THE ASSETS PERSPECTIVE

The Rise of Asset Building and its Impact on Social Policy

Edited by
Reid Cramer &
Trina R. Williams Shanks

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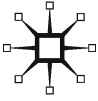

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Acknowledgments

This edited volume is a product of a symposium and ideas summit held in May of 2012 in Washington, DC, which was designed to examine the impact that asset building has had on social policy. The origins of the asset building concept are manifold, but they were especially well articulated in a 1991 book by Michael Sherraden, *Assets and the Poor*. It was his book and subsequent exploration that gave shape to a distinct "assets" perspective and served as a catalyst for the emergence of a broader field of practice and policy. To the extent that this collective work has had an impact, Michael provided the spark. He has also been a colleague in the best sense of the word, collaborating and guiding a broad research program and influencing a meaningful policy agenda. To acknowledge Michael's role and influence since the publication of his book twenty-one years ago, the symposium was called Assets@21: Lessons from the Past, Directions for the Future.

The original seed for the symposium was planted by former colleagues at the New America Foundation. Ray Boshara, the founding director of the Asset Building Program, first hatched the idea of a convening to take stock of developments in the field in the two decades since the publication of Michael's seminal book. We refined it in conversations with another colleague, Anne Stuhldreher. Ray is a source of countless ideas, and is passionate about policy because he cares about people. He has been a tremendous mentor and collaborator. Anne is a consummate policy entrepreneur who has a knack for getting decision makers to become policy champions and spend their political capital on implementing innovative ideas. In different ways, they both helped shape this book from behind the scenes and Ray's keynote was a highlight of the conference proceedings.

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REID CRAMER
TRINA R. WILLIAMS SHANKS

Chapter One
The Rise of Asset Building and Its Impact on Social Policy

Reid Cramer and Trina R. Williams Shanks

Poverty has long been assessed according to the extent to which immediate needs are satisfied. It makes a certain amount of sense to gauge hardship in terms of whether or not someone is adequately clothed, housed, or fed. To simplify these dimensions, income has historically been used as a standard measure of economic health because it serves as a proxy for consumption and can be used to purchase the most basic goods and services. However, from another perspective, there are limitations to reducing a person's economic prospects to their circumstances at a particular moment in time. While poverty entails material hardship, it is also accompanied by deficits to opportunity, information, and other resources. The compounding of these deficits over time can be particularly debilitating. In fact, poverty is especially problematic not as an episodic condition but when it becomes persistent and intergenerational. For this reason, assessments of economic well-being would be strengthened by considering the factors that help families navigate their economic lives over an extended period of time.

For many families, being able to move up and out of poverty requires gaining access to an array of resources, including their own savings and assets. This insight was at the core of Michael Sherraden's critique of the prevailing approach to welfare policy described in his 1991 book, *Assets and the Poor*. In that seminal work, he presented an alternative perspective that emphasized the role assets play in promoting social development over the life course. Building on this framework, he articulated a set of novel policy interventions, such as Individual Development Accounts, matched savings initiatives, and universal children's savings accounts provided at birth, designed to assist families to save and build up their asset base. In subsequent years, a growing number of practitioners, funders, researchers, and advocates sought to explicitly connect antipoverty welfare strategies with economic security and mobility objectives.

Employing a shared perspective, a discrete asset-building field emerged, which recognized a set of policy failures, pursued a focused research agenda, and incubated a broad agenda for public policy action. The advent of the Great Recession and its painfully slow recovery offer a poignant backdrop for examining the impact of this collective work. This edited volume offers a series of perspectives on the relationship of the asset-building concept and social policy. They are presented in the hopes of facilitating honest reflection in the pursuit of new ideas that can inform contemporary debates and craft social policies that create accessible pathways to economic opportunity and security.

The Assets Perspective

As a point of departure, it is worth identifying the core principal convictions that animate and unite those looking at the world from an "assets perspective." One is that the path to future economic security requires access to both income and assets. People cannot be expected to spend their way out of poverty. Rather, they will need to build up or gain access to a set of resources. The power of assets is not just that they can be deployed productively or tapped to weather unexpected events, but that owning assets have behavioral effects that can change the manner in which people think about and plan for the future. The hypothesis is that there are asset effects that extend beyond the sum value of resources that may appear on a household balance sheet. Another belief is that expanding asset ownership—whether through saving or investment—has the potential to meaningfully connect economic opportunity with economic security and ensure that every member of society is afforded a stake in the commonwealth. Helping people accumulate assets, as opposed to increasing their income momentarily, may provide the stability that allows them to become financially stable over the long term and thereby permanently escape the cycle of poverty. As the economy continues to change and income volatility rises, the prospects for personal success will increasingly have an assets component. Yet it remains an open question as to whether or not opportunities to achieve financial security will be open to everyone, especially those among us who start out with fewer resources.

This outlook has naturally sparked interest in a wave of policy ideas that seek to complement income maintenance objectives with ones that promote asset-building activities. One set of ideas focused on promoting a process of accumulating savings, which are an especially flexible resource and can be converted into a variety of forms and used to build wealth, cover emergency expenses, support retirement security, and be passed on to endow future generations. Another area garnering attention relates to the process of acquiring assets, specifically the acquisition of a home. Beginning in the mid-1990s, it is fair to say that these areas received greater attention among policymakers. The concept of promoting asset building through matched savings accounts gained currency and led to the creation of a small federal program that provided funds to support local efforts. At the state level, these types of accounts were selectively integrated into some public assistance programs. Other large-scale policy efforts, based on the theory of asset building, were proposed, such as Universal Savings Accounts, Child Development Accounts, and expanded affordable homeownership programs. Support among policymakers was initially wide, if not deep, attracting proponents across the political spectrum. Conservatives saw a way to reinforce personal responsibility and appreciated its openness to market forces, while liberals approved of its focus on expanded opportunity and the supportive role of government.

The policy discourse emerging from the "assets perspective" was also grounded in a critique of existing policies, specifically those embedded in the tax code. A prevailing feature of our current policy paradigm is how many it excludes. While middle- and upper-income households benefit from tax breaks that subsidize mortgage payments, contributions to retirement savings accounts, and other investments, families with lower incomes cannot benefit from these policies. This approach, and poorly designed, safety-net policies, fails to provide many families with the means to accumulate the resources necessary to achieve financial security and economic mobility. Rather than creating a new poverty program centered on assets, the policy challenge is to extend the asset-building policies already in place to lower-income families, opening up pathways to move up the economic ladder.

Concurrently, an expanded set of researchers began to scrutinize the broad question of the impacts of holding assets. They sought out evidence that might prove that having

savings or owning assets changed behavior and led to particularly beneficial outcomes. These outcomes may include a more positive orientation to the future, household stability, health and well-being, educational performance, and civic engagement. Limitations in available data initially narrowed the scope of these investigations, leading to a focus on observable outcomes, such as homeownership, and there were enduring challenges in distinguishing between correlation and causality. Still, it was notable that a distinct community of researchers appeared to coalesce, sharing an interest in learning more about "asset effects" on a range of populations and identifying the need for additional data sets and impact measures.

The research community benefited from the initiation of several large-scale demonstration projects, funded by a coalition of large national foundations. The America Dream Demonstration (ADD), conducted between 1997 and 2002, was designed to test the potential impact of offering saving accounts where lower-income participants would have their deposits matched if the accumulated resources were used to purchase discrete assets (Schreiner and Sherraden 2007). The ADD program opened almost 2,400 accounts, called Individual Development Accounts (IDAs), through a range of community organizations and financial institutions. The purpose of the demonstration was to determine whether people with lower incomes could save if given access to the right mix of accounts, incentives, and support services. The research confirmed that asset building by the poor can work if properly supported. However, beyond this basic question, ADD provided a multidimensional learning opportunity for researchers and policymakers alike. The experience was assessed through a number of different research methods, including implementation assessment, participant case studies, cross-sectional survey, account monitoring, in-depth interviews, cost analysis, experimental impact evaluation, and assessment of community effects.

Following the ADD, the Saving for Education, Entrepreneurship, and Downpayment (SEED) initiative was conducted to explore the impact of offering saving accounts to children and youth. The impetus behind this effort was to offer access early in life to saving opportunities, which might trigger behavioral change and offer greater opportunities as children grow. Through this effort, begun in 2003, almost 1,200 Child Development Accounts (CDAs) were opened and administered by twelve community organizations (Sherraden and Stevens 2010). A second component of SEED is being implemented in the State of Oklahoma, where a large sample of children was enrolled in the state's 529 College Savings Plan, along with a control group to facilitate a comparison. This experiment, along with the research findings, will continue to unfold in the years to come.

Through both demonstration projects and other efforts to establish IDA and CDA programs, a field of practice has emerged in tandem with heightened policy and research interest. The ability of local, nonprofit organizations to offer saving opportunities to their constituents was greatly enhanced by the passage of the Federal Assets for Independence Act in 1998, which created a funding stream to support the matching of deposits in IDAs. While it is a modest program, typically funded at $25 million a year, it has provided a steady stream of financial resources since its passage. This has enabled a growing number of organizations across the country to not only administer IDAs but also pursue an expanded set of services designed to support asset-building objectives. As a result, they increasingly described their work as connected to a growing field of asset building.

This field has been able to provide an overarching frame for a broad spectrum of organizations and networks. It has been a means to connect groups focused on supporting affordable homeownership, providing access to public assistance, promoting education and college access, and connecting people with high-quality, low-cost financial services. For instance, as a national network of groups emerged to offer free tax preparation services to lower income families to facilitate access to the benefits of the Earned Income

Tax Credit (EITC), participating individuals and organizations began to embrace a set of asset-building objectives. Collectively, these groups saw value in focusing their services in ways that helped people manage their finances and support long-term financial goals, which often included paying down debt and building up savings.

Given these multifaceted developments, the asset-building field today can be seen as encompassing a range of actors and organizations interacting with a broad array of public policies and programs. The field is unified by an antipoverty and social development strategy that aims at helping people move toward greater self-sufficiency and financial security. However, it embraces a broad set of pathways and asset types, recognizing that the full range of productive assets includes savings, investments, a home, a business, postsecondary education and training, and a nest-egg for retirement.

Key Issues in the Rise of Asset Building

Two decades ago when *Assets and the Poor* was written, the prevailing assumption was that poor people could not save given their low earnings and would not save because of their preferences. This assessment was not based on any particular evidence, but it was the basis for the belief that any program promoting assets and saving would be an ineffective use of time and resources. The subsequent research conducted in the field, which has tested a variety of approaches to saving and asset building, played a significant role in engaging with critics who were initially skeptical.

The combination of pilot projects, demonstration programs, and longitudinal research conducted in a range of locations generated a body of evidence that anchored the discourse. The research findings to date have generally served to confirm the core hypothesis that assets have beneficial effects. Simultaneously, the experience of those running programs based on this model has increased support for some of the most underlying themes of asset-based interventions. Practitioners working with lower-income families found that building assets opened up new options for economic growth and mobility. By improving long-term economic security and providing alternative means for short-term consumption, assets potentially transform the calculus of one's life in a way that maintaining regular employment income might not.

Some critics remain skeptical. They may consider the research findings generated by pilots and demonstration projects to be insufficient justifications for a large-scale policy change. Or they may believe that, regardless of whether the poor can save and the positive role assets can play in economic security, it makes more sense to prioritize jobs and income as the most crucial contributors to success in US society. Nevertheless, the quality and seriousness of the research agenda and the increasing experience of practitioners has led to a more sophisticated discussion.

While many questions remain, the conversation has advanced. Today most people who think about social policy and poverty acknowledge the complex set of conditions families confront, many of which are beyond their control. Poverty is not a result of individual defects. Similarly, there is a greater recognition that people will seek out opportunities to improve their economic situation, despite constraints, and strive to be active participants in their own mobility. There is also an appreciation that there is no "one size fits all" package for social development and building economic security. For some, education and training might be the path to career enhancement and upward mobility, for others, starting a business enterprise with sufficient support and capitalization might be the turning point, while for still others, establishing a reasonable budget to manage current resources with a priority toward reducing debt and putting away for retirement is what is needed.

There are groups within the asset-building field working in all these areas, continuing to expand opportunities for vulnerable populations. At times, this diversity has diluted the coherence of asset building as a discrete field of practice, but in other respects, it has expanded the relevance of the “assets” framework in both issue areas and among diverse populations. Even though much of the initial work focused on the poor, asset-based policy concepts are germane for families up and down the economic ladder. In fact, there is a case to be made that accumulating and controlling a pool of assets is inextricably linked to the types of economic security most American families aspire to achieve.

These aspirations are what made the experience of the Great Recession such a disruptive force. Its impacts have been sobering. Not only did it destroy wealth, erode assets, and generate large income shocks, but it also forced many to reconsider their assumptions about the economy and role of social policy. For many, the reality has become greater employment insecurity with even well-educated individuals facing long-term unemployment. This also contributes to greater income volatility. In addition, inequality has increased but taken on a new form. Prior to the recession, the income distribution had become increasingly skewed with the most significant growth occurring among the top 1 percent of earners. Meanwhile, median incomes were largely flat. The shock of the recession may have temporarily slowed incomes at the top, but the bursting of the housing bubble led to declining home values across the board and many people have lost their homes to foreclosure. In recent years, the stock market has rebounded but the housing market has not, which has dramatically exacerbated wealth inequality.

This represents a new challenge for the asset-building field. It should stimulate some reflection about the inherent risks and security assets provide. Yet economic volatility also reinforces the potential value of having a significant degree and diversity of asset holdings. Having access to savings and investments can create a valuable degree of economic resiliency where people are better able to weather income disruptions and financial shocks. Future economic uncertainties typified by income stagnation and volatility justify an expanded role for assets as a feature of social policy. Ideally, asset-based policy and programs would include counter-cyclical approaches that protect the most vulnerable so they do not lose hard-earned assets during economic downturns. For many, protecting existing assets is just as valuable as acquiring new ones.

For these policies to be most effective, they need to include everyone and be implemented across the life-course. This, in fact, was central to Sherraden’s original conception. He proposed creating an account for every child starting at birth that could provide assistance at key life cycle moments. The call was for policy that was universal, progressive, and lifelong. Although this concept was never fully implemented in the United States as a comprehensive federal policy, there are examples in other country contexts of what such an approach would entail. Two specific models are found in the United Kingdom and Singapore. The United Kingdom launched the Child Trust Fund in 2005 under which every newborn child was offered an initial deposit (£250) that could be used to open a designated child account, with more money progressively going to low-income households (Cramer 2007). The money cannot be accessed until the child turns eighteen and has led to increased saving rates among the poor. With a change of government in the United Kingdom, these initial deposits are no longer offered, but children who currently have accounts are allowed to maintain them. Singapore’s system, implemented through their Central Provident Fund, is truly lifelong (Loke and Cramer 2009). There are accounts established for babies where accumulated resources can be used for developmental purposes. When the child begins school, any leftover funds are put into a college savings account. Once the child completes schooling and enters the workforce, residual resources are designated for retirement security purposes and additional contributions

are facilitated through the workplace. Thus, universal, progressive, and lifelong asset-building policy is possible, but has not yet been achieved in the United States.

Examining the policy structures in other national settings is more than an academic exercise. It helps illuminate the potential role of large-scale policies and mechanisms that can be used to support saving and wealth accumulation, which are often administered through institutions. In this context, institutional arrangements are defined as "purposefully created policies, programs, products, and services that shape opportunities, constraints, and consequences" (Beverly et al. 2008). The emphasis is on the explicit conditions put in place to generate a specific outcome. When people are not connected to these arrangements, they may be excluded from the activity or outcomes, which in fact is the reality for many lower-income and economically vulnerable populations. In this manner, the lack of access to institutional structures can become a barrier for opportunity and economic advancement.

It is helpful to consider the range of institutional features that help promote the process of saving. Along with others, we have suggested, seven constructs that influence the ability of people to save and accumulate asset (Beverly and Sherraden 1999; Beverly et al. 2008; Sherraden and Barr 2005). These include (1) access, (2) information, (3) incentives and disincentives, (4) facilitation, (5) expectations, (6) restrictions, and (7) security. Examples of these constructs include workplace benefits, distance to financial institutions, availability of financial education, subsidies, rates of return, automatic enrollment, payroll deduction, match caps, rules for use, and level of trust in financial institutions. These features are often bundled together in various combinations. Greater detail on these ideas can be found in other places, but the foundational point to make here is that there are a range of factors that determine outcomes that extend beyond individual preferences and attributes. For example, we know people participate in workplace savings at significantly higher levels when they are automatically enrolled and accumulations are greater when there are automatic payroll deductions and an employer match. These insights about the role of institutional features should inform how we think about policy and product development in order to maximize participation and saving outcomes.

There is still work to be done to further develop the theory, research, and practice of asset-building strategies. The rest of this book highlights current research. Opportunities abound to connect this intellectual work to contemporary policy discussions at all levels of government, and even political discourse—such as that which has emerged via the "Occupy Wall Street" protests. Shared interests among "the 99 percent" could create new avenues for greater participation in saving and wealth building as a requisite to achieve security regardless of where one starts on the economic scale. But being able to participate is not enough; the marketplace needs to be safe. The proliferation of high-cost and low-quality financial products and services played a part in the recent financial crisis and was a primary justification for the creation of the newly formed Consumer Financial Protection Bureau (CFPB). This agency is being tasked to oversee the financial service marketplace to ensure the playing field is level and participates can be connected with appropriate products and services. During its initial rollout, the CFPB has sought out and will need public feedback to make sure it becomes an effective regulator, one that is capable of transforming our financial marketplace in ways that significantly improve outcomes for lower-income households.

Organization of the Book

The book is laid out in three sections, which focus on the changing landscape, pathways to asset building, and directions for the future, respectively. Each section includes a series of chapters that explore distinct topics related to the broader theme. A diverse set of perspectives is deployed, with some chapters emphasizing developments in the policy arena

while others describe new research findings. In many cases, the authors are assessing recent information that has emerged out of the experience of the Great Recession, which served as a particularly disruptive force for families, communities, and the national economy.

The first section focuses on how the social policy landscape in America has changed over time. Three chapters are presented that describe the evolution of policies, economic conditions, and the provision of financial services.

Trina Shanks provides a broad overview of the evolution of public assistance programs. She identifies discrete periods of policymaking, such as the New Deal, the Great Society, and welfare reform efforts of the 1990s, that shape current approaches to poverty and social insurance. When examining the contemporary array of welfare programs, Shanks observes that many of the programs with highest levels of participation, such as the Supplement Nutrition Assistance Program (SNAP) and Medicaid, primarily facilitate consumption rather than overall social development. Meanwhile, programs that prioritize social development and economic growth tend to have little funding and thus low participation rates. However, enactment of welfare reform in 1996 has created an opening for the consideration of alternative approaches. In this context, the rise of an assets perspective has increasingly influenced how social policy is debated and discussed, even though it has not yet produced large-scale policy reforms.

Clinton Key presents an analysis of the typical household balance sheet after the Great Recession. With the most recent data available, he describes patterns of asset holding and liabilities for a series of household types. Using a novel methodological approach, he is able to offer an insightful look at what families own and what they owe and finds much diversity. Despite the idiosyncratic quality to the balance sheet of American households, several themes emerge that indicate a pervasive financial insecurity among many family types. For example, many subgroups of the population were found to have low levels or a complete absence of savings dedicated for retirement. His analysis also reveals the unique role housing plays in the family balance sheet, representing the largest asset and liability. The illiquid nature of housing assets he describes contrasts with the extent to which families have liquid assets. In fact, many families do not own a stock of liquid assets necessary to maintain a standard of living in the case of income loss or fluctuation. Households at or near the federal poverty threshold are even more disadvantaged with respect to assets and debts. He describes how the Great Recession has left many families exposed to financial risk by leaving them with few assets and substantial consumer debts.

The advent of the Great Recession offers a new backdrop for a reexamination of the ways in which families access financial services. Devin Fergus takes readers on a tour on the various ways that the provision of basic financial products and services has changed over the last three decades. Fergus seeks to connect the path to the financial crisis with a series of regulatory policy changes that undermined consumer protections, especially as they were applied to four spheres of contemporary life that had served as traditional pathways to upward mobility: housing (subprime mortgages and home equity loans), education (student financial aid system), employment (payday loans), and transportation (auto insurance). He traces how trends toward deregulation allowed for the rise and codification of consumer finance fees in each of these areas. The rise of the consumer fee, what Fergus calls “financial fracking,” is shown to function as a means to extract equity and wealth, and thus ultimately to exacerbate economic inequalities.

