Project Name:

Auto Savings

Team Name:

Buzzworthy Trifurcators

Team Participants:

Kim Vu Assistant VP, Private Banking Technology Credit Union San Jose, CA kvu@techcu.com	Michael Murphy Executive Vice President / COO Motorola Employees Credit Union Schaumburg, IL mmurphy@mecunet.org	Tim Mislansky Senior Vice President Wright-Patt Credit Union, Inc. Fairborn, OH tmislansky@wpcu.coop
Lori Hall Vice President of Marketing and Operations American Airlines Federal Credit Union Fort Worth, TX lori.hall@aacreditunion.org	Steve Fifield VP of Branches, Sales & Service Cyprus Federal Credit Union West Jordan, UT sfifield@cypruscu.com	David P. Faleski VP | Marketing Coastal Federal Credit Union Raleigh, NC dfaleski@coastalfcu.org

Opportunity -- Solution

America is a country of consumption, a land of people wanting to keep up with the Joneses. Today, the vast majority of American's must have the latest gizmo and stay current with the newest trends. Beyond their investment in a home and contributions made to their employer's retirement plan, Americans simply aren't saving. In fact, during 2006 the personal savings rate in this country reached a negative one percent of disposable income.[1] Too many people live paycheck to paycheck and are a small step away from financial disaster. At the same time American's are not saving, they are increasing their debt burdens. Seven out of ten low and middle income households reported using their credit cards as a financial safety net rather than savings.[2]

Despite these discouraging facts, 77 percent of Americans still look for ways to save but find it difficult because they lack discipline.[3] Consumers who are able to save often employ unorthodox means, such as using their tax refund as a method of forced savings. It is clear that for many undisciplined savers, an "out of sight out of mind" approach is the key to a successful savings strategy. In addition, most Americans find it more satisfying to buy things rather than save. An opportunity exists to tie savings to consumption.

There are a number of examples of successful ventures where a savings component has been tied to purchases. Some recent examples include Bank of America's "Keep the Change Program" where debit card transactions are rounded up to the next dollar and the funds are placed into a savings account. Another example is Upromise[4]- where merchants pay a percentage of sales to a college savings account. These savings programs have several common themes. They are easy to enroll. They are simple to participate in. They put savings "out of mind" as it occurs in conjunction with the consumers' buying habits. As many Americans want to build savings, they struggle to change their habits. Successful savings program do not try to alter consumers' behavior, but rather capitalize on it.

The lack of savings has lead to a number of groups working to develop solutions. New public policy is being designed to find innovative methods to encourage consumers to save and build financial strength. The Aspen Institute is a leading policy program working to create smart solutions that help Americans save, invest and own thereby creating a savings culture.[5] According to the Aspen Institute, nearly half of working Americans do not own any type of personal retirement account. Current federal savings programs don't reach one in three Americans.

Our "Auto Savings" innovation moves down the road to build savings around the transaction of borrowing money to buy a vehicle. This simple, yet effective solution promotes forced savings implemented as a contractual add-on to an auto loan. Members borrow from the credit union to purchase (consume) an automobile and sign a contract with the credit union to add a specific amount to each loan payment in order to accumulate savings. Substantial penalties are applied to members who break the contract.

Surveys conducted during the development of this concept indicated that—if offered—members would be likely to tie a savings component to their car loan payment. In the responses of over 3,300 members, the survey indicated:

- 60%of respondents answered, “I don’t save” or “I don’t save outside my retirement saving.”
- 58% of respondents answered they would be “likely” or “very likely” to participate “If given the option of adding a fixed dollar amount (say $20) to your loan payment to go into a saving account, how likely would you be to use it?”
- 64% of respondents answered, “It would be easier to save if it were included in my loan payment.”
- The likelihood of usage of Auto Savings increased at lower income levels and at younger ages, but not by significant margins.

Member Benefits

The Auto Savings program offers several distinct advantages over traditional forced savings methods (like awaiting a tax refund or placing money in an envelope), or the alternative, not saving at all. Consumers who opt for this savings program will benefit in several ways:

- Starting the process requires little effort on behalf of the member
- Building saving balances through an easy and effective method
- Establishing sound savings habits that are reinforced with each loan payment
- Creating an emergency fund and peace of mind

The member can easily enroll at the same time they complete their loan paperwork. They determine the amount to save and electronically transfer the savings amount with their regular loan payment. Then, each month, the “new” loan payment is made and the extra funds to be saved are automatically transferred to a special certificate (or other sub-savings account as determined by the credit union). The member is able to track their progress through online banking or via their monthly statement.

