

CREDIT Connect

March 2007

Prepare for the Prepaid

Consider the many faces of prepaid card programs

Increasingly, consumers are choosing electronic payment tools over checks, a fact which is leading many credit unions to enter the world of prepaid cards. According to IDC Financial Insights, consumers spent \$160 billion on prepaid cards in 2004 and were projected to spend \$290 billion in 2006. Clearly, prepaid cards are an emerging market worth close examination.

However, as consumer interest in prepaid cards has risen, so has the variety of prepaid cards available. For credit unions seeking to enter the prepaid card market, these new possibilities can make launching a prepaid card program a complicated endeavor. The prepaid gift card began simply enough – functioning basically as the traditional gift certificate of old, except that it could be used almost anywhere. Cards grew from there to include instant-issue and reloadable options. Now the evolution of the market has produced variations for many niche markets such as travel cards, teen cards, health savings account cards and payroll cards.

The support and infrastructure necessary for the different types of prepaid cards vary greatly. So how does a credit union determine which types of prepaid cards will benefit their members and prove profitable? The first step is learning more about the options available and the major considerations inherent with each.

Reloadable Cards

Reloadable cards take gift cards to the next level. Instead of a one-time-use gift, they become a money management tool. Reloadable cards most often can be reloaded at the facility where they were purchased, over the phone or online. Reloadable cards often provide a better option for some members and some potential members of the underserved population than a traditional checking account.

Many reloadable cards are used to target a specific niche market and are a relatively easy step into expanding a basic prepaid card program. These cards offer a way to market prepaid cards that reach beyond gift-giving opportunities. Specialized cards like teen cards and travel cards help members view prepaid cards in a whole new way.

Teen cards, such as the Visa® Buxx Card, offer convenience and independence to teens and security and control to parents. With this program, parents can load the card online or over the phone. Teens learn responsibility and

independence, and parents are still able to monitor spending. Parents and teens can check account balances and purchases online to train teens in money management. Teens have the opportunity to try their hand at managing their finances without the risk of it becoming a costly experiment.

The VISA Buxx cards, available to anyone but targeted to teens, can be used for emergencies or as a main payment method. The Visa Buxx card can be used everywhere a Visa debit card is accepted. According to The Point for Credit Union Research and Advice, Bellico Federal Credit Union in Wyomissing, Pennsylvania added this prepaid card to their youth program in answer to their youth advisory board's desire for a no-fee debit card.

Credit Union Management magazine reports that young people from 13 to 19 are one of the fastest-growing population segments, according to 2000 U.S. Census data. A teen prepaid card program can offer credit unions the opportunity to capture this potential business as well as attract new members and strengthen relationships with existing members in this crucial age category.

Travel cards work much the same way as teen cards. This program is positioned as a safe and convenient alternative to traveler's checks and cash. The Visa TravelMoney card can be reloaded where the card was purchased or by phone, and can be used to obtain local currency at Visa ATMs around the world. It also offers credit card-like benefits, such as lost luggage reimbursement, purchase security and travel and emergency assistance. GCUA will launch a turnkey general-purpose reloadable card through the Illinois Credit Union League in 2007.

Payroll Cards

One of the newest prepaid card options is the payroll card. This card, designed to take the place of payroll checks, is gaining attention among many companies throughout the United States. Payroll cards look and act just like debit cards that are loaded with value by employers each payday. According to Financial Insights, a Framingham, Massachusetts-based research firm, about 10 percent of Americans currently use payroll cards.

Companies are attracted to payroll cards by the cost-savings they represent. Payroll cards eliminate the administrative costs associated with printing and distributing paper checks. For employees, payroll cards eliminate the time it takes to cash checks as well as check-cashing fees.

Is there a downside? From a credit union perspective, there could be. Implementation and administration of these cards can be costly. For a credit union to offer payroll cards to a field of membership, consisting of many small SEGs, would be impractical and cost-prohibitive at best.

However, there are situations where payroll cards can be the key to strengthening or solidifying a relationship with a large sponsor group. If a single-sponsor credit union's sponsor company desires to convert its payment system to payroll cards, adding this program could be vital.

