



IMPACT OF FINANCIAL COUNSELING ON FINANCIAL STABILITY ANALYSIS OF THE NEW YORK CITY MODEL

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Financial counseling may be an effective way to improve individuals' financial behavior and outcomes. However, its impacts have not been adequately studied. Previous studies show weak positive effects of counseling, but are subject to a number of limitations. Most significantly, individuals who choose to attend counseling are not representative of the general public, making it difficult to measure counseling's true impact. This study, a collaboration between the Center for Financial Security and the New York City Department of Consumer Affairs Office of Financial Empowerment, partially addresses this issue by comparing the effects of one-on-one financial counseling to generalized financial education. In both cases individuals are seeking financial assistance. The study will use credit report data and knowledge assessments in combination with self-reported information to gain a comprehensive picture of counseling's impacts on financial knowledge, behavior, and outcomes. This report—a progress update at the study's midpoint—describes the study design and presents baseline data.

The current economic recession emphasizes the barriers to financial security faced by low- and moderate-income households in the United States. Financial counseling programs offered by the public and non-profit sectors may help individuals overcome these barriers. Financial counselors typically work one-on-one with individuals to address personal financial issues, usually focusing on basic financial management skills (Collins and O'Rourke 2010). Counseling aims to improve an individual's financial situation through specific actions taken by a counselor or client. It is often geared towards individuals facing immediate issues like mortgage default, bankruptcy, or significant credit card debt. At the same time counseling also has preventative value, empowering individuals with the skills and resources needed to successfully manage their finances and avert future financial crises.

However, relatively little is known about counseling's true impacts. This project will

identify whether financial counseling services help clients make sustained behavioral changes that promote greater financial stability.

Counseling aims to improve an individual's financial situation through specific actions taken by a counselor or client.

Previous studies measuring the impact of financial counseling suggest that it may improve financial knowledge, behavior, and outcomes (Collins 2010). However, these studies are limited by a number of factors. Most significantly, individuals who seek financial assistance are not representative of the general population. For example, previous research demonstrates that individuals in counseling are generally more motivated, in greater financial distress, and less financially experienced than the general public (Elliehausen, Lundquist, and Staten

2007). Some of these traits, such as motivation levels, are particularly difficult to observe and adequately control for (Caskey 2001). Given limited opportunities and resources to randomly assign individuals into programs, measuring the true impact of counseling is challenging.

The study in progress addresses this problem by comparing the impacts of individualized financial counseling to general financial education on a variety of financial indicators, including credit scores, debt levels, and financial knowledge. In both cases, study participants have sought financial assistance, and are therefore more likely to exhibit similar unobservable characteristics that may affect their financial outcomes. Counseling is more resource-intensive than providing general educational information; thus this study will also provide insight into the value of the personalized advice provided by counseling programs.

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This study has also been designed to address other limitations of previous research. Previous studies often use self-reported outcome measures, which are less reliable than administrative data (Agnew and Szykman 2005; Caskey 2006; Collins et al. 2008). Additionally, positive impacts on knowledge may not translate to changes in behavior (Lyons and Scherpf 2004). This study uses administrative data and knowledge assessments in combination with self-reported information to gain a comprehensive picture of counseling's impacts on financial knowledge, behavior, and outcomes. This provides an opportunity to compare administrative and self-reported

data, as well as differential impacts on various elements of financial health.

This project has the following research goals:

1. Identify the financial impact of participation in financial counseling, particularly on debt levels and credit scores.
2. Determine whether financial counseling helps low- and moderate-income individuals achieve sustained behavioral and/or psychological changes enabling them to improve their financial stability.
3. Determine what programmatic features correlate with higher levels of financial and behavioral impact (e.g. site variation, duration of counseling, certain milestones achieved).
4. Examine differences in financial knowledge and future-orientation and identify appropriate metrics for the field.

Research Design

Study participants were recruited into the counseled group and the comparison group (composed of individuals who attended financial education workshops) over a five-month period.

