and the rapid growth of the check-cashing industry have made the policies of CCOs far more relevant than the policies of banks for many segments of the population.

This observation has led to suggestions that

the check-cashing industry be more widely regulated. Those advocating that more states, or perhaps even the federal government, should regulate the industry point out that many check-cashing customers are relatively unsophisticated consumers, with little social or economic power. These customers might be grossly overcharged by an unscrupulous operator, some of whom may have local monopoly power. Thus, there is concern that many poor and moderate-income individuals could spend a large percentage of their limited disposable incomes for basic financial transactions.

Indeed, evidence supports the concern that some check-cashing firms levy relatively high fees. For example, the survey by the Consumer Federation of America (1989) found that 11 percent of the firms charge 3 percent or more for cashing government entitlement checks. In New Jersey, for example, check-cashers are limited by law to charging 1.0 percent on in-state checks and 1.5 percent on out-of-state checks. Of 662 customers there who reported the amount of the check they cashed and the amount of fee they paid, 49 percent were charged more than the legal maximum (New Jersey Department of the Public Advocate, p. 29). On average, check-cashers overcharged by about 44 percent of the ceiling rate, and in some cases the excess charge was substantial. To cite two examples from the report: a Hispanic woman who could not speak English was charged \$25 for cashing a \$268 social security check, and another woman was charged \$16 for cashing her \$525 AFDC check.<sup>24</sup>

Interestingly, in its response to the study by the Department of the Public Advocate, the New Jersey Department of Banking, which oversees check-cashing outlets, reported that it had received only one check-cashing complaint over two years (GAO, p. 9). It appears, therefore, that the vast majority of people who were charged more than the legal maximum in New

Jersey did not complain to the oversight agency, perhaps because they were unaware of the overcharge, felt a complaint would be ineffective, or did not know how to file an official complaint or felt that the effort was greater than the cost of the overcharge.<sup>25</sup>

Those who favor limits on check-cashing fees need to be aware of possible consequences, however. Mandating very low check-cashing fees could kill the industry and hurt the low and moderate-income people who have no realistic alternatives for cashing their checks. Prior to 1989, for example, Delaware limited check-cashing outlets to charging a fee of 0.5 percent of the face value of the check or \$0.25, whichever was greater. In 1989, the state raised the limit to 1.0 percent or \$4.00, whichever is greater, noting that no CCOs were operating in the state under the old law.

On the other hand, it is clear that CCOs can flourish in urban areas when the ceiling rate is around 1.0 to 2.0 percent.<sup>26</sup> In New York, for example, the ceiling rate is 0.9 percent or \$0.50, whichever is greater. Yet over 400 check-cashing outlets operate in the state. Illinois, which permits check-cashers to charge up to 1.2 percent of the face value of the check plus \$0.90, has more CCOs per capita than any other state.<sup>27</sup>

The evidence suggests, therefore, that if regulation of CCOs is deemed desirable, states can set limits on check-cashing fees to protect consumers against the highest charges and yet permit the industry to flourish. The evidence from New Jersey also suggests, however, that the state must devote resources to enforcing compliance with the statute. In New York and Illinois, where the state banking departments conduct annual on-site surveys of CCOs, firms do not appear to charge more than the legal maximum. Presumably, annual license fees from CCOs can provide the states with the revenue to cover the costs of monitoring the industry and enforcing state legislation.

### *The role of CCOs in the financial system*

The 1980s have seen increased emphasis on the access lower-income households have to affordable basic financial services. Legislatively, this concern has been expressed in congressional hearings or proposals to force banks to cash government entitlement checks for free and to offer "basic," or "life-line," bank accounts (U.S. Senate, U.S. House 1989).<sup>28</sup> Such accounts would permit a consumer to conduct a limited range of basic financial transactions for a very small fee or no fee. Regulators and community activists have also used the Community Reinvestment Act and other means to bring pressure on banks to keep branches open in low-income areas and to improve banking services in these communities.<sup>29</sup>

However, the possible cost or effectiveness of these proposals has also caused concern. For example, if banks are forced to provide these services without sufficient compensation, the burden might not be shared equally among banks. Indeed, banks with existing branches in low-income areas could be most affected. Moreover, imposing such policies on banks but not their competitors could place banks at a competitive disadvantage and, perhaps, lead to an acceleration of bank branch closings.

Recognition of the growing importance of CCOs, however, suggests that they might play a role in providing basic financial services to low-income households. CCOs specialize in delivering a narrow range of payments services. With experience, they have learned which financial services are most in demand by lower-income households and have learned to minimize the cost of providing these services. CCOs already compete for locations that are most convenient for the low-income and moderate-income households that make up their customer base.

By viewing CCOs as an integral part of the financial system, federal, state, and local

governments may be able to work with them to ensure that they deliver affordable basic payments services. Indeed, a number of states already appear to be taking this approach, using CCOs in the distribution of public benefits and services. For example, residents of New York City and Chicago can elect to receive their AFDC payments or food stamps through local CCOs. In New York, the state pays the CCO to distribute AFDC benefits in cash. In Illinois, the CCOs handle the distribution of AFDC checks for free, but if the recipients cash their checks at the CCO, they pay the regulated state fee. And, in Illinois, many CCOs have the right to handle automobile registrations and title transfers.

The suggestion that CCOs be used as delivery points for government services is linked with the view that they be more widely regulated. This is true for two reasons. First, in a state where CCO fees and services are regulated, the industry is likely to have a better public image and therefore is more likely to be trusted for distributing public services. Second, because permitting CCOs to distribute AFDC payments, handle automobile registrations, or provide other public functions is profitable for CCOs, such opportunities can be traded for lower ceilings on the fees CCOs levy for basic financial services.

Realistically, however, advocating broader regulation and reliance on CCOs for the delivery of basic financial services does not require abandoning efforts to improve the accessibility of banks for lower-income households. While CCOs provide some basic payment services,

they are not substitutes for banks. CCOs do not take deposits, so residents of a community served only by CCOs would not have a safe and convenient outlet for their savings. And, CCOs also do not make loans, so the economic development of a community served only by CCOs may suffer.

### *Summary*

This article has surveyed the role check-cashing outlets play in the financial system. CCOs provide basic financial transaction services to many low-income and moderate-income households. And, measured by the number of outlets, CCOs may be the most rapidly growing segment of the financial system. Households that consistently use CCOs appear to devote a larger fraction of their incomes on average to pay for financial transactions than do families that rely on banks. Some use of CCOs appears to be voluntary. Consumers may turn to them rather than to banks because CCOs have a more convenient location or longer hours of operation. However, some consumers may turn to CCOs because they cannot afford to meet minimum balance requirements at banks.

For many moderate-income and low-income households in urban areas, a CCO may be the most important financial institution in their daily lives. This observation has led an increasing number of states to regulate CCOs and suggests that CCOs might be employed in the delivery of basic financial services and government benefits.