Section II offers a series of chapters that feature different pathways to asset building. It begins with a chapter on the racial wealth gap by Thomas Shapiro and his colleagues Tatjana Meschede and Sam Osoro at the Institute on Assets and Social Policy at Brandeis University. They present a set of findings that describe not only the extent of the current racial wealth gap but also how it has significantly widened to become one of the most dramatic manifestations of intergenerational poverty and decreasing economic mobility.

Their analysis is one of the first to examine the impact of the Great Recession, and they empirically examine the main reasons behind the rise in the racial wealth gap over the past 25 years, paying close attention to a set of factors embedded in contemporary institutions.

The following two chapters focus on one of the most significant mechanisms used by families to build their asset base over time: homeownership. Carolina Reid takes a close look at the history of policy efforts to promote homeownership, uncovering its potential as an asset-building strategy as well as its real-world pitfalls. Reid describes how innovations in mortgage lending and asset-based policies and programs led to a significant expansion of homeownership demonstrating the promise of policies that use targeted incentives to promote savings (principle reduction) and wealth building (equity accumulation). Gains in homeownership since the 1990s, especially among families with lower incomes, opened up new avenues for asset accumulation and a means to narrow racial wealth inequities. These gains were completely undermined by the subsequent rise of subprime and predatory lending practices that left many families exposed when housing prices collapsed. There were substantial regulatory failures that ultimately resulted in the foreclosure crisis that unfolded with the Great Recession. From this experience, Reid extracts a series of insights to guide future policy in support of responsible homeownership. Her analysis identifies that the foundation for sustainable funding requires finding the balance of government policies that can promote equal and fair access to credit while at the same time protecting consumers from abusive lending practices.

Allison Freeman and Janneke Ratcliffe add to this discussion with their chapter that articulates a series of insights derived from a large-scale and innovative homeownership initiative. They consider the experience of a portfolio of over 46,000 home-purchase mortgages made to lower-income households through Self Help's Community Advantage Program (CAP) and aim to counter critics who argue that affordable, sustainable homeownership cannot help lower-income households build long-term wealth. They do so by contesting five emerging suppositions about homeownership, which have risen to prominence since the mortgage lending crisis began. They demonstrate how homeownership does not crowd out other investments, lead to excessive borrowing, cost more than renting, or need to be restricted to those with large initial downpayments. Instead, they show how the CAP experience reveals that a primary determinant of a successful homeownership experience is the quality of the loan underwriting. While buying and owning a home is not for everyone, when qualified lower-income households are provided with the right tools and structures, epitomized by a well-underwritten loan, it can offer lasting benefits.

Another promising pathway toward asset building is found in savings programs. One of the initial ideas proposed by Sherraden in his 1991 book was support for matched savings that could be used for asset purchases. The direct match to deposits served as an accessible incentive to encourage contributions. The challenge of scaling up this policy was the public subsidy required to fund the match. In the intervening years, insights from the field of behavioral economics have emerged, which can be deployed to develop savings programs, many of which can be successful without a public subsidy. In their chapter, Piyush Tantia, Shannon White, and Josh Wright describe key principles of behavioral economics (including suboptimal decision making, intention-action gaps, depletion, and scarcity) that have relevance in program design and policy implementation. Their work shows how the behavioral perspective is particularly useful when thinking about scalable and sustainable savings programs.

The next two chapters focus on the potential impact of connecting children with savings accounts. William Elliott III gathers the available evidence of the links between savings and children's college progress. His chapter reviews the disparities in college attendance and completion rates by socioeconomic class, and describes the increasingly critical role that education plays in employment and economic mobility. For some, this

evidence is used to justify increased access to student loans, but there are even greater advantages to promoting saving for college well before a student begins to pursue a postsecondary degree. The accrual of savings has been shown to play a role in keeping students "on course" to complete degrees and in reducing "wilt," whereby students who are expected to graduate from college fail to do so. This reveals the salience of financial barriers, rather than a lack of desire, as a critical roadblock in the path to a college degree. Elliott shows that having savings changes the way children think about college.

Terri Friedline examines asset building as a strategy for improving young people's well-being, specifically by extending savings accounts early in life. She describes the emergence of this concept over the past two decades and examines the theoretical underpinnings for why this might prove beneficial, focusing on the impact of connecting youth to financial services at various stages of their development and reinforcing a set of perceived social norms. Friedline examines the research on how and why young people from lower-income households may be at a disadvantage for experiencing the positive effects of saving. She reviews the growing array of programs and policies that have been developed to redress barriers in access to savings accounts and considers a set of policy implications.

The final chapter in this section examines how the interaction of tax policy and the tax-filing process create opportunities for families to engage in savings and asset-building activities.

David Rothstein and Rachel Black describe how the creation and subsequent expansion of the earned income tax credit has transformed tax refunds into an "asset" in their own right. In fact, for many families, their tax refund is now the largest single influx of income they will receive all year. Tax filing is now a time for managing household finances, when families can consider and pursue a range of financial objectives in ways previously unavailable through traditional public assistance programs. As the size of refunds has grown, so too has a network of support organizations that offer free tax preparation services to lower-income families. This network has focused on connecting families with opportunities to leverage their refunds in constructive ways. This network has played a number of important functions, such as connecting families with an array of financial and social services as well as serving as a testing ground for innovative policies and programs that might be taken to scale nationally. As such, Rothstein and Black make a case for expanding these types of services and explore the potential of policy reforms that can increase the capacity of this network and make tax time a more effective financial management opportunity for families.

Section III features two chapters that consider directions for the future. In the first chapter, Reid Cramer makes the case for using an assets perspective to inform contemporary approaches to social insurance, economic inclusion, and mobility. He describes a rationale for an expansion of asset-based social policy, identifies a set of informative policy guideposts that can shape effective policy formulation, and describes a specific set of policy proposals that have emerged as key components of an asset-based policy agenda. Prosavings and asset-building policies can be implemented across the life course and in ways that promote greater economic security and resiliency. While the "assets agenda" is not designed to replace traditional social insurance or safety net programs, there are benefits for creating new policy mechanisms that help families build up their asset base.

In the closing chapter, Michael Sherraden offers his perspective on the people and organizations that helped guide the development of the asset-building field as well as how the future of asset building can intersect with current social policy. When he first published his book *Assets and the Poor*, there was a different set of assumptions than there is today that guided social-policy thinking. He provides a detailed defense of the evidence base for asset building and offers potential strategies for its expansion over the next two decades.

The work presented in this volume is a testament to Sherraden's influence in elevating the consideration of assets in social policy discussions. Yet more consequentially, the chapters reflect a variety of ways that the social policy landscape has been transformed over the last two decades. Today, it is widely acknowledged that policies designed to combat poverty over the long term must extend beyond facilitating a minimum level of consumption. This has connected traditional antipoverty work with a broader set of issues connected to financial inclusion, economic resiliency, and ultimately social mobility.

Accordingly, greater attention has been given in recent years to helping families rebuild their balance sheets by lowering debt and raising their assets. This has led to increased scrutiny of the delivery of financial services, the extent to which families are excluded from the financial mainstream, and the overall distribution of wealth and assets. Other work has focused on creating new opportunities for families to save and build wealth, whether at tax time, when they participate in public benefit programs, or as homeowners.

While the points of connection will vary across a diverse population, the central insight of the assets perspective appears to have relevance in a variety of circumstances. People benefit when they gain control over an array of financial resources that can be accessed and deployed strategically to help them move forward in their lives. This is where assets come in. They are the rungs that facilitate the climb up the economic ladder. We believe there is a collective interest in making sure this ladder is available to each and every member of our society.

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Part I

The Changing Landscape

Chapter Two
The Evolution of Antipoverty Programs

Trina R. Williams Shanks

America's approach to assisting poor families and individuals has changed substantially over its history. In America's early years, there was little federal policy directed toward lower-income people. However, over the course of the twentieth century, a unique welfare state emerged, despite the reluctance of many federal policymakers to fully embrace it. Within the past two decades, policy approaches to addressing poverty have shifted again and now encompass concepts from the field of asset building. This recent evolution of antipoverty programs reflects a different social policy landscape from that which prevailed during either the Great Society period of the 1960s or the welfare reform debates of the mid-1990s. By summarizing broad trends in US antipoverty programs, this chapter aims to place the asset-building perspective into a larger policy context. Today there is much more attention given to providing low-income families with a set of appropriate supports that permit social development and upward mobility. In this chapter, the concept of social development refers to opportunities for educational attainment, household economic stability, and the ability to plan for the future, especially promoting children's economic mobility. A survey of existing programs and policies demonstrates that the federal programs best suited to this purpose have the lowest participation rates and least funding. The discrepancy between social policy intention and practical policy implementation is indicative of both the current limitations of the welfare state as well as the potential of the "assets perspective" to inform future social policy efforts.

Historical Overview

The original colonies and early United States closely followed British Poor Laws, most notably the Elizabethan Poor Law of 1601, in defining three major categories of dependents: children, the able-bodied, and the incapacitated or "worthy" poor (Trattner 1999). Over time, the United States developed a particular set of preferences that shaped the general outline of antipoverty programs. These include the following:

- a limited federal role with most authority at the city or county level and great variety across states;
- widespread perception that voluntary and private charitable institutions were preferable to public (i.e., government-funded) ones;

- the idea that trained professionals were needed to provide appropriate aid to the poor; and
- a long-standing tradition for funding child welfare and public health, but less willingness to aid able-bodied, working-age adults.

In times of economic stability and within smaller communities where people knew one another, local county systems functioned relatively well. Yet when economic downturns hit or cities grew to hold large urban populations, local systems (both private and public) became quickly overwhelmed.

In the history of the United States, there were two periods of major policy change that substantially shifted options available to the poor. The first followed the Great Depression when President Franklin D. Roosevelt created a set of programs and agencies collectively known as the New Deal. The second was during a period of relative prosperity when President Lyndon B. Johnson declared a "war on poverty" and instituted the Great Society programs of the 1960s.

The New Deal era transformed the US policy landscape at the federal level. With unemployment rates as high as 25 percent in 1933, the federal government definitively took on the role of providing relief to struggling families. The response included large infrastructure projects such as the Tennessee Valley Authority, public works programs to provide jobs to the unemployed, the establishment of fair labor standards, as well as programs to help reform the banking system to protect small savers and investors alike, with the creation of the Federal Deposit Insurance Corporation and the Securities and Exchange Commission. Many long-standing programs to assist the poor established under the New Deal continue to exist in some form today: Social Security, unemployment insurance, commodities programs that became food stamps and are now known as SNAP (Supplemental Nutrition Assistance Program), Aid to Dependent Children, which became the TANF program (Temporary Assistance for Needy Families), and the Federal Housing Authority that is now part of the cabinet-level Department of Housing and Urban Development.

The Great Society programs were announced as an effort to eliminate poverty, which remained persistently high at levels around 19 percent leading up to 1964. During this period, Congress passed the Economic Opportunity Act, which established the Office of Economic Opportunity designed to expand the role of the federal government to directly provide programs and services to assist poor families. Many criticized the programs for being woefully underfunded and for not actually creating jobs or giving income to the poor, but rather supporting education, training, and social services that would only be relevant in a time of continued economic growth (Trattner 1999). However, medical insurance coverage expanded during this time with the creation of Medicare and Medicaid. In addition, many of the core programs established in the 1960s continue to exist today: community action agencies, Head Start, Volunteers in Service to America (VISTA), Legal Aid, Job Corps, and Upward Bound.

Both of these periods of policymaking have exerted a lasting legacy on the American welfare system and the manner in which social policy is conceived and implemented. Recent history has been characterized by a set of minor additions and discrete "tweaks" that have reformed the delivery systems or modestly expanded benefits for programs that were created during earlier periods. For example, the Earned Income Tax Credit (EITC), which offers a refundable tax credit to low-income working families that functions as a wage subsidy, was introduced by the Tax Reduction Act of 1975. The value of the EITC has periodically been expanded over the years, but its basic form has remained the same since it was created. In an effort to reduce malnutrition, the WIC (Special Supplemental Nutrition Program for Women, Infants, and Children) Program was introduced in 1972 as a focused addition to existing food programs and made permanent in 1975. An addition

to the Higher Education Act in 1972 brought assistance to low-income students and eventually came to be known as the Pell grant program, which has also been reformed and expanded in subsequent years. Additionally, almost every presidential administration has its own approach to providing training for low-income youth and adults. Under Richard Nixon, the Comprehensive Employment and Training Act (CETA) was passed in 1973. Under Ronald Reagan, the Job Training Partnership Act (JTPA) was passed in 1982. Under Bill Clinton, the Workforce Investment Act (WIA) was passed in 1998. At times even when the actual program remained essentially the same, there have been shifts in eligibility making enrollment either easier or more restrictive.

A larger policy debate around public assistance occurred during the 1990s and culminated in the enactment of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, an act now known as "welfare reform." Signed by President Clinton, this law transformed the largest federal welfare program from an entitlement program that offered cash benefits to families into a state-run block grant program called TANF. Under TANF, means-tested cash benefits are no longer an entitlement, and lifetime limits for receipt have been imposed. States typically responded to these changes by keeping enrollment and benefit levels low. The new limitations embodied in the TANF program provided an impetus for considering alternative antipoverty approaches. A new political space emerged in the wake of these changes to explore programs that better supported self-sufficiency, asset building, and economic empowerment.

One result of this political shift was the 1998 passage of the Assets for Independence Act (AFIA), which provided a small amount of federal funds to support IDAs. These accounts are designed to help participants save resources that can eventually be used to pay for training, education, small business development, or a downpayment on a home. While the scale of this effort has been modest, it reflects an emerging interest in policy options that emphasized social development and long-term economic mobility rather than immediate consumption and an emergency safety net. Additional experimentation has occurred at the state and local level. For example, conditional cash transfer (CCT) programs, which offer direct cash support linked to specific actions or behaviors, are popular both in developing countries and in the United States. CCTs have been tested in New York City, although they are not yet part of the federal policy landscape. In fact, CCTs may illustrate one of the fundamental characteristics of recent social policy discourse. New policy ideas and approaches have been incubated with applicability for all levels of government, but few large-scale changes have been enacted at the federal level. Instead, experimental pilot and demonstration programs have been implemented, funded by private philanthropy, which have led to policy insights that are further informing policy discussions.

Social Welfare Typologies

To make sense of the evolution of US social policymaking and programs, it is useful to compare the United States and its approach to social welfare policies for the poor to other developed nations. In his original typology, Esping-Andersen (1990) classified the United States as a pure type of the liberal model of welfare capitalism characterized by market dominance and private provision, where the state rarely interferes to address poverty or provide for basic needs, relying primarily on means testing when it does. This is in contrast to the pure social-democratic model in countries such as Sweden where universal access to benefits and services is the norm, with greater individual autonomy and less reliance on the family and markets. Although many other countries (such as Canada, the United Kingdom, and Australia) have also been classified as liberal, this category is less cohesive (Ferragina and Seeleib-Kaiser 2011). According to this classification scheme, it is often presumed that the federal government in the United States

will remain unlikely to expend many resources to protect individuals, poor or otherwise, from being dependent on market forces and that there will be high levels of inequality and social stratification. Even if this classification were an accurate portrayal of US policy priorities in the past, it is possible for them to evolve toward a greater emphasis on social development given changing conditions.

Others have questioned the idea that the United States has a small welfare state as well as the underlying assumption that a larger welfare state undermines economic growth. When Garfinkel, Rainwater, and Smeeding (2010) include public education and employer-provided benefits as part of social welfare expenditure, the United States is no longer a laggard in the proportion of GDP spent, and becomes very similar to other rich English-speaking nations. Considering this more expansive definition of social welfare, the United States spends more per capita than almost all other countries (Garfinkel, Rainwater, and Smeeding 2010).

If spending on cash relief and public benefits for the poor are combined with spending on public education and social insurance to comprise all social welfare spending, the United States spends a substantive amount on its welfare state, similar to other rich nations (Garfinkel, Rainwater, and Smeeding 2010). Yet, the US system is a patchwork of programs that supports certain designated populations with cash and in-kind benefits, but leaves out portions of the poor and allows some to remain in deep poverty—defined as less than 50 percent of the federal poverty line (Ben-Shalom, Moffit, and Scholz 2012). The demographic groups most helped are the elderly and disabled; the groups most underserved are nonelderly, nondisabled families without some member continuously employed (ibid.). Thus, the question becomes whether social welfare expenditure in the United States could be adjusted to reach more people in need and do a better job of reducing inequality and enabling social development. The best point of analysis may not be simply dollars spent on social welfare, but how well this expenditure reaches those at the very bottom of the economic ladder and does so in ways that promotes economic mobility and improved life chances.

A policy emphasis on social development can be explained in the way that Amartya Sen and Martha Nussbaum describe investment in expanding capabilities or the "real opportunities you have regarding the life you may lead" (Sen 1987, 36). Sen (1999) notes how individual agency and social arrangements complement each other. When social action (or policy) offers genuine opportunity, this provides a context wherein individuals have the freedom to take initiative to overcome poverty and deprivation. Nussbaum (2011) builds upon this work to highlight that a society promotes human capabilities by supporting the development of internal ability within individuals as well as the political social and economic environment that allows them to thrive. Thus, rather than just accepting what market forces allow, policies with a social development focus will intentionally strive to increase individual capabilities by creating structures that expand and even accelerate mobility.

Similarly, john powell [sic] (2012) prioritizes targeted universalism as a way to enable greater social development. Given that there are social and economic inequalities in the United States (historically along racial and ethnic lines), some people will naturally begin at different starting points and may need more assistance than others to fully develop their capabilities. Thus, powell suggests setting clear goals for everyone and then developing feedback loops to closely monitor whether they are achieved. Because "we are situated differently in relation to social structures and the environment, . . . strategies to provide opportunities for progress toward these universal goals must be targeted for greatest effectiveness" (powell 2012, 233). For example, if the capabilities goal is for citizens to be well-educated (which could be defined as a high-school diploma and some postsecondary education or training), reaching this goal may require more resources, effort, and attention in a low-income community than in a wealthy one. Although a social development emphasis could include universal resources for social insurance or common needs, there

are also situations where greater and targeted investment may be required to achieve economic mobility for the most disadvantaged. This would require a shift in the current US policy landscape to actively invest in populations beyond the elderly and disabled.

Take-up and Social Development Impact

The tables in this section present basic funding and participation levels for major antipoverty and social policies in the United States. The goal is to assess the various programs that make up the current US welfare state and identify trends associated with social development objectives. According to the Center for Social Development, social development innovation in public policy enables individuals, families, and communities to formulate and achieve life goals and contribute to the economy and society. This is similar to Sen's concept of expanding capabilities. Ideally, such policy would offer initial investments that explicitly support individual economic mobility, without ongoing dependency. A good historical example of this is the Homestead Act where millions of families were deeded national land that provided an asset that could be developed to contribute to the agricultural economy of the time and passed down to future generations. It is estimated that one-quarter of the US population in 2000 was the descendent of a homesteader (Williams 2003; Williams Shanks 2005).

Another example is the GI Bill where at least 12.4 million World War II veterans were able to successfully transition to civilian life and be positioned to enter the middle class. This included 7.8 million who received education benefits (college, graduate school, or other education/training); 4 million who received a VA-guaranteed loan to finance a home, farm, or business; and another 8.4 million who received unemployment benefits or "readjustment allowances"; 78 percent of veterans received at least one of these benefits (Althschuler and Blumin 2009). Although the benefits of the bill were made available to all returning veterans, the majority of recipients at that time were white men. In addition, discrimination in residential access and college admissions left many people of color out of desired universities and new suburbs (Quadagno 1996). Promoting a similar mandate today for the civilian population that is inclusive and reaches the most vulnerable would be a helpful addition to the current policy mix while achieving social development objectives.

Although most major programs are covered in the tables in this chapter, the list is not meant to be exhaustive. Included are programs that deal directly with individuals or households and substantially impact low-income populations. For example, Community Action Programs are not included because they do not fund specific support directly to low-income individuals, but rather comprise an array of programming in local communities, typically through Community Action Agencies. Unemployment Insurance is also excluded because its greatest contribution is to support higher-income workers after job loss. In fact, low-income workers are the least likely to receive unemployment insurance (Enchautegui 2012; GAO 2006; Gould-Werth and Shaefer 2012).

