Executive Summary

From Ashland to Paducah and every community in between, Kentucky's lower-income working families often pay a premium for goods and services, making it difficult for them to build wealth, save for their children's futures, and invest in their upward mobility.

Higher prices start with the morning drive to work: Lower-income workers in Kentucky (those earning less than $20,000 per year) are more likely to pay above average rates for auto loans, pay nearly $400 more for car insurance, and pay a higher sticker price for their car than their higher-income counterparts. Those who leave for work from a home they own are twice as likely to have a high-cost mortgage as are their higher-income neighbors, often costing thousands of dollars more over the life of the loan. On the way back from work, more lower-income workers use nontraditional financial services, paying higher fees for cashing a check or taking out a short-term loan. Taken together, these higher prices add up to hundreds, sometimes thousands, of dollars in extra costs for already tight family budgets.

The good news is that state and local leaders around the country are rallying behind new, innovative, practical, and low-cost initiatives to lower these prices. With these and other initiatives as models for action, public and private leaders in Kentucky can now also reduce these higher costs of living, and do so in ways that defy the substantial budgetary, economic, and partisan pressures that limit so many efforts to grow the middle class. Through a combination of initiatives that lower business costs, curb unscrupulous behavior, and boost consumer knowledge, public and private leaders can bring down these prices.

This report is a roadmap for how to reach this goal and improve the spending power and economic security of lower-income Kentuckians. In short, we find:

Kentucky's lower-income families tend to pay higher than average prices than other consumers for basic necessities

Depending on where lower-income consumers live and what combination of necessities are consumed, lower-income families can pay up to thousands of dollars more than higher-income consumers every year for basic financial services, cars, car loans, car insurance, home insurance, home loans, furniture, appliances, electronics, and other basic necessities. In particular:

- ***Cashing Checks:*** According to our survey, about 35 percent of regular customers of high-cost check-cashing establishments in Kentucky earn less than $20,000 annually, and about 62 percent earn less than $40,000. Unlike most other states, Kentucky places no limits on the fees that establishments can charge for check cashing. A random survey of such establishments in Kentucky found that fees to cash a check range from 1 to 10 percent of the face value of a check.
- ***Short-Term Loans:*** Nearly 70 percent of regular customers of high-cost payday loan and pawnshops in Kentucky are lower-income residents. In Kentucky, maximum fees for these loans are $15 every two weeks on a $100 loan, or a rate 38 times higher than that charged by the average credit card company for the same

loan amount. Among Southern and border states, such fees range from zero (in Georgia, Maryland, North Carolina, and West Virginia, where this industry is banned) to 17 percent of a loan's value or higher in Alabama and Mississippi. The number of high-cost payday lenders in Kentucky has more than doubled since 1999, from 353 to 779 establishments, opening at a rate of one every four days in 2006.

Kentucky pawnshop fees, another source of high-cost loans in lower-income markets, are limited to 22 percent per month. Fees for pawnshops in other Southern states range from no limit (in Arkansas, Maryland, and West Virginia) to 20 percent or more (in nearly every other state in the region).

- ***Tax Services:*** According to our survey of Kentucky households, about one in three lower-income households pays a for-profit tax preparation service to do their taxes. These same lower-income households are two to six times more likely as all others to use refund anticipation loans, carrying fees that generally range between $10 and $80.[1]
- ***Car Prices:*** More than 72 percent of lower-income households in Kentucky own a car. Nationwide, consumers from lower-income neighborhoods pay up to $500 more, on average, to buy the same car that a consumer from a higher-income neighborhood buys.

- ***Car Loans:*** Nationwide, lower-income consumers pay at least 2 percentage points more for an auto loan than the average among all other consumers. No Kentucky data are currently available to measure auto loans prices in the state.
- ***Car Insurance:*** In a sample of prices from three insurance companies, drivers from lower-income Kentucky counties and neighborhoods pay, on average, $384 more per year for auto insurance than drivers in high-income neighborhoods, holding other factors constant. The highest fees are charged in lower-income neighborhoods in Louisville and in many of Kentucky's rural eastern counties. Prices may be even higher because of other factors—considered by some companies in the calculation of insurance prices—that are correlated with household income, like credit report information, educational attainment, and occupation.
- ***Home Loans:*** In 2005, 41 percent of the mortgages to lower-income households in Kentucky were defined by the Federal Reserve as high-cost mortgages, compared with just 16 percent of mortgages sold to the highest-income households in the state.
- ***Home Insurance:*** In a sample of prices from three insurance companies, homeowners in Kentucky's lower-income neighborhoods pay, on average, at least $363 more annually for home insurance than homeowners in high-income neighborhoods, holding other factors constant. Prices may be even higher because of other factors—considered by some companies in the calculation of insurance prices—that are correlated with household income, like credit report information, educational attainment, and occupation.

