

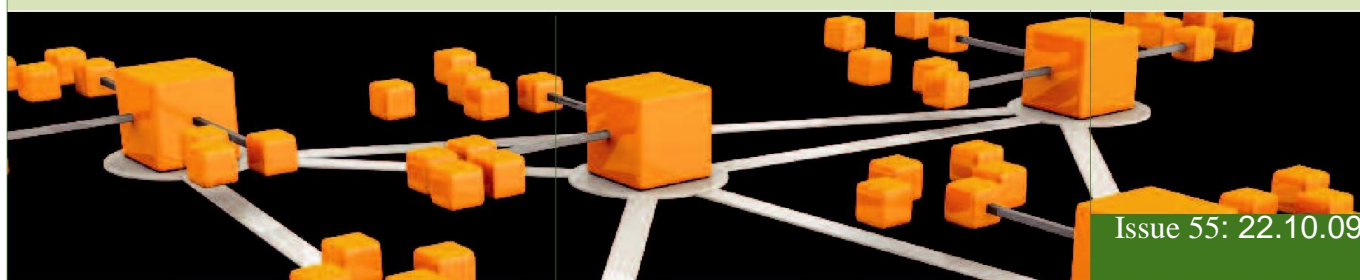


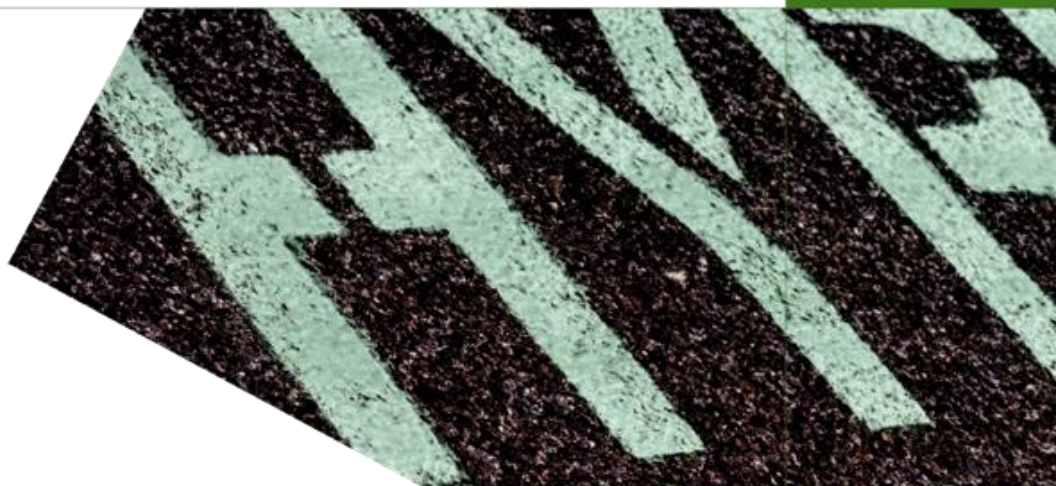
GLOBALPREPAIDEXCHANGE

Independent Intelligence from the World of Prepaid

Market Report

# iQ. Market Report.





# Hybrid Cards

By  
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Prepaid Exchange

## Section 01

When asked to describe 'prepaid' you can reply by asking people to think of credit, which is 'pay later', then think of debit, which is 'pay now', and then consider prepaid, which is 'pay before'.

Oh, if only life was so simple. Now we have a new category of prepaid, the Hybrid Prepaid Card, which provides a credit line on a prepaid card. The term is so new it wasn't even included in our Prepaid Glossary published earlier this year. This iQ explains the different types of Hybrid Prepaid Card and provides case studies of each type. It then considers whether this is a variant of prepaid that opens up opportunity for the whole industry, or a niche product that caters for specific needs of a minority. You can use it to help you assess whether to develop hybrid products for you and your customers and to discover innovative ways to avoid some of the current and likely future restrictions around regulations of

prepaid and credit cards after the CARD Act in the USA.

So what is a Hybrid Prepaid Card? A Hybrid Prepaid Card is a prepaid card that offers the consumer a credit facility. There are two types of Hybrid Prepaid Card:

- Credit Builder Cards
- Credit Line Cards

### Part one: Credit Builder

Credit Builder prepaid products help customers improve their credit history. Three different business models exist:

#### Type 1: Structured Loan

When the card is purchased consumer takes out a small loan. This is repaid with a small payment each month so that at the end of the year, the user can report a complete loan repayment track record.