Each program discussed is designated a category based on how much it emphasizes social development: low, medium, or high. The tables highlight how many people actually receive the benefit, the amount of federal funding expended, and an analysis of how the policy or program ranks in terms of social development in an attempt to characterize its potential for improving individual capability. In developing a plan of analysis to determine where various programs fit, each is examined on two dimensions. The first dimension is whether there is an initial transfer of cash or real economic resources as opposed to ongoing in-kind programs and services. If generous and dependable, cash transfers allow individuals multiple options to pursue their own paths to improve economic mobility and social development. Although any in-kind provision can be important and beneficial, it

is by definition limited to one area of need and is not as flexible in providing a variety of options for people to improve their capabilities or reach social and economic goals.

The second dimension is whether there is an intentional focus on social development that can improve life chances over an extended time horizon versus short-term consumption. Any worthwhile endeavor that is not already underway takes time and intention. Whether improving human capital by pursuing educational attainment, starting a business, purchasing a home, or making other worthwhile investments, it takes time to complete courses, raise money, and be successful. In addition, participants must actively plan and complete their established goals. Almost by definition, any assistance that is provided in-kind and/or has limited ability for individuals to participate in their own progress over time is less likely to achieve as much social development.

Policies that support ongoing in-kind programs or services for immediate consumption without an intentional goal of promoting social development will be ranked as "low." For this classification schema, social development is defined as increasing educational attainment, generating household economic stability, and promoting strategies to plan for future mobility, especially expanding life options for children. Income support alone is not enough to rank as "high" on social development, even if it brings a household above the poverty line, because any money received is likely to be used for consumption unless particular goals or restrictions are required. Policies that rank as "high" provide cash or real economic benefit as well as strategically design their program offerings to improve economic and life outcomes for children and family members. All of the low-end programs are in-kind and focused on short-term consumption. Most of the middle programs are a hybrid, a combination of either in-kind services focusing on a social development goal or cash transfers with little explicit focus on social development. The high-end programs tend to include both cash transfers and a social development emphasis (although it is also possible to provide an intense emphasis on social development at key transition periods while offering mostly in-kind programming). Another important dimension is whether the policy or program is intended to be universal and the actual participation rates. As we will see, this distinction appears to be associated with the degree to which a program supports social development objectives.

Table 2.1 Programs with "low" social development emphasis

Program	*Participation*	*Federal funding*
Medicare	49.4 million beneficiaries as of 2012.[1]	$548.3 billion appropriated for FY-2012.[2]
Medicaid/ CHIP	In FY-2011, 8.0 million children enrolled in CHIP; 35.6 million enrolled in Medicaid.[3]	$283.4 billion appropriated for FY-2012.[4]
SNAP	47.1 million participants as of August 2012.[5]	$88.6 billion appropriated for FY-2012.[6]

Notes:
[1] The Henry J. Kaiser Family Foundation. 2013. "Total Number of Medicare Beneficiaries, 2012." State Health Facts.
[2] US Department of Health and Human Services. Centers for Medicare and Medicaid Services. 2012. "Justification of Estimates for Appropriations Committees, Fiscal Year 2013."
[3] US Department of Health and Human Services. 2012. "2011 CHIPRA Annual Report."
[4] US Office of Management and Budget. "Fiscal Year 2012 Budget of the U.S. Government."
[5] US Department of Agriculture, Food and Nutrition Service. 2012. "Nutrition Assistance Programs Performance Report: October Performance Report."
[6] US Department of Agriculture. 2012. "Fiscal Year 2013 Budget Summary and Annual Performance Plan."

Table 2.1 summarizes programs placed in the low category for social development. These include Medicare, Medicaid/CHIP, and SNAP. Medicare and Medicaid reach millions of people and offer essential access to health care for the poor, disabled, and elderly. Furthermore, they include a renewed emphasis on enrolling eligible children and pregnant women. These two programs are also among the largest in terms of federal expenditure and the fastest growing in cost (Ben-Shalom, Moffitt, and Scholz 2012). Although good health can provide a foundation for social development and mobility, it does not ensure them. In addition, these funding mechanisms decide what medical care is covered under what circumstances, but does not necessarily influence the quality of care, lifestyle choices, or level or risk. There is a rich literature on the health disparities that continue to exist in spite of these important medical insurance programs (Braveman and Egerter 2008; Escarce 2007; Williams and Mohammed 2009).

Similarly with SNAP, it is beneficial to provide food to households with limited financial resources, especially those with children, to prevent starvation and malnutrition. Food programs are nearly universal for those eligible, yet families continue to face food insecurity (Nord, Andrews, and Carlson 2009). Poor nutrition influences health and can be a precursor to a lack of social development. Yet even if all nutritional needs were met, this would not necessarily lead to greater realization of social development.

In short, all of these "low" social development programs only offer in-kind services as a safety net when households do not have sufficient resources to provide for themselves. They provide emergency food and medical care, but a person can utilize them for a long time and still not improve their social or economic circumstances.

Table 2.2 summarizes seven programs placed in the "medium" category for social development. These include Social Security, the EITC, Pell Grants, TANF, WIC, housing assistance programs, and the WIA. Old-Age Social Security (OASI) has existed since the New Deal era as a public social insurance program to keep the elderly from being poor and dependent on others as they grow older and retire from employment. The benefit is also weighted progressively so that low-wage workers receive a higher proportion of their monthly income in retirement. Thus, it exists to provide greater economic security for a vulnerable population. These facts alone permit the possibility for economic planning over the life course, which allows more options, especially as individuals consider exiting the workforce. Over time, the program has also expanded to include survivors and disability insurance, so many nonelderly and children also receive benefits. It also includes a provision for work incentives in certain situations. For example, the Plan to Achieve Self-Support (PASS) allows individuals with a disability to receive assistance to save toward a plan to help them return to work, including training, equipment, or supplies to start a business. Social Security is a cornerstone of our social safety net in that it provides nearly universal benefits and has helped significantly reduce poverty rates among the elderly and most vulnerable. It has also been indexed to keep up with inflation so the cash benefits maintain their value over time, although this provision has been reconsidered during recent policy debates.

The EITC has expanded rapidly with the number of recipients growing from 12.5 million to 19.8 million between 1990 and 2003. During this same time period, the maximum benefit grew from $953 to $4,204 per family (Currie 2012). It is a tax credit proportional to earnings up to a cutoff point and earnings levels are indexed to inflation. It probably does more to lift children out of poverty than any other program. The goal is to encourage work among recipients, which are largely single mothers. A recent study concludes that the EITC not only increases employment, but also results in work that experiences earnings growth over time (Dahl, DeLeire, and Schwabish 2009). These facts alone can set the stage for greater social development. Although EITC recipients often say that they plan to

Table 2.2 Programs with "medium" social development emphasis

Program	*Participation*	*Federal funding*
Social Security	55.4 million beneficiaries as of 2011.[1] 68% participation rate for all eligible parties.[2]	$817 billion appropriated for FY-2012.[3]
EITC	26.2 million participants as of 2011,[4] roughly 75% of eligible individuals.[5]	$58.6 billion credited in FY-2011.[6]
Pell Grants	Over 9 million students receiving aid in 2011.[7]	$35.7 billion awarded in FY-2011.[8]
Temporary Assistance for Needy Families (TANF)	4.4 million participants in FY-2011.[9]	$16.7 billion appropriated for FY-2012.[10]
Women, Infants, and Children (WIC)	8.95 million participants as of August, 2012.[11]	$6.6 billion appropriated for FY-2012.[12]
Housing (Section 8 and other assistance programs)	In FY-2011, 2.2 million families receiving housing choice vouchers; 1.1 million utilizing public housing; 1.2 million assisted by Section 8.[13]	$33.5 billion appropriated for FY-2012 (18.3 to HCV, 9.3 to Section8, 5.9 to public housing).[14]
Family self sufficiency	As of September, 2011, 56,600 families enrolled in the program.[15]	$75 million appropriated in FY-2011.[16]
Workforce Investment Act (WIA)	8.7 million served in 2011 (7.1 in adult program, 1.3 in dislocated worker program, 267 thousand in youth programs).[17]	$2.8 billion appropriated for FY-2012 (770.8 million to adult program, 824.4 million to youth program, 1.2 billion to dislocated worker program).[18]
Job corps	57,000 students served in 2010.[19]	$1.7 billion appropriated for FY-2012.[20]

Notes:

[1] Social Security Administration. 2012. "Social Security Beneficiary Statistics." Actuarial Publications.
[2] Shanks, Trina R. Williams, and Sandra K. Danziger. 2011. "Anti-poverty Policies and Programs for Children and Families." In *Social Policy for Children and Families: A Risk and Resilience Perspective*, edited by Jeffrey M. Jenson and Mark W. Fraser. Thousand Oaks, CA: Sage Publications.
[3] US Office of Management and Budget. "Fiscal Year 2012 Budget of the U.S. Government."
[4] US Department of the Treasury. Internal Revenue Service. 2012. "EITC Statistics."
[5] Hirasuna, Donald P. 2010. *Research Examines the Receipt of Earned Income Tax Credits Among Welfare Recipients*. Minneapolis, MN: Federal Reserve Bank of Minneapolis.
[6] US Department of the Treasury. Internal Revenue Service. 2012. "EITC Statistics."
[7] US Department of Education. Office of Postsecondary Education. 2012. "2010–2011 Federal Pell Grant Program End-of-year Report."
[8] US Department of Education. Office of Postsecondary Education. 2012. "2010–2011 Federal Pell Grant Program End-of-year Report."
[9] US Department of Health and Human Services. Administration for Children and Families. Office of Family Assistance. 2012. "TANF: Total Number of Recipients: Fiscal and Calendar Year 2011."
[10] US Department of Health and Human Services. Administration for Children and Families. 2012. "Temporary Assistance for Needy Families: Fiscal Year 2013 Budget."
[11] US Department of Agriculture. Food and Nutrition Service. 2012. "Special Supplemental Nutrition Program for Women, Infants and Children (WIC): Data as of November 9, 2012."
[12] US Department of Agriculture. 2012. "Fiscal Year 2013 Budget Summary and Annual Performance Plan."
[13] Center on Budget and Policy Priorities. 2012. *National and State Housing Data Fact Sheets.*
[14] Center on Budget and Policy Priorities. 2011. "HUD Program Funding for FY 2012." Memo.
[15] Department of Housing and Urban Development. 2012. *Public and Indian Housing Family Self-Sufficiency Coordinators: 2013 Summary Statement and Initiatives*.
[16] Department of Housing and Urban Development. 2012. *Public and Indian Housing Family Self-Sufficiency Coordinators: 2013 Summary Statement and Initiatives*
[17] US Department of Labor. Employment and Training Administration. 2012. "WIA State Annual Reports and Summaries: National Summary of Annual Performance Data."
[18] US Department of Labor. 2012. "FY 2013 Budget in Brief: Training and Employment Services."
[19] US Department of Labor. Job Corps. 2011. "National Performance Results—Program Year 2010."
[20] US Department of Health and Human Services. Administration for Children and Families. "FY 2012 Head Start Funding Increase."

use their refund for economic security and social mobility purposes such as savings, most end up spending the majority of it on consumption (Mendenhall et al. 2010; Meyer and Sullivan 2004; Barrow and McGranahan 2000; Romich and Wiesner 2000; Smeeding et al. 2000). According to one study that did a follow-up survey of EITC recipients, about half of the total refund went toward current consumption, and about 24 percent went toward paying back debt, overdue bills, or prepaying bills. At the six month mark, almost 7 percent of the refunds remained in savings (Mendenhall et al. 2010). Another recent study shows that as single mothers saw their EITC benefits rise, they likely used refunds to prevent a rise in unsecured debt rather than build assets (Shaefer, Song, and Williams Shanks 2012). Given that EITC is distributed through the tax system providing a lump sum of unrestricted money that often represents a large proportion of recipients' salary, it easily could be modified to have an even greater impact on economic security and social development if it were directly linked to savings or other social development purposes. Rothstein and Black (chapter 11, this volume) provide much more detail about how tax time could be used to benefit low-income households financially.

The TANF program provides cash assistance to qualifying poor families. In this respect, it is a flexible income transfer program. The 1996 reforms introduced time limits and work rules. However, the number of people actually served is significantly smaller than the eligible population; many who qualify for support do not apply for assistance. In addition, the real value of this cash assistance varies widely by state and has been declining over time (Rowe and Giannarelli 2006). Even with increased work supports and requirements, TANF is not well suited to greatly improve individual capabilities. Requiring 20–30 hours of "work activity" might actually limit time one can spend going to school and developing the human capital to move ahead. Although one of the stated goals is to promote work, some argue that the real impact of the reforms has been to reduce state caseloads (Danziger 2010; Trattner 1999).

WIC provides food, nutrition counseling, and access to health services for low-income women, infants, and children. It encourages breast feeding and prioritizes reaching participants that are nutritionally at-risk. Although WIC is an in-kind program, it is placed in the "medium" category because it is a time-limited intervention with a specific social development focus, which is improving health and nutritional outcomes for at-risk families with children under the age of five. It targets pregnant women who are vulnerable even before the child is born. Evaluation studies have found that children participating in WIC are less likely to be of low- or very low-birth weight or have iron-deficiency anemia (Owen and Owen 1997). Children are more likely to receive medical care and be up to date in their immunizations as well as have improved vocabulary and cognitive development as they prepare to get ready for school (USDA Food and Nutrition Service 1987).

Housing assistance programs through public housing construction and Section 8 vouchers help subsidize a major household expense. Beneficiaries pay a rent that is 30 percent of their adjusted income. In many parts of the country, securing affordable housing is a real problem. Therefore, rental assistance can help a household free up more money to devote to other developmental needs. The main problem with housing programs in the United States is that not everyone eligible receives assistance. Demand greatly outstrips supply and in many cities even the waiting lists are closed; thus, lucky families receive a generous subsidy while others get nothing (Currie 2012). Additionally, in traditional housing assistance programs, there is a disincentive to raise earnings because it increases rents. There is a modest-sized program run by the US Department of Housing and Urban Development, called Family Self-Sufficiency (FSS), that has explicit social development goals (Cramer and Lubell 2005). The FSS Program was established by the National Affordable Housing Act in 1990 as a strategy for helping families receiving public assistance to become financially self-sustaining. It allows for

a participant to identify a set of goals associated with financial independence and to establish an escrow savings account. If household income increases, any additional rent that would be collected by the housing authority goes into the escrow account. Once the household reaches their personal goals, they receive access to the resources that have accrued in their escrow account. The FSS program currently has limited participation, but with a few reforms to make it more appealing to local housing authorities, it could reach more residents and result in a substantive improvement to existing housing programs (Williams Shanks 2012; Cramer 2004; Rohe and Kleit 1999; Sard 2001).

Programs under the WIA include at least one program, Job Corps, that could be ranked in the high category of social development. Job Corps provides academic support and vocational training to disadvantaged youth from age 16 to 24. The majority of participants leave home to reside in a Job Corps Center. The program provides a small biweekly stipend plus extensive support for educational preparation, career planning, and vocational training. An experimental evaluation found that the program had substantial effects on educational attainment, employment, earnings, and arrest rates compared to a control group (Schochet, Burghardt, and Glazerman 2001; Schochet, Burghardt, and McConnell 2008). It provides recipients a chance to build their capabilities at a crucial stage of life, that is, as they are leaving (or dropping out of) compulsory secondary education and attempting to establish a place in the formal labor market. In 2010, 57,000 students were served.

However, the bulk of WIA funding goes directly to state and local governments where a significant portion of the money funds one-stop shops that provide general assessments and job search assistance. Only a small number of participants receive intensive training and education services. In addition, programs vary from region to region and funding for specific programs can be unpredictable from year to year, especially for youth employment. Thus, although this workforce and training funding provides beneficial options for many, it is not nearly sufficient to address the diverse needs of the unemployed and underemployed. William Darity (2010) has proposed a radical, but potentially, game-changing solution—full employment through a National Investment Employment Corps, designed to be a permanent version of the Civilian Conservation Corps of the 1930s. The federal government would offer a jobs guarantee for those desiring work, with a minimum salary and benefits. By eliminating the threat of unemployment, most of those left out in the current array of safety net programs would have a way to build their capabilities and provide for their families.

The Pell Grant Program provides need-based grants to low-income students to promote access to postsecondary education. Grant amounts are dependent on the student's expected family contribution (EFC); the cost of attendance (as determined by the institution); the student's enrollment status (full time or part time); and whether the student attends for a full-academic year or less. The maximum award was $5,500 for the 2011–2012 academic year. The program might easily be characterized as high in social development because it provides financial assistance toward higher education that does not have to be repaid. Yet, because it is in-kind, it typically does not cover the full cost of college tuition and kicks in only when a student is already considering postsecondary education and applying for financial aid. Therefore, Pell grants may not be enough to assure that low-income students actually attain the very important milestone of obtaining a college degree.

One reason federal funding for college does not substantially impact college attainment is that many low-income students do not even apply for a Pell grant (or any financial aid) because of the substantial paperwork and administrative hurdles required, starting with filling out the complex FAFSA (Free Application for Federal Student Aid) form. In addition, there is uncertainty concerning the exact amount of aid until the final semester of high school, which may delay college decision making (Deming and Dynarski 2009). A second more substantive reason federal funding is not effective as it could be is that

although college enrollment has increased over time, college receipt has remained low, especially for the most disadvantaged students such as first generation college attendees and those from low-income households and households of color (College Board 2010; Deming and Dynarski 2009). Targeted scholarship programs that offer financial incentives combined with services (such as tutoring, peer-advising, and study groups) seem to do best in increasing college attendance and persistence, particularly among marginal students at high risk of dropping out (Deming and Dynarski 2009).

Table 2.3 summarizes three programs placed in the "high" category for social development. These include Head Start, CCT programs, and AFI. Head Start was created to provide comprehensive services to improve school readiness and overall life chances for low-income children age birth to age five. These are explicit social development goals. There is evidence of the long-term benefits of quality early child-care intervention (Barnett 1985; Schweinhart 2002). Nobel laureate James Heckman argues that investing in disadvantaged children "is a rare public policy initiative that promotes fairness and social justice and at the same time promotes productivity in the economy and in society at large (2006)." There is some debate as to whether Head Start programs in practice are exactly like the experimental designs that brought positive long-term adult outcomes (Schwienhart 2002). Another difficulty is that Head Start programs do not reach everyone who is eligible and vary in quality from center to center (Currie 2012). In addition, some of the academic benefits that are achieved in its preschool programs are lost when students transition to low-performing public school systems (Barnett and Hustedt 2005; Lee and Loeb 1995). However, the evidence to date demonstrates that early childhood learning programs are beneficial and can have a lasting developmental impact when done well.

To complement Head Start and other federal efforts to assist low-income students, a coordinated strategy for encouraging child capabilities over time that starts as early as infancy and continues through secondary school and beyond can provide a more sustainable and effective foundation for increasing economic mobility and breaking cycles of disadvantage. The Harlem Children's Zone has modeled this type of "Cradle to College" philosophy and Promise Neighborhood grants are trying to replicate its success, but the federal government has yet to implement a process to legislate such a coordinated system (Tough 2008).

Table 2.3 Programs with "high" social development emphasis

Program	*Participation*	*Federal funding*
Head start	1.1 million enrolled in 2012.[1]	$7.9 billion appropriated for FY-2012.[2]
Conditional cash transfers	About 13,500 served annually (until program's end in August 2010).[3]	Roughly $57 million appropriated annually.[4]
Assets for independence	Around 8,300 IDAs opened in 2009; near 60,000 IDAs opened through FY-2009.[5]	$9.4 million appropriated for FY-2012.[6]

Notes:

[1] Annie E. Casey Foundation. 2012. "Head Start enrollment by age group (Number)—2012." Kids Count Data Center.

[2] US Department of Health and Human Services. Administration for Children and Families. "FY 2012 Head Start Funding Increase."

[3] NYC Center for Economic Opportunity. 2013. "Opportunity NYC: Family Rewards, Work Awards, and Spark."

[4] NYC Center for Economic Opportunity. 2013. "Opportunity NYC: Family Rewards, Work Awards, and Spark."

[5] US Department of Health and Human Services. Administration for Children and Families. Office of Community Services. 2010. "Assets for Independence Program: Status at the Conclusion of the Tenth Year."