- ***Furniture, Appliances, and Electronics:*** Fifty-nine percent of rent-to-own customers earn less than $25,000 a year. Reported prices for buying from rent-to-own businesses can double the price of a product.
- ***Groceries:*** While smaller, and often more expensive, grocery stores are generally found in Louisville and Lexington's lower-income neighborhoods, the statewide picture in Kentucky is quite different. In fact, large grocery stores, which typically offer lower prices, are present in 35 percent of lower-income neighborhoods, while among the highest-income neighborhoods, only 19 percent have large stores.

Kentucky has made substantial investments in helping to boost the income of lower-income workers, but it has done little to address problems on the other side of a family's ledger

Chronicled in the Governor's Summit on Quality of Life report, Kentucky is already moving forward on many fronts to reduce poverty by increasing educational attainment, creating job opportunities, and making work pay.[2] State lawmakers have heavily invested in the quality of education, both at the K-12 and postsecondary levels. The Kentucky Housing Trust Fund is one of several initiatives to build wealth among lower-income families. Statewide outreach to increase participation in programs such as the federal Earned Income Tax Credit (EITC) have ensured that millions of dollars are returned to Kentucky's families and likely spent in the local economy. These efforts, along with other well-established state and federal initiatives, are central to helping lower-income workers move up the economic ladder and join the middle class.

Yet, Kentucky still stands out for its low wages and very high poverty rates. According to the most recent census data, Kentucky has the sixth lowest median income in the country, the fourth highest poverty rate, and the eighth highest child poverty rates. What's more, the Appalachian region of the state is among the poorest areas in country.[3] Thus, although progress has been made, much more is needed.

Among the reasons why poverty in Kentucky has persisted despite the state's antipoverty investments is that Kentucky, like most other states, has focused almost all of its antipoverty investments on strategies to boost the income of the poor. That emphasis makes sense to some extent: Without rising incomes, no one can move up the income ladder. But, earnings and assets represent only one side of the family budget ledger. In fact, the spending side—the cost of living—is also an obstacle to upward mobility. Higher prices for basic necessities diminish the ability of earnings to foster economic mobility by thwarting efforts to save and invest in their children, education, homeownership, and retirement. Higher costs of living also erode the impact of investments in the poor by making these programs more costly than they need to be and preventing more people from climbing up the rungs of the economic ladder.

In fact, some of the highest prices for basic necessities in Kentucky are in its poorest areas, including the Appalachian region, where everything from mortgages to insurance is comparably more expensive than in most other areas of the state. Faced with these higher prices, a dollar earned by these families does less to help them get ahead than if it were earned by someone with a higher income.

Kentucky can lower these higher prices and do so in ways that defy the traditional politics and fiscal costs of initiatives that focus on boosting the income of Kentucky's poor families. The poor do not need to pay more.

The moment is ripe for public and private leaders to reduce both real and perceived higher costs of doing business with lower-income consumers, curb market abuses that inflate prices, and invest in consumer education

State and local leaders and their private-sector partners should enact reforms that reduce the unnecessary cost burdens faced by these same families. Specifically:

- ***Public and private leaders should lower real and perceived roadblocks to doing business with lower-income markets by promoting market-based solutions.*** Businesses will respond to profitable opportunities to engage lower-income consumers and in doing so create more options for these families to lower their costs and get ahead. Engaging the business community should occur in concert with community outreach to help promote mainstream businesses among lower-income households in Kentucky.
- ***Public and private leaders should weed out high-priced businesses in lower-income neighborhoods.*** At the local level, leaders can use their licensing and zoning authority to curb the development of these businesses. At the state level, leaders can enact stricter regulations as well—as long as there are responsible mainstream alternatives in place.
- ***Public and private leaders should help consumers navigate the complex choices in today's market.*** Ultimately, consumers must be able to make smart bets on getting ahead, which requires considerable consumer savvy amid an increasingly complex market. Among the many choices consumers now face are hundreds of different mortgage products, dozens of mortgage and insurance companies, new breeds of financial services, and the growing importance of credit reports and scores. To increase consumer awareness, Kentucky's leaders should expand access to the Internet (with its wealth of consumer information) among lower-income families (64 percent of Kentucky's lower-income consumers lack such access currently). Kentucky's public and private leaders also should build on financial education investments by a) evaluating the gaps in financial education delivery in their jurisdictions; b) using best practices to fill those gaps; and c) establishing a method for measuring the impact of investments in financial education. ■

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