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THE ASSETS AGENDA

Policy Options to Promote Savings and
Asset Ownership by Low- and Moderate-
Income Americans

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The current economic downturn, triggered in part by excessive household debt and deflating housing prices, underscores the central role asset ownership plays in the economic security of American families and the broader economy. Broad asset ownership, whether through savings or investment, has the potential to connect economic opportunity with economic security and ensure that every member of society is afforded a real stake in the commonwealth.

Assets are important not only because they can be deployed productively or tapped to help individuals and families weather unexpected events, but because they have behavioral effects that can change the manner in which people think about and plan for the future.

Past efforts to democratize access to property, capital, and credit have had positive effects. Yet the most notable feature of our current policy paradigm is how many it excludes. Through targeted tax breaks, affluent families are given many options to acquire assets, while those with fewer resources are offered less attractive ways to build wealth. The poorest families among us are given limited access to income supports and social services. This approach misses the potential of assets to help chart a path out of poverty. If we are to successfully broaden savings and assets ownership, our policy efforts must be expanded, strengthened, and directed toward those with the greatest need.

The purpose of this report is to outline a federal public policy agenda to broaden savings and asset ownership opportunities for lower-income Americans who have limited resources at their disposal. In developing our thinking on the subject, we have drawn on the research and

expert analysis of many others in the field. The agenda we present here includes calls for new structures and policies at the federal level, as well as changes to existing tax systems, government programs, and financial products.¹ Some of these policies are well developed, others need more seasoning, but all of them have the potential to contribute to the economic well-being of millions of American families.

The purpose of this report is to outline a federal public policy agenda to broaden savings and asset ownership opportunities for lower-income Americans who have limited resources at their disposal.

This edition of New America's *Assets Agenda* is the most comprehensive to date, with 83 innovative asset-building ideas. Following the introduction, it is organized in 13 sections, each beginning with a brief synopsis of a problem, followed by specific policy proposals. ➤

Establish Children's Savings Accounts

One of the most promising ways to achieve a universal, progressive asset-building system over time is to provide every child with a restricted “start in life” asset account at birth; an idea first proposed by researcher Michael Sherraden and, separately, by former Internal Revenue Service commissioner Fred Goldberg.² Child Savings Accounts (CSAs) would be designed to facilitate future saving and lifelong asset accumulation. The introduction of such accounts would also serve as a tool for teaching personal finance basics to children and their parents. While every child would have an account, ownership would especially benefit the 26 percent of white children, 52 percent of black children, and 54 percent of Hispanic children who start life in households without any significant asset holdings.³

One of the most promising ways to achieve a universal, progressive asset-building system over time is to provide every child with a restricted “start in life” asset account at birth.

Current research and successful demonstration projects suggest that CSAs would increase financial inclusion; promote financial literacy and fiscal prudence; protect against economic shocks; improve access to education; improve health and education outcomes; contribute to the development of “future orientation;” and, over the long term, improve livelihoods.⁴ In addition to expanding economic opportunity and improving health and educational outcomes, the holding of assets has other positive spillover psychosocial effects, such as encouraging risk-taking and increasing personal efficacy, social influence, and civic participation.

There is no single template for the design of such accounts and various proposals have been put forward. Under one possible scheme, an account would be automatically opened by the government at a child's birth—or during the first year of primary school enrollment—in the child's name at a local bank. The government might “seed” the account with an initial contribution and/or provide matching contributions to deposits made over the years by the child and the child's family. The child could only use the accumulated funds for specific purposes, such as paying for higher education, purchasing a home, or starting a small business.

Most CSA proposals, even those that are not meant to be universal, have some, if not all, features in common. They are: (a) *incentivized* (e.g., “seeded” through up-front external funding or matched in response to the account owner's deposits or behavior), (b) *progressive* (i.e., designed in favor of lower-income children and households), and (c) *restricted* to specific uses (e.g., education, microenterprise, or the purchase of a productive asset).⁵ The design choices for a specific CSA policy or product will depend on the capacity and constraints, as well as the particular goals, of the implementing party.

In the United Kingdom, where universal and progressive CSAs were established in 2002, the government mails parents/guardians a £250 voucher (worth about \$500) upon the birth of a child, which the parent or guardian uses to open a savings account in a commercial bank on the child's behalf. As of September 2007, 2.5 million child trust funds had been opened in the U.K., of which 24 percent had received additional contributions beyond the government's seed money.⁶

Several countries are experimenting with targeted CSA programs. South Korea has begun implementing a program with plans to reach all of its most disadvantaged children; Canada offers CSAs for all low-income kids for higher education. Australia, Hungary, and Hong Kong are also considering CSA proposals. The specifics of these policies and policy proposals vary. Several involve public-private partnerships, including the active participation of the financial services sector and civil society organizations. The privately funded SEED Initiative, a multi-year national initiative to develop, test, and impel matched savings accounts and financial education for children and youth in 12 sites across the United States, is providing highly valuable insights into policy design.

If families are to be able to build up their asset base, parents should be encouraged to save for their children's future.

Policy Options

The ASPIRE Act

The America Saving for Personal Investment, Retirement, and Education Act (ASPIRE Act) proposes the creation of a system of universal children's savings accounts. Under the act, which was introduced in 2005 with bipartisan

support, the federal government would provide every child with an account at birth—a KIDS Account—endowed with \$500 and backed by progressive, targeted incentives. At age 18, account holders could use accumulated funds to pay for college, buy a home, or build up a nest egg for retirement.⁷ Children from households with incomes below the national median would receive a one-time supplemental deposit of up to \$500 and would be eligible to receive an additional \$500 match for voluntary savings deposited each year. Voluntary contributions to the account would be tax free and could not exceed \$1,000 a year. Access to account funds would be restricted until the account holder reached the age of 18, and parents or legal guardians would control investment decisions until that time. Financial education would be offered to kids and their parents to help them make good investment decisions. The bill was reintroduced in the 110th Congress in September 2007, cosponsored by Representatives Patrick Kennedy (D-RI), Phil English (R-PA), Jim Cooper (D-TN), Rahm Emanuel (D-IL) and Tom Petri (R-WI). Sen. Charles Schumer (D-NY) intends to introduce a bipartisan Senate version of the bill in 2008.

Young Saver's Accounts

Presently, there are no age restrictions on owning a Roth Individual Retirement Account (IRA), but only individuals with earned income are eligible to set up and contribute to such accounts. As a result, most children are unable to take advantage of this tax-advantaged savings vehicle. Young Saver's Accounts (YSAs) would fill this void in the savings continuum by creating a place for children's savings with favorable tax treatment. Like existing Roth IRAs, YSAs would permit penalty-free withdrawals for postsecondary education and the purchase of a first home. Allowable contribution levels would be determined by parents' earned income, and contributions could be made by children, parents, grandparents, and others. Contributions to a child's YSA would count toward the parent's annual limit for Roth IRAs (now \$5,000 for those aged 49 and under). Contributions made by low-income families would qualify for the Saver's Credit, and the amount deposited would be excluded in determining eligibility for means-tested programs. Initially introduced by Sen. Max Baucus (D-MT) in March 2006 as part of the Savings Competitiveness Act, the provision was adopted by Senators Hillary Clinton (D-NY) and Gordon Smith (R-OR), and included in the New Saver's Act, which they introduced in the summer of 2007.

PLUS Accounts

Senator Jeff Sessions (R-AL) has proposed that the federal government open a Portable, Lifelong and Universal Savings (PLUS) Account for every U.S. citizen born after December 31, 2007, and that such accounts be endowed with a one-time deposit of \$1,000. Senator Sessions also proposed that individual PLUS accounts be established for all working U.S. citizens under the age of 65, beginning January 1, 2009, with a mandatory one percent of a worker's pre-tax paycheck withheld and automatically deposited into his or her account. In addition, workers would be allowed to voluntarily contribute up to 10 percent of their pretax income. Employers would be required to contribute at least one percent (and up to 10 percent) of an employee's earnings. No withdrawals from PLUS Accounts could be made until the account holder reached the age of 65, although there would be a loan program for pre-retirement uses.

401Kids Savings Accounts

First introduced in 2006 by Rep. Clay Shaw Jr. (R-FL) and other House Republicans, H.R. 5314 would convert Coverdell Education Savings Accounts into 401Kids Savings Accounts. The new account would have expanded uses, and could be rolled over into a Roth IRA. This proposal would make it possible for a restricted, tax-advantaged savings account to be opened in a child's name as early as birth, with up to \$2,000 in after-tax contributions permitted each year. The funds could be used for the K-12 and postsecondary education expenses currently allowed under Coverdell Education Savings Account rules as well as for other qualified uses, including the purchase of a first home or retirement. The bill was reintroduced in the 110th Congress by Rep. Judy Biggert (R-IL).

Lifelong Learning Accounts

In January 2007, Los Angeles mayor Antonio Villaraigosa, a member of the U.S. Conference of Mayors working group on antipoverty policy, proposed making investment in lifelong learning and skills development the centerpiece of a national antipoverty agenda. He proposed creating a savings account for every child at birth. Access to account resources would be restricted until after high school graduation. At age 18 account holders could use their savings to pay for expenses associated with postsecondary education and career-directed workforce training.

Savings Bonds as a Means of Saving for Children

A recent pilot project by the Doorways to Dreams (D2D)

Fund and four community partners revealed a strong awareness of and demand for U.S. Savings Bonds among low-income tax filers. Notably, roughly four-fifths of bonds purchased in this pilot project included co-owners, generally children or grandchildren.⁸ If encouraged to do so, the parents and grandparents of low-income children would likely be willing to begin saving for their children and grandchildren with a product that already exists, has a low minimum purchase amount, and has no restrictions on purchase based on prior credit history. Promoting Savings Bonds to low-income families could be the most immediate way to encourage the opening of a large numbers of savings accounts for children.

529 College Savings Plans as the Basis of a Universal Children's Savings Account

529 College Savings Plans are state-administered tax-advantaged accounts designed to help children and their families save for postsecondary education. As the New America Foundation and the Center for Social Development have suggested, a revised version of the

existing program could form the basis of a universal children's savings account policy and be used for other asset building purposes.⁹ Current 529 features, such as public sector oversight, centralized accounting, limited investment options, and the ability to subsidize the cost of small accounts (which may be unprofitable) with larger ones (with higher profit margins) could serve as the "plumbing" for a more inclusive children's savings system. One of the problems with the existing program is that lower-income families cannot take advantage of the built-in tax incentive. Already a number of states are expanding their efforts to create incentives for lower-income families to contribute to such plans. The Center for Social Development and the state of Oklahoma have set up a program—SEED for Oklahoma Kids. Under this experiment, a seed grant of \$1,000 will be deposited in each of the 529 plans of 1,300 newborns selected from a random sample of Oklahoma birth records. Over seven years, various child and family will be compared to a control group of 1,300 newborns who do not receive a SEED for Oklahoma Kids account with any deposits. ➡

Create Incentives To Save

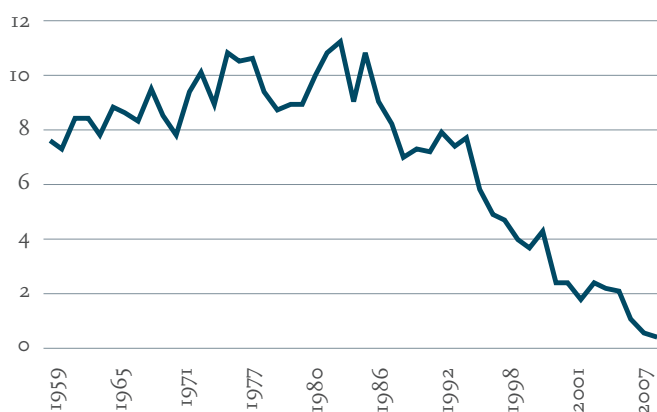
Savings are a critical component of economic security for families and the nation as a whole. From a national perspective, savings are important because they create pools of capital for investment purposes that promote productivity and keep interest rates low. At the household level, personal savings help protect individuals and families against unexpected loss of income, smooth out their consumption over the life cycle, help maintain a reasonable standard of living in retirement, and serve as the basis of intergenerational wealth transfer. For those with few resources, the value of savings is that they can be converted to assets, and thus chart a path toward greater economic stability and opportunity.

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There has been a precipitous decline in the U.S. personal savings rate since the late 1980s. In the last three years, the rate has hovered close to zero, which means that Americans are spending almost all of their disposable income.¹⁰ In 2007, U.S. households saved \$42.9 billion, or only 0.4 percent of total disposable personal income.