The Auto Savings is a simple, yet effective savings solution for members.

Credit Union Benefits

The Auto Savings solution can greatly impact a significant number of members. In fact, the altruism of program should be realized up front and actually become the overall objective. More than “people helping people,” the Auto Savings is designed specifically to help those of modest means build and achieve wealth. It takes credit unions back to their original concept of helping create thrift.

In addition to providing the benefit of promoting sound savings habits, the program can be added to a credit union’s menu of products with a low cost and easy administration.

The Raddon Financial Group reports that the average savings account costs less than $60 per year for most institutions. Typically, credit unions have the ability on their computer systems to open any number of sub-savings accounts and are willing to do so simply at the request of and for the convenience of the member. Once the account has been opened, the fixed costs associated with maintaining the account are essentially nullified by the fact that we have to perform the same activities—like generating regular statements—for the member’s primary share account anyway. Establishing the Auto Savings as a “no transactions” or “automatic deposit only” account reduces the annual overhead of the account by half.

While the minimum savings deposit required of the program will be set by each credit union to meet their own business needs, a $25 minimum is recommended. Members should be empowered to select any certificate term they desire with no minimum balance required to open the account. If an institution’s core system requires a certificate to be funded at opening, simplicity suggests matching the amount of the planned regular contribution or opening the account with $1. Standard early withdrawal penalties (for certificate accounts) should be imposed to reinforce and motivate the savings behavior and to prevent the account from becoming transactional in nature thereby allowing the member to slip into old habits of not saving.

As the amount of financial and resource investment required is minimal, a credit union would be justified in adopting an Auto Savings program because it fosters wealth building behavior among its members, attracts additional deposits, and establishes deeper relationships that extend beyond the life of the loan.

Target Market

The Auto Savings program is a great way for any member to start saving while financing a vehicle. However, there are certain markets that make sense to directly target for this innovation:

- Younger members, specifically age 18 to 25, to help them start a sound savings program especially when buying their first vehicle
- Members of any age who maintain low balances in the credit union and most likely do not have savings accounts elsewhere
- Members who purchased a vehicle through an indirect dealer
- Members who have auto loans that are approaching full payment

The target market can easily be accessed via traditional communication channels like newsletter, website, in-branch advertising, etc. The best opportunity to market the program is at the point-of-delivery. Since the Auto Saving is an add-on, the loan officer can easily incorporate the program pitch into the regular sales process. Additionally, the use of direct mail might be a tactical strategy used to target loans generated through an indirect lending program.

Operational and Other Considerations

The Auto Savings program utilizes two core credit union products. Therefore, product development is minor. Since the savings component is a contractual additional.

The Auto Savings program will be delivered to borrowers at the point-of-sale when they are pre-approved or apply for a vehicle loan and through direct mail to members financing a vehicle through an indirect channel. Little member service “sales” time is required as this new saving product will be sold as a contractual add-on to the loan much like Credit Life and Credit Disability, Guaranteed Auto Protection (GAP), or Warranty, etc. Once credit union staff members have been trained on the new program, the operational investment is limited to the resources required to close the loan and set-up the automatic payment transfer. Limited staff training is needed to support the program.

Automation is the key to the economic success of this program. It only works if the payment/deposit is made automatically via ACH, payroll deposit/deduction, or automatic transfer. This is necessary for both the credit union from an expense standpoint and for the member in acquiring the product due to their self-admitted lack of saving discipline.

Typically, it is the core system of an institution that is the roadblock when setting out to create a new product or means of doing things. Attempting to squeeze out of the box thinking quite literally into a computer system’s box is frequently where developmental costs skyrocket during project implementation.

Not so in this case. The Auto Savings program simply takes two existing products and marries them together. Notice here that they are said to be married, not integrated. This is an important distinction as no systems programming is necessary to get this project off the ground. The two products remain separate.

The loan remains intact and more importantly . . . untouched. There are no Truth-in-Lending issues with which to contend. The setup of the savings vehicle—which is the only real variable in the entire equation—is totally at the discretion of the credit union implementing the program.