Counseled group subjects were recruited from New York City's network of Financial Empowerment Centers ("Centers"). The program was launched as a pilot in 2008 and expanded in 2009, offering one-on-one financial counseling services to New Yorkers needing specialized assistance with complex finances. These financial counseling services are available in over 20 locations across the City, free of charge. Centers are embedded into existing human services agencies, such as homelessness prevention programs, workforce development centers, and court-related services. Counselors help clients individually on a range of financial needs, such as money management, budgeting, credit and debt assistance, and selecting safe and affordable financial products.

Centers largely serve vulnerable populations, including minority families and foreign-born residents. Clients seeking financial counseling services are typically minority females with at least one child and annual incomes less than \$20,000 a year. More than a quarter of clients do not have a bank account and over half have some amount of outstanding debt. Families' median debt is \$11,000. Among households with debt, the average level is about \$45,000. Only one in five families indicates they have some type of savings. Furthermore, just over 40 percent of the elderly client population indicates they are still working, and 80 percent have no savings.

Using a standard protocol, counselors work with clients to identify specific financial needs during the first 20 to 25 minutes of the session. Counselors and clients jointly set financial goals and develop appropriate service plans to help achieve them. Clients may return for unlimited follow-up sessions that last 40 to 60 minutes on average. Outcomes are tracked in several areas of financial stability: banking, budgeting, establishing credit, improving credit, saving, and reducing debt. Specific financial milestones are attached to each outcome, for example reviewing a credit report, creating a budget, including a savings plan in a budget, and researching the right banking options. Although session length varies based on individuals' needs, on average about half of counselors' time is devoted to credit and debt issues while the remaining time is focused on banking, saving, and budgeting.

The comparison group is composed of study participants receiving financial education provided by three non-profit organizations from New York City's Financial Education Network (FEN). The FEN is a collaborative of more than 70 financial education providers who offer free

or low-cost financial education services. These organizations serve a high volume of low- and moderate-income individuals and families in New York City every year.

The organizations offer free two-hour workshops with an average of 15 to 25 participants. While the curricula differ, workshops generally address budgeting, saving and banking, credit and debt management, and in some cases identity theft. Services are delivered in a lecture format, but questions and dialogue between participants and teachers are encouraged.

Data & Methodology

This study will assess the financial outcomes of counseling and workshop participants mainly through changes in credit scores and debt levels. This information is taken from participants' credit reports at program intake and a follow-up period 6 to 12 months later. Additional measures from the credit reports include debt levels by type (e.g. installment debt and debt from revolving credit), amount past due, number of accounts with positive balances, and number of credit cards. Credit reports provide objective data that complement self-reported information, and may be more reliable than self-reports.

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Additional self-reported data will be provided by baseline surveys completed at intake, as well as a follow-up survey. The baseline survey was adapted from a Financial Health Assessment (FHA) used at the Centers. The survey asks questions about demographic characteristics, income and expenses, debt and savings levels, banking status, and financial behaviors. It also asks respondents which services they are seeking

(e.g. assistance with debt reduction or filing for bankruptcy). Finally, it asks participants about their sense of financial stress and control.

About six months after they receive counseling or education, participants are mailed a follow-up survey. The survey focuses on respondents' financial behavior and use of various financial services in the prior months. For example, the survey asks if respondents have negotiated with creditors to reduce debt or develop a payment plan, used a budget, contributed regularly to savings, and used various banking and alternative financial services. Additionally, the survey asks respondents about their income and expenses, debt and savings levels, and self-assessed financial behavior and well-being. To evaluate the impacts of counseling on financial literacy, it asks respondents to self-assess their understanding of money management, and respond to questions designed to test financial knowledge. The survey also attempts to measure future orientation.

We expect to find that financial counseling is more effective than financial education. Therefore, we expect that counseled individuals will demonstrate greater positive outcomes than the comparison group.

Baseline Data

From January through May 2011, the Centers conducted counseling sessions for about 2,200 new clients, and the FEN partners held 62 workshops for about 1,060 individuals. Approximately 520 participants who received financial counseling and 270 participants

who received financial education were recruited into the study.

Table 1 shows summary statistics for the sample. In terms of demographic characteristics, the counseled group—which is representative of the Centers' general clientele—is different than the comparison group. Individuals in the comparison group are younger and have more children. Fewer have a 4-year college degree or are married.