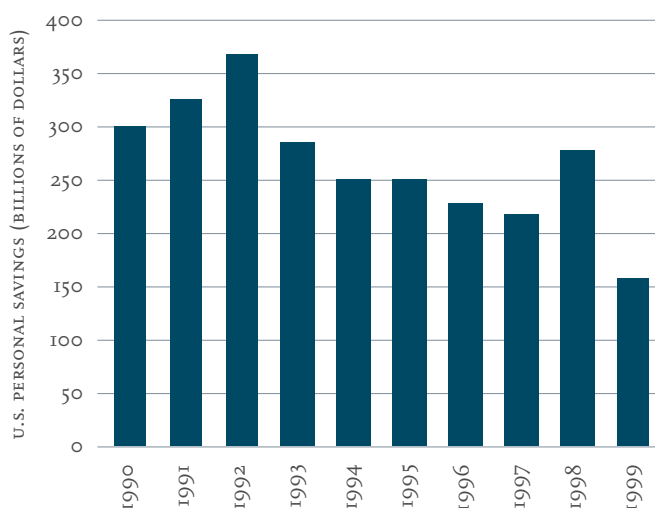
Personal Savings Rate 1959–2007

PERSONAL SAVINGS AS A PERCENTAGE OF DISPOSABLE INCOME



Source: U.S. Department of Commerce, Bureau of Economic Analysis, "Personal Saving Rate January 1, 1959 to 2007," March 1, 2008.

Personal Savings Amounts 1990–99



Source: U.S. Department of Commerce, Bureau of Economic Analysis, Comparison of Personal Saving in the National Income and Product Accounts (NIPAs) with Personal Saving in the Flow of Funds Accounts (FFAs), April 30, 2008.

According to a recent poll by the Consumer Federation of America and Wachovia, 52 percent of adults do not believe they are saving adequately, and 17 percent say that they "cannot afford to save at all."¹¹ Insufficient earnings, consumer debt, and regular and unexpected expenses hinder household saving efforts, according to the study's more in-depth analysis of discouraged savers. At the same time, rising life expectancy means that higher savings are required to see people through to the end of their lives.

The serious decline in the personal savings rate to near zero is cause for concern because household savings are essential for asset accumulation. However, we should recognize that different households have different savings needs. While savings policy has traditionally focused on retirement needs, many households would benefit from building up a pool of flexible savings that could be tapped in an emergency.

According to a national representative sample, only 40 percent of Americans reported setting aside funds for emergencies, and only about half of emergency savers did so through automatic and regular transfers from a checking account to a savings account.¹² Younger, lower-income, and minority households are less likely to have emergency funds, compared to 58 percent of households earning \$75,000 or more.

The lack of accessible savings can undermine household stability and make long-term planning difficult. It contributes to asset poverty, consumer debt, and higher bankruptcy rates.¹³ In 2004, nearly one in five households had zero or negative wealth levels, and close to one in three had a net worth of less than \$10,000.¹⁴ On the other end of the spectrum, the top five percent of households in terms of income distribution held 59 percent of all net worth and 68 percent of all common stock (excluding pensions). Housing equity was more evenly distributed, with the top five percent of households holding 32.4 percent and the bottom 80 percent holding 34.6 percent.¹⁵

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In 2004, 12.2 percent of families were heavily indebted, that is, their debt exceeded 40 percent of their income.¹⁶ According to the six most recent Survey of Consumer Finances (1984–2004) conducted by the Federal Reserve Board, families earning less than \$20,000 had the greatest share of debtors with debt to income ratios that exceeded 40 percent. Over this period, more than a quarter of families in this income group were heavily indebted. Since 2004, the problem of indebtedness has worsened, as reflected in a number of indicators, including bankruptcy filings. Changes in the bankruptcy laws led to a decline in the number of bankruptcy filings in 2006. But mounting household and mortgage debt, along with the continued rise in medical debt, has pushed bankruptcy filings higher again. Between January and March 2008, consumer bankruptcy filings increased 27 percent nationwide, totaling 86,165 in March alone.¹⁷

If families are to be able to save and build up their asset base, we need to provide incentives to encourage saving and create accessible mechanisms to make saving easier.

U.S. Bankruptcy Cases Commenced, 2000–06

2000	1,253,444	2004	1,597,462
2001	1,492,129	2005	2,078,415
2002	1,577,651	2006	617,660
2003	1,660,245	2007	850,912

Source: U.S. Federal Courts, "Total Bankruptcy Cases Commenced, Terminated and Pending, Calendar Years 2000–2006," <http://www.uscourts.gov/bkrcpctstats/statistics.htm#fiscal>; and U.S. Federal Courts, press release, April 15, 2008.

Policy Options

Create an Automatic, Accessible, National "AutoSave" Plan

Reid Cramer of the New America Foundation has proposed an automatic national savings plan, available to all workers, which could facilitate the accumulation of non-restricted, pre-retirement savings.¹⁸ Under this "AutoSave" plan, employers who make direct deposit salary payments into an employee's checking account would also make deposits in to AutoSave on behalf of their employees (the self-employed would be able to make deposits at their discretion). Money deposited in this system would belong to the individual worker, and since deposits would be in after-tax dollars, normal tax rules would apply. As the name of the plan suggests, workers would be automatically enrolled unless they opted out. Individuals would have the flexibility to opt out of the system or withdraw their savings at any time. The default contribution rate might be set at two percent of pay. At that rate, an individual earning \$50,000 a year would have \$832 diverted directly into savings. A pilot AutoSave program is being designed to test the concept in the private sector. An AutoSave program might include financial and non-financial incentives to encourage longer-term savings, as well as financial education. By requiring individuals to opt out if they did not want to participate in the program, AutoSave would depend for its success on the tendency on the part of many toward inertia.

Enact a “Saver’s Bonus” Linked to Existing Tax Credits

Under this program, targeted households would be rewarded with a Saver’s Bonus for making a commitment to save a certain sum when they filed their tax returns. Contributions of up to \$500 annually to eligible savings products, such as an IRA or a 529 College Savings Plan, or for the purchase of U.S. Savings Bonds, might be matched on a one-to-one basis. Anyone qualifying for the federal Earned Income Tax Credit (EITC) would be eligible to receive the bonus, which would be delivered through the tax filing and refund process. The matching funds would be delivered as a higher refund—thus the “Saver’s Bonus”—and would be deposited directly into the savings product specified by the taxpayer. Such a program might be more politically acceptable than creating a new refundable tax credit. Alternatively, eligible taxpayers could report contributions they made to their savings accounts during the previous year and claim the match through a higher refund amount. The taxpayer might receive a higher refund directly, or, ideally, the higher refund would be redirected to the specified savings product. The cost of this proposal would depend on the size of the bonus and the number of people eligible. Individuals who did not own bank accounts would be able to open accounts and gain access to savings products by means of their tax returns. In addition to providing financial support to lower-income working families, the Saver’s Bonus would provide them with a meaningful incentive to save and ensure that the “un-banked” were given access to mainstream financial services.

If families are to be able to save and build up their asset base, we need to provide incentives to encourage saving and create accessible mechanisms to make saving easier.

Improve the Saver’s Credit

The 2001 tax bill created a new voluntary individual tax credit—the Saver’s Credit—to encourage low-income workers to contribute to existing retirement products, such as IRAs and 401(k)s. Under the Pension Protection Act of 2006, Congress, at the behest of President Bush, made the Saver’s Credit permanent and indexed the contribution limits to inflation. However, the Saver’s Credit is

flawed in that it is not refundable and offers only a modest matching contribution. Consequently, it benefits only a small proportion of low-income individuals. Only about 20 percent of filers get any benefit, while only one in a thousand receives the full benefit. Mark Iwry of the Brookings Institution, who helped design the Saver’s Credit, suggests three ways to improve the program: (1) make it refundable; (2) expand eligibility—instead of a 50 percent credit that phases down to 20 percent for joint filers with adjusted gross income over \$30,000, the 50 percent Saver’s Credit should be expanded to cover joint filers with significantly higher incomes, so households earning up to \$60,000 a year would receive the full benefit and households earning up to \$75,000 would receive a reduced benefit; (3) smooth the phase-down of the credit to resemble IRA income eligibility, instead of the “cliffs” now in effect.

Expand the List of Products Eligible for the Saver’s Credit

If the goal is to promote all forms of saving among low-income workers, not just saving for retirement, a range of existing savings products—529 plans, Coverdell Education Accounts, Health Savings Accounts, U.S. Savings Bonds, and Individual Development Accounts—could be added to the list of products that would trigger the Saver’s Credit. Such an expansion of the Saver’s Credit is justified, it might be argued, because maintaining one’s health and acquiring pre-retirement assets—especially a first home and postsecondary education—are critical elements of retirement security. This is not much of a stretch, since individuals are already permitted to make penalty-free withdrawals from their IRAs to buy a first home and pay for postsecondary education. And low-income savers are more likely to be able to purchase U.S. Savings Bonds—which have a range of holding terms—than to invest in stocks or mutual funds for their retirement.¹⁹ President Bush recommended expanding the Saver’s Credit in his budget proposals for Fiscal Years 2008 and 2009.

Expand Individual Development Accounts

Individual Development Accounts (IDAs) are matched savings accounts generally aimed at helping lower-income households buy a first home, pay for postsecondary education and job training, or start a small business. Such accounts might usefully be expanded in three ways:

Reauthorize and improve the Assets for Independence Act (AFIA). In 1998, Congress authorized a five-year, \$125

million demonstration program to award grants on a competitive basis to community-based organizations to run IDA programs. The AFIA demonstration program, which now provides the vast majority of funding for IDAs throughout the country (a significant portion of all state and private sector IDA programs also receive funding through the AFIA program) and is the only such program with a significant evaluation component at its core, should be reauthorized by Congress. In the reauthorization process, Congress should relax the requirement that federal grants must be spent for the exact same purpose as the nonfederal funds that must be raised in order to secure federal AFI funds.²⁰

Enact the Savings for Working Families Act (IDA Tax Credit). The proposed Savings for Working Families Act would expand access to individual development accounts and also provide a tax incentive for working families to save. The bill would authorize tax credits to financial institutions that set up and matched (up to \$500 per person, per year) such accounts for 900,000 low-wage working individuals over a seven-year period. (The proposal was previously supported by the Bush administration.) The tax-preferred savings accounts could be used for postsecondary education expenses, first-time homebuyer costs, business capitalization, and rollovers for retirement.

Allow Prize-Linked Savings Products

Inaugurated by the British in 1694, lottery or prize-linked savings products have since proven to be an effective vehicle for encouraging household savings by low- and moderate-income families across the globe. Peter Tufano of the Harvard Business School is currently exploring the potential of this type of product to encourage new savings. While the specific products vary, the concept of a prize-linked savings account is simple: individuals invest or save in a product with no risk of principal loss (savings account, government bond, etc.) and accept a reduced return (interest payment) for the chance to win randomly drawn cash prizes.²¹ Unfortunately, laws governing state-sponsored lotteries in the United States inhibit financial service providers from offering innovative lottery-type products. Changing these laws would allow for greater innovation in the development of potentially attractive savings opportunities.

Issue “Work Bonds” to Match Household Savings

In an effort to move saving incentives out of the tax code, presidential candidate John Edwards proposed the development of state-issued “work bonds” to match the savings of low- and moderate-income families. Families earning less than \$75,000 a year would be eligible to receive a one-to-one match on dollars saved, up to \$500 a year. The match would be delivered in the form of a savings bond. This was one of the more innovative savings proposals that emerged during the presidential campaign.²² Although the idea was not fully developed, it merits additional consideration. ♦

Expand Access To Quality Financial Services

Gaining access to mainstream financial services and products is often the first step in building assets and wealth. According to one estimate, up to 10 percent of all American households and 30 percent of low-income families are “unbanked,” meaning they lack a basic checking or savings account.²³ According to another survey, while 95.5 percent of white non-Hispanic families have a checking account, only 80.6 percent of nonwhite or Hispanic families do.²⁴ And according to the U.S. Census Bureau, 14 percent of U.S.-born white families are without a bank account, compared to 34 percent of U.S.-born Hispanic families and 46 percent of U.S.-born black families.²⁵ Moreover, there appear to be pronounced disparities between ethnic groups. Greater levels of financial exclusion exist for Mexican immigrants than for other Latin American immigrants, and both groups have more unbanked members than Asian and European immigrant families.²⁶

According to one estimate, up to 10 percent of all American households and 30 percent of low-income families are “unbanked,” meaning they lack a basic checking or savings account.

According to new research by the Center for Financial Services Innovation, as many as 106 million families are “underbanked.” Such families may or may not have a bank account, are not fully integrated into the financial mainstream, and have conducted at least one financial transaction at a non-bank institution within the past 12 months. They pay more for basic financial transactions and are more likely to be exposed to predatory practices that may trap them in a cycle of ever-increasing debt. The result is a two-tiered financial system, with mainstream banks for higher-income consumers and non-bank financial service providers for lower-income consumers. Recognizing the mismatch between mainstream market offerings and the preferences of lower-income consumers, non-bank institutions are developing products and services to meet the transaction and credit needs of this group, but such products and services come at a higher cost.