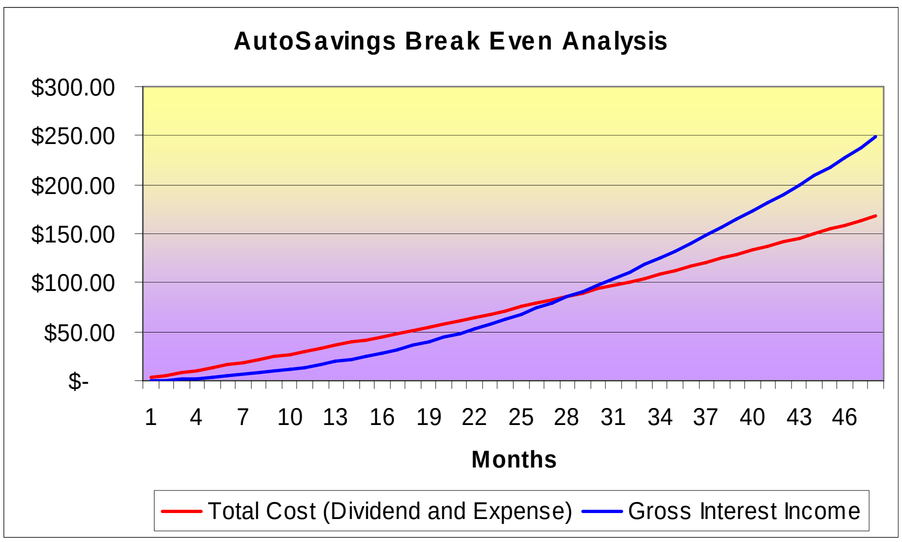
Pricing will be dependent on the savings account type. Since the account type can be a simple savings account or certificate product, setting the rate and dividend yield is an individual decision for each credit union that will depend primarily upon the institution's current rate structure. While market conditions and the competition's savings rate offerings may be an influence, this need not be a primary concern as the ideal candidate for this program currently receives a zero rate of return from the government by utilizing the "tax return savings plan." Dividend rate, account terms or both can be adjusted to motivate member behavior or to meet the unique business needs of a particular credit union.

Financial Analysis:

Each product is well established and will continue to exist independent from the Auto Savings program. Typically in the credit union industry, the average life of an auto loan is 30 months or less. However, the term on the savings portion of the program will be set at the full length of the loan. Even if the member ends the loan relationship early, the savings relationship should be encouraged for an extended period of time. If vehicle re-financing does occur, on average, it will do so two months past the point of profit equality.

The analysis does not attempt to take into account any incremental loan volume that may result from Auto Savings. It is possible that a credit union can generate additional loan volume by offering this unique program. However, we did not attempt to calculate the amount.

Assumptions:	
Dividend rate	1%
Gross yield to CU on funds deposited	5%
Annual cost to maintain a savings account	$30
Monthly deposit	$50
Term in months	48



Financial summary (based on the above assumptions)

- The break-even point occurs after 28 months
- Net profit of $80 per account over 48 months

Additional Considerations:

Credit unions may want to consider helping their members set a targeted savings goal and utilize various tools to keep them apprised of their progress. For example, a credit union might show the goal within home banking and illustrate using a chart how far the member needs to go to reach the goal. Or a credit union may use email alerts when the member achieves certain milestones, such as reaching $500 in the account.

The positive aspect of these approaches is that it keeps the member interested in the program and encouraged as they build larger balances. The downside to this is the potential for increased cost in development and implementation of these tools.

Proof of Concept

Auto Savings was piloted at two credit unions, Day Air Credit Union and American Airlines Federal Credit Union.

Day Air Credit Union:

Day Air Credit Union has nearly $150 million in assets, located in Kettering, Ohio. The credit union has about 22,000 members and serves a variety of SEGs and communities. Day Air launched Auto Savings on July 1, 2007. The product was branded as “Auto Loan Plus” to its membership.

The program was designed to have members contractually agree to increase their automated car loan payment by a fixed amount. The increased amount goes into a share certificate with a maturity date that matches the loan payoff date. The credit union pays an interest rate that matches their 60 month share certificate rate.

Day Air took a strong stance against signing up for Auto Loan Plus without a strong commitment and established significant penalties for accessing the savings. These include: Funds can be withdrawn without penalty from the share certificate at the end of the loan term or for repairs to the vehicle (with proof of repair). A request for the funds with an early loan payoff results in the loss of 180 days of interest. All other withdrawals require the loss of 180 days of interest and a $50 fee. The savings component can be cancelled with a $25 fee and forfeiture of all dividends paid.

Day Air also paid a $50 incentive to any member who took out a new loan with the Auto Savings component. The product was marketed via standard channels such as in branch signage, newsletter, and local newspaper under the tagline of “Wish you were better at saving? We can help! Introducing the loan that helps you save!” In addition, staff was cross-trained to include a payment amount for the savings component into the loan payment.