Although still experimental and small scale, CCT programs offer cash incentives when low-income households attain prestipulated social development goals. Thus, participating poor families receive preventative health care and dental cleanings alongside a sum of cash for doing so. Similarly, when children attend school and achieve academic milestones that prepare them for college, they also bring more cash into their households. Thus, the programs meet a short-term financial need while encouraging a long-term investment in human capital and development. These CCT programs are well established in Latin America and many developing countries (Fiszbein and Schady 2009), but are just getting started in the United States. From the evaluations that have been done (including New York City's privately funded Family Rewards program), researchers know that CCTs reduce current poverty and material hardship, increase savings, increase school attendance and grade advancement, increase preventive health-care visits and dental care, but have not been as effective in raising academic achievement—specifically standardized test scores (Aber and Rawlings 2011; Fiszbein and Schady 2009; Riccio et al. 2010). There is still much to be learned about CCTs and the theory is just being developed (Wolf, Aber, and Morris 2012), but they offer a range of innovations that could provide a model for federal policy interested in promoting social development. In particular, they provide a precedent for incentivizing not just work for work's sake, but promoting efforts proven to improve child outcomes and household economic stability.

AFI provides money through matched savings in IDAs for thousands of low-to-moderate-income households to purchase homes, fund businesses, and pursue higher education. Along the way, participating households also receive financial education and case management support for their asset-building aspirations. Setting and achieving long-term financial goals not only increases economic security, but can also change the way that others view the accountholders and the way the accountholders view themselves (Schreiner and Sherraden 2007a). This definitely helps increase capabilities. The combination of a generous match that offers real economic benefit and structured support as participants pursue their self-determined goals provides a pathway of opportunity for low-to-moderate-income families.

Results from the ADD show that among the 2,350 low-income participants in IDA accounts across fourteen sites, 52 percent saved $100 or more to accumulate a net IDA savings of $32.44 per month. The average participant accumulated a total of $1,609 in IDAs (principal and matched), which is the equivalent of $576 per eligible year. About two-thirds of participants made at least one unmatched withdrawal (i.e., a withdrawal for purposes other than those specified match eligible). Among the matched withdrawals, 21 percent were for home purchase, 11 percent were for postsecondary education, and 12 percent were for microenterprise (Schreiner and Sherraden 2007a). One of the fourteen ADD sites recruited participants using an experimental design. Rates of homeownership are statistically higher among members of the experimental group than among their control-group counterparts. However, evidence is inconclusive on whether participation in the experiment increases participants' overall net worth (Schreiner and Sherraden 2007b; Mills et al. 2008). Although consistent savings can be difficult on a limited income, 71 percent reported saving regularly after participation (compared to 24 percent that saved before). This same qualitative analysis offers that respondents reported increased feelings of security, self-confidence, and hope for the future. They also reported an increased ability to set and achieve goals as well as a greater sense of responsibility (Sherraden, Moore McBride, and Beverly 2010). A long-term follow-up of the ADD experimental site has also shown that men participating in the program are more likely to increase their educational attainment (Grinstein Weiss et al. 2013).

The programs ranked both "low" and "medium" in social development are a mix of New Deal and Great Society programs as well as recent tweaks. Since the federal government has been involved in antipoverty programs, there has been an impetus to

meet demonstrated need and anticipate ways to alleviate the pressures faced by families in poverty. Each era has introduced new policies upon which families now depend. From food assistance and medical insurance to Social Security, Head Start, and EITC, an array of programs are utilized by low-income families. Outside of programs for the elderly, all are means tested.

In contrast, the programs ranked as "high" in social development tend to be more recent policy additions or, in the case of CCTs, still being piloted at the local level. Head Start is not new, but particular "Cradle to College" strategies are gaining support that aim to build upon progress in early childhood. Although means tested, these "high" programs are only funded to reach a small proportion of the eligible population. The existing policy landscape provides benefits to many low-income participants, but if the goal is "high" social development—where economic resources are invested primarily to reduce dependency and achieve lasting social mobility—the support structures in place are not designed to achieve these outcomes.

In spite of their demonstrated success and potential for more, the three programs ranked high in social development reach the fewest number of people relative to the others. Participants number in the thousands or just at one million annually rather than the millions that other antipoverty programs serve. The high-category program with the most funding (Head Start at $7.9 billion) receives less than all the other low-category programs and most medium-category programs. Even as there is growing interest in more innovative programs that increase capabilities and enhance social development, this analysis indicates that most federal spending and emphasis continues to go to policies and programs that offer short-term, in-kind emergency assistance and social insurance for specific demographic groups deemed worthy of ongoing support.

Asset-building Policy and Its Influence

If policies that promote social development by building the capabilities of low-income individuals are an important contribution to antipoverty strategies, then there is a case to be made for shifting the emphasis of current policy approaches. With lessons learned from evaluation research and new frameworks such as behavioral economics, there is a knowledge base to build upon to support a more effective social welfare system that does more to increase social development, break intergenerational cycles of poverty, and reduce the need for short-term emergency assistance. This might entail increasing targeted investments in poor families and poor children up front and setting aside money for a generous jobs program or other innovative ways to support long-term economic security.

As this book highlights, the asset-building perspective got its first full expression with the publishing of *Assets and the Poor* by Michael Sherraden in 1991. In his initial thinking, Sherraden wanted an alternative to income-support policies that would help low-income families to save and invest in assets to increase their wealth and long-term economic security—ideally with individual savings accounts starting at birth. Institutional structures and tax incentives help higher-income individuals accomplish such long-term social development goals that ensure their economic stability, but little support has existed for those at the low end of the income continuum. Although much more needs to be done, this paucity of publicly funded, asset-building alternatives for the poor has begun to change since welfare reform was enacted in the mid-1990s. This section will describe a set of ideas, demonstrations, and proposals that have emerged from the asset building field and support high social development objectives. The ideas are gaining traction, but have not yet been fully implemented at the federal level.

The main policy idea that came from this asset-building perspective was that of IDAs. This idea received widespread national attention with the launch of the ADD

project in 1997, which tested 2,400 IDAs in thirteen sites. Then in 1998, the AFIA was enacted, funded with $125 million over five years. This provided federal funding to support IDA accounts at community-based sites that were then paired with a local source of match funding. Several other proposals were introduced or announced soon after, although none passed at the federal level. In 1999, the Savings for Working Families Act was introduced and proposed creating $12.5 billion in tax credits to financial institutions that set up and matched IDAs. This concept was endorsed by President Bush as a central piece of his "Ownership Society" agenda, and subsequently was included in his federal budget proposals throughout his Administration. Although it was never implemented, the bipartisan support for this type of policy and at this scale reflected a significant growth of support for this policy idea and the asset-building concept.

In a similar vein, the asset-building framework has influenced the retirement policy arena. In his 1999 State of the Union address, President Clinton proposed a large-scale system of Universal Savings Accounts (USAs). These retirement accounts would be accessible by low- and moderate-income (LMI) workers, subsidized with $500 billion over ten years. While not enacted, the USA proposal created political space for the argument that more families need to participate in the retirement saving process, which ultimately led to the creation of the Saver's Credit starting in 2002, which was a subsidy for targeted lower-income families that made deposits to retirement accounts, such as IRAs and 401(k)s. The Saver's Credit was not designed as a refundable tax credit, so it could only benefit families that had positive tax liabilities. This made it useful to only families with eligible incomes. Still, it signaled a recognition that savings and asset building were important policy goals for lower-income families, a major change from earlier periods of social policymaking.

After the early success with AFI, some were disappointed that there was not another large asset-building policy passed at the federal level. But as Ray Boshara notes, "Modest policy advances should not detract from the field's most significant accomplishment: . . . offering a truly new perspective on poverty and social policy debates, and bringing real attention . . . to the size of our nation's wealth gap, which dwarfs the income gap" (2012, 7).

Another offshoot of Sherraden's asset-building perspective is children's savings accounts (also known as child development accounts or CDAs). While IDAs were introduced into law as federal policy, the private nonprofit sector has conducted more experimentation and innovation with CDAs. For example, the Saving for Education Entrepreneurship and Downpayment (SEED) initiative was launched in 2003 as a ten-year demonstration to test, inform, and promote matched savings accounts for children and youth. Working with twelve community-based sites throughout the country and in Puerto Rico, more than 1,300 accounts were created in multiple settings and across a range of ages (Sherraden and Stevens 2010). The ASPIRE (America Saving for Personal Retirement and Education) Act was introduced to Congress in 2004 and again in 2006 as a way to promote savings and financial literacy by establishing accounts at birth for every child. The proposal leveraged the SEED demonstration in a similar manner that IDAs built upon the ADD experience, but at a much larger scale. Although the ASPIRE bill had bipartisan support, it did not pass either time.

At the state and local level, child savings account initiatives have been successfully implemented. A state-wide experiment to test CDAs is underway in Oklahoma (Zager et al. 2010). In Maine, children are offered 529 college savings plans at birth through private funding (called the Alfond challenge). The city of San Francisco has begun offering a college savings account starting with an initial $50 deposit to every child enrolled in its public school kindergarten (Stuhldreher and Phillips 2011). There are several other CDA programs being planned or implemented throughout the country. Examples

include the Mississippi College Savings Program (College Savings Mississippi 2009) and the KIPP (Knowledge Is Power Program).

There have been other developments that honor the spirit of the asset-building perspective, although they do not explicitly provide new funding streams for matched savings or dedicated accounts. In 2006, the IRS adopted a policy change that allows individuals to direct their refunds toward multiple accounts. The ability to split tax refunds creates an infrastructure that supports saving and asset-building activities. Following the $aveNYC demonstration to test short-term savings using tax refunds, the federal government funded several SaveUSA and BankOn pilots throughout the country. In addition, the recent creation of the CFPB by the Dodd–Frank Act of 2010 will help protect LMI families from fraud and shoddy financial products as well as support innovative financial products that can help them build assets over time. Most recently, the Department of Education has considered supporting a large-scale college savings account demonstration in the GEAR UP program, which is designed to promote college readiness.

As various asset-building policies and programs have been implemented on the ground in local communities, the number of people and organizations that understand and could support such efforts has multiplied. The expertise and infrastructure is in place to move beyond small community-based models. While federal policy victories have been modest, work in the asset building field continues to advance.

In their purpose and orientation, these efforts are not designed to replace the social safety net programs of last resort. There are strong policy cases to be made for having food assistance, medical care, housing, and emergency cash assistance programs that reach children and families during times of need and funding them at sufficient levels. Even if there is little emphasis on social development, such benefits can help prevent the type of dire circumstances that are known to have long-term negative consequences. However, if the federal government prioritizes social development and upward mobility, a case can be made for devoting greater resources to programs that emphasize human capital enhancement, asset building, and sustaining economic security. Given that these programs currently receive among the least amount of federal funding of all antipoverty programs, a modest increase in their funding levels would not represent a large increase of the federal budget. In addition, existing programs that already emphasize social development could be refocused to better ensure the long-term development of household capabilities.

For example, having public housing assistance that only reaches about 25 percent of eligible households with incentives for people to remain in poverty so as not to lose the benefit is not ideal for social development. In contrast, a program that reaches all that need housing assistance while also providing a viable path to homeownership or stable housing without ongoing public subsidy (perhaps by expanding FSS) would be more effective in terms of promoting long-term social development. Similarly, providing affordable options for postsecondary education or training (including paid internships and jobs of last resort) that are available to anyone that is unemployed or underemployed could improve long-term career options across the board as well as help strengthen the overall workforce and eventually the economy.

A universal asset-building policy that offers opportunities to all Americans, not just those with low incomes, would create a more equitable path to economic security. Such a policy would incentivize homeownership, entrepreneurship, and postsecondary education. If allowances are made for short-term savings along the way, such an approach would reduce the need for separate programs that only address specific issues and emergency circumstances. It could also be targeted to provide higher incentives or more supports for the most vulnerable populations. A life-long account that could be used for multiple asset building purposes is what was originally proposed by Michael Sherraden in 1991. The idea

has come a long way in just two decades, but there is still more to be accomplished for this asset-building perspective to have an enduring influence on the poor in large numbers.

Federal policy has evolved from almost no role in antipoverty efforts to longstanding programs that provide social insurance for the elderly and disabled, emergency assistance for food and medicine, and a patchwork of programs to incentivize work or education and provide temporary assistance. There are a few examples of programs that emphasize "high" levels of social development, but these are not well funded and only reach relatively small numbers of people. Existing programs in housing and workforce development as well as the EITC could be modestly amended to have a greater emphasis on social development. But rather than simply reacting during times of high unemployment or increasing poverty, making strategic choices to invest in the capabilities of all citizens, especially the most disadvantaged, could change the landscape of antipoverty policy in similar ways that occurred during the New Deal and Great Society eras. It may take great investment and intense interventions to increase social mobility and reduce wealth inequality. Yet, policy innovation that captures the imagination and productively engages low-income participants can also bring a positive jolt to the wider economy. The "assets perspective" has provided ideas and examples to inform the next policy innovation. Now the decision must be made to take this evolution toward greater social development to the next level.

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Chapter Three
The Finances of Typical Households After the Great Recession

Clinton Key

The recession of 2007–2009, the so-called Great Recession, brought human and economic suffering to millions of American households. In a few short years, perilous housing markets and anemic labor markets washed away decades of accumulated wealth. Households of all types experienced significant losses in assets between 2007 and 2009. Because the assets on a household's balance sheet are the sum of their economic past and the foundation upon which they build their future, the state of household balance sheets during and after the Great Recession is an important concern.

This chapter offers a description of household finances and economic well-being. It presents a snapshot of household balance sheets after the recession and an assessment of patterns and trends. Using the most recent and comprehensive data available from 2007 to 2010, this chapter describes the asset and debt levels of American households, with particular focus on demographic subgroups of the American population. This descriptive work is crucial to identify pervasive needs in the American population and to inform the design of programs to address those needs.

The balance sheets of American households are typified by their diversity. Households store their assets in a stunning array of formal and informal financial vehicles and ordinary objects—ranging from checking and savings accounts to ornamental weaponry, to currency notes. These households also owe myriad debts to diverse creditors. The balance sheets of American households are dominated by physical property, such as homes and cars. In contrast, relatively few households possess significant financial assets or high liquid asset balances. Given these low levels of readily available financial resources, many households meet conventional definitions of asset poverty, even when their incomes would classify them as part of the middle class.

The balance sheets of American households, in their heterogeneity, tell a story of a population with many asset-building needs. A clear sense of where those needs lie will help to assess the effectiveness of existing policies as well as to develop, target, and deliver programs to help families have more sustaining, sustainable financial lives.

Household Balance Sheets

Household balance sheets are a conceptual tool for understanding the economic positions of different households. In various literatures, the term carries distinct

connotations. A common use is to denote the flow of funds through a household, juxtaposing revenue and consumption in a manner similar to the way a firm's balance sheet might (e.g., income spending in a typical month). A related use refers to the same concept, aggregated across the entire population, comparing gross domestic product and gross consumption. This is how the Bureau of Economic Analysis estimates the national personal saving rate, which is defined as the residual between income and spending across the entire economy.

However, this chapter will apply a third approach to understanding the condition of the household balance sheet, which is an encapsulation of a household's asset ownership and debt obligations at a moment in time, like taking a snapshot with a camera. By examining the various balances of assets and debts for a sampling of households, a picture of typical households can be conveyed. This approach will facilitate comparisons of "typical" households of different subpopulations, and allow us to better understand the financial health and economic security of different household types during and after the Great Recession. These typical balance sheets are compared and contrasted with one another to gain a better understanding of the financial positions of different groups of American households.

A conceit of the concept is that it freezes the condition at a moment in time, even though balances, such as the equity held in a home or the amount of money in a checking account, constantly fluctuate. This simplifies the comparison across households as well as within and between groups. On the other hand, the snapshot of the balance sheet may be biased by factors, such as the timing of data collection relative to pay cycles. For instance, a checking or savings account that has a high balance after payday will almost certainly have a much lower balance as the next payday nears. However, the prevailing assumption is that, over the breadth of the sample, such variations will even out.

In addition, it should be noted that there are myriad pathways and decisions that produce similar household balance sheets. For instance, a low level of liquid assets could result from a household that never saved or from a household that saved regularly but had just experienced a shock to income or consumption. A large pool of financial assets such as stocks could result from a lifetime of careful saving and investing, an inheritance from a rich uncle, or the proceeds from a worker's compensation settlement. As a result, the reality behind the aggregated numbers presented here is different for individual households. Independent of the pathway that brings a household to a particular balance sheet, the contents of the balance sheet have important implications for the future of the household, the risks it faces, and the opportunity it is able to pursue.

The data presented in this chapter are presented without judgment or censure. Regardless of their origin, the current state of household balance sheets is critical to inform asset-building policy and countless other social and fiscal decisions that federal, state, and local governments might make.

For the purposes of this work, the household balance sheet is a snapshot of the assets and liabilities held by a household, indicating the household's financial position. Table 3.1 details the components of the household balance sheet included in these analyses.

Most of the assets and liabilities mentioned in table 3.1 are well known to those in the field and the general public. In the data used, the "miscellaneous" category is a broad catchall that captures anything with what the respondents perceive as cash value that is not captured by other items in the measure. For instance, under other assets, respondents often report not only currency but also collectables, such as stamps or coins, household items that hold value, such as appliances, electronics, and more

Table 3.1 Components of net worth on the household balance sheet

Assets		*Debts*	
Liquid	Checking Savings	Credit	Credit cards Other consumer debt
Physical	Home Other property Business Cars Other vehicles	Housing	Mortgage(s)
Financial	Mutual funds CDs Savings bonds Other bonds Stocks Brokerage accts. Annuities	Other physical	Debt to business Car(s) Other vehicles
Retirement	IRA 401(k) Pension	Education	Student debt
Misc.	Life insurance Personal debt owed Business debt owed Other (Cash, valuables)	Misc.	Other lines of credit Margin loans Other
Net worth = total assets – total debts			

esoteric items. Crucially, in both assets and debts, the data collection goes to extreme lengths to include all items perceived by the respondent to store value so they may be included in the balance sheet, just like more conventional vehicles used to hold money. It is essential to have a holistic measure because in the balance sheet all assets and debts are substitutable. As indicated in table 3.1, all of the reported assets and liabilities are summed to measure total assets and total debts. Net worth is the simple difference between total assets and total debts.

In these analyses of household balance sheets, special attention is given to a household's liquidity, or the amount of money they have available immediately with low or no transaction costs. Liquidity is given extra attention because it is the grease that helps households squeeze through tight money situations. Liquid assets are the stock of assets that households can access quickly to meet emergent needs in the event of shocks to income (a reduction of work hours or mandatory furlough, e.g.) or consumption (such as an emergency medical expenses or home repair). These liquid funds are the basis of the economic security for households in the short run (Lopez-Fernandini 2010) and the buffer that allows a household to meet unexpected expenses without incurring debt, particularly short-term and high-cost debt like that offered by a payday lender or a credit card (McKernan, Ratcliffe, and Vinopal 2009).

In addition to liquid assets, several other items in the household balance sheet are given special attention. Credit card debt is highlighted because it is by far the most common form of short-term, high-cost debt held by American households and is regularly used as a proxy for financial distress (Garcia 2007). Recently, media reports and public inquiries have devoted special attention to an increasing rate and amount of student loan

debt, particularly among the young (Baum and Schwartz 2005). Although not prevalent in the population at large, student debt is highlighted to assess its role in shaping balance sheets now and assessing how that may change in the future. Finally, dedicated retirement savings, savings held in tax-privileged accounts such as IRAs, and 401(k)s are considered. Numerous public and nongovernmental programs, in addition to incentives in and proposed for the tax code, seek to stimulate retirement savings and make households less reliant on public programs to sustain themselves after their working years are over (Duflo et al. 2006).

Data from the Federal Reserve's Survey of Consumer Finances

Because it is difficult to collect accurate data on the components of household balance sheets, the data on the wealth, assets, and debts of households are much more limited than other economic measures such as income. Large-sample, frequently fielded surveys that form the backbone of statistical evidence on the American people like the Current Population Survey and the American Community Survey do not collect data on balance sheets. While several prominent longitudinal panel surveys, the Panel Study of Income Dynamics (PSID) and the Survey of Income and Program Participation (SIPP) collect some balance sheet data on their panels, neither is an ideal data set to describe the American population (Ratcliffe et al. 2008). In particular, they struggle to capture the asset holdings of particular subgroups in the population. The PSID, initiated in 1968, requires substantial manipulation to draw conclusions for the population as a whole. The SIPP's sample size and large proportion of item-missing balance sheet data make it challenging to use for subsamples of households.

This chapter explores household balance sheets using data and supporting documentation from the Survey of Consumer Finances (SCF). The SCF is fielded triennially by the Federal Reserve Board of Governors and is generally thought to be the best available data for studying the status of household balance sheets. The material presented includes data collected in 2010, after the formal end of the recession (Bricker et al. 2012). In 2010 and most survey years, the SCF is cross-sectional, which means it draws a new panel of American households from across the income distribution. To facilitate studies looking at the impact of the Great Recession on households, the 2007 SCF panel participants were reinterviewed in 2009 (Bricker et al. 2011). Not only does the reinterview give us information on the state of household balance sheets in 2009, it lets us see the change in a given household's balance sheet from 2007 to 2009. The newest data from 2010 are derived from a different sample, but still provide a valuable means of making comparisons and identifying trends.