Families of modest means living paycheck to paycheck avoid traditional checking accounts because of their minimum balance requirements, high overdraft penalties, monthly maintenance fees, and delayed deposit of checks.²⁷ The un- and underbanked routinely turn to the lightly regulated non-bank financial service providers for routine financial transactions such as check cashing and bill paying. These businesses will cash paychecks for a per transaction fee, for example, but typically do not offer customers a safe place in which to save their money and earn interest. Nor do they offer access to reasonably priced credit. The Center for Financial Services Innovation estimates that the underbanked spend more than \$13 billion a year on over 340 million non-bank transactions.²⁸

If families are to be able to save and build up their asset base, they need low-cost, accessible, convenient, and transparently priced financial services.

Policy Options

Encourage Bundling of Savings Products with Existing Consumer Products and Services

One innovative way to help households increase savings is to bundle a “savings purse” with the most common financial services and products. Bank of America’s Keep the Change Program™, for example, automatically rounds up debit card purchases to the nearest dollar and deposits the difference in a designated savings account.²⁹ Bundling has great potential for spurring new savings, especially when combined with debt products such as mortgages and auto loans. When a family makes its monthly mortgage payment, for example, they might consider making a small deposit in a reserve savings account that the family could use to refinance or make important home repairs and improvements. The government should encourage financial service providers to offer more financial products bundled with a saving purse. In addition to providing resources for pilot studies and private sector innovations, government-sponsored enterprises such as Fannie Mae could be encouraged to spur innovation through their purchase of home loans that include a savings purse.

Fix the Electronic Transfer Account (ETA) and Expand Its Availability

Currently, Electronic Transfer Accounts are available to Americans who receive a recurring federal payment, like

Social Security. Approximately two percent of federal benefits recipients have opened an ETA. Yet it is estimated that at least 4.5 million federal benefit recipients do not have bank accounts. The take-up rate is low because the ETA is not attractive to either consumers or banks. For consumers, the account lacks functionality. For banks, the volume of these modest accounts is too small. The Treasury Department should give banks greater flexibility to offer customers a range of options with different fee structures, so long as they continue to offer at least one low-cost option that is available to any federal benefit recipient regardless of past banking history. There is a pressing need for basic bank accounts for low-income households and the ETA represents a potentially useful infrastructure for providing access to financial services—particularly if account eligibility guidelines were expanded. Further, ETAs should be made available to a broader segment of unbanked consumers, especially those who receive tax refunds.

Strengthen the Community Reinvestment Act and Improve the Service Test

The Community Reinvestment Act (CRA) has been successful in encouraging banks and thrifts to provide credit and make investments in communities in which they have branches. It has been less successful in ensuring that CRA-regulated institutions are actually serving the transactional, savings, and investment needs of low-income communities, and in encouraging those institutions, and their credit-providing affiliates, to provide products with appropriately risk-based prices and terms.

To score well on CRA service tests, banks and thrifts should be required to demonstrate that they provide and effectively market fairly priced products and services that meet the needs of lower-income consumers.

To score well on CRA service tests, banks and thrifts should be required to demonstrate that they provide and effectively market fairly priced products and services that meet the needs of lower-income consumers. Greater consideration is required of how to encourage banks and thrifts to extend their best lending beyond their assessment areas. Holding company affiliates should be fully covered under both CRA

and related consumer protection laws in order to ensure that all lending within the holding company family is well priced and delivered on fair terms.

Increase Accountability and Responsibility of Financial Institutions

While the Community Reinvestment Act has been quite successful in improving the corporate responsibility and accountability of banks and thrifts toward the low- and moderate-income communities where they have branches, the financial services world has changed dramatically since the act became law in 1977. Not only do the institutions subject to CRA requirements have a smaller portion of the consumer's financial "wallet," but the government's financial safety net has been extended to other financial services providers, particularly to investment banks.

The industry as a whole is governed by laws relating to unfair trade practices, and there are laws and regulations covering its various parts (with highly variable levels of supervision and enforcement), but there is no overall obligation to serve low- and moderate-income consumers and communities, and to do so in a manner that is fair to the consumer. The ongoing mortgage market debacle makes it imperative that we extend corporate responsibility requirements to the entire financial services sector.

Credit unions, mortgage bankers and brokers, insurance companies, securities firms, and providers of all sorts of alternative financial services, from check cashing businesses to pawnbrokers, compete for the consumer's financial business. The industry as a whole is governed by laws relating to unfair trade practices, and there are laws and regulations covering its various parts (with highly variable levels of supervision and enforcement), but there is no overall obligation to serve low- and moderate-income consumers and communities, and to do so in a manner that is fair to the consumer. The ongoing mortgage market debacle makes it

imperative that we extend corporate responsibility requirements to the entire financial services sector.

Capitalize an Innovation Fund for Financial Institutions to Facilitate Research and Development Focused on Underbanked Consumers

The Treasury Department should create an Innovation Fund to spur systemic change throughout the financial services industry by providing seed money for financial services companies to develop products and services for underbanked consumers. This would encourage banks—and other financial services firms—to engage in the kind of intensive research and planning they undertake in developing products and services for higher-income consumers. The fund would seek to increase the reach of mainstream financial institutions into the underbanked market by encouraging innovation both in how products are structured and in how they are marketed and delivered. Ideally, products would serve multiple functions, include a savings feature where feasible, use incentives creatively, and be competitively and responsibly priced.

Encourage Public Assistance Recipients to Open Bank Accounts

Having a bank account is often one of the first steps toward building savings and assets. Yet many recipients of public assistance, such as those receiving Temporary Assistance for Needy Families (TANF), are unbanked and lack a basic transaction account. One way to assist this population, while potentially cutting the cost of delivering benefits to recipients, is to have benefits electronically transferred to an account. Federal law neither requires nor prohibits the electronic delivery of TANF cash assistance. Many states distribute TANF cash assistance via electronic benefit transfer (EBT) to a debit or stored-value card, with access to funds via ATMs. States should be encouraged to offer welfare recipients the option of having cash benefits directly deposited into a basic bank account provided by a bank or other financial institution. Welfare recipients no longer in need of assistance could be permitted to maintain such accounts in order to have a safe place to deposit wages and other sources of income in the future.

Reform the Use of Chexsystems

Before an individual is able to open a bank account, the financial service provider typically reviews that individual's status on ChexSystems, a database that tracks an individual's history with depository accounts in financial institu-

tions. Individuals with negative marks are often barred from opening a new account.

Banks should be encouraged to help as many individuals as possible open accounts, either by overlooking minor past infractions or requiring the applicant to undergo financial education training.

Demerits can be given for having an account closed due to unpaid fees or insufficient funds. Banks generally take a broad-brush approach and may decline to open accounts for individuals whose infractions may have occurred many years previously. They should be encouraged to help as many individuals as possible open accounts, either by overlooking minor past infractions or requiring the applicant to undergo financial education training.

Encourage and Facilitate the Use of Alternative Data to Inform Credit Scoring

Small differences in credit scores can often translate into big differences in the availability and cost of financial products, including mortgages. Under our current credit-scoring system, an unpaid bill or a high credit card balance is enough for individuals to be labeled as credit risks, forcing them into the subprime market of high-cost financial products. In order to give working families the opportunity to build positive credit, the sort of data used to determine an individual's credit score should be expanded to include such indicators as timely payments to utility companies. The federal government should work with state utilities to facilitate the transfer of information to credit-scoring companies.

Update Regulations for Prepaid, Electronic, and Pooled Accounts

Recent innovations in the private sector have led to a dramatic increase in the use of prepaid, electronic, and pooled accounts. These new account structures—which may appear to the end user to operate as a simple transaction account—offer new and exciting opportunities to provide underserved consumers greater access to valuable financial services. However, their growth necessitates a series of important regulatory changes. First, FDIC coverage should be extended to cover this new universe of accounts

as consumers begin to rely on these new products to meet their savings and transaction needs. Second, “know your customer” and anti-money-laundering regulations implemented under the Bank Secrecy Act and the USA PATRIOT Act must be clarified regarding these accounts. This will provide firms with the guidance and assurance they need to pursue further innovations in this area that can include lower-income consumers.

FDIC coverage should be extended to cover prepaid, electronic, and pooled accounts as consumers begin to rely on these new products to meet their savings and transaction needs. “Know your customer” and anti-money-laundering regulations implemented under the Bank Secrecy Act and the USA PATRIOT Act must be clarified regarding these accounts. These regulatory changes will provide firms with the guidance and assurance they need to pursue further innovations in this area that can include lower-income consumers.

Encourage Mobile Banking

As the day-to-day interaction with financial services providers continues its migration from the local bank branch to the computer screen and hand-held device, the regulatory environment must adapt. Mobile or cellular banking (transactions made from a mobile phone) has been tremendously effective in providing families in rural communities across the globe with instant access to financial institutions and unprecedented control over their financial holdings. The Center for Financial Services Innovation estimates that as many as 17 million Americans could benefit from mobile banking services.³⁰ However, the Bank Secrecy Act and a host of risk-management and compliance regulations at the state and federal levels may slow the movement toward mobile banking in the United States.

Permit and Encourage Banks to Accept Alternative Forms of Identification

Access to safe, quality financial services should not be barred to individuals who are not legal residents or who lack traditional forms of identification. While many banks have successfully adopted new identification standards, accepting, for example, consular identification cards for opening an account, the regulations governing account ownership and access prevent the industry from adopting more inclusive identification standards. ➡

Connect Tax Refunds To The Savings Process

The tax system can be a gateway to building savings and assets. Last tax season, the Internal Revenue Service issued refunds averaging \$2,200 to 114 million tax filers and refunded over \$250 billion altogether.³¹ These cash infusions are often the best chance families have to save money on an annual basis. This is particularly true for lower-income families. According to Internal Revenue Service data for 2005, \$80 billion was refunded to households with adjusted gross income of \$30,000 or less.³² Over 20 million lower-income families—one in six taxpayers—also received more than \$1,700 on average from the Earned Income Tax Credit (EITC), a refundable tax credit designed to reward work. In 2006, the IRS processed 22.4 million EITC returns, paying out \$43.7 billion.³³ The Child Tax Credit (CTC)—which is partially refundable—is another vital source of tax refunds for low-income families.

The table below shows projected federal “outlays” for the Child Tax Credit and Earned Income Tax Credit for 2009. The column on “tax expenditures” refers to money not taken in by the government as a result of the lowering of tax liabilities.

Funding Levels for the Earned Income and Child Tax Credits, FY 2009 (in millions of dollars)

	Outlays	Tax Expenditures	Total
Child Tax Credit	16,780	29,950	46,730
Earned Income Tax Credit	41,020	5,440	46,460

Source: Office of Management and Budget, Executive Office of the President, Budget of the U.S. Government, Fiscal Year 2009, “Analytical Perspectives,” table 19-1.

According to a recent analysis by the National Consumer Law Center and the Consumer Federation of America, nine million taxpayers took out refund anticipation loans in 2006 (tax year 2005), and spent \$990 million in loan and other fees. Over 10 million filers spent more than \$300 million on related financial products, such as refund

anticipation checks, which, unlike refund anticipation loans (RALs), are nonloans issued to the unbanked tax filer from a temporary bank account. A disproportionate share of these customers are low-wage workers, with EITC recipients, who constitute less than 20 percent of all tax filers, making up 63 percent of RAL clients in 2006.³⁴

If families are to be able to save and build up their asset base, they should be given the opportunity to connect the tax filing process to the savings process.

Policy Options

Create an Assets and Transaction Account (ATA)

Despite a rise in the number of tax refunds delivered through electronic direct deposit, almost half of all tax filers still receive their refunds by means of a paper check. Almost half of these checks go to households with an adjusted gross income of \$30,000 or less. These are the households that typically lack access to reasonably priced transaction and savings products, and are most likely to be paying a disproportionate share of their income to conduct routine financial transactions. These paper check refunds represent potential savings, which financial institutions could take advantage of by making a low-cost transaction and savings product available to lower-income consumers.

The proposed federal Assets and Transaction Account (ATA) is a prepaid account that would be delivered to tax filers who did not choose to have their refund directly deposited in an existing account or to receive a paper check. Financial institutions would issue, deliver, and service the ATA. While a tax refund would be the initial deposit into the ATA, account holders would ideally also have the option to load wages and salary, as well as federal and state benefits and entitlements throughout the year. To facilitate savings, five percent of the tax filer’s refund would be automatically deposited in a savings purse. At a minimum, the ATA would be FDIC-insured, branded with Visa, MasterCard or other network provider, available for web- and phone-based bill payment, and allow account holders to access their money through an ATM and make purchases at grocery stores, restaurants, and other point-of-sale terminals. By leveraging billions of dollars in annual tax refunds, ATAs would benefit consumers, industry, and the government alike. And with enactment of federal legislation, the ATA could serve as the “plumbing” for large-scale asset funding targeted at lower income families.

