

## A TALE OF PRODUCT INNOVATION

by [Steve Brown](#)

The hottest product in banking remains the remote deposit via mobile device. Pioneered by USAA and made available to the mass market by Chase, the product has also made it into dozens of community banks with strong customer acceptance. While we have not had a chance to review profitability, our guess is that the product is well on its way to prove itself not only for how it increases balances, but also how it decreases interest rate sensitivity. Before you think that your bank has to be "bleeding edge" to adopt remote check deposit for retail, we highlight the forerunner to this service first introduced by Pennsylvania State Employees Credit Union (PSECU), a 300k member credit union based out of Harrisburg, PA.

Back in 2001, PSECU introduced its "UPost@Home" product that allowed qualified (i.e. credit worthy) customers to go online to register a check they would like to deposit. Customers would fill out the required information such as Payee, amount, routing number, etc. and then enter the information into PSECU's database. The customer would then get immediate credit for up to \$8,000 (most customers start with a \$1,500 limit) and have 10 days to mail in the check (otherwise a penalty is assessed and a possible hold is put on the account). The process is made easier by the postage paid envelopes that PSECU supplies.

When we highlighted the product back in 2004 at our High Performance Workshop, many banks laughed and said the product would never get by their compliance department for fear of fraud. While we understand the concern, similar to remote deposit capture via scanner or phone and online account opening, fraud and compliance turns out to be a convenient proxy many use for fear of the unknown. While PSECU had the same internal debate, their position is that if their mission is to really serve the customer, then they should learn to trust the customer. PSECU decided to take a chance in a pilot program, in order to actually see what kind of fraud would occur. The ironic part is, despite dozens of meetings, hours of analysis and many naysayers, fraud has played little role so far in this system that largely relies on the honor of the customer. In fact, many customers recognized the trust that was being placed in them and went out of their way not to abuse the system, by making sure checks were mailed right away.

As of the end of 2010, PSECU had processed more than 4.5mm items through this product worth over \$1.4B (an average check amount of about \$315) of deposit balances. Penetration is about 23% of its customer base and the product produces a steady stream of about 100k items per month. The cumulative total of losses since inception has been \$74k - a loss rate of 0.5bp or 1.6 cents per item. To put these numbers in perspective, the average per check loss rate for our industry (through all channels) is about 3.5 cents per item. Despite much lower handling costs and inspection time, the loss rate for this product is below the rate for about 70% of community bank branches! Further, what PSECU lost in fraud, it more than made up for in savings of interchange fees had customers deposited checks through ATM networks.

While this product isn't for all retail community banks, it is a shining example of financial service innovation. While low tech in process, the system is brilliant in execution and shows that creativity, not technology, is often the limiting factor when it comes to designing bank products.

# BANK NEWS

## **FHA Waiver**

The FHA will allow banks with assets below \$500mm to submit their 4Q Call report in lieu of audited financial statements for FHA lender approval or renewal. The waiver applies only to the audited financial statements requirement and these banks would still need to provide an independent auditor's opinion of internal control and compliance with HUD programs.

## **No Equity**

FHLMC is reporting the percentage of homeowners that refinanced their loan last quarter that took out a mortgage for a larger amount than the original loan dropped to only 23% - the lowest level in 15Ys. Meanwhile, 26% chose to pay down part of their previous mortgage, while the rest refinanced for the same amount.

## **More Arbitration**

Large banks stung by consumer lawsuits have turned to mandatory arbitration to reduce legal costs. A recent survey finds 75% of 265 account types offered by the 10 largest US banks had mandatory arbitration provisions.

## **Competition**

Banks are arguing that Wal-Mart's significant expansion into check-cashing and prepaid debit cards indicate the company is a "larger participant" in financial services that should be subject to inspections from the Consumer Financial Protection Bureau.

## **Scary Stat**

In NV, the worst state in the country for foreclosures, the NAR reports 23% of delinquent borrowers walked away from their homes by choice (strategic default).

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