Individual Development Accounts

All Nebraska families deserve the opportunity to live "the good life," but for many years, policies that encourage families to build & sustain assets as a means of financial security have left lower income families out. New ways to help families build assets have demonstrated success and are a potential tool in helping more families become financially secure.

Poverty is damaging not only to individuals who experience it but to communities and our society as a whole. Though governments and private organizations have sought to address poverty, the number of people living in poverty has continued to grow both nationally and in Nebraska. These growing numbers suggest that the current methods of addressing poverty have largely failed. In order to address poverty, we need to increase efforts focused on evidence-based solutions that lead to longer term financial stability.

Over the last couple of decades, evidence has emerged that helping lower income families build and sustain assets has the potential to help more families and ultimately communities to greater financial stability. Research has demonstrated not only that lower income families can save but also that incentivizing asset building in public policies and programs for lower income families – in the same way that we do for higher income families with things like mortgage deductions – can lead to better outcomes.

This issue brief explores Individual Development Accounts (IDAs) as a promising model for helping more families attain greater financial stability.

Issue Brief

Individual Development Accounts: A Pathway to Economic Stability

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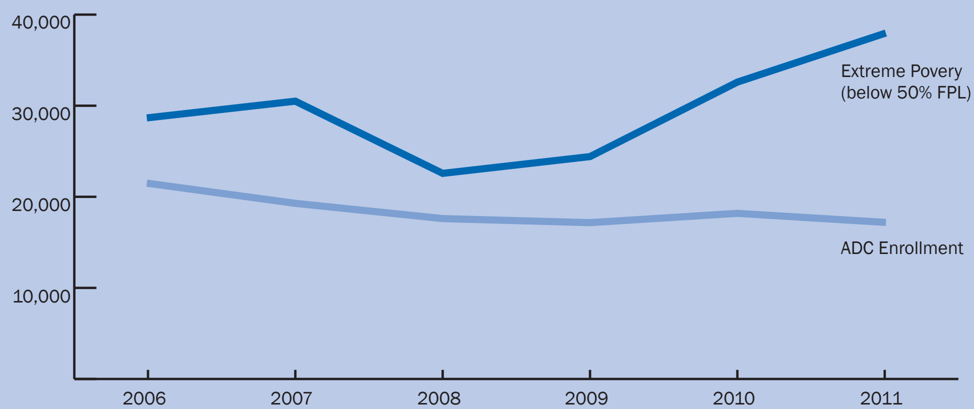
Poverty in Nebraska

Although Nebraska's economy has fared better than many other states, statewide poverty numbers have increased significantly over the past decade -- from 10% in 2000 to 15% in 2012.[1] Poverty numbers in the state have remained high despite relatively low unemployment, meaning that many of those living in poverty are working. In fact, 23% of Nebraska working families with children are considered to be low-income, defined as making less than twice the poverty level, or less than $46,100 per year for a family of four.[2]

Public Assistance Alone Has Not Reduced Poverty

For many years, the main governmental methods of addressing poverty were focused on sustaining a family's resources and income until they could return to financial stability. In 1997, the government's main cash assistance program, then known as Aid to Families with Dependent Children (AFDC) was converted to a new program known as Temporary Assistance for Needy Families (TANF). The new program contained a 5-year lifetime limit for participants as well as new work requirements. It also gave states more flexibility in the use of funds. Data shows that participation in the state's TANF program, known as Aid to Dependent Children or ADC, has remained flat while the number of children living in extreme poverty, defined as 50% or less of the federal poverty level (less than $11,525 per year for a family of four), has increased.

Children recieving ADC vs. children in extreme poverty (2006-2011)



Children in extreme poverty data are from U.S. Census Bureau, American Community Survey 1-Year Estimates, Table B17024. ADC numbers are from Financial Services, Operations, Nebraska Department of Health and Human Services (DHHS).

The goal of the new TANF program was to move families to greater financial stability, but the numbers suggest that the program has largely failed to impact child poverty, even among the poorest children in the state. One of the issues with the TANF program is that it underemphasizes one element that plays a key role in longer term financial stability – assets. An asset is

1. *Kids Count in Nebraska 2011 Report, (Omaha, NE: Voices for Children in Nebraska, 2012), 55.*
2. *Kids Count Data Center, http://datacenter.kidscount.org/NE.*

something that has value – a home or car; a bank account; an investment that has a cash value.