There are several data concerns in SCF that need to be addressed in the analytic approach. First, the SCF oversamples high- and very high-income households to be able to describe their wealth position. Thus, analyses of the data need to include adjustments so that outcomes accurately capture household balance sheets. Analyses in this chapter use the population weights developed for the SCF by Bricker et al. (2012). Second, in all studies of household balance sheets, there is a larger proportion of item-missing data than encountered in other survey topics. Respondents may not know if they hold or feel uncomfortable sharing the value of a particular type of asset or debt. To address this, the SCF is released with five "multiply imputed data files" (Kennickell 2011). Each of the five "implicates" has the same cases and variables, but may contain a different estimate generated for an item-missing value. This means that for questions where a person did not answer, each version of the data set uses a different plausible estimate of what that

value might be. The analyses presented below are performed on each data set and then merged together to produce accurate estimates that account for this procedure.

The "Typical" US Household

The first striking aspect of household balance sheets is that there is no typical household. Most households do not own or owe most of the items on the balance sheet. The presence and level of each component varies wildly across all households and also within groups. The idiosyncratic pattern of balance sheets complicates the description of balance sheets generally, especially if one is more interested in distinct components rather than aggregates, such as net worth, total assets, or total debts.

Because most households do not own a component of the balance sheet (such as student loan debt), the median value is zero. For households that do have the component, it is an important part of the balance sheet and should be captured. Likewise, some households have unusually high balances on one or several components. Including these cases skews the estimate for the population as a whole at the mean, making it difficult to make claims about balance sheets that accurately reflect the experiences of most households.

To talk about the typical household in general and typical households in subgroups, this chapter takes the mean asset holding for each component of the balance sheet among households that are between the twenty-fifth and seventy-fifth percentiles of the distribution on that component and uses that central point to give us useful information on what a typical or representative household might look like. For example, to estimate the typical household's educational debt, we first examine the distribution of educational debt in all households. The 25 percent of households with the least education debt and the 25 percent of households with the most education debt are excluded. Among those households that remain, those in the center of the distribution, we take the average educational debt and call it the education debt of the typical households.

The same approach is used to calculate typical values for total assets, total debts, and net worth (table 3.2). Rather than just summing up the individual components, a similar calculation is used to estimate these aggregate figures to minimize the impact of those with low and high assets and debt. This provides a better picture of those in the middle, helps to look at large numbers of households, and facilitates a comparison of key aspects of their balance sheet. It does, however, mean that the individual components shown in the tables will not sum to the aggregates in the same table.

In 2010, the typical household had a net worth of $164,647. This is the mean net worth for households between the twenty-fifth and seventy-fifth percentile of net

Table 3.2 The typical household balance sheet, 2010

Assets *($)*		*Debts* *($)*	
Liquid assets	3,142	Credit	440
Physical	121,427	Housing	16,306
Financial	42	Other physical	891
Retirement	2,807	Education	0
Misc.	25,655	Misc	0
Total	241,067		43,576
Net worth		$164,647	

worth. These households, whose total annual income was about $49,000, primarily hold their assets in physical items. The typical household had a lower net worth than a typical household in 2007, but higher than the typical household in 2009. The typical household's physical property accounts for about half of the value of their assets. About 58 percent have dedicated retirement savings, but the typical retirement account balance among these households near the middle of the income distribution is just over one month's gross income (see table A3.1 in appendix 3.1 for sample characteristics). Almost two-thirds of these households report being able to access $3,000 for an emergency expense, as is reflected by the estimate of $3,142 in liquid assets at the mean among households between the twenty-fifth and seventy-fifth percentiles of on liquid assets.

Since 2007, these typical households have experienced a diminution of asset value, coupled with a small decrease in debt, producing a decrease in wealth (figure 3.1). The typical household's 2010 balance sheet reflects the impact of the Great Recession. In particular, the typical household has lower levels of housing assets, reflecting both housing price declines and lower rates of ownership in the sample.

The typical household holds more liquid assets than in 2007, consistent with the liquid asset growth observed between 2007 and 2009. This may reflect unease and lack of confidence in the economy. At the same time, the typical households have fewer dedicated resources for retirement, pointing at the potential for the asset loss of the recession to reverberate down the years. The differences in retirement savings could also represent sample differences between the 2007 panel and the 2010 sample. On the other hand, some evidence suggests that early withdrawals from retirement vehicles increased in recent years. Overall, debt levels are slightly lower in the typical household in 2010 than in 2007, suggesting retrenchment in the typical household.

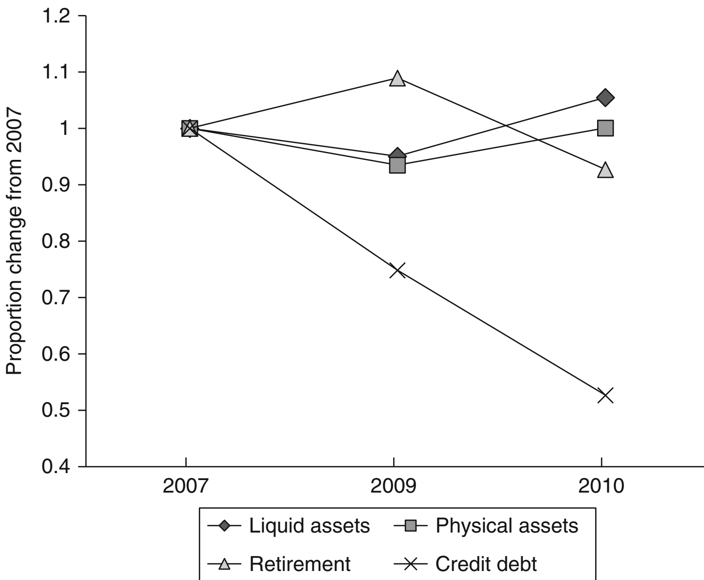

Figure 3.1 Changes in the balance sheets of typical households.

The typical 2010 balance sheet reflects the economic realities of the period from 2007 to 2009 and the typical household's perceptions of their position in the current economy.

Comparison of Household Balance Sheets across Income Subgroups

The typical lower-income household differs from the typical household in important ways, beyond the defining difference in income. Households whose income is below the poverty line and households whose income is between the poverty line and the median are less likely to be banked, own a home, have health insurance, or be able to find \$3,000 for an emergency expense than the typical household. They are also more likely to have experienced unemployment among wage earners in the household in the past year and to report monthly spending in excess of monthly income (data shown in the sample characteristics table in appendix 3.1). By the same token, typical households among those with income between the fiftieth and eightieth percentiles of the income distribution have balance sheets that are more robust than the typical household.

The balance sheets of lower income households also differ substantially from the balance sheets of the typical household. Notably, households below the poverty line held about \$520 in liquid assets, about one-half of their typical gross monthly income. The disparity in liquid asset holding between income groups is substantial, as seen here (figure 3.2).

The value of physical assets is substantially lower, reflecting a lower rate of homeownership. Interestingly, the typical household with below-poverty-level income holds relatively few debts. Although the typical household has debts equal to income generated over the course of an entire year, below-poverty households has debts at levels between one-month's and two-month's income. This could result from a lack of access

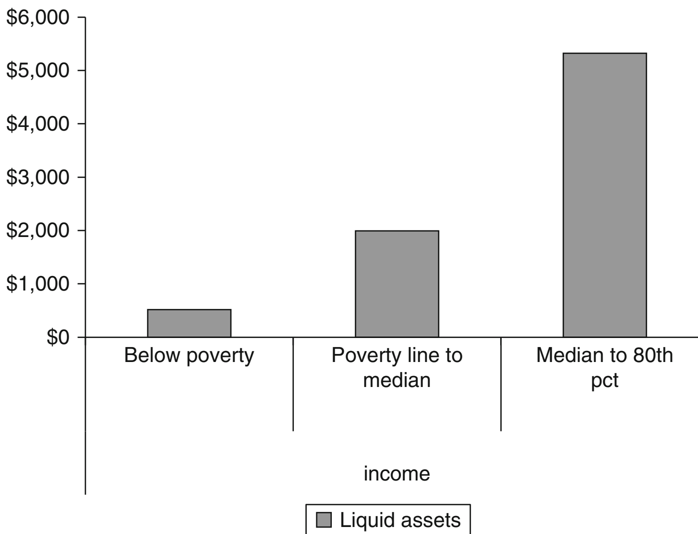

Figure 3.2 Liquid asset holdings by income category.

Table 3.3 2010 Balance sheets by household poverty status

Assets *($)*		*Debts* *($)*	
Below the poverty line			
Liquid assets	520	Credit	34
Physical	13,387	Housing	0
Financial	0	Other physical	0
Retirement	0	Education	0
Misc.	1,265	Misc.	0
Total	38,973		1,862
Net worth		$26,108	
Poverty line to median income			
Liquid assets	1,995	Credit	219
Physical	81,267	Housing	3,006
Financial	1	Other physical	121
Retirement	671	Education	0
Misc.	10,306	Misc.	0
Total	156,231		14,076
Net worth		$104,827	
Median income to the eightieth percentile			
Liquid assets	5,325	Credit	804
Physical	180,915	Housing	33,363
Financial	317	Other physical	2,611
Retirement	8,319	Education	0
Misc.	83,411	Misc.	0
Total	372,678		79,463
Net worth		$259,949	

to credit markets, particularly loans for housing and other physical property that are the primary driver of debt levels in higher-income populations. It should be noted that below-poverty-line-income households typically have no financial or retirement assets (table 3.3). This is interpreted as fewer than 25 percent of these households holding these assets at all.

Households with an income between the poverty line and the median have a typical net worth about four times that of households below that poverty line. The poverty line to median income group holds much higher values in physical assets. While their liquid asset balances are also higher than below-poverty-line households, about 56 percent of households between the poverty line and the median think they could locate enough cash or credit to pay for a $3,000 expense.

The typical household between the fiftieth and eightieth percentiles of the income distribution has a healthy balance sheet, reflecting the relationship between income

Table 3.4 Change in assets and net worth by income group: 2007–2010

	Net worth (percent)	*Physical assets (percent)*	*Financial assets (percent)*
Below poverty	−23	−46	0
Poverty to median income	−8	2	−97
Median income to eightieth percentile	−16	−14	−70

and economic well-being. Of particular note are the substantially higher holdings in liquid assets, which allow a household to respond to emergencies and seize opportunities (table 3.4). In addition, it should be noted that this typical household carries a larger debt burden than the lower-income groups. While households in this group are more likely to hold retirement savings (about 70 percent have dedicated retirement savings), the typical level of those savings will still may not be sufficient for the household's needs at retirement.

The typical household in all income groups suffered a significant decline in net worth between 2007 and 2010. The disproportionately large decrease in physical asset holdings among below-poverty-line households is particularly noteworthy. It is the key driver of this subgroup's larger decline in assets and wealth than either the typical household with an income between the poverty line and the median or the typical household between the median and eightieth income percentile. Without substantial income or liquid assets, physical assets were additionally exposed in lower income households.

At the same time, higher income households in 2007 had much larger holdings of financial assets than higher income households in 2010 (the typical below-poverty household did not own financial assets at either time point). This reflects both precipitous drops in financial markets, households moving resources to safer harbors, and households selling assets to meet short-run consumption needs. This suggests that though no households were uniquely exposed to the economic consequences of the Great Recession, the drivers of wealth loss between 2007 and 2010 differed among groups.

Marital Status and Gender

Table 3.5 presents the balance sheet of households where the head of the household is an unmarried, noncohabiting woman and where the head of the household is married.

These tables show balance sheet differences between the two types of households, both in the magnitude and type of assets held and debts owed. In the snapshot presented in table 3.5, it is important to remember that in these snapshots, the direction of causality between subgroup membership and balance sheet holdings is ambiguous. For instance, the added earning potential (and inheritance pool) of a spouse could be driving the higher wealth levels enjoyed by married households. On the other hand, it is possible that the economic position of a person, in particular, one lacking assets or owing substantial debt, makes it less likely for a person to be in a stable, married relationship. A causal direction either way is possible and, indeed, the causes from both sides can exist simultaneously.

Table 3.5 2010 Balance sheets of households by marital status

Assets *($)*		*Debts* *($)*	
Single, female-headed			
Liquid assets	1,873	Credit	143
Physical	64,735	Housing	1,991
Financial	1	Other physical	6
Retirement	327	Education	0
Misc.	8,984	Misc.	0
Total	126,111		11,588
Net worth		$82,266	
Married			
Liquid assets	5,772	Credit	562
Physical	205,244	Housing	27,915
Financial	577	Other physical	2,306
Retirement	11,880	Education	0
Misc.	62,609	Misc.	0
Total	438,062		73,218
Net worth		$318,104	

Table 3.6 Financial asset holdings by household type—single or married

	2007 *($)*	*2010* *($)*
Single female headed	140	1
Married	1,965	577

In the SCF data, being married is associated not only with larger stocks of assets, but also with more debt than an unmarried-headed household reports. The typical married household is more likely to own their residence and own substantially more assets of all types. There is a particularly notable difference between the two subgroups on other assets. The typical married households also have exponentially more retirement savings than the typical household headed by an unmarried woman living without a partner in the household.

Also of note, in the period from 2007 to 2010, both the single-female-headed and the married households lost a huge proportion of their financial assets, with those of the typical single-woman-headed household reduced to under $200, reflecting a very low rate of financial asset holding. The typical household in both subgroups lost about a third of the original value of their physical assets through a combination of asset loss and declining value (table 3.6).

Education Level

Although student debt is a cause for concern in the future, in 2010 a minority of households owe student debt. For those who hold it, though, debt is a crucial component of the balance sheet. Interestingly, those who graduated college hold student debt at the same rate as those who started college but did not finish.

The most interesting contrast in student debt is between younger and older people. Three times as many households under forty hold student debt than among households over forty. This reflects changing costs of, and financing options for, college, and could suggest a balance sheet challenge down the road (table 3.7).

As one might expect, household balance sheets in general differ markedly by level of education. The typical household headed by a college graduate holds assets worth almost five times the value of assets held by the typical household headed by a person who achieved a high school degree or less. A household with some college but no degree has a balance sheet that is more consistent with that of a high school graduate than a college graduate. The typical college-educated household has liquid assets with more than ten times the value of the typical high-school-educated household, though the college-educated household also has higher monthly expenditures. The balance of liquid assets grew from 2007 to 2010 in the typical college educated household, while it fell in the typical high school educated household. While the typical college-educated household holds more debt generally, it should be noted that a minority of college-educated households owe student debt, resulting in the typical student debt value of four dollars.

Nonetheless, student debt in college-educated households likely contributes to the larger volume of total debt owed in these households compared to high school-educated households. It should also be noted that households with some college are more likely to owe education debt and owe more than college graduate households (table 3.8).

Although the high-school-educated households and some college households have a much thinner cushion of precautionary savings than college-educated households, the amount of credit card debt of a typical household in each subgroup carries does not differ proportionally. Credit debt rose faster from 2007 to 2009 in the groups with lower educational attainment (table 3.9).

Table 3.7 Student debt on the balance sheet, 2010

		Among those who owe		
	Percent who owe	*25th percentile ($)*	*Median ($)*	*75th percentile ($)*
Less than high school	7	4,000	7,900	12,000
High school grad	13	3,000	8,000	16,000
Some college	26	6,000	11,000	24,000
College grad	26	7,900	16,000	34,000
Grad school	24	13,800	30,000	77,300
Overall	19	6,000	13,000	30,000
Under 40 years old	37	5,800	13,000	30,000
Over 40 years old	12	6,000	13,000	29,000

Table 3.8 The 2010 balance sheet by education level

Assets *($)*		*Debts* *($)*	
High-school degree or less			
Liquid assets	1,511	Credit	198
Physical	82,172	Housing	3,875
Financial	0	Other physical	291
Retirement	305	Education	0
Misc.	9,709	Misc.	0
Total	147,497		12,418
Net worth		$101,433	
Some college			
Liquid assets	3,227	Credit	595
Physical	118,109	Housing	15,436
Financial	46	Other physical	1,189
Retirement	3,892	Education	16
Misc.	34,386	Misc.	0
Total	260,078		45,468
Net worth		$174,152	
College degree or more			
Liquid assets	12,267	Credit	307
Physical	283,105	Housing	40,835
Financial	5,330	Other physical	2,252
Retirement	39,593	Education	4
Misc.	132,288	Misc.	0
Total	671,325		109,023
Net worth		$500,210	

Table 3.9 Value of credit debt by educational attainment, 2007–2010

	2007 *($)*	*2010* *($)*
High school or less	303	198
Some college	876	595
College or more	654	307

Race and Ethnicity

Racial gaps in the distribution of wealth and barriers to wealth accumulation that differ by race have been documented in other places, even though they require further examination (Shapiro, Meschede, and Osoro, chapter 5, this volume). The SCF snapshot data on household balance sheets confirm that long-observed wealth inequalities remain. There is also a suggestion in the 2010 SCF data that the racial wealth gap may be exacerbated by changes in wealth observed in the 2007–2009 data. The balance sheet data affirm that the effects of the Great Recession hit historically disadvantaged households particularly hard. These households lost a larger proportion of wealth during the recession than did white households.

Racial and ethnic differences are also seen in the experience of change from 2007 to 2009. The typical households in all racial and ethnic groups were worse off on their balance sheets in 2009, but nonwhite households lost more ground during the two-year period. From 2007 to 2009, the typical African American household lost about 13 percent of their net worth and the typical Latino family lost over 10 percent of their net worth, while the typical white family lost about 6 percent. These data show that the impact of the recession on balance sheets was not equally distributed and suggest ongoing racialization in labor and housing markets.

Figure 3.3 shows the proportion of each racial group that lost wealth and that lost a large percentage of wealth between 2007 and 2009. Over half of all respondents and similar proportions of each racial group reported lower values of wealth in 2009 than in 2007.

At the same time, though, black and Latino households were more likely to experience large loses in net worth. Over 30 percent of black and Latino households reported a 2009 net worth that was less than half what they reported in 2007. White households did not experience large proportional losses in net worth at the same rate (table 3.10).

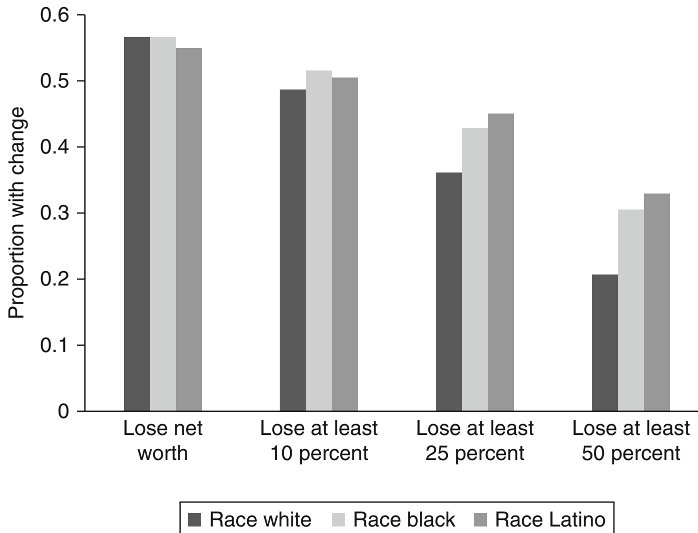

Figure 3.3 Change in net worth between 2007 and 2009 by race.

Table 3.10 The 2010 balance sheet by race

Assets ($)		*Debts ($)*	
White			
Liquid assets	5797	Credit	369
Physical	176,171	Housing	19,199
Financial	821	Other physical	1282
Retirement	8,815	Education	0
Misc.	38,832	Misc.	0
Total	361,082		53,411
Net worth		$266,076	
African American			
Liquid assets	1041	Credit	176
Physical	47,808	Housing	1,979
Financial	0	Other physical	128
Retirement	141	Education	0
Misc.	21,653	Misc.	0
Total	115,659		12,065
Net worth		$76,253	
Latino/a			
Liquid assets	989	Credit	263
Physical	49,786	Housing	5,020
Financial	0	Other physical	176
Retirement	15	Education	0
Misc.	4,702	Misc.	0
Total	92,691		13,029
Net worth		$48,941	

In 2010, the typical white household holds substantially more assets in every asset category than either the typical African American household or the typical Latino household. While the white household holds about three times as much in assets, it owes four times as much in debt. Still, the typical minority households are substantially more leveraged. This, combined with the patterns of holding physical assets and physical and housing debt, could reflect historic patterns of inequality. Minority households are thought to have less access to family-owned assets either through living transfer or inheritance and may instead use debt to finance purchases (Oliver and Shapiro 2006). This is also seen in the higher rate of holding student loan debt among African American households.