Health Savings Account Cards

Prepaid cards linked to Health Savings Accounts are growing in popularity. Legislation to establish Health Savings Accounts (HSAs) was signed into law by President Bush in 2003. These tax-sheltered savings accounts allow tax-free contributions and withdrawals for purchases earmarked for medical expenses. Individuals with high-deductible medical plans are eligible to open HSAs. Funds from an HSA not used in a calendar year stay in the account and continue to accrue interest on a tax-favored basis.

Prepaid cards linked to HSAs provide consumers a simple way to pay medical expenses directly, rather than filling out reimbursement forms to cover eligible expenses. Use of a prepaid HSA card is as easy as swiping a card. The purchase amounts are then deducted from the linked HSA account. Members are required to limit their own spending from these accounts to approved medical expenses only and document these expenses for tax-reporting purposes. Credit unions are not required to monitor how the money is spent.

Prepaid HSA cards offer credit unions the opportunity to tap an emerging market for interchange income. This service can also provide credit unions with a tool to acquire deposit accounts and retain members. This year, TowerGroup estimated that HSA deposits would grow to more than \$26 billion by 2010.

However, the market is not without competition. Not only are financial institutions beginning to offer HSAs, insurance providers also see the HSA market as an emerging opportunity. Blue Cross has started Blue Healthcare Bank and United Health Group has started Exante Bank in order to provide HSAs to individuals who are insured via a high-deductible health plan (HDHP).

Some credit unions have found that by offering lower fees and administrative costs, it is easy to compete with these large providers of HSAs. Credit unions can have an advantage by establishing early relationships with their SEGs as they begin to offer HDHPs. If the credit union knows when SEGs are going to offer these types of health plans, they can work with the groups from the beginning to meet the changing needs of their employees, reinforcing the benefit of the credit union relationship. The SEG has the ability to offer HSA options to employees when they sign up for the HDHP.

Such is the case for The Coca-Cola Company Family Federal Credit Union. Their sponsor company is rolling out their "Catastrophic Insurance Plan" option in 2007. Early in their

planning stages, they approached the credit union about providing HSAs. The credit union developed a simple savings program with an ATM card, which will be ready for deposits in January 2007.

"We are positioned well as we are closely aligned with our single sponsor and conveniently located to our most likely users," says Anna Copello, Vice President of Operations for The Coca-Cola Company Family FCU. "Early demand for HSAs across the industry seems to be more for investment and less for transaction use. As demand for HSAs grow and as the account owners change how they use the account, our program can be updated and expanded to offer more options like checking or share certificates."

The major consideration for credit unions is a cost verses demand analysis. The results of a 2006 Wolters Kluwer Financial Survey indicate that 57 percent of respondents that currently do not offer HSAs cite low customer demand as the reason for their decision. However, demand for HSAs may soon be on the rise. The annual deposit ceiling will be increased in 2007 and members will be permitted to make a one-time contribution from an IRA to an HSA account. These changes indicate that legislators are working to make HSAs a more attractive and viable option for employees without health insurance or with HDHPs. Credit unions with large sponsor groups that choose high-deductible health plans and contribute to employees' HSAs may find prepaid HSA cards a boost to income and a valuable member-retention tool. Beyond the costs associated with offering prepaid HSA cards, the largest consideration is the need for the introduction of risk management profiles associated with the product.

The expansion of the prepaid card market provides almost all credit unions an opportunity to grow business, earn income and retain members. However, determining which type of card will work in a specific situation can be a challenge. Credit unions that are seeking help to find the right prepaid card program may contact Dawn Colegrove at (800) 768-4282 or dawnc@gcu.org. Credit Unions may also contact Maureen Bock at maureenb@gcu.org.

EFT Council Meeting

March 2, 2007
Commerce Club
Atlanta, Georgia
10:00 a.m. – 1:30 p.m.

Topics include:

VISA Security Strategy

Eduardo Perez, Vice President, Payment System Risk
Visa U.S.A., Inc.

Health Savings Accounts

Scott Harward, President
Pilot HSA

Health Savings Accounts

Bruce Fafard, Vice President, Sales and Service
Connex Credit Union

To register, contact Cindy Tuttle or Dawn Colegrove
770-476-9625.