Why Assets Matter

Almost a quarter of all Nebraska households – 23.5% -- were considered asset-poor in 2012,[3] defined as lacking the resources to survive at the poverty level ($23,050 per year for a family of four) for three months in the absence of income. This not only tells us that the loss of a job would put these families in significant financial peril, but also tells us that they are not well-positioned to weather common financial emergencies – like a car repair or significant medical bill. Further, it means that both generations of the family are unlikely to have adequate resources to prepare for the future – like a retirement account for aging parents and a college savings account for growing children.

Having assets can significantly increase the financial stability of a family. Our major public benefit programs aimed at helping low-income families have taken some steps toward recognizing the importance of assets. The federal governement has given states the flexibility to eliminate so-called "assets tests" to qualify for programs. Forty-three states, including Nebraska, have minimized or eliminated assets limits in the food stamp (now known as SNAP – or the Supplemental Nutrition Assistance Program) and several others have done the same in TANF and Medicaid.[4]

In his 1991 book, *Assets and the Poor: A New American Welfare Policy,* Michael Sherraden presented the idea that poverty was characterized not just by a lack of income, but by a lack of assets. He also argued that poor people, with help and encouragement, can save. He further demonstrated that government programs to encourage assets were not new, but were overwhelmingly tilted toward the middle class and above, in the form of the home mortgage interest deduction, Individual Retirement Accounts, and other policies.[5]

Individual Development Accounts: A New Method of Promoting Economic Stability

Individual Development Accounts (IDAs) are a concept that was first championed as a solution to the assets issues highlighted in *Assets and the Poor.* An IDA is a goal-directed matched savings account for lower income families. The participant agrees to contribute a monthly amount in earned income to a special savings account over a specific duration. Agreed upon contributions are matched from a public or private source and the savings is ultimately used toward an asset purchase – most commonly for a down payment on a home, to start or improve a small business, or educational expenses. During the savings period, the participant is also required to accomplish three short-term financial goals: attend financial education

3. Center for Enterprise Development, "Assets and Opportunities Scorecard." Last modified 2012. Accessed November 30, 2012.
4. Sprauge, Aleta, and Rachel Black. "State Asset Limit Reforms and Implications for Federal Policy." . http://www.newamerica.net/publications/policy/state_asset_limit_reforms_and_implications_for_federal_policy (accessed November 30, 2012).
5. Sherraden, Michael. Assets and the Poor: A New American Welfare Policy. New York: Russell Sage Foundation, 2001.

The Problem
Asset poverty among low-income households.

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The Intervention
IDA programs that offer financial education and savings incentives.

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The Intended Outcomes
- Savings accumulation leading to asset acquisition.

- Improved financial management.

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The Intended Long-term Outcomes
- Economic benefits such as increased income and wealth.

- Social benefits such as greater personal efficacy and community involvement.

Rohe, William, Lucy Gorham, and Roberto Quercia. "Individual Development Accounts: Participants' Characteristics and Success." Journal of Urban Affaris. 27. no. 5 : pp. 503-520.

classes, attend an asset-specific class or training, and establish a consistent pattern of savings. The intended result is that participants leave the program not only with an asset but also better equipped with positive financial behaviors.

The Federal government has recognized the promise of asset-building in multiple ways. The 1996 TANF reforms allowed program funds to be used for IDAs. In 1998, the federal government established the Assets for Independence (AFI) Program. This program provides federal funds for IDA programs aimed at the acquisition of the three common assets mentioned previously – homeownership, small business and education. Nebraska received its first AFI grant in 2000 and most recently received a grant in 2010 aimed at providing more accounts statewide. The most recent grant was given to Community Action of Nebraska, and has been sub-granted to programs in eight communities across the state. In addition, there have been several privately funded IDA pilot programs in Omaha and other communitiessince 2000.

To date, 42 states have enacted state IDA programs, although not all were funded in the most recent fiscal year.[6]

Funding Source	State
General Funds	CT, IN, MN, MO, NC, NM, OH, PA, TN VT
TANF and Welfare-to-Work funds	AR, CO, HI, IL, IA, MI, MO, MT, NJ, OH, OK, PA, SC, TN, TX, VA, WA
Community Development Block Grant	AR, NC, TN, VA
Tax credits to entities or individuals that provide match funds, or directly to accountholders	AR, CO, CT, HI, IN, KS, ME, MO, OR, PA
Housing trust funds	NC, OH

Note: Includes both active and inactive state programs
Sources: CFED survey of state agencies and/or state program administrators, July 2011. Supplemented with information from: N. Warren and K. Edwards, "Status of State Supported IDA Programs in 2005," St. Louis, MO: Center for Social Development, 2005

6. *Center for Enterprise Development, "Resource Guide: State IDA Program Support." Last modified 2012. Accessed November 30, 2012. http://cfed.org/assets/scorecard/2013/rg_StateIDAProgramSupport_2013.pdf.*

Research Shows that Low-Income Families Have the Ability to Save

One assumption that many people have is that low-income families don't have the ability to save. In fact, the majority of the policies that provide savings incentives – like tax incentives for education or retirement savings – have traditionally left lower income families out. While it's true that many low-income families are living paycheck to paycheck, research has found that many low-income families can save, and that they are more apt to do so with supports in place to facilitate savings.