Age

In economic theory, household balance sheets and their composition are expected to vary substantially over the life course (Ando and Modigliani 1963). Saving can be understood

as the expression of a preference for consumption in the future over consumption now. Debt is a mechanism to increase consumption now while reducing it in the future, smoothing across periods of different earning. As expected, household balance sheets differ substantially by the age of the household head. Younger households hold fewer assets and have proportionally more debt than do older households. In table 3.11, the typical households with heads below and above age 40 are compared.

The difference between older and younger households is largest in the value of physical assets and retirement savings. While the threshold value we use to define younger households is high, the differences that emerge highlight that the accumulation of certain asset classes occurs over time. The difference in physical assets, in particular, demonstrates how the accumulation of savings and earnings across the life course can not only yield high value holdings, but may also hide a period effect. The current housing market may not facilitate the accumulation of physical assets as readily as in years past.

The debt holdings of younger households are also notable. First, the overall pattern of debt holding suggests consumption smoothing, as suggested by economic theory. Households acquire debt in the expectation that their earning power will rise over time. The typical household with a head under forty also owes student loan debt, unlike the typical older household. Those under forty were more likely to attend postsecondary education, were more likely to finance it with debt, and have had less time to retire debt they did accumulate. Still, this may suggest a changing pattern of debt holding that will persist in younger cohorts and color the balance sheets of these households going forward.

Several aspects of the household balance sheet of typical younger households should give pause. First, in a period of stagnant wages and uncertain labor markets, the life-cycle consumption model's assumption that increased debt taken on early in life will be

Table 3.11 The 2010 balance sheet by age

Assets *($)*		*Debts* *($)*	
Under 40			
Liquid assets	2,003	Credit	322
Physical	55,238	Housing	13,106
Financial	0	Other physical	860
Retirement	919	Education	593
Misc.	22,290	Misc.	0
Total	137,276		41,630
Net worth		$69,043	
Over 40			
Liquid assets	5,335	Credit	323
Physical	182,628	Housing	14,685
Financial	906	Other physical	983
Retirement	8,812	Education	0
Misc.	33,449	Misc.	0
Total	356,315		35,415
Net worth		$271,270	

Table 3.12 Net worth by age, 2007–2010

	2007 ($)	*2010 ($)*
Under 40	74,296	69,043
Over 40	307,878	271,270

offset by future earnings may not uphold (Sandoval, Rank, and Hirschl 2009). This is particularly the case for those entering the labor market at the height of the recession that may suffer lower lifetime earnings from their early difficulty.

At the same time, the typical household whose head was under age 40 was the only household presented here whose net worth increased between 2007 and 2009. Younger households increased holdings in every asset category, compared to older households that lost value in every category except for liquid assets. This increase could not only demonstrate an improvement in material condition in spite of the economic turmoil, but could also result from lower investment in volatile housing and financial markets as of 2007 among younger households and their prime-years earning capacity. It is noteworthy that younger households in 2007 and younger households in 2009 had very similar net worth. This suggests that the change observed among younger households over the 2007–2009 panel was a life-cycle process, rather than a change in the economic fortunes of younger workers generally (table 3.12).

Homeownership

A common theme running through the balance sheets of the typical households depicted in the data presented here is the outsized place of physical assets, particularly homes, in the balance sheets of households in 2010 and in the change households experience from 2007 to 2009. An owned home is unique in the balance sheet of American households. First, it is the only asset that a typical household can purchase with substantial leverage. Second, mortgage payments act as forced saving, reducing consumption but building equity. Finally, an owned home may confer a stability that facilitates the development of other assets. At the same time, the magnitude of the initial expense of homeownership may put households into a risky situation with regard to liquid assets, may impose high transaction and ongoing ownership costs that inhibit the development of other assets, and may crowd out other assets, leaving households uniquely exposed to what has recently been shown to be a volatile market in many regions and has fueled marked reductions in wealth between 2007 and 2009.

The presentation of the typical balance sheets of owners and renters highlights the dominance of the balance sheet, as both an asset and a source of debt for homeowners. The typical home-owning household holds almost half of its assets in physical assets, compared to the typical renting household whose physical assets are about one-fifth of their total (primarily in vehicles). Housing debt also accounts for about half of the debt load on the balance sheet of typical home-owning household (table 3.13).

The preponderance of physical assets on these balance sheets may have exacerbated the impact of the recession on the typical household. It is possible that more diversified asset holding would better protect households in the face of a localized downturn. A larger proportion of homeowners than renters lost wealth between 2007 and 2009. On the other hand, much larger proportions of 2007 renters lost at least a quarter or at least

Table 3.13 The 2010 balance sheet by housing tenure

Assets *($)*		*Debts* *($)*	
Owners			
Liquid assets	7401	Credit	540
Physical	244,258	Housing	46,066
Financial	1,574	Other physical	2155
Retirement	14,918	Education	0
Misc.	85,833	Misc.	0
Total	483,702		97,935
Net worth		$357,793	
Renters			
Liquid assets	975	Credit	121
Physical	8,371	Housing	0
Financial	0	Other physical	17
Retirement	17	Education	0
Misc.	7,185	Misc.	0
Total	37,250		2,850
Net worth		$27,411	

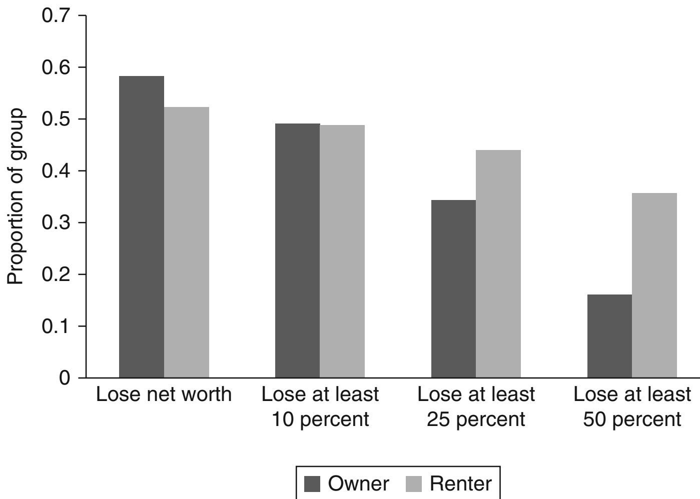

Figure 3.4 Change in net worth between 2007 and 2009 by homeownership status.

half of their net worth as was observed among 2007 home owners. This is driven in part from the lower 2007 net worth of renters compared to homeowners (figure 3.4).

Still, the renting households were not particularly diversified and also suffered substantial physical asset losses from 2007 to 2009. The downturn in the economy, not only in the housing market but also in the labor market, ensured that the impact was felt by renters and owners alike. In fact, between 2007 and 2009, renters lost a much larger proportion of their 2007 net worth than did owners.

Asset Sufficiency

Asset sufficiency is a concept designed to capture the extent to which a family has access to a minimum stock of accessible resources. It seeks to estimate how useful the household's balance sheet would be in the event of a shock to income or consumption (Shapiro, Oliver, and Meschede 2009). Alternately, it is a measure of exposure and a reflection of the one role that assets have in the balance sheet and households' financial lives, that of securing a household against a downturn (Hacker et al. 2010).

Asset poverty (and its inverse, asset sufficiency) carries many definitions. In general, it focuses on liquid or quasi-liquid assets held by a household that can be mobilized quickly (usually by being converted to cash) to cover emergency expenses. In this analysis, we examine liquid assets for their level and for sufficiency to meet household needs. The level of assets is simply the balance held in liquid vehicles like checking or savings accounts. This measurement approach may undercount the assets a household could quickly mobilize with minimal transaction costs. Many of the assets lumped together as miscellaneous assets, including cash and currency, obviously fit this bill, while others would require long lead times, transaction costs, and discounting to be used to cover shortfalls (such as appliances or collectables).

Many households also rely, appropriately, on market and nonmarket sources of credit when faced with shortfalls. Our measure of asset poverty does not include credit access. Using debt to smooth consumption is an important coping strategy, but it has long-term costs for the balance sheet and for future consumption. Here, we focus on the sufficiency of already held liquid assets. It should be noted that the one-month asset sufficiency measure presented in table 3.14 aligns closely in proportion with a perceptual measure in the SCF of whether a household could identify money to pay for $3,000 in emergency expenses.

Many studies adopt the consumption at the poverty line in their construction of a measure of asset sufficiency. Most consumption of most households, however, is fixed, particularly in the short run. Most people are, for instance, locked into mortgages or leases that make it prohibitively expensive and difficult to reduce housing costs on short notice. The portion of a household's spending that could be cut immediately is thought to be quite low. Moreover, for households already at or below the poverty line, it makes little sense to expect their consumption to increase rather than decrease in response to a shock. Instead, we adopt 75 percent of base monthly total household income as the basis of our sufficiency measure. Other cut-offs are possible and the budget flexibility of different types of households requires more empirical investigation.

The data presented here reveal that most households meet conventional definitions of asset poverty. The stocks of liquid assets held by households in general and households in specific subgroups provide a thin cushion against income and consumption shocks. It should be noted that the types of shocks under consideration here are anomalous but not at all atypical in the course of a household's life. Between 15 and 20 percent of households in the study experienced an unemployment spell in the year prior to the 2010

survey and about 20 percent report spending more than they earn in a typical month. At the income level of the typical household, about $4,000 per month before taxes, a single trip to the hospital or a major car or home repair could represent a 75 percent loss of income to be used for other purposes in that month.

About half of all households could not replace 75 percent of one month's income with their stock of liquid assets. Faced with such a shock, most households would likely resort to debt, particularly high-interest, unsecured short-term debt. Over 70 percent of all households could not replace the 75 percent of three months of income. Asset poverty and its attendant insecurity affect households all across the economic ladder. The incidence of asset insufficiency among households with income below the poverty line is higher than among those in the middle 50 percent of the income distribution, but not meaningfully so. Almost half of households between the fiftieth and eightieth percentile of income and over a third of households whose head is a college graduation lack the liquid assets to replace 75 percent of one month's income. A generation of low saving rates has left most households exposed to unexpected expenses or loss of income. The income shocks and asset loss associated with the Great Recession further diminished the economic preparedness of American households and left many, if not most households unprepared for unexpected expenses or loss of income.

Conclusion

The household balance sheets of American households are highly idiosyncratic and heterogeneous. Focusing on typical households not only allows us to identify key themes, but also illuminates the vast differences in holdings within subgroups. The difference between the typical holdings in the categories of assets and the typical value for total assets in the tables in the chapter suggests that across all subgroups, households tend to concentrate their asset and debt holdings into relatively few boxes. The most prominent example of the concentrated asset holdings is the domination of balance sheets, among the poor and the better off, by physical assets.

Across all subgroups, household balance sheets reveal several shortcomings that are ripe for the next generation of asset-building policies and interventions. First, in spite of substantial efforts to increase retirement savings through nongovernmental programs and governmental tax incentives, retirement savings remain a small component of the balance sheet of the typical household. Even in groups like college graduates that are relatively advantaged in their balance sheets and in their labor market position, the typical stock of retirement saving may not be enough to make a substantial contribution to supporting a given level of consumption after retirement. Of greater concern are the 40 percent of households that have no dedicated retirement savings at all. These households face a stern challenge in paying for retirement and may rely on public programs exclusively.

The balance sheets of many typical households in 2010 still bear the scars of the Great Recession. Viewed in the context of the widespread loss of wealth between 2007 and 2009, the balance sheets reveal a population that, with the Great Recession over for a year, has yet to recover in a meaningful way. As the economy improves, broad based and targeted programs to nurture balance sheets back to health is necessary. These efforts will need to focus not only on recouping massive losses on physical assets but also on addressing diminished retirement savings, increased debt loads, and other challenges on both sides of the balance sheet.

In particular, the asset poverty of households across the socioeconomic spectrum is notable. Typical household balance sheets reveal that households of all types hold low levels of liquid assets that could be used as precautionary savings in moments of

Table 3.14 A measure of 2010 sufficiency of liquid assets to replace 75 percent of income

	Proportion who lack		
	1 month	*2 months*	*3 months*
All households	0.51	0.65	0.72
Middle 50 percent	0.52	0.67	0.75
Below poverty line	0.63	0.72	0.78
Poverty line to median income	0.55	0.69	0.75
Median income to 80th percentile	0.49	0.64	0.73
Single, female-headed	0.55	5.67	0.72
Married	0.49	0.65	0.73
HS degree or less	0.62	0.74	0.8
Some college	0.52	0.69	0.76
College education or more	0.34	0.5	0.6
White	0.44	0.59	0.68
African American	0.69	0.82	0.86
Latino	0.71	0.84	0.88
Under 40	0.59	0.75	0.83
Over 40	0.47	0.61	0.69
Home owner	0.41	0.57	0.66
Renter	0.66	0.78	0.84

imminent need. If a shock to consumption or income occurs, these households would be forced to incur debt or be unable to meet their obligations.

New generations of asset-building programs should recognize the diverse needs of households. It is unlikely that one-size-fits-all asset promotion strategies would meet the needs of such a diverse set of balance sheets. Likewise, households at different stages of asset development may have different needs. For instance, households may need help or incentives to develop short-term precautionary saving before they have the asset sufficiency and economic stability to build longer term, more productive, and diversified physical, financial, and retirement assets. Other households may benefit from reducing high-cost debt loads before accruing substantial new assets. The need is substantial, but healthy household balance sheets are the foundation for households to build and develop economically.

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Appendix 3.1

Table A3.1 2010 Sample characteristics of typical households

	Income				*Marital status/gender*	
	Middle of the income dist.	*Below the poverty line*	*Between the poverty line and median income*	*Median-80th pct*	*Single Female*	*Married*
Income (mean)	$44,991	$13,975	$31,746	$63,529	$25,099	$63,295
Proportion of households						
Asset ownership						
Banked	0.96	0.78	0.93	0.98	0.89	0.95
Own home	0.65	0.32	0.55	0.75	0.50	0.73
Have dedicated retirement savings	0.57	0.13	0.42	0.70	0.37	0.64
Own stock	0.11	0.04	0.08	0.16	0.08	0.19
Own savings bonds	0.11	0.04	0.08	0.14	0.07	0.16
Own a business	0.10	0.05	0.08	0.15	0.04	0.18
Own a car	0.91	0.68	0.88	0.93	0.75	0.94
Debt presence						
Have educational debt	0.19	0.15	0.17	0.23	0.17	0.21
Have credit debt	0.71	0.38	0.59	0.82	0.57	0.76
Material hardship						
Household had unemployment in the past year	0.14	0.29	0.19	0.12	0.17	0.15
Have health insurance	0.88	0.79	0.85	0.93	0.90	0.90
Could find $3,000 for emergency	0.63	0.46	0.56	0.72	0.54	0.68
Spend more than income	0.19	0.26	0.21	0.18	0.24	0.18
Demographics						
Married	0.58	0.27	0.49	0.69	0.00	1.00
Have kids under 18 in the household	0.10	0.09	0.10	0.10	0.05	0.10
Race: white	0.71	0.62	0.66	0.75	0.64	0.74
Female headed	0.26	0.50	0.34	0.17	1.00	0.01
Education: college degree or more	0.27	0.13	0.20	0.36	0.27	0.35
Received public assistance in past year	0.05	0.31	0.12	0.02	0.19	0.08

Education			Race			Age		Homeownership	
High school or less	Some college	College grad or more	White	Black	Latino	Under 40	40 and over	Owner	Renter
$31,118	$44,146	$76,235	$49,635	$29,694	$32,911	$38,628	$46,608	$59,957	$25,836
0.87	0.95	0.99	0.96	0.81	0.83	0.89	0.94	0.98	0.84
0.54	0.60	0.76	0.69	0.44	0.43	0.41	0.71	1.00	0.00
0.36	0.55	0.74	0.59	0.38	0.32	0.48	0.55	0.66	0.31
0.06	0.13	0.29	0.18	0.06	0.03	0.10	0.17	0.20	0.06
0.07	0.12	0.19	0.15	0.08	0.03	0.10	0.13	0.15	0.06
0.09	0.11	0.20	0.16	0.06	0.06	0.09	0.15	0.17	0.08
0.83	0.87	0.91	0.90	0.72	0.80	0.82	0.88	0.94	0.75
0.11	0.26	0.25	0.19	0.24	0.15	0.37	0.12	0.17	0.22
0.53	0.69	0.88	0.75	0.45	0.48	0.59	0.72	0.82	0.44
0.20	0.16	0.13	0.15	0.23	0.22	0.26	0.13	0.12	0.25
0.85	0.88	0.94	0.91	0.84	0.75	0.83	0.91	0.93	0.80
0.52	0.63	0.80	0.70	0.40	0.49	0.64	0.63	0.71	0.51
0.21	0.19	0.17	0.18	0.24	0.20	0.19	0.19	0.18	0.22
0.57	0.54	0.63	0.61	0.39	0.61	0.57	0.58	0.68	0.42
0.12	0.09	0.05	0.07	0.13	0.18	0.15	0.07	0.06	0.14
0.66	0.70	0.78	1.00	0.00	0.00	0.62	0.75	0.79	0.58
0.28	0.31	0.23	0.24	0.43	0.27	0.25	0.28	0.22	0.36
0.00	0.00	1.00	0.35	0.21	0.17	0.30	0.33	0.39	0.21
0.19	0.09	0.02	0.07	0.24	0.21	0.16	0.09	0.04	0.24

Table A3.2 Typical household balance sheets

2007				*2009*				*2010*			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		*Debts ($)*	
Liquid assets	2,979	Credit	836	Liquid assets	2,831	Credit	625	Liquid assets	3,142	Credit	440
Physical	121,340	Housing	15,858	Physical	113,454	Housing	17,446	Physical	121,427	Housing	16,306
Financial	176	Other physical	1,933	Financial	169	Other physical	2,214	Financial	42	Other physical	891
Retirement	3,027	Education	0	Retirement	3,298	Education	0	Retirement	2,807	Education	0
Misc.	28,459	Misc.	0	Misc.	25,782	Misc.	0	Misc.	25,655	Misc.	0
Total	248,675		43,741	Total	246,436		47,521	Total	241,067		43,576
Net worth		$172,555		Net worth		$159,332		Net worth		$164,647	

Table A3.3 Balance sheets by race

2007				*2009*				*2010*			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		*Debts ($)*	
White											
Liquid assets	5,516	Credit	428	Liquid assets	5,544	Credit	422	Liquid assets	5,797	Credit	369
Physical	182,017	Housing	19,541	Physical	171,975	Housing	18,991	Physical	176,171	Housing	19,199
Financial	1,879	Other physical	1,704	Financial	1,897	Other physical	1,873	Financial	821	Other physical	1,282
Retirement	10,339	Education	0	Retirement	10,591	Education	0	Retirement	8,815	Education	0
Misc.	39,776	Misc.	0	Misc.	41,109	Misc.	0	Misc.	38,832	Misc.	0
Total	374,436		50,468	Total	365,228		51,448	Total	361,082		53,411
Net worth		$287,732		Net worth		$275,519		Net worth		$266,076	
African American											
Liquid assets	1,212	Credit	411	Liquid assets	1,074	Credit	290	Liquid assets	1,041	Credit	176
Physical	57,523	Housing	5,928	Physical	52,759	Housing	6,090	Physical	47,808	Housing	1,979
Financial	0	Other Physical	461	Financial	0	Other physical	738	Financial	0	Other physical	128
Retirement	514	Education	0	Retirement	500	Education	53	Retirement	141	Education	0
Misc.	23,700	Misc.	0	Misc.	25,593	Misc.	0	Misc.	21,653	Misc.	0
Total	132,388		22,464	Total	131,089		27,053	Total	115,659		12,065
Net worth		$92,544		Net worth		$81,233		Net worth		$76,253	

continued

Table A3.3 Continued

2007				2009				2010			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		*Debts ($)*	
Latino/a											
Liquid assets	1,555	Credit	509	Liquid assets	1,569	Credit	621	Liquid assets	989	Credit	263
Physical	73,960	Housing	8,671	Physical	56,746	Housing	7,940	Physical	49,786	Housing	5,020
Financial	0	Other physical	1,738	Financial	0	Other physical	1,112	Financial	0	Other physical	176
Retirement	202	Education	0	Retirement	419	Education	0	Retirement	15	Education	0
Misc.	5,972	Misc.	0	Misc.	4,969	Misc.	0	Misc.	4,702	Misc.	0
Total	117,486		32,238	Total	115,076		27,811	Total	92,691		13,029
Net worth		$64,422		Net worth		$56,823		Net worth		$48,941	