The two groups also face a significantly different financial situation. The comparison group has a lower average income, and more individuals who are unbanked. However, individuals in the comparison group have significantly less self-reported debt, and fewer report feeling they have no control over their finances or are very worried about their finances.

TABLE 1
Baseline summary statistics

| | Counseled group | Comparison group |
|-----------------------------|-----------------|------------------|
| Age | 43*** | 32 |
| Female | 0.67 | 0.72 |
| Married | 0.23*** | 0.12 |
| Number of children | 1.0*** | 1.8 |
| White | 0.078*** | 0.020 |
| Latino/a | 0.34*** | 0.47 |
| African-American/Black | 0.55** | 0.47 |
| Foreign-born | 0.11 | 0.09 |
| 4-year college degree | 0.23*** | 0.07 |
| Total monthly income | 1,100*** | 800 |
| Total reported debt | 25,000*** | 3,000 |
| Unbanked | 0.35*** | 0.69 |
| Receiving public benefits | 0.33 | 0.29 |
| No control over finances | 0.39*** | 0.26 |
| Very worried about finances | 0.51*** | 0.36 |
| Observations | 522 | 273 |

Source: authors. Statistically significant differences from comparison group indicated: *** p<0.01; ** p<0.05; * p<0.1

Overall, these differences are expected, because there may be different reasons clients choose to attend counseling versus education. The counseled group may be more similar to the comparison group than the general population in terms of unobservable traits that affect the decision to seek financial assistance. However, the data demonstrate that additional statistical strategies will be needed to control for baseline differences between the counseled and comparison groups.

Preliminary Findings

A preliminary analysis of counseling data collected from Center clients in 2009 and 2010 suggests that positive impacts of counseling may be largely a result of counselors' intervention with creditors on behalf of clients (Collins et al., forthcoming). The sample was divided into two groups based on the milestones achieved during counseling sessions: clients who received direct assistance with creditors and clients who did not. Direct assistance includes milestones such as negotiating with creditors, creditors reducing payments/fees, and entering a payment plan with a creditor. Milestones that did not qualify as direct assistance included reviewing the client's credit report, developing a payment plan, and creating a debt management worksheet.

Among clients who received direct assistance, the number of counseling sessions received was positively associated with higher credit scores and lower debt levels—particularly debt from open, revolving lines of credit. Effects among clients who did not receive direct assistance were smaller or not statistically significant.

It seems likely that debt levels may prove a more useful outcome measure than credit scores, in part because in the short run credit scores may not respond to changes in

debt levels. These initial findings will shape analysis of the data collected in the current study.

Implications for Vulnerable Populations

The current study holds promise for demonstrating the impacts of financial counseling. Previous research and analyses of earlier client data suggest that financial counseling helps individuals improve their financial health. However, the credit report and survey data under collection for this study provide an opportunity for a more rigorous analysis of counseling's impact on financial literacy, in addition to financial behaviors and outcomes. The data will provide variation in financial services received—specifically counseling versus education—offering more robust identification strategies than previous studies.

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The findings will have substantial implications for low-income households in the United States. Demonstrating the effects of financial counseling is important for justifying public funding of counseling programs, which are often geared toward this demographic. In addition, identifying which elements of counseling influence financial outcomes would provide opportunities to maximize its effectiveness, better helping clients achieve financial stability.

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The Financial Literacy Research Consortium

The Financial Literacy Research Consortium (FLRC) consists of three multidisciplinary research centers nationally supported by the Social Security Administration. The goal of this research is to develop innovative programs to help Americans plan for a secure retirement. The Center for Financial Security is one of three FLRC centers and focuses on saving and credit management strategies at all stages of the life cycle, especially helping low and moderate income populations successfully plan and save for retirement and other life events, including the use of Social Security's programs.

The Center for Financial Security

The Center for Financial Security at the University of Wisconsin-Madison conducts applied research, develops programs and evaluates strategies that help policymakers and practitioners to engage vulnerable populations in efforts which build financial capacity. The CFS engages researchers and graduate students through inter-disciplinary partnerships with the goal of identifying the role of products, policies, advice and information on overcoming personal financial challenges.

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