An Urban Institute study looked at approximately 3,000 families from 1994 to 2007 and tracked how often these families fell below the poverty line over the 13 year period and how their net worth ultimately increased or decreased over time. Over this time period, 40 percent of the families whose incomes fell below the poverty line for more than half of the time saw an overall increase in net worth. The same study also looked at a cohort of families who were both low-income and asset poor from 1989 to 1995 and assessed the same families again from 2001 to 2007. In total, 44 percent of those families had saved enough over that time period to escape poverty.[7]

Through an initiative in New York called "Save NYC," lower income tax filers are offered matching funds if they save a portion of their tax refund. Sixty-one percent of the first year participants, who on average had an annual household income of $15,000, contributed at least $500 to their account.[8] Matching funds are an important part of incentivizing savings for lower income households and have the potential to address the gap in savings policy incentives for lower income families. A 2006 field experiment conducted with a paid tax preparer offered varying match rates to a randomized sample of tax filers across income ranges for Individual Retirement Account (IRA) contributions. The study found that those who were offered matching funds were more likely to contribute to an IRA and the higher matching rates resulted in higher take up rates.[9]

These studies suggest not only that lower income families can save but also that matching funds, like those that are offered to higher income families through many 401(k)s, are an effective incentive.

Is the IDA Program Model Effective?

Research on IDA programs done over the past decade has shown them to be an effective tool for increasing the financial stability of lower income families. The first systematic study of IDAs was the American Dream Demonstration (ADD)—a foundation-funded national demonstration of IDAs that ran from 1997 to 2003. The first report on this project, published in

These studies suggest not only that lower income families can save but also that matching funds, like those that are offered to higher income families through many 401(k)s, are an effective incentive.

7. McKernan, Signe-Mary, Caroline Ratcliffe, and Trina Williams Shanks. "Can the Poor Accumulate Assets?." Opportunity and Ownership Facts. no 23. June (2012).
8. New York City Center for Economic Opportunity, "Evidence and Impact." 2010.
9. Duflo, Esther, William Gale, Jeffrey Liebman, Peter Orszag, and Emmanuel Saez. "Savings Incentives for Low and Middle Income Families: Evidence From a Field Experiment with H&R Block." The Quarterly Journal of Economics. no. November (2006): 1311-1346.

2002, evaluated the outcomes of 14 programs from across the United States through 2001. Key findings were:

- Average monthly net deposits were about $19 per participant, or 1.6% of monthly income,
- Net deposits averaged $528 per participant and totaled $1,543 with matching funds,
- Thirty-two percent had withdrawn funds for an asset purchase and of those 32% were used for home purchase, 23% for small business and 21% for education.

The report also found that differences in income levels and demographics among program participants largely did not have an impact on ability to save.[10] These results again suggested the important role that programs and policies can play in encouraging savings for all families.

A follow-up to the initial report on the ADD was published in 2004 and looked at one project site over a 48 month period. The report compares program participants with a control group of non-participants. The findings showed a net increase in asset accumulation for the participant group, especially with regard to homeownership. The report failed to demonstrate, however, an overall increase in net worth for program participants.[11]

A 2009 study explored how IDA program participants fared over the longer term by surveying both those who had completed and those who had dropped out of a program in Ohio. The survey found that:

- Participants who had completed the program reported a higher annual household income, were more likely to be employed full-time, and were more likely to own an investment account
- IDA graduates also had significantly higher post-program financial assets than dropouts,
- Of the respondents who chose a home as their asset purchase, all but one still owned the home purchased with the IDA funds,
- Of the respondents who saved for higher education, only two left their educational program without a degree, and
- Three-quarter of respondents who saved to open a small business were able to sustain the business.[12]

Another study followed up with successful IDA program graduates, those who did not complete IDA programs, and a comparison group of low-income households who had never participated in an IDA program. Those who had completed an IDA program reported higher household savings than those

10. Center for Social Development, "Saving Performance in the American Dream Demonstration: A National Demonstration of Individual Development Accounts." 2002.
11. Mills, Gregory, Rhiannon Patterson, Larry Orr , and Donna DeMarco. Abt. Associates Inc., "Evaluation of the American Dream Demonstration." 2004.
12. Loibil, Cazilia, and Beth Red Bird. "Survey of Former IDA Program Participants: How Do They Fare?." Journal of Extension. 47. no. 6 (2009): pp. 1-12.

who had left the program early as well as the comparison group.[13]

Taken together, these findings suggest that IDA programs can be successful in supporting savings and asset acquisition and can have a lasting impact on a family's financial stability.