Table A3.4 Balance sheets by household structure

2007				2009				2010			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		Debts ($)	
Single, female-headed											
Liquid assets	2,179	Credit	358	Liquid assets	1,984	Credit	147	Liquid assets	1,873	Credit	143
Physical	77,103	Housing	2,036	Physical	65,886	Housing	1,427	Physical	64,735	Housing	1,991
Financial	140	Other physical	70	Financial	179	Other physical	50	Financial	1	Other physical	6
Retirement	1,069	Education	0	Retirement	679	Education	0	Retirement	327	Education	0
Misc.	8,570	Misc.	0	Misc.	8,329	Misc.	0	Misc.	8,984	Misc.	0
Total	151,267		10,574	Total	134,413		10,237	Total	126,111		11,588
Net worth		$114,054		Net worth		$95,527		Net worth		$82,266	
Married											
Liquid assets	6,533	Credit	707	Liquid assets	6,675	Credit	660	Liquid Assets	5,772	Credit	562
Physical	243,048	Housing	36,384	Physical	230,005	Housing	38,172	Physical	205,244	Housing	27,915
Financial	1,965	Other physical	3,759	Financial	1,829	Other physical	4,173	Financial	577	Other physical	2,306
Retirement	17,694	Education	0	Retirement	16,771	Education	0	Retirement	11,880	Education	0
Misc.	106,099	Misc.	0	Misc.	126,250	Misc.	0	Misc.	62,609	Misc.	0
Total	520,350		85,829	Total	520,399		89,728	Total	438,062		73,218
Net worth		$394,800		Net worth		$387,532		Net worth		$318,104	

Table A3.5 Balance sheets by educational attainment

2007				*2009*				*2010*			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		*Debts ($)*	
High school degree or less											
Liquid assets	1,813	Credit	303	Liquid assets	1,894	Credit	374	Liquid Assets	1,511	Credit	198
Physical	91,786	Housing	5,066	Physical	80,034	Housing	4,297	Physical	82,172	Housing	3,875
Financial	4	Other physical	667	Financial	3	Other physical	919	Financial	0	Other physical	291
Retirement	623	Education	0	Retirement	842	Education	0	Retirement	305	Education	0
Misc.	11,875	Misc.	0	Misc.	11,712	Misc.	0	Misc.	9,709	Misc	0
Total	160,660		14,006	Total	155,359		13,895	Total	147,497		12,418
Net worth		$115,620		Net worth		$105,913		Net worth		$101,433	
Some college											
Liquid assets	3,343	Credit	876	Liquid assets	3,027	Credit	1,003	Liquid assets	3,227	Credit	595
Physical	130,998	Housing	17,301	Physical	119,750	Housing	18,037	Physical	118,109	Housing	15,436

Financial	516	Other physical	2,190	Financial	258	Other physical	2,704	Financial	46	Other physical	1,189
Retirement	5,301	Education	0	Retirement	4,705	Education	0	Retirement	3,892	Education	16
Misc.	32,508	Misc.	0	Misc.	36,516	Misc.	0	Misc.	34,386	Misc.	0
Total	279,470		48,268	Total	272,854		52,629	Total	260,078		45,468
Net worth		$200,730		Net worth		$189,026		Net worth		$174,152	
College degree or more											
Liquid assets	12,126	Credit	654	Liquid assets	12,172	Credit	397	Liquid assets	12,267	Credit	307
Physical	321,921	Housing	45,487	Physical	306,008	Housing	45,728	Physical	283,105	Housing	40,835
Financial	9,642	Other physical	2,521	Financial	9,455	Other physical	2,213	Financial	5,330	Other physical	2,252
Retirement	52,356	Education	0	Retirement	33,032	Education	0	Retirement	39,593	Education	4
Misc.	146,877	Misc.	0	Misc.	167,887	Misc.	0	Misc.	132,288	Misc.	0
Total	742,713		106,473	Total	727,930		108,988	Total	671,325		109,023
Net worth		$596,010		Net worth		$560,995		Net worth		$500,210	

Table A3.6 Balance sheets by age

2007				*2009*				*2010*			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		Debts *($)*	
Under 40											
Liquid assets	2,319	Credit	558	Liquid assets	2,126	Credit	579	Liquid assets	2,003	Credit	322
Physical	57,167	Housing	13,577	Physical	66,694	Housing	17,939	Physical	55,238	Housing	13,106
Financial	25	Other physical	1,977	Financial	17	Other physical	2,044	Financial	0	Other physical	860
Retirement	908	Education	227	Retirement	1,378	Education	608	Retirement	919	Education	593
Misc.	20,119	Misc.	0	Misc.	33,617	Misc.	0	Misc.	22,290	Misc.	0
Total	136,214		41,254	Total	174,444		51,952	Total	137,276		41,630
Net worth		$74,296		Net worth		$92,687		Net worth		$69,043	
Over 40											
Liquid assets	5,475	Credit	412	Liquid assets	5,279	Credit	343	Liquid assets	5,335	Credit	323
Physical	196,151	Housing	18,228	Physical	174,529	Housing	16,136	Physical	182,628	Housing	14,685
Financial	1,908	Other physical	1,366	Financial	1,723	Other physical	1,538	Financial	906	Other physical	983
Retirement	12,314	Education	0	Retirement	11,197	Education	0	Retirement	8,812	Education	0
Misc.	40,382	Misc.	0	Misc.	38,276	Misc.	0	Misc.	33,449	Misc.	0
Total	391,917		46,352	Total	358,377		36,913	Total	356,315		35,415
Net worth		$307,878		Net worth		$275,360		Net worth		$271,270	

Table A3.7 Balance sheets by homeownership status

2007				2009				2010			
Assets ($)		*Debts ($)*		*Assets ($)*		*Debts ($)*		*Assets ($)*		*Debts ($)*	
Owners											
Liquid assets	7,495	Credit	701	Liquid assets	7,215	Credit	615	Liquid assets	7,401	Credit	540
Physical	262,923	Housing	41,438	Physical	245,161	Housing	45,904	Physical	244,258	Housing	46,066
Financial	3,241	Other physical	2,766	Financial	2,823	Other physical	3,632	Financial	1,574	Other physical	2,155
Retirement	18,498	Education	0	Retirement	17,532	Education	0	Retirement	14,918	Education	0
Misc.	88,393	Misc.	0	Misc.	107,032	Misc.	0	Misc.	85,833	Misc.	0
Total	525,564		88,907	Total	509,177		99,082	Total	483,702		97,935
Net worth		$410,082		Net worth		$383,229		Net worth		$357,793	
Renters											
Liquid assets	1,006	Credit	174	Liquid assets	983	Credit	209	Liquid assets	975	Credit	121
Physical	8,194	Housing	0	Physical	5,101	Housing	0	Physical	8,371	Housing	0
Financial	0	Other physical	222	Financial	0	Other physical	119	Financial	0	Other physical	17
Retirement	40	Education	0	Retirement	40	Education	0	Retirement	17	Education	0
Misc.	5,611	Misc	0	Misc.	5,057	Misc.	0	Misc.	7,185	Misc.	0
Total	36,035		3,999	Total	30,006		3,715	Total	37,250		2,850
Net worth		$24,892		Net worth		$21,081		Net worth		$27,411	

Chapter Four
Financial Fracking in the Land of the Fee, 1980–2008

Devin Fergus

In 1986, Tito Manor went shopping for a car. At the lot, the car salesman informed Manor that he would need someone to cosign, which his aunt, Gloria Young, ultimately agreed to do. The car salesman, who passed the completed loan application on to Fidelity Consumer Discount Company, notified both Manor and his aunt that the loan had been approved. Then, the salesman instructed them to come to the dealership and bring the aunt's house deed, just as verification that she was indeed a homeowner. However, the dealer never informed Young that the house was being used as security for her nephew's car loan. The lender, Fidelity, took a first mortgage on Young's home at an interest rate of 36 percent—far in excess of the Pennsylvania state usury cap of 24 percent. Unable to keep up with the principal and interest on the car note after several months, Tito suggested that he return the car to Fidelity, to which the lender responded, according to uncontradicted deposition testimony: "We don't want the car. We want your aunt's house" (Mansfield 2000, 512–17). The steep loan terms made seizing the home not simply more likely, but also a more profitable alternative than seeing the loan terms satisfied.

The law making this possible was the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA). Among its other features, this law preempted state usury laws while also removing interest rate ceilings on any loan secured by residential property (Remarks of the President at the Signing Ceremony for the Depository Institutions Deregulation and Monetary Control Act of 1980). According to legal scholar Cathy Mansfield, "It didn't take long after DIDMCA was adopted for some second mortgage lenders, and for other lenders who had been making high-cost consumer loans, to notice that DIDMCA appeared to allow them to charge an unlimited amount of interest provided they took a first lien on the borrower's home" (Mansfield 2000, 511). Thus, a number of lenders, who would not have otherwise made first-lien home equity loans before DIDMCA, began to cast car loans, small consumer loans, and second mortgage loans as very expensive home equity first-lien loans (Mansfield 2000). High-cost lenders used the new deregulatory acts to bilk borrowers out of their cars and homes. Such loan practices were made possible because of federal preemption that allowed lenders to bypass state usury law. As the Manor Young case illustrates, beginning in the 1980s, financial deregulatory laws such as DIDMCA would erode consumer protections that had shielded

borrowers against predatory financial practices since the 1930s. This paved the way for the rise of fringe financial services and the abuses that accompanied it.

For nearly a generation, interest in asset building has been steadily spreading across the antipoverty policy landscape. Asset-building programs and policies were first touted by antipoverty advocates in the early 1990s who wished to navigate a third way between the direct income-transfer ideas of the left and the benign neglect adherents on the right (see Friedman, Vaughan, and Steinbach 1988; Haveman 1988; Sherraden 1988; Regan and Paxton 2001). Asset-building strategies would emerge as one of the four favored antipoverty, market-centered technologies of choice—along with microfinance,conditional cash transfers, or CCTs (in which money is granted to poor families on the condition these households promise to make specific investments like vaccination or high-school attendance for their children), and place-based projects such as President Clinton's New Markets Initiative (Katz 2011, 113–50). While these interventions were gaining traction in think tank and policy circles across the political spectrum, a parallel, shadow movement was afoot, eager to make a profit from the very same low-income and working-class households that Michael Sherraden and other architects of the asset uplift school aimed to help.[1] This extractive trend too has been abetted by government policies. Specifically, a series of deregulatory choices, mostly though not exclusively at the federal level, have turned a blind eye to equity stripping and have incentivized a sort of "financial fracking" that extracts wealth yet leaves behind a bevy of negative externalities. The result has been greater economic inequalities between upper-income and lower-income households. This chapter describes the rise and codification of consumer finance fees and its impact on four once-reliable paths to upward mobility—homeownership, higher education, employment, and transportation. Central to my study is the role played by deregulation, which has helped create an operational space for the spread of wealth-extracting consumer finance fees since the 1980s.

Why Employment and Transportation Matter to Mobility

The first two spheres—homeownership and higher education—focus on traditional pathways to upward mobility. Employment and transportation may also be considered pathways to upward mobility, if not in quite the same ways as a home or college degree. These four domains are complementary, not mutually exclusive. While homeownership and higher education tend to encompass single financial expenditures—for example, a 30-year mortgage or 15-year student loan—the latter two spheres (employment and transportation) take into account the cumulative effect of more quotidian transactions (e.g., daily accrual of interest of a payday loan, the options of monthly or even weekly auto insurance contracts) consumers may experience. In each domain I examine how consumer financial products may exacerbate inequalities. In so doing, the chapter demonstrates that upward mobility is not simply about the episodic (buying a home or borrowing a student loan) but also the everyday, that is, it reminds readers that seemingly mundane consumer financial expenses (such as auto insurance and payday loans), especially when extrapolated over time, serve to extract wealth and exacerbate socioeconomic immobility.

While employment is of course a pathway to upward mobility, the payday loan, the consumer financial product that was created expressly to address problems of work-related paycheck shortfalls, may well have the opposite unintended effect. First, as its very name intimates, a payday loan is virtually impossible to receive without a job—a fact that cannot be stated for almost any other form of short-term, consumer credit. Unemployed children, life partners, and even pets have all been known to have access to credit; not so with payday loans, where a pay stub is a must for any borrower. In this sense, a payday loan more

closely correlates to employment and wages than any other consumer financial product. Second, while payday lending is certainly about access to credit, to focus exclusively on credit would be to merely focus on conditions of the supply and not the reasons for demand: mainly, the payday loan industry's explosive growth and tremendous impact on working and middle class families, directly correlates to not only deregulation but also a declining standard of living spurred largely by wage stagnation. Third, payday lenders themselves recognize that their industry's success is borne of wage stagnation. "There are multiple reasons fewer people are able to meet the[ir] expenses. First of all, overall wages have been stagnant for a long time," to quote web communications of the Personal Money Store, an online marketer for the alternative short-term and mortgage consumer finance market (PayDay Loan Advocate 2010). Similarly, a report on payday lending in America, conducted by the Pew Research Center in 2012, indicated that 85 percent of borrowers assume these loans to cover ordinary living expenses (utilities, gas, groceries, and credit cards) or unexpected expenses (car repair and emergency medical treatment)—the sort of expenses traditionally covered by a worker's paycheck (PayDay Lending in America 2012). Moreover, the Pew report also suggests the negative impact payday lending may have on upward mobility as an antisavings mechanism. According to Pew, borrowers are more likely to be renters than nonborrowers in the same income brackets. For example, 8 percent of renters earning $40,000–$100,000 have used payday loans, compared with only 6 percent of homeowners earning $15,000–$40,000, according to Pew (PayDay Lending in America 2012). For renters, the high-cost transactions associated with a payday loan, relative to less expensive short-term credit options, may well strip wealth from future possible homeowners, creating another financial hurdle to increasing the personal savings that are necessary for such long-term, wealth-building investments, such as the purchase of a house.

Although traditionally not thought as such, transportation also is an area that has become critical for upward mobility, especially for a key demographic that the asset-building school looks to serve: the nation's urban poor. Labor economists, sociologists, and urban policy historians have all documented the geography of opportunity around access to reliable transportation (Squires and Kubrin 2005, 47–68; Vale 2007; Briggs 2005; Jackson 1987; Raphael and Rice 2002,118). Specifically, the "transportation gap" that has grown over the last five decades is not only because of deindustrialization, which has led to the outmigration of manufacturing and industrial jobs from central cities to suburbs, the US South, and abroad. It is also that declining white support for mass transportation and the principle of integrated residential housing, evinced in numerous public opinion polls since at least the 1960s, have exacerbated changes in the structural economy (Wilson 1996, 202). As the sociologist William Julius Wilson has written about the disappearance of upward mobility in the nation's inner cities, "among two-car middle class and affluent families commuting is accepted as a fact of life . . . In a multitiered job market that requires substantial resources for participation, most inner city must rely on public transportation systems that rarely provide easy and quick access to suburban locations" (Wilson 1996, 39).

Within the realm of reliable transportation, auto insurance remains an inescapable financial expenditure. "Owning a car creates expenses far beyond the purchase price, including insurance, which is much more costly for city dwellers than it is for suburban motorists," Wilson writes (1996, 40–41). Driving without insurance results in imprisonment, fines, not to mention, in the event of an accident, astronomical reparations for loss of life and property. It's not that urban motorists are, in the abstract, unable to afford insurance; rather, it is that the zip code calculus used by insurers exacts a high-cost premium for urban motorists, often pricing them out of the market altogether. Likewise, labor economists too have identified vehicle insurance as a sine qua non for upward mobility. One particular study, matching state data on auto insurance premiums to

microsample information on car ownership and labor market outcomes, found that those with cars are 27 percent more likely to be employed, work on average 11–16 hours more a week, and earn 40 percent more per hour than those without cars (Raphael and Rice 2002, 109–130). In this way, the study's authors concluded that not having auto insurance or any other hurdles to legally operating a car is one form of income shock: "Losing access to a car is equivalent to a reduction in income" (Raphael and Rice 2002, 112).

The Nature of Consumer Finance Fees

Fees as Hidden Charges

Over the last 30 years, Americans have been increasingly subject to fees they may have little idea are being charged, largely because they are consumers in an increasingly underregulated financial marketplace. We pay at home, at work, at school, and in our cars. "Unexpected or hidden fees" ranks as the single biggest everyday annoyance of American consumers, according to a recent survey by *Consumer Reports* (Consumer Reports Money Advisor 2010). Consumers regularly complain about bank teller, overdraft, and minimum balance fees, IRA or 401(k) maintenance fees, airport fees, cash advance or balance transfer fees on credit cards, activation and early termination fees doled out by cable, cell, and Internet service providers, along with mutual fund load fees, 529 college accounts fees, among other fees.

"Hidden" does not mean that a cost, charge, or term is missing from the actual agreement any more than a parent playing a game of hide and seek with her child is missing or disappears from the house. Hidden simply means that costs and terms are buried in fine print or impenetrable legal language that even contract attorneys often have difficulty detecting, with the onus placed on the consumer to discover the unexpected terms and actual costs associated with the good or service being provided by the lender or insurer. All too often the devil is in the details.

In 1980 a typical consumer credit contract was one and a half pages, according to the *Wall Street Journal*; by the early 2000s, it was over thirty pages (Pacelle 2004). These additional pages are not about protecting companies from lawsuits. As Elizabeth Warren, the architect of the recently created CFPB (Consumer Financial Protection Bureau) wrote in 2007, these companies have found other effective ways to insulate themselves against litigation (Warren 2007). The contracts pack unexpected and unreadable terms; they are effectively the printed equivalent of the last ten or so undecipherable seconds, fast talking we have all heard on our radios at the end of car commercials. By inserting unexpected and unreadable terms into the fine print, lenders and other financial service companies make billions of dollars each year at the expense of families. These fees have the potential to add up over time, to levels that can significantly change the economic prospects of a household.

I call these hidden expenses trick-and-trap (TNT) fees. By TNT fees, I mean a collection of cryptic charges on subprime mortgages, loans and grants for higher education, high-cost equity and payday loans, and zip-code-based insurance premiums. TNT fees often hide in plain sight. Because the true and total costs of these financial products and how these costs are determined are often buried in fine print, undisclosed and tightly guarded pricing structures, and impenetrable legal language, customers—whether by accident or design—are often "tricked" into paying exorbitant costs for consumer finance products.

Once ensnared into paying higher costs, consumers find themselves "trapped" in an almost inescapable web of debt. Even for the so-called good debts, such as college student loans, the final amount borrowed can easily increase to three or four times more than the original loan. What makes TNT fees most dangerous is that they have exploded in housing, higher education, employment, and transportation. Unlike more indulgent

mediums of exchange like credit cards, these four areas of consumer finance are particularly important because they have provided the traditional pathways to upward mobility for low-income and working-class families. It is in these areas that fees have proved so costly to the American consumer. Studies from the Brookings Institution and elsewhere have suggested that abolishing these and other TNT fees would save consumers more than $650 billion, an astonishing sum that exceeds the budgets of Mexico and Canada combined (Fellowes 2006). This figure also amounts to nearly 20 percent of the projected 2012 US budget (United States Executive Office of the President of the United States, Office of Management and Budget 2011; Montgomery 2011). Nationally, reducing fees for families by just 1 percent would translate into as much as $6.5 billion each year in new spending power—additional monies families could use to reduce household debt, save, or invest in retirement and income-generating assets.

These fees shape life choices. Even in highly lucrative professions such as medicine that we most closely identify with the nation's wealthy and upper middle classes, life choices can be dictated by debt or the fear of it. For example, nearly one in three medical students cite concerns about medical school debt as a chief factor in determining their area of specialization.[2] For Americans on the working margins, the reality is even starker: fear of student loan debt ranks as a primary deterrent to pursuing a college degree (Cunningham and Santiago 2008; Moltz 2008).