Day Air decided to offer the program because they wanted to help their members build stronger savings habits and felt the implementation of Auto Savings would not be difficult. “There is a need to teach savings. The only savings products that seems to be working are 401(k)s,” said Melissa Johnson, Day Air Senior Vice President of Member Services. “Out of sight, out of mind, is working.”

Day Air’s results have been impressive so far. During the first two months, the credit union opened 37 Auto Loan Plus accounts on 222 newly originated vehicle loans–-equating to a take-up rate of almost 17%. Results varied dramatically among Day Air’s branches, but were a staggering 76% (13 or 17) at one of their branches. The Assistant Branch Manager at that location was responsible for developing the training materials and wrote the procedures used in launching Auto Loan Plus to the credit union’s staff. On top of this success, 15 additional members added the savings component to an existing vehicle loan with the credit union.

Other results from the pilot include[1]:

	Average	Median
Loan Amount	$12,867	$10,999
Loan Term	52 months	60 months
Car Loan Payment	$287 per month	$273 per month
Savings Component Amount	$17.34 per month	$16.04 per month
Total Possible Savings if saving plan completed to term (excluding dividends)	$871	$720
Credit Score of Primary Borrower	659	694
Age of Primary Borrower	41	37
Annual Income	$42,215	$42,996
% of Area Median Income	70.6%	71.9%

Day Air plans to continue offering the Auto Loan Plus program and has no plans to modify the program.

[1] Results are only reported for newly opened Auto Loan Plus accounts and do not include add-ons to existing vehicle loans.

American Airlines Federal Credit Union:

American Airlines Federal Credit Union serves anyone in the Air Transportation Industry and their families. The credit union has over $4.4 billion in assets and serves 210,000 members. The Auto Savings program, branded as “TurboSave” at this credit union, was designed with a standard auto loan attached to a secondary share club account. The club account paid the same dividend rate as the primary share/savings account (currently 4.75%) and was limited to one annual withdrawal. Members were also given the option to keep the payment the same and extend the term by a few months to apply funds to the Auto Savings program.

Information and training on the new product was initially available online for all employees in each of AA Credit Union’s 43 branches; however it was focused on the Phone Loan Department and one branch in Miami, Florida. Marketing was done primarily through a direct mailing and through the sales force. Between July 15th and August 31st, twenty-eight TurboSave Accounts were opened in these two locations which equated to 4% of total autos funded. The average age of members originating a TurboSave product from AA Credit Union was 42 years with an average annual income of $44,000. The average additional payment was $34.00.

The TurboSave product was positioned as an add-on to an auto loan account, similar to GAP insurance, or a vehicle warranty. However, a similar rewards program was not structured for employees originating a TurboSave, which most likely impacted the results. Because AA Credit Union offers such a high dividend on share accounts, it was not economically feasible to offer additional incentives to members or employees who originated a TurboSave product.

While the volume of accounts was below expectations, the testimonials provided by members were so positive that the credit union plans to continue offering the program and potentially further enhance the program. They have recently shared experiences with representatives from Day Air Credit Union and are considering revisions to their program to improve results based on their findings.

Testimonial:

Lisa Mensah, Executive Director of the Aspen Institute’s Initiative on Financial Security stated, “The U.S personal savings rate has been on the declining side for years and raising the rate of personal savings is a significant challenge. The time to address the nation’s savings crisis is now. It will require innovative savings solutions like those we at the Aspen Institute are proposing as well as fresh savings opportunities presented by financial institutions, like the Auto Savings program.”

How to Get Started

Again, the ease of implementation and administration, make the Auto Savings a desirable product.

1. Select the savings account product (savings or certificate) that will be used for the Auto Savings and establish account parameters:
    a. Minimum (and/or maximum) amount of deposit
    b. Interest rate paid on deposit
    c. Prepayment penalty
2. Implement new contract for savings component as part of the auto loan package.
3. Consider development of methods for members to track their activity.
4. Develop marketing promotions.
5. Develop staff training materials and train staff.

---

[1] Associated Press, February 1, 2007

[2] www.creditcards.com/statistics/statistics.php
[3] CUNA News Now, January 24, 2007, Pew Research Center
[4] www.upromise.com
[5] www.aspeninstitute.org/ifs

Appendix 1: Auto Savings Loan Contract Addendum
Appendix 2: Marketing Materials – Day Air Credit Union
Appendix 3: Marketing Materials – American Airlines Federal Credit Union
Appendix 4: Credit Union Journal article