Promote the Split Refund Option

Tax time presents a unique opportunity for all families, especially low-income households, to grow their personal savings. Last year was the first time that individuals had the opportunity to split their tax refund among three bank accounts. Over 80,000 tax filers, 41 percent of whom earned less than \$29,000, used Form 8888 to do so. The IRS should work to educate both individual filers and tax preparers about the split refund option, encourage taxpayers to take advantage of this simple savings mechanism, and encourage the financial services industry to make certain that targeted savings products, such as IRAs and 529 College Savings Plans can receive these refunds directly.

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Allow Tax Filers to Open Accounts Directly on Their Tax Forms

Another way to encourage saving is to enable tax filers to open a transaction, savings, or investment account directly on their tax forms. Such a program is likely to appeal to low-income families who receive refunds but may not have an account with a financial institution, and it could make a major difference in the savings take-up rate. The IRS could solicit proposals for private financial institutions to provide low-cost, quality accounts nationwide. Or it could create and maintain a Web-based directory of financial institutions that are willing to open low- or no-cost accounts online for tax filers. The directory's URL address would be printed on all tax forms, and the directory would be searchable by zip code.

Set Goals and Performance Measures for the IRS to Promote Savings

The Treasury Department and the IRS should develop performance measures in order to track the government's prog-

ress in increasing the number of tax returns that are sent by direct deposit to tax filers' bank accounts and the percentage of tax filers who make deposits in IRAs as part of the tax filing process. Increasing the number of electronic refunds would not only decrease IRS costs but spur more tax filers to open bank accounts, a prerequisite for the direct deposit of refunds. The first performance measure should relate to the number of tax filers who elected to receive their refunds by direct deposit, with the target set at perhaps 80 percent of all tax filers. Refunds sent to the temporary accounts set up for refund anticipation loans would not count toward this goal. The second performance measure should relate to the number of tax filers who used their refund to open or make contributions to established IRAs in connection with the tax filing process. Finally, the IRS should set a reasonable deadline for achieving its goals in these areas (say, 2010) to enable it to work productively with financial institutions

Expand the Earned Income Tax Credit

An expansion of the Earned Income Tax Credit, in addition to enabling more low-income Americans to save, would provide tax relief to lower-income working families. Previous expansions of the EITC have proven to be effective at providing work incentives and lifting families out of poverty. A well-crafted expansion would increase the maximum credit for working families with three or more children, expand the credit for married, two-earner couples, and expand the credit for families with two or more children. An enhanced EITC program would lead to larger tax refunds, which in turn could be linked to savings products. A saver's bonus, linked to EITC eligibility, could also serve to expand the reach of the EITC, while at the same time promoting saving and investment.

Increase Funds for Tax Preparation Sites in Aid of Financial Education and Counseling

Congress should increase federal funding for important IRS education and counseling initiatives aimed at low-income families by \$50 million. If families were able to connect to financial services and products, and to learn about investments and savings, through the federally funded tax preparation sites for low-income tax filers, they could begin to save and build up their asset base. To achieve these goals, tax preparers need resources to hire and train counselors, and to develop software to maintain client information. Supporting such outreach will improve efforts to identify families who qualify for assistance and maximize potential income tax return benefits. ▣

Rebuild the U.S. Savings Bond Program

Savings bonds have a long history of financing government while simultaneously meeting the savings needs of “small investors.” At various times, such instruments have been called War Bonds, Liberty Bonds, or Patriot Bonds, but they are an enduring brand. Today, U.S. Savings Bonds are viewed by the Treasury Department and many policymakers as primarily a way to finance government, rather than as a way to help Americans save.

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This is a lost opportunity because U.S. Savings Bonds are a unique and well-designed financial instrument. They are secure, provide market-rate returns, may be purchased in small denominations, and do not require clearance through the ChexSystem registry or a bank account. These characteristics make them well suited to small savers and attractive to a broad range of the public, to lower-income individuals in particular.³⁵ Preliminary results from pilot tests conducted during the past two tax seasons (2007 and 2008) by the nonprofit Doorways to Dreams Fund suggest that awareness levels of—and demand for—Savings Bonds among low-income individuals may be significant and more pronounced than for competing saving products, such as savings accounts or IRAs.

If families are to be able to save and build up their asset base, they should have access to a Savings Bond program that meets the needs of small savers.

Policy Options

Put Savings Bonds Back on Tax Returns

When U.S. Savings Bonds could be purchased directly on a tax return in the early 1960s, tax filers had to use their entire refund to do so. With the recent implementation of the Treasury Department’s split refund policy, tax filers should be permitted to use a portion of their refund to

purchase Savings Bonds. Bonds could be issued in the primary filer’s name or bought by taxpayers for their children, grandchildren, or others. Apart from the internal administrative costs to develop the necessary forms and systems, this proposal would cost the federal government nothing.

Offer Savings Bonds with Preferred Terms for Lower-Income Individuals

To encourage lower-income Americans to purchase Savings Bonds, a new Series “O” (for “Opportunity Bonds”) could be offered to tax filers reporting income below the national or regional median or claiming the Earned Income Tax Credit. Series O Bonds might offer a half-percentage point higher interest than comparable I Bonds, or could be purchased at three-quarters face value (rather than at full face value, as with Series I Bonds). Series O Bonds purchased for children in low-income families might also offer even better rates or discounts, provided the bonds were held until the child reached age 18 and were used for higher education, a first home, or held until retirement. By linking the purchase of O Bonds to the tax filing process, eligibility could be verified efficiently using data provided on tax returns, and tax refund recipients would not need out-of-pocket cash to make a purchase.

The Doorways to Dreams Fund is exploring the mechanics of this proposal. As with all savings bonds, the interest on Series O Bonds would not be taxable until the bond is cashed in. However, such bonds could be rolled over, tax free, into either a 529 College Savings Plan or Roth IRA. According to data from the fund’s multi-site VITA pilot projects, low-income individuals are purchasing U.S. Savings Bonds for others, and the product is widely recognized in low-income communities. Over 80 percent of bond purchasers bought one or more bonds for a child, and 75 percent of all tax filers were aware of them. With 54 percent of the Savings Bond buyers in these pilot projects reporting low personal savings, it makes sense to offer tax filers the opportunity to purchase bonds with their tax refunds.

Offer Tax Credits to Expand the Payroll Savings Plan to Promote Savings Bonds

Presently, through the Payroll Savings Plan, Savings Bonds can be purchased through some 40,000 employers (although, in practice, it may be substantially fewer than that). Under this proposal, tax credits would be offered to employers who enrolled their lower-income employees in the Payroll Savings Plan. A modest tax credit could

be offered to offset the costs of outreach efforts; a more ambitious credit could be offered if the employer covered some of the cost of purchasing a bond. Similar tax incentives could be extended to financial institutions, which already offer and redeem Savings Bonds for the general population.

Encourage Low-Income Individuals to Redeem Their Savings Bonds to Pay for Homes, Higher Education, and Retirement Products

Presently, Series I and EE Savings Bonds issued after 1990 may be redeemed tax free if used for postsecondary education. This provision, however, is of limited value to lower-income individuals who generally pay little or no income tax. If longer-term asset accumulation by lower-income Americans is the goal, the federal government could offer incentives for redemption for certain purposes, instead of incentives for purchasing them. For example, bondholders who redeemed their bonds at a participating asset provider for the purpose of paying for postsecondary education, obtaining a mortgage, or contributing to an IRA, might receive a bonus payment offset fully or partially by the federal government through a tax credit or direct reimbursement. A change in the law would be required to allow Savings Bonds to be assigned to or redeemed by third parties. Another option would be to designate a new class of redemption agents to include nonprofit housing and community development agencies, educational institutions, and asset-building organizations. A third option would be to authorize the existing bond redemption network (banks and credit unions) to pay the bonus to bond redeemers who presented evidence of qualified purchases (for education, housing, etc.). Bond redeemers would be required to declare on their next tax return whether the qualified purchase went through; if not, the “bonus” would have to be repaid through the tax filing.

Under current rules, Savings Bond holders cannot convert their bonds tax free into an IRA or other tax-preferred retirement product. Creating a “rollover” provision for Savings Bond redemptions would encourage long-term saving and ensure that individuals who began saving with bonds could easily maintain their saving momentum once their bonds reached maturity.³⁶

Improve the Marketing of and Access to Savings Bonds

Improving the marketing of Savings Bonds should increase their appeal. The federal budget line item for marketing savings bonds should be restored. Also, the places where bonds can be purchased should be extended beyond banks and the Internet-based TreasuryDirect to include check cashing businesses, retail outlets, post offices, credit unions, and other such places that serve low-income individuals. Financial incentives could be provided to these outlets to promote Savings Bonds to their lower-income customers.

Reduce the Minimum Holding Period

Like all Americans, low-income Americans need savings tools to meet short, medium- and long-term needs. When the Treasury Department changed the minimum holding period on Series I and EE bonds in January 2003 from 6 months to 12 months, this had the effect of making Saving Bonds less appealing to many lower-income Americans. On the other hand, the longer minimum holding period encourages longer-term saving—a worthy goal. It is not clear which of these options is better. One possible solution might be to maintain the new rule but allow early penalty-free redemptions in the case of a family emergency. The Treasury Department currently allows early redemption only in the case of a natural disaster or other widespread emergency. 📌

Strengthen Asset Protection Laws

Unscrupulous providers of questionable loans and financial services thrive in a poorly regulated U.S. marketplace. Subprime loans are often loaded with unnecessary expenses and provisions that can lead to the loss of equity: predatory mortgage lending is responsible for stripping an estimated \$9.1 billion in assets from low-income families and communities each year.³⁷ High-cost tax refund anticipation loans are marketed to low-income taxpayers receiving EITC refunds; often tax filers receive their cash payment only days before they would have received their refund. Likewise, payday lenders, who provide needed short-term loans to low-income individuals, often charge excessive fees—such as annual interest rates as high as 400 percent or more—which cost low-income families an estimated \$4.3 billion a year.³⁸

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In certain cases, the rise of alternative financial service providers has created value for consumers, but more often there is a poor match between the consumer and the financial products being offered. The complex nature of financial products makes it difficult for many consumers to judge whether the products being offered to them are appropriate to their financial situation. At present, there is no place where less knowledgeable consumers can go to get the advice they need.

If families are to be expected to save and build up their asset base, there should be strong consumer protections in place to govern the provision of financial services.

Policy Options

Reduce the Cost of Tax Preparation and Restrict the Marketing of Refund Anticipation Loans

The IRS should continue to expand the provision of free electronic filing of tax returns, so people can file their taxes electronically without paying a fee to commercial

preparers. Further, it should ensure that this service is easy for eligible tax filers to access and navigate. On the flip side, regulators must work to limit unscrupulous asset-stripping business practices that divert tax refunds into the pockets of lenders. Refund anticipation loans—short-term cash advances against a tax filer’s anticipated tax refund—are generally offered at high rates of interest but often only speed the tax filer’s access to cash by a few weeks. Tax filers who do not understand the refund process or the terms of such loans are especially vulnerable to a hard sell of such products.

Increase Scrutiny of Payday Loans

Payday loans—which are short-term, low-dollar loans secured by a postdated check—have become a serious asset-depleting form of lending, especially in moderate-income, working-class communities. Automobile title lenders and pawn shops also contribute to this problem. While some states have enacted laws that limit or reduce payday lending, others have more permissive statutes. Following revelations about the damage this type of lending was having on military families, Congress passed the Talent Amendment to the Defense Appropriations bill in 2006, establishing strict standards for consumer lending to members of the military and their dependents. The statute served to focus attention more broadly on why there is a growing demand for such credit, why the demand for short-term credit is not being met by traditional financial institutions such as banks and credit unions, and how consumers can be better served in this respect. The FDIC has issued proposed guidelines to encourage banks to provide both payday loan alternatives and savings products to reduce the need for such loans, and is considering a pilot program to explore how banks could get back into this business in a sustainable manner while helping customers move toward more constructive forms of credit. It is important that the FDIC’s efforts be encouraged and that other bank and credit union regulators take similar steps.

Prevent Credit Card Abuses

The terms under which most credit cards are issued are virtually impossible for many consumers to understand and present a substantial trap for the unwary—especially those who are financially stressed. Congress has recently held hearings that have highlighted some of the worst abuses, such as double-interest and universal default clauses, and some financial institutions have begun to change their most egregious terms. But there is need for

additional action to help card issuers who are willing to improve their terms not be undercut by competitors and to ensure that credit cards are offered on terms that are fully and accurately disclosed, easily understood, and fairly enforced. Special protections are also needed regarding card offers to youth and to consumers already showing signs of financial distress.