IDA Programs in Nebraska

At the end of fiscal year 2009, nationwide about 60,000 participants in the federal Assets for Independence (AFI) program had saved over $56 million dollars. Over 23,000 participants had made asset purchases with homeownership being the most popular, followed by small business and education.[14]

In Nebraska, the AFI grant that Omaha area agencies received in 2000 ended with 22 successful program participants who saved a combined total of $26,900. Fifteen participants purchased homes, four participants started a small business, and three participants used the funds for educational expenses.[15]

The AFI grant received in 2010 and currently operating in eight communities in Nebraska has to date helped lower income families participating in the program save over $20,000 collectively.[16]

Since 2009, there has also been a program in the Omaha area called "Opportunity Passport," which is operated by Family Housing Advisory Services (FHAS) and funded by several private foundations. The program is specifically for young people who were or currently are in foster care. This program allows for additional uses of IDA funds beyond the three common assets. To date, program participants have used the funds for 88 cars, 14 houses, 11 debt consolidations, and 8 Certificates of Deposit (CDs). Of the remaining completions, 5 were used for educational expenses, 3 for medical expenses and 3 for small businesses. This program has given young people who may lack parental support additional resources and financial tools as they enter young adulthood.[17]

Additional Benefits of IDA Programs

In addition to facilitating an asset purchase and promoting sound financial behaviors, IDA programs have additional benefits. One is that they connect lower income consumers with mainstream financial services. Lower income families are more likely to be unbanked or use alternative financial services

Of the successful participants in Nebraska's 2000 AFI grant:

15 purchased homes

4 started a small business

3 used funds for educational expenses

13. Loibil, Cazilia, Michal Grinstein-Weiss, Min Zhan, and Beth Red Bird. "More Than a Penny Saved: Long-Term Changes." The Journal of Consumer Affairs. 44. no. 1 (2010): pp.98-126.
14. Assets for Independence Program, "Report to Congress: Status at the Conclusion of the Tenth Year." 2009.
15. Julia Craig, e-mail message to author, November 12, 2012.
16. Julie Farwell, e-mail message to author, November 15, 2012.
17. Julia Craig

-- like check cashers and payday loans.[18] IDA programs can provide a pathway for connecting or reconnecting families with mainstream financial services.

Another benefit of IDA programs is the common use of these funds for homeownership. Homeownership has benefits for both the individual and the community. Numerous studies have found that homeownership is associated with desirable community outcomes like increased civic participation and reduced crime.[19] Another benefit of using IDA programs for homeownership came to light during the recent nationwide increase in foreclosure rates. Foreclosure rates among homeowners who purchased their home through and IDA program were significantly lower than a comparison sample of low-to-moderate income homeowners.[20] This suggests that the financial education and case management component required in IDA programs may have played a mitigating role on foreclosure rates for these homeowners.

Finally, asset ownership has been correlated with better health and psychological well-being for families.[21] Although studies are unable to determine a causal relationship, research suggests that asset ownership has benefits that extend beyond the financial realm.

Conclusion

In recent years, research has emerged that demonstrates that encouraging lower income families to build assets is an effective means of promoting economic stability. Research has found that lower income families can save and benefit from policy incentives for asset accumulation similar to those that many higher income families have access to.

Individual Development Accounts (IDAs) provide a promising pathway for asset accumulation for lower income families. Nebraska should scale up existing IDA efforts by enabling legislation for a state funding source, as 42 other states in the country have done. This will provide an additional tool for moving more families toward greater financial stability and ultimately improving the financial stability of our state as a whole.

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19. National Association of Realtors, "Social Benefits of Homeownership and Stable Housing." 2010.
20. Rademacher, Ida, Kasey Wiedrich, Signe-Mary McKernan, Caroline Ratcliffe, and Megan Gallagher. Center for Enterprise Development and the Urban Institute, "Weathering the Storm: Have IDAs Helped Low-Income Homebuyers Avoid Forclosure?." 2010.
21. Lerman, Robert, and Signe-Mary McKernan. The Urban Institute, "Poor Finances: Assets and Low-Income Households." 2008.