#### Case Study: CreditBuilder *From Advanced Payment Solutions*

The consumer takes out a card but the fee of £59.40 is an Installment Loan. The consumer then makes 12 monthly payments of £4.95 at 0% APR. On complete payment of the loan, this is reported back to Experian, a credit reference agency, and the cardholder receives an improved credit score.

The value to consumers is that they have access to a CashPlus Card, there is no 'real' credit outlay and – crucially – it allows them to build or repair their credit rating as the £59.40 is treated as a loan. Moreover there is a 100% approval rate, compared with increasingly high rejection rates for many credit card applications.

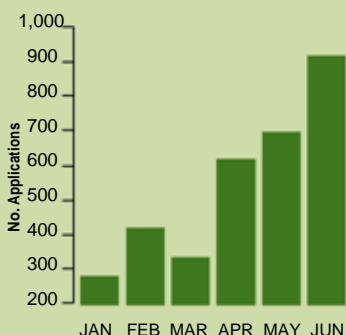
The results have been impressive and the number of cardholders is growing fast: there were 1,000 applications in June 2009 alone.

*Based on research by*  
**David Parker,**  
Polymath Consulting

Section 01: Hybrid Cards

The account holders are three times more active than holders of APS' standard prepaid product. 90% of cardholders continue to use the card once the loan has been paid off. The average load on CreditBuilder is £250 per month compared to the average load on a standard product of £300 per month. And CreditBuilder in July 2009 accounted for 8% of the total of APS' portfolio.

CreditBuilder's growing portfolio, 2009



**Type 2: Loan-Back**

The card contains three 'accounts' that are used to enable different buying behaviours: banking, borrowing and spending. The user can report a successful loan repayment history while having the versatility of a payment card.

**Case Study: Ultra VX Card**  
*From Ultra VX*

The Ultra VX Card has three accounts:

**Account 1: The Cash Account**  
Used for cash loads, Money Transfers, ATM transactions, and Bill Payments. The cardholder must add cash to cover the automatic monthly minimum payment

**Account 2: The Secured Account**  
Used to secure the line of credit. Money is transferred from the Cash Account into the Secured Account to increase the credit line. Funds in the Secured Account are not accessible. These funds are used to secure the credit line through Credit-On-Demand

**Account 3: The Credit Account**  
Used for all purchases, and consists of three parts:

- The Credit Line is how much total credit on the account
- The Available Credit is the amount of credit they have to spend
- The Outstanding Credit Balance is how much of their credit limit they have spent, which is thus how much they owe

Cardholders can only borrow/spend the amount already in the secured account. So while providing credit, the user must 'pre fund' that credit first. Ultra VX then reports the successful payment of the loans to the credit agencies. There are

two ways in which the card programmes generate reports about an improved credit history. In the first scenario the prepaid card becomes the method of payment of everyday household bills. The issuer reports to the credit agency that the consumer has paid these bills.

**Case Study: The AccountNow card**  
*From Palm Desert National Bank (PDNB)*

A consumer activates AccountNow Bill Pay and adds the FREE AccountNow Credit Builder service. Every time the consumer makes a bill payment, AccountNow sends bill payment information to PRBC, a national credit reporting agency just like Experian, Trans Union, and Equifax.

PRBC is the first agency to give consumers a choice and an opportunity to show that they pay their bills on time. This creates a bill payment history that demonstrates credit-worthiness when applying for housing, credit, insurance and employment, simply by doing what the consumer already does today: paying rent, electric, cable, insurance, and phone bills on time. And only Bill Pay transactions are shared with PRBC. Regular debit transactions are not reported.

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Section 01: Hybrid Cards

In this second case study run by Eufora, regular payments to the card are reported to the credit agency in order to demonstrate the consumer's creditworthiness.

**Case Study: Eufora Prepaid MasterCard**  
*From Eufora*

Eufora has three cards in the program: Associate, Preferred and Elite cards. The consumer is charged annual fees of \$29.95, \$59.95 and \$99.95 respectively to receive additional benefits, including a Credit Builder facility on the top two levels. The customer then makes a 2-year membership commitment with additional monthly fees. The Credit Builder monthly payments begin on the 2nd day of the month approximately 30 days after the Eufora Prepaid MasterCard® is issued. Eufora will then continue to automatically charge the Eufora Prepaid MasterCard on the 2nd day of each month thereafter.