Create a Financial Savings and Credit Commission

The last two decades have witnessed tremendous innovation in financial services, specifically in the number and variety of products offered to low- and moderate-income families. While this has given many families access to credit for such significant investments as homeownership and education, many families have fallen victim to preda-

tory practices. To help families navigate the increasingly complex world of financial services, while preserving the benefits provided by the introduction of these new products, a Financial Savings and Credit Commission should be established. Such a commission, initially proposed by Elizabeth Warren of Harvard University and supported by several of the Democratic presidential candidates, would be charged with reviewing the myriad products available to and designed for low- and moderate-income families. The reviews could lead to formal endorsement of “gold standard” products and services. The commission could also serve to increase transparency by ensuring that firms disclose all terms and fees associated with their products and adequately inform consumers of their rights and responsibilities. ▣

Foster Savings for Higher Education and Skills Training

The price of higher education continues to rise. In 2007, the total cost of attending a four-year public university jumped 5.9 percent from a year earlier to \$13,589—an increase that far exceeds the rate of inflation at a time when median wages are largely stagnant.³⁹ As government and institutional aid fails to keep pace with increased costs, fewer families can expect to afford higher out-of-pocket education expenses. For families wary of taking on costly and onerous levels of debt, savings are an essential element in financing higher education.

In 2007, the total cost of attending a four-year public university jumped 5.9 percent from a year earlier to \$13,589—an increase that far exceeds the rate of inflation at a time when median wages are largely stagnant.

In 2003–04, the cost to a low-income family of sending one full-time student to a public four-year college or university amounted to 39 percent of household income.⁴⁰ In contrast, middle-income families spent 16 percent and high-income households spent 10 percent of family income for this purpose.⁴¹

Despite the rising costs, the investment in higher education and skills training has numerous individual asset affects, as well as a host of positive societal effects, such as lower unemployment and poverty rates, increased tax revenues, greater civic participation, and improved health outcomes.⁴² Employment and earnings are closely linked to an individual's level of education and training. In 2006, the unemployment rate for individuals holding a bachelor's or higher degree was half that for individuals whose highest level of education was a high school diploma and less than a third of that for adults without a high school degree.⁴³ Median annual earnings rise with every educational degree achieved. In 2006, the median annual income for a male with some high school education but no diploma was \$24,090, compared to \$55,430 for a male with a bachelor's degree and \$67,900 for a male with a master's degree.⁴⁴

Tax-benefited education savings accounts, commonly called 529 College Savings Plans after the section of the tax code relating to them, were created in 2001. These state-sponsored plans, with their low administrative fee, centralized accounting, and lifecycle investing features, have the potential to deliver many benefits of traditional savings plans. Although these plans are growing in popularity, many families with lower incomes and fewer resources do not take advantage of them.

If families are to be able to save and build up their asset base, they should have access to an effective and inclusive savings platform to help them afford postsecondary education and training expenses.

Policy Options

Publicize and Facilitate Comparison of 529 College Savings Plans

Because they are created by state governments, 529 plan investments are not subject to federal security laws such as those covering most mutual funds. In addition, research shows that individuals saving in broker-sold 529 plans were frequently doing so in out-of-state plans, though they would potentially benefit more from saving in their in-state plans because of state tax incentives. This raises the question of whether brokers recommend plans that benefit themselves rather than seeking the best plan for their client. At a minimum, brokers should be required to inform clients about benefits they may derive by investing in in-state 529 plans. In addition, the federal government should support efforts to promote the easy comparison of all plans in a particular state and among states. Existing Web sites, such as savingforcollege.com, provide a simple means of comparing 529 plans that could be promoted or serve as a model for a federal Web site. Finally, states should be encouraged to market their direct-sold plans to their residents, which are usually a less expensive alternative to the broker-sold options.

Collect Better Data on Who Invests in 529 Plans

Because data regarding 529 plan account holders' socioeconomic details are generally not collected, we do not know how plan ownership varies by income and which segments of the population benefit from the tax incentive the most. Such information could help policymakers shape future improvements to ensure that tax breaks

and other incentives are serving their intended purpose. Useful data about the saving habits of low-income families with respect to 529 plans could be gathered from states that offer matching grants since they require applicants to disclose their income.

Create an Innovation Fund

A variety of state and private sector actors have enacted innovative programs within their 529 plans primarily to help low-income children save for college. For example, a few nonprofit organizations offer targeted families a match to deposits made to 529 plans. In SEED for Oklahoma Kids, 1,300 newborns will receive a 529 plan with a starter deposit of \$1,000. Financial information and matching deposits will be available as incentives for families to add to these accounts. Coalitions are being formed in states such as Kentucky and Michigan to look into the possibilities of universal 529s for every child in the state, with progressive savings incentives incorporated to help low-income families. The federal government could sponsor an innovation fund through which states could receive awards on a competitive basis to help seed such initiatives.

Add 529 Plans to the List of Products Eligible for the Saver's Credit

The Saver's Credit currently provides a 50 percent match—in the form of a nonrefundable tax credit—to low- and moderate-income individuals who contribute to a retirement account such as a 401(k) or IRA. To further promote savings in general, a range of savings products, including 529s, could be added to the list of products that trigger this credit; the administration proposed such a change as part of its Fiscal Year 2008 and 2009 Budgets. Pre-retirement assets—especially a postsecondary education—are a critical element of retirement security, and it should be noted that IRAs already permit tax- and penalty-free withdrawals for postsecondary education.

Support 529 Matching Grants to Low-Income Savers

Currently, 529 plans are greatly underutilized by low- and middle-income families. Seven states—Colorado, Louisiana, Maine, Michigan, Minnesota, Rhode Island, and Utah—provide matching funds to low-income savers who contribute to 529 plans, and Arkansas will begin providing targeted matches in this year. These incentives appear to be working.

Use 529 Plans as a Platform for Lifetime Education Savings

529 plans have qualified uses that include a range of postsecondary educational expenses. These uses should be clarified and expanded. While commonly associated with saving for a child's education, these accounts can work just as well to help working adults save for their own further education and skills training. For workers looking to command a higher wage in their current field, or to switch fields, higher education and job training is essential. For individuals who cannot pay for tuition, books, and fees out of pocket—and are wary of taking on onerous debt—saving is the answer. Instead of creating new workforce training accounts, the federal government should provide incentives and work with states to promote 529 plans for working adults.

Require Employers to Offer Payroll Deduction for 529 Plans

One of the most effective ways to encourage families to save is to make the process automatic. Millions of Americans have already opted to direct a portion of their paycheck into such restricted accounts as IRAs and 401(k)s, allowing them to save for retirement with minimal effort. Payroll deduction should also be used to facilitate saving for higher education. Employers should be required to offer their employees a payroll deduction option for contributions to 529 plans. Small and medium-sized employers that do not already offer payroll deduction for other purposes could be offered a small tax credit to cover the costs associated with implementing the change. ■

Encourage Saving for Retirement

Savings that occurs over the life course should include planning for retirement. Yet many workers either near or in retirement have low levels of savings and are not prepared to maintain their desired lifestyle. Recent data show that almost 40 percent of households headed by an individual near retirement age (55–64) and almost 60 percent of households headed by an individual of retirement age (65–74) had no retirement assets.⁴⁵ Further, 47 percent of working Americans lack access to tax-preferred retirement accounts, such as a 401(k), at their place of employment.⁴⁶ Equally troubling, nearly 20 percent of eligible workers in jobs with employer-sponsored retirement plans do not participate in them. Workers earning less than \$15 an hour are a third as likely as their better-off counterparts to have access to defined benefit plans and nearly two-thirds less likely to have access to any retirement benefit.⁴⁷ In contrast, unionized workers are more than four times as likely to have access to and participate in a defined benefit retirement plan as non-unionized workers.

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With the decline of traditional pension plans and the limits of Social Security, there is a need for more workers to start saving for retirement and for everyone to save more. As of late 2007, 50 million seniors were receiving Social Security benefits, with payments averaging just \$1,079 a month.⁴⁸ For lower-income retirees, this payment accounts for over 80 percent of their total income.⁴⁹ According to a recent report by the Government Accountability Office, not having access to an employer-sponsored retirement plan has significant implications for worker savings and therefore has a significant impact on worker retirement security.⁵⁰

Minorities, African Americans and Hispanics in particular, are less likely than white Americans to have non-retirement savings or to save money outside of an employer's plan, according to data from the 2007 Minority Retirement Confidence Survey. An estimated 29 percent

of black and Hispanic households headed by an individual between the ages of 47 and 64 are not retirement ready;⁵¹ the comparative figure for white households is 24 percent.⁵² According to the 2004 Survey of Consumer Finances, the average Hispanic household has \$9,949 in retirement assets, compared to the \$59,844 in retirement savings held by the average U.S. household.⁵³

With American workers having to take on greater responsibility for planning and saving for retirement, access to quality, retirement-specific financial education and affordable financial planning is essential.

With American workers having to take on greater responsibility for planning and saving for retirement, access to quality, retirement-specific financial education and affordable financial planning is essential. A recent survey found that the vast majority of workers near retirement age were unable to answer even simple questions about compound interest or risk diversification, and more than four-fifths said that they were not engaged in successful retirement planning.⁵⁴

If families are to be expected to save for retirement, they should have access to quality, low-cost retirement savings products and institutional structures that make it easy for them to achieve their retirement savings goals.

Policy Options

Create Accessible and Automatic IRAs

Only about half of private employers offer 401(k) retirement plans. This means that over 70 million workers do not have access to an institutionally supported retirement plan. Firms not offering 401(k)-type plans should still facilitate deposits in a retirement savings product. The Brookings Institution, the Heritage Foundation, and AARP have proposed creating “Automatic IRAs,” which would require medium and large firms to institute a payroll deduction option, with funds to be directly deposited in a low-cost, diversified individual retirement account. Employers would have the choice of either automatically enrolling employees or requiring employees to “opt out.”

Under the Automatic IRA proposal introduced in Congress, firms that set up such accounts would qualify for a small, one-time tax credit to offset their administrative costs. This credit could be expanded to cover matching funds provided to lower-income employees.

Encourage Firms to Adopt “Auto Enrollment,” “Auto Investment,” and “Auto Escalation”

Even when firms offer retirement savings plans, approximately a quarter of workers do not take advantage of them. The problem is that many workers are required to actively choose to participate in a 401(k) plan, that is, they have to “opt in.” Saving for retirement should be made as easy as possible. Research studies have shown that participation in retirement savings plans increases if workers are automatically enrolled rather than compelled to sign up. In one study by researchers Brigitte Madrian and Dennis Shea, this “opt out” approach was found to increase participation from 36 percent to 86 percent, and the increase was higher for lower-income workers. The Pension Protection Act of 2006 laid the groundwork for opt-out enrollment, and many companies have since adopted this form of enrollment. More employers need to be made aware of this option, and incentives may have to be provided to encourage greater numbers of employers to switch. Moreover, not all of the companies making the switch have moved to the “next generation” of 401(k) enrollment: Auto Investment and Auto Escalation. Auto Investment gives firms the ability to put their employees’ contributions in balanced, low-cost investment options. Auto Escalation gives firms the ability to automatically increase the amount of money their workers contribute to their 401(k) plan, often in association with pay raises.⁵⁵

Make Retirement Savings Plans Universal and Accessible

Universal 401(k)s, proposed separately by Michael Calabrese of the New America Foundation and Gene Sperling of the Center for American Progress, would offer all Americans, regardless of their employment status, generous savings incentives and automatic savings opportunities similar to those currently offered to employees enrolled in employer-provided 401(k)s. The components of a citizen-based, Universal 401(k) include: (1) government matching contributions for the initial savings of lower- and middle-income families; (2) a new flat, refundable tax credit of 30 percent for savings by all

workers; and (3) a single, portable account that benefits families by continuing to provide strong savings incentives for parents who take time off to raise children or who are between jobs. To facilitate deposits in Universal 401(k)s, automatic payroll deductions would be offered by employers. A “clearinghouse” (modeled after the federal Thrift Savings Plan) could be set up to create “default” accounts for workers with very low incomes who might initially have minimal account balances, or who were otherwise unable to navigate the process of setting up and managing a private account.

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Enact a Retirement Investment Account (RIA) Plan

The Retirement Investment Account Plan, developed by the public policy initiative Conversation on Coverage, would create a government-authorized, privately run central clearinghouse to accept worker contributions to retirement savings accounts. Under the RIA Plan, individual workers whose employers do not offer a retirement plan would have access to an automatic payroll-deduction retirement savings account through their workplace. Employers could provide such access without significant new burdens, since they would not have to administer a retirement plan or take fiduciary responsibility for the investment choices of their employees. Employers could make contributions to the employee’s RIA. This plan could also be designed so that progressive government contributions and matches of employee contributions were possible.

Improve the Administration’s Retirement Savings Account (RSA) and Lifetime Savings Account (LSA) Proposals

The Bush administration has proposed creating new tax-preferred savings accounts, including Retirement Savings Accounts (RSAs) and Lifetime Savings Accounts (LSAs). Retirement Savings Accounts would of course be restricted

to retirement savings. Lifetime Savings Accounts would encourage saving for any purpose. Annual after-tax contributions to LSAs and RSAs would be capped at \$2,000 and \$5,000, respectively, but earnings and withdrawals would be tax free. These accounts would be open to everyone, regardless of income or age. As currently proposed, they would offer higher-income households tax sheltering opportunities, but they would offer no savings incentives to lower-income households. The administration's proposals could be improved by placing an income limit on eligibility and providing matching deposits for lower-income families to be delivered through existing refundable tax credits or tax credits to financial institutions that offered such accounts.

Provide Workers Insurance for 401(k) Plans

With the decline of defined benefit pension plans, more and more Americans are working to build their own retirement security by saving in defined contribution retirement accounts such as 401(k)s and IRAs. As with any investment, however, these plans carry a certain element of risk: unforeseen swings in the market can seriously undermine an individual's retirement security. To hedge against these risks, the government should work with private firms to provide insurance for retirement security plans. As described by the Democratic Policy Committee, these new products would go beyond the basic coverage currently offered to employers to provide individual employees with some degree of protection against loss.⁵⁶ 

Promote Responsible Homeownership

Homeownership is a key wealth-building strategy for many families. Owning a home often confers benefits derived from the forced savings required of mortgage payments, the ability to borrow against the property, potential capital appreciation, and a broader set of “assets effects.”⁵⁷ Although the rising number of foreclosures and defaults reflects the limits and challenges of homeownership as an asset-building strategy, the beneficial aspects of homeownership are significant.

Owning a home often confers benefits derived from the forced savings required of mortgage payments, the ability to borrow against the property, potential capital appreciation, and a broader set of “assets effects.”

Although the overall U.S. homeownership rate was 68 percent in 2007, only 51 percent of minorities, on average, are homeowners. It was only in the year 2000 that the homeownership rate for blacks caught up to the white ownership rate of 1940.⁵⁸ In 2006, the median net wealth of black homeowners was \$81,581 (the median net wealth of black renters was \$1,810), compared to \$213,730 for white homeowners (and \$6,200 for white renters).⁵⁹

Home prices are declining nationwide and are expected to continue along this trajectory in 2008. Median sales prices for new and existing homes dropped 5.4 percent and four percent, respectively, from the fourth quarter of 2006 to the fourth quarter of 2007. During the same period, the nation experienced a 28.6 percent decline in housing starts. This reduction in housing activity contributed to a 1.2 percent overall reduction in U.S. gross domestic product at the end of 2007.⁶⁰

The availability of subprime mortgage credit with adjustable rates, which increased significantly over the last 15 years, was initially seen as a positive innovation allowing more families to become homeowners.⁶¹ Subprime lending, virtually nonexistent in the early 1990s, made up 20.1 percent of loan originations in 2006, a rate nearly double that of 2001.⁶² Today, however, nearly a third of families with subprime mortgages originated in 2005 and 2006

have “under water” loans, meaning they owe more on their mortgage than the value of their home.⁶³

Housing affordability remains a widespread problem. Households spending more than a third of their income on mortgage or rent payments are considered “cost burdened,” and households that devote more than half their income to housing costs are classified as “severely cost burdened.” In 2005, 37.3 million households were cost burdened and 17 million were considered severely cost-burdened. Over 13 million homeowners spent more than 35 percent of their income every month on their homes (mortgage, taxes, etc.).⁶⁴ More than three-fourths of the severely cost burdened made \$23,000 or less. Cost-burden rates rose in nearly every state in recent years.⁶⁵

Over 13 million homeowners spent more than 35 percent of their income every month on their homes (mortgage, taxes, etc.). More than three-fourths of the severely cost burdened made \$23,000 or less.

Cost-burdened homeowners who are unable to refinance their mortgage are often forced into foreclosure. Foreclosures have economic and social costs for the associated neighborhood and local government. One foreclosure can erode nearby property value and home equity by up to \$220,000.⁶⁶ The estimated cost to local government of one foreclosure for inspections, legal action, unpaid utility bills, and the like is \$34,000.⁶⁷

In the fourth quarter of 2007, 83 out of every 10,000 mortgage loans were in foreclosure, compared to 78 out of every 10,000 in the third quarter of 2007, and 54 out of 10,000 a year ago.⁶⁸ At the end of the fourth quarter of 2007, one in 20, or almost six percent, of all outstanding mortgage loans for one-to-four unit residential properties were delinquent. It is estimated that 43 percent of recent subprime loans will be lost to foreclosure.⁶⁹

Falling home prices and rising foreclosures and loan defaults will erode the asset base of many families. Projections for 2008–09 are for over 2.26 million homes lost to foreclosure. The spillover effect from these fore-

closures will drive down prices for nearly 41 million surrounding homes and decrease the home values/tax base by \$356 billion.⁷⁰

If families are to be able to save and build up their asset base, they should be assisted in finding a path toward responsible homeownership.

Policy Options

Reform the Homeowner's Mortgage Interest Deduction

The Homeowner's Mortgage Interest Deduction provides \$89 billion a year in tax relief. Since the mortgage deduction is not refundable, the majority of the benefits go to higher income families who have larger tax liabilities. Fifty-four percent of the homeowner's deduction goes to households earning more than \$100,000 a year, and nearly 90 percent of this benefit goes to households with adjusted gross income over \$50,000.⁷¹ Making the deduction refundable for more households earning under \$50,000 would open up this subsidy to families on the cusp of achieving the American dream of homeownership. This change could be implemented in a revenue neutral manner by limiting the mortgage amount to which the deduction applies to half of its current rate of \$1 million and restricting the deduction to one home per family. Alternatively, the deduction could be converted to a credit and made available to all taxpayers, regardless of their tax liability. In 2005, The President's Tax Reform Panel proposed a 15 percent credit, which could be adjusted regionally to take into account varying housing prices.

Enact a Refundable First-Time Homebuyer's Tax Credit

The years immediately following a home purchase can be ones of financial hardship. Family income may be largely devoted to mortgage payments, and there are often many additional expenses related to home maintenance. Thus there is a need to help lower-income families sustain homeownership after the initial purchase. In addition to giving new homeowners access to information and services to prevent foreclosure, many homeowners would benefit from getting some financial relief in the years immediately after home purchase. A Homebuyer's Tax Credit should be available to qualifying households for the three years after the purchase of a first home. Qualifying households

would apply for the tax credit directly on their tax returns. Since the credit would be refundable, it would benefit families even with low or no tax liabilities. The benefits would appear as a lower tax liability or as a tax refund.

Increase Use of the Family Self-Sufficiency Program

The Family Self-Sufficiency (FSS) Program is one of the nation's largest programs designed to help working poor families increase their savings. When earnings increase for Section 8 or public housing program participants, their rising rent payments are diverted into an escrow account to which they have access after achieving self-sufficiency goals. While public housing authorities have the ability to open escrow accounts, they are required to identify designated case managers. In recent years, the funding to support case managers has been restricted, and the program has been plagued by bureaucratic complexity.

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The Department of Housing and Urban Development (HUD) should stabilize these funding streams, increase their capacity to hire case managers, and more effectively seek partnership with agencies already in the case management business. FSS has proven to be a successful model, and HUD should expand it by encouraging local partnerships between organizations with complimentary skill sets. Developing and publicizing FSS partnership arrangements will provide support for FSS practitioners by sharing best practices and entrepreneurial approaches to program growth. Beyond these reforms, the FSS approach should be dramatically expanded. The number of participants should double within the next four years. Furthermore, policymakers should consider making the link between increased earnings and savings accounts a central feature of the provision of housing assistance.

Expand Homeownership Uses from Restricted Accounts

In recent years, the number of tax-preferred savings products that are defined by rules governing contributions and withdrawals has continued to grow. While many of these accounts are associated with retirement, they have many allowable pre-retirement uses, including for the purchase of a first home. Though some have described these uses as “leakages,” accrued savings can be used productively to help build a bridge to retirement. Policymakers should consider making these uses more robust, especially by updating the provisions related to first-time homeownership. First, policymakers should amend the rules for IRAs and Roth IRAs to raise the one-time homeownership use allowance from \$10,000 to \$20,000, making it more in line with current down payment requirements. Second, rules that govern 401(k) and 403(b) plans should be amended to permit savers to use their funds for first-time homeownership and made consistent with the rules for IRAs.

Create Tax-Deferred Individual Homeownership Savings Accounts

Congress should establish a tax-advantaged product exclusively designed to help working families save to buy a home. As proposed by Sen. Christopher Dodd (D-CT), such accounts would be similar to existing specific-use savings vehicles such as IRAs and Section 529 higher education savings accounts. Under the Dodd proposal, the federal government would match deposits up to \$500 annually.

Increase Federal Funding for Housing Trust Funds

Housing trust funds are typically state- or city-run entities charged with expanding the stock of affordable housing for renters and helping low- and moderate-income families achieve the dream of homeownership. Congress should increase federal funding for these organizations to help them design and implement a strategic plan to address the specific housing needs of local communities.

Create a Shared Equity Trust

One of the most significant barriers to homeownership for many American families is putting together the funds for a down payment. Senator Dodd has proposed the creation of a national shared equity trust from which low-income

homebuyers would receive a grant toward a down payment if they agreed to return a portion of the home’s appreciation to the trust when the home was sold. Similar shared equity trusts tested at the state and local levels have been found to be effective.

Improve Oversight of the Housing Finance Market, Especially in the Subprime Sector

The existing consumer protections regarding high-cost and other potentially dangerous home loans must be improved. This includes prohibiting equity stripping practices, such as excessive prepayment penalties and fees for payoff information, modification, or late payment; requiring a borrower to receive counseling before entering into a high-cost loan; and prohibiting mandatory arbitration clauses on high-cost loans. Consumers need to be far more effectively informed of all the terms of a loan—especially likely changes in payments arising from the expiration of “teaser” rates. Lenders should be required to adhere to stricter underwriting requirements to ensure that borrowers will be able to make payments after teaser rates expire and full amortization begins. More effective state oversight of mortgage brokers and others under their jurisdiction is needed.

Promote Strategies to Avoid Foreclosure

Overall foreclosure rates, and in particular foreclosure rates for subprime loans, have hit record high levels and are expected to continue to increase, damaging not only families but also whole communities. Borrowers need access to information to enable them to understand the potential for trouble while they still have the ability to refinance or to otherwise avoid foreclosure as well as to nonpredatory alternative mortgage products. In neighborhoods at risk of large numbers of foreclosures, lenders should be encouraged to make available homes vacated by borrowers who must move at no or low cost to community-based organizations that can resell the homes to borrowers who can afford the home, using an affordable mortgage product. Modifications to loan contracts (especially those that use pre-payment penalties to lock borrowers into loans they cannot pay), securities terms or laws (to allow modification of securities to allow loan prepayment or payment at less than par), and the Bankruptcy Code (to allow the secured part of a mortgage obligation to be reduced to no more than the value of the house) may also be required. ▀

Support Small Business Ownership

Building business equity is a significant asset-building opportunity for Americans. Small businesses, enterprises with fewer than 500 employees, make up 99.7 percent of all U.S. employer firms and employ half of all private sector employees. This sector comprises approximately 26.8 million businesses, including 5.9 million that hire employees and 19.5 million that are sole proprietorship.⁷² Small firms are essential drivers of the U.S. economy, contributing important patented innovations, goods exported, and the majority of jobs on net. Small businesses employed 58.6 million people in 2004, and almost half—21.2 million—were employed by firms of fewer than 20 people.⁷³

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Between 2000 and 2005, microenterprises—defined as businesses with five or fewer employees that can benefit from a modest start-up—added 4.5 million new jobs to the U.S. economy.⁷⁴ Microenterprises can supplement entry-level employment opportunities, reduce a family's reliance on public assistance, and offer flexibility when families try to balance work/life issues. Employee ownership—where workers have a shared stake in a business entity—is another approach to expanding access to business equity. Cooperatively owned businesses also help to create job opportunities and promote economic development in urban and, especially, rural areas where nearby job opportunities may be limited

If families are to be able save and build up their asset base, low-income entrepreneurs should be encouraged to build and expand business equity.

Policy Options

Provide New and Informal Businesses with Better Information about Self-Employed Tax Options

Filing taxes is a key formalizing event in the life of a business. Moving businesses from the informal to the formal

economy could provide incentives for small business owners to invest more in their businesses, and also enable these entrepreneurs to gain access to the tax-favored asset-building features that are only available through filing tax returns. Many low-income, self-employed households claim EITC benefits, which can in part offset the liabilities of the self-employment tax. A self-employment-specific tax credit could expand on this. It should be coupled with a new high-profile business and tax-literacy campaign, informing new sole proprietors about business taxation and asset-building options, and enabling them to make fully informed decisions about filing.