**Part Two: True Credit Line Cards**

There are currently three types of True Credit Line Cards offered in the market.

**Type 1: Payday Loans**

Many of the companies offering True Credit Line Cards are similar to Payday Loans, that have been designed for small, short term payments to tide consumers over until pay day. As cheque guarantee cards do not exist in the USA, the model is that once consumers have established a history of putting their pay into their account each month for several months, they can obtain a small loan for a few days until their pay arrives. In the UK the model is slightly different and closer to Type 3 below where 4 times the value of the cheque guarantee card is given as a loan.

In the USA there are significant costs and fee controls apportioned to issuing a credit card compared with issuing a prepaid card. This means that companies offering products that provide small credit lines their prepaid card try to avoid cards qualifying as a credit card. One of these avoidance mechanisms is what is called 'overdraft protection'. This is a 'fee per event' model that accesses a specified amount based on a financial institution's rating of the cardholder. Interestingly, the cardholder used to be told what that

amount was, but this has evolved into a 'black box' where the charges are variable. This avoids the perception that these fees are an effective interest rate. Another avoidance mechanism is to make sure that payment using the credit line on a prepaid card is presented as only one fulfillment option.

**Case Study: The ipower® Card**  
*From Jackson Hewitt*

The iAdvance Line of Credit from MetaBank helps the user secure short term loans for unexpected expenses. By simply establishing a direct deposit they can then obtain the iAdvance. This allows the user to borrow money 24 hours a day, 7 days a week and use a short term loan whilst avoiding overdraft charges and the high fees that often come with payday advances.

**Case Study: Advance**  
*From Wells Fargo*

Consumers may qualify for a line of credit up to \$500 that can be deposited immediately into a checking account for a cash advance and access via their debit card. There is a Finance Charge of \$2 for each \$20 advanced, which equates to an Annual Percentage Rate (APR) of 120%. Ouch! The amount advanced, plus the Finance Charge, is deducted automatically from a customer's incoming paycheck or other recurring electronic deposit or must be paid in full by a specified due date to avoid a late fee and to continue to use the service.

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Section 01: Hybrid Cards

To qualify, a consumer must have a paycheck or any other recurring amount of \$100 or more electronically deposited to their checking account.

**Case Study: FastCash Preferred**  
*From Palm Desert National Bank*

The FastCash solution is similar to other Payday Loans except that the card is limited to the STAR, Pulse and NYCE debit card accepting retail and ATM networks. Only consumers who have taken out a 500 FastCash loan and have successfully paid off an initial loan are eligible to receive a FastCash Preferred Card. Once such a card has been issued then future loans can be paid onto the card in about one hour. Cardholders are allowed one free cash withdrawal per month from a fee-free ATM. A monthly management fee is also charged if funds are left on the card.

**Case Study: Emerald Advance**  
*From H&R Block*

The H&R Block card offers a choice between a Pay Day Loan and Credit Builder type product by offering a choice of either a small loan based on payroll history, i.e. an advance on payroll, or a loan based on equal funds held on deposit. Consumers can also have their federal and state income tax refunds downloaded into their Emerald card accounts. In addition, cardholders can take advantage of Emerald Advance, which is a line of credit that H&R Block offers Emerald prepaid cardholders.

H&R Block charges a 36% annual percentage rate on the loan. Cardholders can cut the interest rate on the loan to 9% by opening a deposit account with H&R Block Bank. Last year, H&R Block issued 887,000 Emerald Advance cards.

**Type 2: Pawn Broker Credit**

Pawn Brokers pay funds from pawned goods directly onto prepaid cards. CashPlus has been particularly successful in gaining distribution amongst pawn brokers in the UK.

**Case Study: CashPlus**  
*From MasterCard®*

The cashplus prepaid Gold MasterCard is an award-winning prepaid card that can be used anywhere that accepts MasterCard and can be used to withdraw cash at ATMs. Cardholders can manage their account online, via a 24-7 telephone service and can receive information by text. Although not overtly marketed by APS, the card is being used by pawnbrokers across the UK as a means to give its customers easy access to spending money and some are marketing it as a card that will

help the user with budgeting. The card be loaded with cash or with the value of held by the pawnbroker. Customers simply need to pass standard KYC/Customer Due Diligence. While members get the exclusivity of a gold card without any credit, interest or penalty fees, there is an issue fee and fees for cash withdrawals and other card usage.