Create an Alternative Source of Funding for Small Business and Incentives for Saving

Individual Retirement Accounts are an important asset-building tool. Currently, penalty-free withdrawals from IRAs for small business start-up costs are not permitted, nor can individuals borrow against these assets to capitalize their businesses. The rules governing IRAs currently allow several pre-retirement uses that promote asset building and retirement security, including paying for a first-time home purchase and postsecondary education. Expanding these uses to small business capitalization makes sense, as doing so could provide another incentive for people to save and accrue assets. In addition, entrepreneurs could be given the option of taking a loan against their IRA assets, instead of making an early withdrawal, which would help mitigate the concern that savers might lose their hard-earned assets in ill-conceived, risky ventures. Private lenders or the Small Business Administration could underwrite the loans and evaluate the merits of the proposed business plan, and minimum underwriting standards could be prescribed. More importantly, only partial security for the loan would be permitted, with the lending institution thereby assuming the risk on the loan balance.

Remove the Obstacles Preventing Low-Income People from Pursuing Self-Employment

Obstacles to self-employment, including a lack of affordable health care coverage and, in some states, TANF (Temporary Assistance for Needy Family) requirements that inhibit entrepreneurship, need to be minimized so that entrepreneurship is a more viable option. For example, to afford health care coverage, low-income entrepreneurs need (1) subsidies; (2) an avenue for purchasing health insurance that affords them access to administrative economies of scale and broad risk pooling; and, in the

long run (3) broader health care system reform that will lower the trajectory of health care cost growth relative to wages, prices, and incomes. Association Health Plans are the most likely vehicles for fulfilling these needs.

Under TANF requirements, states can allow recipients to participate in microenterprise development activities, but federal law does not encourage states to make this option available, or assist them in doing so. Changes and clarifications that could be made to federal law that may prove beneficial include: (1) clarifying that self-employment can count as a TANF work activity; (2) clarifying that self-employment preparation can count as a TANF work activity, within the limits that apply to vocational training; (3) clarifying that time spent in active exploration of self-employment potential can count toward TANF job search requirements; and (4) adding language to the TANF state plan requirements specifying that state plans must describe the state's approach to encouraging and supporting self-employment.

Help the Small Business Administration (SBA) Better Serve Very Small Businesses

The mission of the Small Business Administration is to “maintain and strengthen the nation’s economy by aiding, counseling, assisting, and protecting the interests of small businesses and by helping families and busi-

nesses recover from national disasters.” However, the SBA defines a small business as one that has 500 or fewer employees. As a result, microenterprises are all but overlooked. Although the SBA has two programs targeting microenterprises, these programs could be greatly improved in order to better serve very small businesses. For example, the microloan program, which is unique in that it combines training and technical assistance with loan capital, should be opened to a wider range of lenders and incorporate better standards to help document performance. In addition, the SBA’s 7(a) loan program, which offers several types of small business loan products through banks, could benefit from creating a very small business loan initiative that would provide a 75 percent guarantee for loans of \$25,000 or less.

Maintain Programs That Currently Assist Microentrepreneurs

Some currently valuable policies and programs that help create a more hospitable environment for low-income entrepreneurs have been threatened in recent years. In addition to generating new, creative ideas to maximize the potential of entrepreneurial energy among low-income groups, it is important to retain and improve existing programs. These include the Program for Investment in Microentrepreneurs (PRIME) and the Community Development Financial Institutions (CDFI) Fund. ▣

Facilitate Financial Education and Planning

Today's complex financial landscape makes it increasingly difficult to understand and navigate the array of products and services offered by financial service providers. While financial illiteracy is a problem for youth and adults across all socioeconomic lines, those with low incomes—who disproportionately lack both financial know-how and any relationship with financial institutions—are especially vulnerable to being shut out of an increasingly sophisticated financial marketplace.

For middle- and lower-income individuals who have fewer financial resources, a solid grounding in personal finance and a clear understanding of the options and implications of one's financial decisions are especially critical for creating, growing, and protecting assets. However, many households do not have the funds to pay for financial advice, and among certain communities and minority populations in particular, there is a strong distrust of the established, mainstream financial sector.

This has resulted in disturbingly low levels of financial awareness, which can lead to high levels of debt, low savings, and increased financial distress. A 2005 survey by the National Council on Economic Education and Louis Harris & Associates, Inc. found that about half of adults did not know that cash hidden in a piggy bank or under the mattress would lose value due to inflation.⁷⁵ The 2004 Health and Retirement Survey measured the financial literacy of early baby boomers and found that among nearly 2,000 respondents only 18 percent correctly answered a question about compound interest, an important principle underlying the value for saving.⁷⁶ The evidence suggests that financial education and targeted information tools are required to help consumers assess their needs and options, and navigate the financial services world to make sound, forward-looking decisions.

Employer-sponsored financial literacy plans have been shown to have a positive effect on savings and wealth building, as do financial education curricula administered through schools. Students in mandated financial education programs post higher savings and net worth, compared to students who were not exposed to a financial education curriculum in high school.⁷⁷ But financial education alone is not the solution; experience suggests that an iterative relationship exists between financial education and account

ownership. It is widely accepted that financial education coupled with account ownership leads to improved savings rates, asset accumulation, and positive behavior change.⁷⁸

It is widely accepted that financial education coupled with account ownership leads to improved savings rates, asset accumulation, and positive behavior change.

Myriad individuals and programs provide financial counseling to vulnerable, low-income or low-wealth Americans. However, they tend to focus on credit counseling and home purchase. Not only are more dedicated counselors needed, but others who regularly interact with low-income or low-wealth consumers need to be trained to provide more appropriate financial advice. In an increasingly complex, and sometimes predatory, financial services sector, financial education should be seen as a complement to, not a substitute for, other consumer protections.⁷⁹

If families are to be able to save and build up their asset base, they need access to financial education and a set of tools to help manage their finances and make sound financial decisions.

Policy Options

Mandate the Completion of a Personal Finance Course for High School Graduation

To ensure that all children become financially literate, states should require that the subject of personal finance be integrated into high school core courses and included as part of standardized testing. In addition, financial education concepts should be integrated into existing material in grades K–8 and made part of the Standards of Learning tests mandated by the No Child Left Behind Act. States and local school districts should have the flexibility to draw from a variety of existing resources or craft their own curricula. These courses should then be evaluated to discern which curricula and delivery methods work best. Teachers at all grade levels should receive personal financial management training and should be taught how to integrate personal financial management concepts into the curricu-

lum. KIDS Accounts, or other universal accounts for savings and investments tailored to children, could be offered as part of this strategy to ensure that the financial education is relevant and can be acted upon by every child.

Create Opportunities for Adults to Receive “Just-in-Time” Financial Education

Financial education should be provided when consumers are making key financial decisions such as selecting a bank account, saving for retirement, or securing a mortgage. Whenever possible, government programs created to spur savings or help families acquire assets should include a financial education component. Many government-sponsored incentives to build assets through homeownership, matched savings accounts, or other means already include provisions mandating some sort of financial education or counseling. For example, a proposal for zero-down Federal Housing Administration (FHA) home loans requires that participants complete a homeownership counseling class. State housing finance authorities that offer below-market-rate mortgage loans to first-time homebuyers often also have this requirement. These safeguards give participants the best chance of success, while assuring the government offering the program or subsidy a better chance of a return on its investment.

Financial education should be provided when consumers are making key financial decisions such as selecting a bank account, saving for retirement, or securing a mortgage.

Require States to Provide Financial Education to TANF Recipients

Being able to effectively manage finances is an important component of self-sufficiency. States should ensure that public assistance recipients receive appropriate levels of financial education. The proposed TANF Financial Education Promotion Act (S 923) would mandate that states specify in their TANF plans how they will encourage financial literacy among TANF recipients. Additionally, attendance at financial education seminars or classes should count as a qualified work activity for recipients. Some state and local governments have already begun to offer this kind of training on their own. For example, Illinois

Human Services has partnered with Financial Links for Low-Income People (FLLIP) and the University of Illinois Cooperative Extension to provide a 12-hour financial education program that counts as a work activity.

Support Public Awareness Campaigns That Create Demand for Financial Education

While many financial education materials exist, consumer demand for financial education is not high among the general population. This may be because people “don’t know what they don’t know” and are unaware of how their lack of knowledge may be costing them money or opportunities. Public awareness campaigns similar to those regarding smoking, seat belt use, and littering could be one solution to this problem. Such campaigns could teach parents how to talk to their kids about finances and how to model good spending behavior, just as ads now direct parents to resources on how to talk to their kids about drug use and other risky behaviors. Funding for these campaigns could be provided by private sector companies, many of which are now already trying to promote financial literacy. Additional funding could also be generated through financial penalties imposed on financial services firms that engage in illegal predatory practices. One large-scale public awareness program already under way is the National Endowment for Financial Education’s “Get Smart About Money” campaign, which includes educational ads and a Web site with resources for people who want to learn more about managing their personal finances.

Create Incentives for Employers to Provide Financial Education in the Workplace

Financial education offered in the workplace can help employees avoid personal financial problems that can lower their productivity as well as cause higher rates of absenteeism, turnover, and stress-related illness. Recently, the federal government began implementing a retirement financial literacy strategy to ensure that all federal workers get the training and resources they need to set savings goals and take advantage of retirement savings benefits offered as part of their job. In the private sector, a growing number of businesses have developed financial education programs. However, additional incentives and information about best practices is needed to encourage more financial education in the workplace. To spur this effort, and especially to ensure that financial education that goes beyond how to save for retirement, tax credits could be offered to offset the costs to business associated with providing finan-

cial education in the workplace. In addition, the federal government could offer tips on how best to run a financial education program based on the implementation experience with its own employees.

Expand Evaluation of Financial Education Activities

Although there has been a good deal of money spent on various forms of financial education, much of it—especially general financial education not tied to either an event such as buying a home or a crisis such as imminent bankruptcy—has not been evaluated for effectiveness in changing attitudes and behavior. The result is that limited resources are not being efficiently spent. More evaluative research is needed; all funding for financial education should include an evaluative component, and there should be some coordination among researchers to leverage both data and evaluation across programs. One strategy for financial education that needs more study is “coaching”—individualized attention much like financial planning. Such coaching carries a higher price tag but may provide good value for money if it proves substantially more effective than traditional group-based financial education, and is targeted at those most likely to benefit from the more intense approach. The effectiveness of point-of-sale education—which provides information and education during a teachable moment when the individual is making a financial decision—is another strategy that requires study and evaluation.

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Establish a Financial Services Corps to Ensure Access to Financial Planning Services

Today’s complex financial marketplace makes it increasingly difficult for many to understand and navigate the array of products and services available from financial service providers. For middle- and lower-income individuals

who have fewer financial resources to begin with, a solid grounding in personal finance and a clear understanding of the options and implications of one’s financial decisions are all the more critical. While there is a wide range of financial education curricula available, there is a dearth of financial advisors and educators to help middle- and lower-income families understand the complexities of the financial services sector, get assistance when facing financial difficulties, and plan for savings and investment goals. To connect low- and moderate-income families with the targeted financial advice they require, a Financial Services Corps should be established. The corps, which could be made up of financial experts, planners, and advisors, would deliver financial advice and resources to lower-income individuals and families. Corps members would work one-on-one to help families create a plan to repair credit, pay off debt, and save for emergencies and longer-term goals such as homeownership, higher education, and retirement. To help offset some of the costs of training personnel and advising individuals, a tax credit could be awarded to financial planning providers. A second option would be to issue vouchers directly to families who could seek out financial counsel. Finally, a grants program run by the Treasury Department could be developed for community-based organizations to hire and train financial counselors to serve their clients.

Create National Standards for Financial Education

The increased demand for financial education has been met with tremendous growth in the number of individuals serving as “financial educators.” Unfortunately, both educators and financial education curricula vary significantly in quality and effectiveness. In order to ensure that individuals are receiving appropriate, quality financial education, the government should create a basic certification program (or qualifying criteria) for financial literacy educators as well as a rubric for determining the quality and efficacy of specific financial education curricula. ♦

Remove Barriers to Saving

Millions of low-income Americans are hearing two conflicting messages from their government: Save and Don't Save. Over the last decade, a consensus has been emerging among researchers, policymakers, and practitioners as to the importance of enabling low-income individuals to save and build wealth, and state and federal programs have been created to help them do so. Yet, with limited exceptions, the asset limits built into our public assistance programs aimed at such individuals—Food Stamps, Medicaid, and TANF, for example—send the opposite message: Don't Save.

Millions of low-income Americans are hearing two conflicting messages from their government: Save and Don't Save.

To receive various forms of public assistance, impoverished families must demonstrate that they are both income and asset poor. In some cases, program rules are set entirely by the federal government; in others, the federal government lays out broad guidelines and allows each state to devise its own plan and eligibility requirements. The purpose of these asset tests is to ensure that limited federal funds are allocated fairly to the people most in need. However, asset tests can also put low-income families in a precarious position, causing families to deplete their assets to low levels before getting help. Others on their way off the assistance rolls may avoid saving and asset accumulation for fear that it will make them ineligible for benefits if they face future hardship.

A growing body of evidence indicates that asset limits actively discourage low-income families from saving, and it has been shown that low-income individuals avoid relationships with formal banking institutions in part out of fear that owning a bank account would jeopardize their eligibility for public assistance.

A growing body of evidence indicates that asset limits actively discourage low-income families from saving, and it has been shown that low-income individuals avoid relationships with formal banking institutions in part out of fear that owning a bank account would jeopardize their eligibility for public assistance.⁸⁰ For reasons of equity, administrative ease, and helping the poor to achieve economic security, these outdated asset limits should be revised or repealed, and an income test should be substituted to ensure that public assistance reaches only those who need it.

If families are to be able to save and build up their asset base, federal policy must avoid creating rules that serve as barriers to savings.

Policy Options

Reform Asset Limits Under the Temporary Assistance to Needy Families (TANF) Program

Although states were given the prerogative to set eligibility guidelines under welfare reform, Congress has the ability to set the basic parameters that states must follow in the implementation of their TANF-funded cash assistance programs. The federal government should therefore consider the following options for reforming asset limits under the TANF program:

Eliminate asset limits. The structural components of the TANF program have proven to be immensely effective in preserving cash assistance for those in need. Federally mandated and state-enforced time limits and work requirements effectively deter anyone from applying for assistance without having exhausted all other resources. These structural realities, coupled with the social stigma associated with receiving public assistance, prevent anyone with financial resources from considering public assistance.

Since the welfare reform law of 1996, many states have chosen to liberalize asset limits under the TANF program. Two states, Ohio and Virginia, have completely eliminated assets in determining eligibility for TANF cash assistance. Not only have these states reported no increase in fraud or a significant jump in caseloads, Virginia claims to have netted more than \$400,000 a year in administrative savings from streamlining the eligibility process.

Raise the limit and index to inflation. Asset limits should be raised to more realistic levels in all public assistance programs, but especially in TANF, where many states employ an overly restrictive \$1,000 resource limit. Unlike income limits, which are adjusted upward on a regular basis, asset limits in some programs have remained the same for several decades. This has not only made eligibility for public assistance more restrictive over time, but it has also served as a major saving disincentive for the very families that could most benefit from having savings. Further, these limits should be indexed to inflation in order to keep pace with rising costs. Indexing asset limits to inflation will work to ensure that the limits retain their original purchasing power and spare Congress and state legislatures from the need to continually legislate increases.

Exclude certain asset holdings altogether, such as savings for education and retirement, automobile ownership, EITC refunds, and U.S. Savings Bonds. Currently, employer-sponsored 401(k) plans as well as IRAs are sometimes counted toward asset limits in the TANF program. Families needing to go on temporary public assistance therefore may have to spend down these retirement accounts even if they face a penalty for doing so. These families, who likely already lack sufficient retirement savings, will have even less when they reach retirement age—making it more likely that they will have to rely even more on public assistance once again when they are seniors. In line with excluding retirement accounts, contributions to 529 plans and other restricted education savings plans should be excluded from eligibility consideration.

Automobiles are often overlooked as “assets” because they quickly depreciate in value. However, the value of a car should not be measured only by its resale value, but by the utility it provides in giving families access to job opportunities across their region. This is particularly important for families in areas lacking a convenient public transportation system.

Low-income workers who receive an EITC refund should be allowed to save their refund for up to a year after receipt to pay for unexpected expenses, debts, and other purposes. This would help families pay for both expected and unexpected expenses throughout the year and offer greater protection from financial emergencies that could cause them to return to public assistance. This one-year grace

period already applies to the Food Stamp Program, and the Supplemental Security Income (SSI) program allows the EITC to be disregarded for nine months. In order for families to be able to save their refund without jeopardizing their eligibility for public assistance, The EITC refund amount should be excluded from all public assistance eligibility considerations.

Reform Asset Limits Under the Food Stamp/ Supplemental Nutritional Assistance Program

As part of the Food, Conservation and Energy Act of 2008, in May 2008 Congress reformed asset limits under the Food Stamp Program by excluding from consideration savings held in IRAs and higher education savings accounts (529 plans, Coverdell Education Accounts) and indexing the current limit to inflation.

Raise the limit. The asset limit in the Food Stamp Program is currently set at \$2,000 for most families; this number has only been increased by \$250 in 30 years. Congress should raise this limit significantly to enable the low-income working Americans who rely on Food Stamp assistance to save and build wealth. Had the limit set in 1977 been indexed for inflation, the current asset limit in the food stamp program would be nearly \$6,000.

Encourage the adoption of categorical eligibility. Under the 2002 Farm Bill, and reauthorized in 2008, states can streamline the eligibility process for families receiving multiple forms of public assistance by making individuals who receive a TANF-funded benefit “categorically eligible” for Food Stamp assistance. This means that individuals who receive any public benefit funded with TANF dollars—not limited to traditional cash assistance or welfare—do not have to undergo a separate eligibility screening to qualify for Food Stamp benefits. This rule change not only allows social service agencies to streamline the eligibility process but also gives states the ability to circumvent the federally prescribed \$2,000 asset limit in the Food Stamp Program.

Reform Asset Limits Under the Supplemental Security Income (SSI) and Medicare Programs

Asset limits under the Supplemental Security Income and Medicare programs currently impose an implicit tax of 100 percent on all retirement savings. This means that for every dollar withdrawn for use in retirement, an individual’s benefit is reduced by a dollar. Under these program

rules, individuals who saved for retirement during their working years are no better off than if they had not saved at all. SSI and Medicare asset limits must be reformed to restore the incentive for low-income workers to save for retirement by removing, or reducing, the penalty for withdrawals from retirement accounts. Additionally, asset limits in SSI and Medicare are a disincentive to save for pre-retirement uses, such as skills training, homeownership, or home improvement. SSI recipients, who may be capable of working for short periods, are prohibited from saving more than \$2,000; when their disability results in an inability to work, such individuals must spend down their savings in order to re-qualify for SSI assistance. Raising and indexing these asset limits, in addition to excluding all restricted savings vehicles such as IRAs and 529s, could have a tremendous impact on the financial security of this population.

Raising and indexing these asset limits, in addition to excluding all restricted savings vehicles such as IRAs and 529s, could have a tremendous impact on the financial security of this population.

Improve Asset Accumulation Opportunities for TANF Recipients

Many states have incorporated Individual Development Accounts (IDAs) in their TANF programs to help families save and participate in financial education. Presently, TANF rules allow federal funds to be used for IDAs, but specify that savings must come from earned income. These rules should be amended to give states the flexibility to determine the purposes for which IDAs can be used. The requirement that savings come from earned income could be amended to accommodate the needs of recipients who may rely on unearned sources of income, such as Native Americans and people with disabilities.

Congress could also establish a Savings and Ownership Fund to encourage states to incorporate asset-building strategies in TANF state plans. Currently, performance bonuses are awarded to states that lead the way in terms of caseload reduction, job placement, and other measures. Performance bonuses should also be awarded to states that identify innovative ways to achieve asset-building objectives. States could explore options for offering recipients access to children's savings accounts, U.S. Savings Bonds (for themselves and/or for their children), 529 plans, electronic benefit transfer to a bank account, linking EITC refunds to savings opportunities, and other initiatives. The federal government could award grants from the fund on a competitive basis to help with the implementation of these and other innovative efforts. ➡

Advance Asset Building Worldwide

In developing countries, just as in the United States, access to effective, formal financial services and asset-building opportunities is essential for spurring wealth accumulation. Hundreds of millions of poor individuals around the world lack the means to provide themselves or their families with sufficient food, shelter, and medical care. It is nearly impossible for the children in impoverished families to thrive in school and move on to jobs that will allow them to accumulate enough financial assets to move out of poverty and sustainably into the middle class. Indeed, the perpetuation of poverty from one generation to the next is one of the most serious and pervasive problems our global society faces. U.S. policymakers should begin to think more creatively about how to link poor and moderate-income households in developing countries to asset-building opportunities and financial services.

Access to effective, formal financial services and asset-building opportunities is essential for spurring wealth accumulation.

For example, Child Development Accounts (akin to Children's Savings or KIDS Accounts in the United States) could help address poverty, lack of education, and vulnerability to HIV/AIDS in communities affected by the disease. Their availability would encourage communities to be more forward-thinking when it comes to caring for their children, and they might enable children themselves to adopt a more optimistic future orientation and self-protective practices to thwart the spread of HIV/AIDS. In parts of the developing world, CDAs could be used to encourage youth to save while providing them with the resources needed to pay for the costs of education and health care, or to begin a business. Coupled with financial-education training and life skills, CDAs have the potential to revolutionize the way communities are able to care for their children in a sustainable manner.

At the same time, remittances, the funds migrant workers send home to their native countries, are an increasingly important tool for reducing global poverty. In 2006, remittances sent to Latin America and the Caribbean totaled \$62.3 billion. This was more than the combined flows of

net foreign direct investment and official development assistance to these regions.⁸¹ About 75 percent of remittances to this area come from the United States.⁸²

There are many reasons for U.S. policymakers to support asset-building strategies and policies in developing countries, including demonstrating America's commitment to global poverty reduction and the Millennium Development Goals; satisfying constituents who have emigrated from such countries; promoting stability in countries and regions important to national security; serving humanitarian goals; and nurturing new markets for American goods and services.

If families are to be able to save and build up their asset base, policymakers should explore a range of options to promote a global asset-building agenda.

Policy Options

Support Child Development Accounts to Promote Economic and Health Improvements

Owning financial assets not only reduces the problems associated with income volatility but also promotes longer-term planning that may mitigate the risk of future poverty. A promising means of facilitating asset ownership abroad is the establishment of Child Development Accounts, which have the potential to be effective in reducing poverty, increasing access to financial services, and improving some health outcomes. Such accounts offer a potentially powerful tool for meeting strategic development goals that focus on enhancing human capacity, education, health, and social services. The U.S. government should support research and initiatives regarding CDAs as part of its global foreign assistance strategy.

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The Office of the U.S. Global AIDS Coordinator should allocate some Global HIV/AIDS Initiative (GHAII) funds

(particularly those already earmarked for economic development) to seed and support Child Development Accounts policies and initiatives in developing and transitional countries. This would contribute to the expansion of CDA programs throughout the developing world and permit the exploration of their usefulness in coupling economic empowerment and health care interventions. One-half of one percent of FY2008 (estimated) GHAI funds would add up to \$21 million for seeding or supporting CDA efforts across the globe.

Encourage More Effective Use of Remittances

Federal policymakers should support strategies that lead to more effective uses of remittance transfers at home and abroad. Because of the lack of access to effective banking services, the vast majority of remittances are transacted through expensive wire transfer services, such as Western Union, or even more informal, unsecure methods. Thus, an opportunity to link senders and recipients to the formal financial system is being missed and potentially large sums of scarce resources wasted. U.S. policies should be aimed at promoting low-cost ways to remit money to our neighbors in the Western Hemisphere. For example, remitting funds by mobile phone has the potential to obviate the need for brick-and-mortar banks. The United States should also work with governments of recipient countries and the private sector (including banks and mobile phone operators) at home and abroad to introduce a regulatory framework to facilitate the safe

remittance of funds by mobile phones. On the receiving end, the United States could engage in capacity building or public-private partnerships to encourage an environment in recipient countries in which remitted funds are used for asset-building purposes, such as savings, mortgage payments, or other investments.

Federal policymakers should support strategies that lead to more effective uses of remittance transfers at home and abroad.

Provide Capacity-Building Technical Assistance to Improve Financial Inclusion Abroad

More broadly, federal policymakers should find ways to leverage the strength of America's financial services sector, specifically in finance and asset management, to connect poor people around the world with the global financial system. American banks and mutual fund companies can do this by providing local institutions, such as banks, retailers, or mobile phone operators, with technical advice. Also, American financial institutions can partner with institutions in developing countries to create products that let people save and invest their money in either a basket of currencies or an index fund, which would help protect account holders against currency shocks. ▣

About the Asset Building Program

The purpose of the New America Foundation's Asset Building Program is to significantly broaden savings and assets ownership in America, thereby providing all Americans both with the means to get ahead and with a direct stake in the overall success of our economy. This major new direction in public policy promises to be as successful in the 21st century as the Homestead Act and GI Bill were in previous centuries. The Program has also established a Global Assets Project to promote asset-building policies worldwide.

More information about the program and the asset-building field may be found at the following Web sites:

Newamerica.net
AssetBuilding.org
Globalassetsproject.org
Newamerica.net/blog/ladder

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