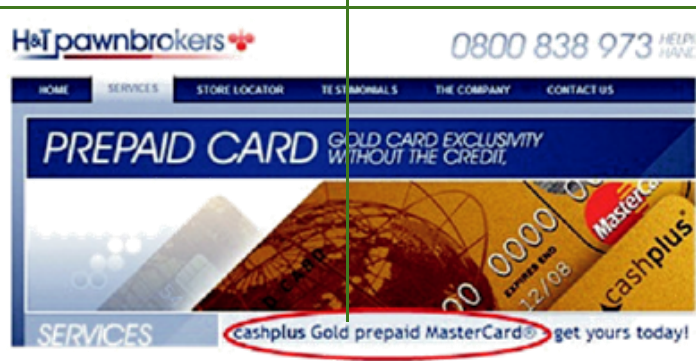
**Type 3: Small Loan-to-Card**

Some consumers want to save a small amount regularly for use later. Others want short term loans with a regular repayment plan that is easy to conform to. In the UK there is an extensive network of agents who visit typically low income consumers to collect small sums of money each week, sometimes to pay for loans agreed earlier and made available on a card, and sometimes to save for a special occasion or a 'rainy day'.

The collected balances, traditionally held in the form of paper vouchers/certificates, less a collection fee, can be used to purchase hampers of produce



The cashplus prepaid Gold MasterCard is an award-winning prepaid card that can be used anywhere that accepts MasterCard and can be used to withdraw cash at ATMs.



Section 01: Hybrid Cards

such as food and drink for a special occasion, such as Christmas. Alternatively the

payments can be made onto a prepaid card that can be used on the internet or wherever the network badge is used. These cards are sometimes personalised, others are purchased for a fixed amount and when the balance has been used, are disposed of. All are chip and PIN cards.

**Case Study: Revel Advance**

Revel Advance claims to be one of the most affordable small dollar-loan programs to be offered to date on a nationwide scale. Qualified customers establish a small dollar line of credit and have advances loaded directly onto the Revel card. The balance must be repaid in installments over a four to 10-week period.



**Our conclusions**

Professor Dan Horne said

recently, I'm confident that

companies in the prepaid industry will innovate their way around whatever constraints might be put on their freedom to operate". Hybrid cards are excellent examples of innovations that aim to solve consumer problems while not contravening increasingly tight regulations. Sometimes the product construction is clever and customer-friendly, such as with the APS products. More often than not, the design and promotion of the hybrid cards seems to be opaque, confusing and complex, and designed for consumers with acute financial needs, but scant ability to buy sensibly. As a result, the potential for consumer exploitation is significant, and rather than helping consumers resolve their financial difficulties, they exacerbate them.

Some hybrid prepaid cards are not universally welcomed. One commentator, who prefers to remain anonymous, said, "I believe this is a disaster in the making." He went on, "The reason for prepaid cards is to prevent or help people live within their budgets and now we are giving a small amount of drugs to an addict and a short term fix until the next pay day. History of our credit cards show just how many are maxed out and in default and now we are pushing another drug to the drug addict." He concludes,

"This does not make sense nor does it seem in the best interest

of the people taking the cards."

In addition, issuers of hybrid prepaid cards must be careful not to contravene regulations. For example, if the organisation is running a prepaid card out of an Electronic Money Institution in Europe then under the Electronic Money Directive the organisation must not carry out any other business than the issuing of e-money and the necessary connected services to be able to do it. This would mean that if the organisation wish to run any kind of Hybrid Product it must be run through a separate legal entity (which could be a subsidiary or group company). If the product is granting credit (like a Credit Builder product) then a separate consumer credit licence would be required in the UK and in other EU countries it may have to be run through an Authorised Credit Institution (i.e. a Bank).

Overall, hybrid cards are a niche product for niche markets. Launching hybrid cards takes considerable preparation and care, and the business model has many variables and considerable risk. APS and HRBlock have proven that a well run business can run a hybrid card well, so opportunities for hybrid cards will certainly exist. But they are not for the faint-hearted.

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Research by David Parker, Director,

Polymath Consulting davidparker@polymathconsulting.com David Parker is CEO of Polymath Consulting. David has worked in open loop prepaid since 2002 and is a leading consultant on prepaid cards. He regularly chairs and speaks at conferences and is the publisher and editor of the Pepper Prepaid Report – the encyclopaedia of the UK consumer loaded open loop prepaid card market that includes fee analysis of over 170 cards currently in the market.