Consumers bear some responsibility. Many fail to read the contract given to them. Others simply do not ask questions about papers they are signing. Yet it is not surprising that so few consumers take the time to do their due diligence, given that contracts have grown exponentially longer with ever-denser legalese over the last 30 years. Even if the consumer has the time, many industries, like the auto insurance industry, typically do not disclose their pricing system, which insurers regard as a trade secret and off-limits to the public (*Consumer Reports* 2012; DeMark, Kolbe & Brodek Law Firm 2012; Reinhardt 2006).

To best understand the problem one must adopt a broad definition of the term "fee," one that takes into account a fee as both a base and an add-on charge. This broad definition reflects the reality facing the American consumer for two reasons. First, fees are often baked into the base price of a good or service, making it nearly impossible for consumers to incur a good or service without paying an add-on fee or to know its itemized cost. For example, in auto insurance, insurers typically charge customers a hidden cost based on their residential location but often do not disclose or itemize the actual price. At other times, these fees are disclosed but—like ingredients on the side of a manufacturer's cake box—they are impossible to sift out of the manufacturer's product. You must buy the cake, or credit product, as baked. That is the case for origination and many transaction fees in mortgages, paydays, and student loans. Second, fees and the base price should be considered together because the growth of fees has become a profitable alternative to raising the base price. Perhaps the most glaring example of these two points may be in higher education, where all institutions—public four-year universities, private four-year colleges and universities, private for-profit universities, and community colleges—encumber students with a bevy of fees, including utterly inescapable registration fees just to attend class, as a backdoor way of boosting revenue without sparking the public backlash that often comes with unpopular tuition or tax hikes. Similarly, agreeing to a student, mortgage, or payday loan often triggers a host of extra charges like origination, transaction, or repayment fees.

Fees as De Facto Tax

These types of financial charges function as a de facto tax. Of course, it is not a formal, government levy like we pay to the IRS or to a municipal or state revenue collector. Yet in so many instances, these fees do the substantive work of a tax since they underwrite

a public good or service (e.g., education, housing, or legally mandated auto insurance) with one group often subsidizing another. During debates in the 1980s and 1990s, senators on both sides of the aisle openly referred to America's financial aid system as a "tax" on students and middle-class families because students—via fees affixed to government lending programs—were being asked not simply to repay their educational loans but also to pay an additional fee to help balance the federal budget (Sanchez 1995).

Many pundits and politicians claim that this tax is paid only by the financially irresponsible, America's urban poor, or working-class residents of the so-called secondhand suburbs. However, the kudzu-like spread of consumer finance fees, which have climbed over and coiled around the bank accounts of many middle-class American consumers in recent years, militates against this view. For example, although many believe that the recent mortgage crisis impacts only borrowers with poor or marginal credit, the average American subprime applicant actually possessed a prime credit score and was eligible for a conventional loan by the time the mortgage market bubble burst in 2007 (United States Financial Crisis Inquiry Commission 2011).

Fees as Profit Stream

Consumer finance fees have been a part of the modern consumer experience throughout much of the twentieth century. What has changed since the 1980s is the evolution of fees from a means of offsetting administrative or risk costs into a source of income itself. That is, fees are a profit stream. Fee-incomes started in earnest in the early 1980s with Paul Perdue, who served as the lead plaintiff in a 1978 class action suit against Crocker National Bank of California. Perdue and others sued Crocker National for charging a $6 nonsufficient funds fee when the actual cost incurred in processing the bounced check was only 30 cents; this transaction effectively netted the bank a 2000 percent profit. Plaintiffs claimed such a profit was unconscionable (SCOCAL 2009).[3] In anticipation of the ruling in *Perdue*, a case that was ultimately settled out of court, the Office of the Comptroller of the Currency (OCC) issued an interpretive ruling in 1985, establishing that service charges were a business decision for banks and thus could preempt state law (A. S. Pratt & Sons 2010). OCC's ruling was followed a decade later by a 1996 OCC revised provision, authorizing national banks to disregard state usury laws.[4]

Still, for bank deposit account holders, bank fees did not rise significantly until 2004, when the OCC enacted expanded preemption regulations, giving maximum latitude to banks in setting fees for both deposit products and consumer loan products. Thus, banks were given the green light to charge limitless fees for limitless amounts without being in violation of state usury laws. Another bank regulator, the Office of Thrift Supervision, made a similar ruling also in 2004 (A. S. Pratt & Sons 2010). By 2009, according to the *Financial Times* of London, US banks were collecting $38.5 billion in customer overdraft fees alone—not to mention other fees like ATM withdrawal, minimum account, and checking balance maintenance fees (Scholtes and Guerra 2009).

Even during the recession, the median overdraft fees increased, from $25 to $26, the first increase during a recession in 40 years. The larger the bank, the more likely the increase. This was understandable, according to the general counsel of the American Bankers Association, which stated that large banks do not know their customers as well as smaller community banks and thus must be compensated for their increased risk (Scholtes and Guerra 2009). Where overdraft fees really dent wallets, however, is when banks let customers take out more than they have at an ATM or through a debit-card purchase (in the past usually without an alert). In these cases, customers are not facing merchant fees, and probably the only consequence of the transaction being denied would be having to put back their groceries (Chu 2005).

Fees in Modern Consumer Life

Our current crisis in consumer finance goes back decades. During the mid-1970s, the federal government enacted a series of laws—the Equal Credit Opportunity Act of 1974, the Home Mortgage Disclosure Act of 1975, and the Community Reinvestment Act of 1977—to encourage the provision of financial services in underserved communities. Yet almost simultaneously, a set of deregulatory policies emerged that quietly made credit, banking, mortgage, and insurance markets less accountable to governments and consumers. The erosion of oversight escalated in the following 30 years, decimating consumer protections and fostering the rise of a new fringe financial sector, one that augured a shift away from denying credit and services to extending credit and services on high-cost terms. The net effect has been a TNT tax in disguise, a de facto levy sanctioned by the laissez-faire policies of successive governments and the private sector on citizen consumers.

Given their role in the 2008 financial crisis, abusive mortgage lenders have received relatively more scrutiny, but they are just one piece of a forgotten history about the rise of consumer finance fees in four spheres that are intertwined and inescapable in modern consumer life: homes, school, work, and transportation.

Homes

Depository Institutions Deregulation and Monetary Control Act

Modern subprime lending in housing started with three legislative acts. The first was the 1980 DIDMCA. DIDMCA was intended to boost the saving rate of Americans, which hovered near a decade low of 7.9 percent in September 1979, when the law was being debated. DIDMCA allowed for higher interest rates and thus functioned as the gateway law creating a new type of mortgage market—subprime loans. DIDMCA is critical to the subprime market for two reasons. First, it made high interest rates and fees legal. Now, effectively free to charge customers any rates they wanted, banks had incentives to make home loans to borrowers with below prime credit records. Second, DIDMCA also allowed the charge of unlimited interest rates for refinancing or second liens, because the law did not distinguish between purchase (or mortgage origination) loans and loans made for other purposes. Thus, as we saw in the introduction of the chapter, lenders looked to charge customers the higher interest, more profitable, first lien loans—the most common type of subprime loan—regardless of the product the consumer was purchasing (Temkin, Johnson, and Levy 2002, 4).

DIDMCA did not trigger immediate massive change in the high-risk mortgage. However, it erected the legal apparatus that was the sine qua non for making high-cost, subprime loans legal. Specifically, DIDMCA abolished the interest caps that had governed mortgage lending since the New Deal, freeing mortgage lenders to charge unprecedented rates to putatively riskier borrowers (Birger 2008; Federal Deposit Insurance Corporation 2012). How would this help the typical savings accountholder? The assumption was that once savings and loan associations (S&Ls) and other savings institutions were free to charge more on mortgage loans, the higher rates would soon trickle down as higher returns for savings accounts of bank and S&L customers. "Most significant of all," according to President Carter, "it [would] help improve our nation's very low savings rate" (Carter 1980). Carter, along with allies in Congress and the mortgage industry, impressed upon a skeptical public that abolishing rate caps would redound to the benefit of the average accountholder by boosting savings. Sold on this idea, even those habitually hostile to laissez-faire economics such as the Gray Panthers, a quasi-socialist band of senior citizens in the 1970s, called for DIDMCA's passage (Rom 1996; Eisenbeis and Kaufman 2011).

While DIDMCA may not be chiefly responsible for the steady decline in the saving rate since this period, the legislation certainly failed to boost savings. In fact, in the decades following the passage of DIDMCA and other complementary financial deregulatory laws, the saving rates among American consumers actually declined, so much so that the average saving rate (3.9 percent) in the years leading up to the financial collapse (ca. 2000–2008) was half the rate it had been when DIDMCA passed (Marquis 2002; Guidolin and La Jeunesse 2007; Jones 2010). DIDMCA had plainly failed to achieve its original intent.

Garn–St. Germain Act

While DIDMCA phased out rate caps, the Garn–St. Germain Act of 1982 introduced to the national market some of the most exotic mortgage instruments that exist today. It did so by empowering banks to preempt state protections that had been put in place to prohibit the interstate use of creative mortgage instruments. These instruments include adjustable rate mortgages (ARMs), excessive prepayment penalties, and balloon payments, which are inflated payments due at the end of a loan agreement that lenders often refuse to refinance, thus leaving borrowers with a huge bill at the end of the loan. All three credit creatures spawned by this 1982 law posed far greater risks at the time of the Great Recession than conventional fixed-rate mortgages, and continue to undermine homeownership stability (Nassar 2008). Specifically, an ARM was 36 percent more likely to default than a conventional fixed-rate mortgage; a mortgage containing a prepayment penalty was 52 percent more likely to default than a loan without one; and a balloon payment mortgage was 72 percent more likely to default than a conventional mortgage (Nassar 2008).

From the outset, these loan practices—blamed for greatly increasing the default and foreclosures rate in recent years—were designed to favor the lender over the borrower (Lewis 2005). That is why, when the Garn–St. Germain Act passed, the *Chicago Tribune* called the new law an "aid bill" for the mortgage industry (Key 1982). The abusive history of the Garn–St. Germain Act stems directly from its troubling legislative origins. Following the money of the act's two namesakes, Fernand St. Germain (D-RI) and Jake Garn (R-UT), reveals the strong collusion between both political parties and the financial services industry. The congressmen profited nearly as much as the industry.

The son of a dye factory foreman, St. Germain, entered the House of Representatives in 1961 as a state legislator and was a millionaire when he left in the 1980s ("Amassing of Wealth, Ties to Bankers Questioned"1987; United States House of Representatives, US House Committee on Ethics 1987). His personal wealth appeared to come largely from realtors, bankers, brokers, and others he was directly charged with legislating and regulating as a member and later chair of the House Banking, Finance, and Urban Affairs Committee. By the mid-1980s, the Rhode Island Democrat was one of the two biggest recipients of campaign contributions from the three financial political action committees (PACs) lobbying for the banking reform legislation that included today's most notorious exploding fees like balloon payments and adjustable rate mortgages ("St Germain Attacks Wall Street Journal" 1985; Jackson and Carrington 1985; Bennett and Loucks 1994; Sherrill 2008). In addition to taking campaign contributions from businesses he was directly charged with legislating and regulating, St. Germain also received preferential investment and real estate deals, including from one investor who, hoping to benefit from the passage of the exotic mortgage bill then being debated in Congress, put up nearly 100 percent of funding for St. Germain to purchase five restaurants (Jackson and Carrington 1985; Jackson 1987; Sherrill 2008). The bill's GOP coauthor, Jake Garn, was equally embroiled. The Utah Republican shilled for the nation's largest high-risk, high-yield securities company, junk bond firm Drexel Burnham Lambert. This firm, along with other financial service lobbyists, repaid the Utah senator's promotion

of DIDMCA and Garn–St. Germain by underwriting Garn's pet project, the Garn Institute of Finance at the University of Utah (Day 1989). Funding tax-exempt foundations such as the Garn Institute constituted another way that the industry, in an effort to circumvent newly created campaign finance and related laws, kept its access to the legislative architects writing the banking rules (Soley 1995, 94–95). Because these rules were conceived and crafted primarily by industry lobbyists, American consumers were always an afterthought.

The point here is not to impute or impugn the motives of the law's architects. More importantly, because Garn–St. Germain—the law that paved the way for so much creative financing of the subprime market—originates from a policy process so awash in industry money, it is impossible to know where lawmakers' public-spirited commitment to free-market principles ends and their loyalties to the narrow interests of the financial services begin.

Tax Reform Act

These two laws—DIDMCA and Garn–St. Germain—combined with a quiet revolution in fiscal engineering, the Tax Reform Act of 1986 (TRA 1986). The third step to subprime, TRA 1986 was steeped in the costly cold war mindset that private property owners were more deserving citizens than renters. Through the home mortgage interest deduction and other tax breaks created by the TRA, Congress rewarded those who purchased homes and subsidized the accumulation of home equity (Graetz 1988). Before TRA 1986, consumers could deduct the interest accumulated from a range of installment purchases (e.g., credit cards, personal loans, and even home equity loans). After the act was passed, only the interest from a primary mortgage and home equity loan (aka second mortgage) was deductible. This misguided principle ultimately created an American debt trap. In order to secure the big tax break, consumers increasingly used their homes as their primary source of investment and savings (Garon 2011). Banks quickly swooped in and began pushing the tax advantages of tapping the equity in one's home to pay for a vacation, car, or wedding. "If you're looking for your cheapest source of money, check your home," advised Chemical Bank in a nationally promoted advertisement (Chemical Bank 1986). As housing prices rose, homeowners took more equity out of their homes. By the late 1990s, only one-third of home equity loan proceeds financed home improvements; the balance went toward paying off school debt, medical bills, weddings, cars, vacations, and credit cards (Garon 2011, 350; Atlas 2003; Canner, Durkin, and Luckett 1998).

The Impact of Housing-related Fees

Without these three legislative acts—the DIDMCA, Garn–St. Germain Act, and Tax Reform Act of 1986—there would be no subprime market. Given how congenitally flawed the DNA of mortgage deregulation was from the outset, readers may well ask not why subprime failed but how it managed to avoid failure for so long. Why were financial institutions and others associated with the real-estate industry so intent on pushing instruments that practically guaranteed failure? A major reason was fees—fees that were hidden in the legalese of a mortgage or a home equity contract, or, when detected, fees that trusted professionals persuaded borrowers they need not worry about (Duffy 2012; Elmer 2012).

By the 1990s, thanks to deregulatory laws like Garn–St. Germain and a tacit faith that government would bail out home lenders, fees had exponentially increased industry profits and the personal incomes of professionals at the expense of consumers. Analysts of the current financial crisis tend to focus on mortgage bundling and credit default swaps – the complex financial instruments Wall Street invented to create vast profits

from nothing (Morrissey 2008; Morgenson 2011; Gandel 2012). However, the roots of our predicament predate those exotic inventions. Initially subprime mortgages were about the money to be made from fees. Aside from paying higher mortgage rates than others, subprime borrowers who are unable to pay a balloon must refinance, thus incurring new upfront charges like origination fees. There are also prepayment penalties in which subprime borrowers are penalized for trying to repay a loan early. These penalties naturally slow down rates of repayment on balance and principal, increasing the likelihood of negative equity during a downturn in housing prices. Even before the collapse came equity stripping—the profitable practice of refinancing a home in such a way that the borrower is charged excessive fees by the lender or broker, stripping the equity out of the home and putting it in the pockets of the refinance company. By 2005, three years before the housing bubble burst, subprime borrowers had surrendered $9.1 billion annually in high interest rates, prepayment penalties, and other related fees (Quercia, Stegman, and Davis 2005 6). That is $9.1 billion each year in equity extracted from the most vulnerable borrowers in the subprime housing market.

Schools

If a home purchase is the most expensive financial investment one can make, postsecondary education ranks second. We normally do not think of higher education as a mechanism of wealth disparity. Indeed, for much of American history, particularly the postwar era, a college degree has been regarded as society's great leveler, a pathway to upward mobility. However, this has been slowly changing in recent years, as the growing costs associated with financing a degree have increasingly made college campuses a site of indebtedness and inequality between the rich and the two out of three students who today take out a loan to attend school (Cunninghman and Kienzl 2011; O'Shaughnessy 2011).

In 2010, student loan debt surpassed credit card debt for the first time (Lewin 2011). The average debt for graduating college seniors with a student loan (approximately two out of every three students) in 2010 was $24,000, and the total debt was likely to top one trillion dollars in 2011 as more young people attend college and borrow money to do so (Shader 2011). Buried in the contract of government and private student loans is a trove of TNT fees that too often go unexplained by financial aid officers and go unnoticed by borrowers. By fees for college financial aid, I mean add-on expenses such as origination charges, deferment and extension costs, early repayment penalties, and default fines in which lenders tack on collection costs as high as 20–30 percent of the loan balance before sending it to the collection agency, a process called "capitalization" (Kirkham 2011; US Department of Education and Consumer Financial Protection Bureau 2012; Wagner 2012).

Private student loans, which took off around 2001 and accounted for 14 percent of all student loans in 2008, often have even more predatory terms than public student loans. For example, some private loans go into default after just one missed payment. The terms of these private loans increase a borrower's costs and default risks—and so risk damaging her credit score and increasing the costs of future credit—without a substantial benefit (relative to a federal student loan) to the borrower. The end result of these TNT fees is exploding debt, resulting in students often owing three to four times the original loan amount. While the costs and terms may not necessarily be hidden, the loan application forms and process are often so complicated, layered in legerdemain, that even the current Secretary of Education Arne Duncan admitted in his 2009 Senate confirmation hearing, "You basically have to have a Ph.D. to figure that thing out" (*Confirmation of Arne Duncan* 2009).

Once trapped in debt, student borrowers are offered very little in the way of consumer protections to help them escape. Unlike other forms of consumer credit, for

example, the key student loan-related statutes do not have private enforcement rights or attorney's fee provisions, so it is difficult and costly to challenge them in court. Unlike conventional debts, borrowers cannot discharge student loan debt in bankruptcy court without clear proof of undue hardship. In addition to these add-on fees, which often hide in plain sight in student loan contracts, the student loan itself could be regarded as an unexpected fee, given that private and unsubsidized loans were originally designed to play only a supporting role in financing students' education.

The financial aid system was not intended to be like this. The Pell grant was originally conceived in the 1970s as the foundation of the federal student aid system, with other federal and nonfederal grant and loan programs originally intended to provide supplemental (not primary) assistance if necessary (Gladieux 1995). However, the Pell grant has long since ceased functioning as the foundation of America's financial aid system. Last year, for example, 82 percent of undergraduate aid came from non-Pell sources. Given that today's Pell covers such a small fraction of the overall cost of college, the government grants function more like an introductory teaser rate. Like most teasers, they entice customers with modest up-front benefits that are too good to last the life of the term and are offset by staggering loan totals that dwarf the initial offer or reward.

Changes in Student Aid

So what went wrong? This trend toward student indebtedness started approximately a generation ago, with its roots in deregulation, fiscal policy, and the changing view of students from future tax contributors to tax eaters. The rise of student loans is directly attributable to the decline of tax receipts once earmarked for higher education. Cuts in higher education funding since the 1980s are the number one reason for the escalation in tuition and fees. Under the guise of deregulation and deficit reduction, the Reagan Administration and their congressional allies aimed to dump students from both the Pell grant and federally subsidized student loan rolls. With this goal in mind, spending on student aid was slashed by some 25 percent between 1980 and 1985 (Rankin 1981; United Press International 1985; Broder 1987). Tax cuts necessitated government doing less with less. Specifically, Reagan's Office of Management and Budget believed that less funding would translate into less federal intrusion (*OMB Director's Review* 1984; see Sunderman 2009). These cuts gave license to reducing the federal role in education, as Reagan rolled back regulation by reducing the enforcement budgets overseeing financial aid in higher education. An exception was the inspector general's office where the operational budget was increased and new personnel and authority were added to make a more muscular enforcement outfit that might crack down on fraud and abuse. The Administration also expanded the office by empowering it to go beyond merely collecting complaints about potential abuse or fraud, its only authorization, to initiate investigations. It added at least 130 additional audits and ten more investigations into criminal activity (*OMB Director's Review* 1984).

Eager to remove students from the rolls, Reagan Administration officials tightened eligibility guidelines for Pell grants and student loans, with dramatic consequences. In the years immediately following guideline changes, from 1980 to 1985, freshman participation in the Pell grant program declined by nearly half (Green 1987). Changing eligibility rules for Pell grants eliminated 267,000 freshmen from these awards between 1980 and 1986. Students who were eligible for grant assistance in their freshmen year were, in year two, told that they had to take out student loans. For nearly nine years running in the 1980s, the purchasing power of Pell grants decreased as college costs grew and outpaced inflation (Boren 1989, 3). As its buying power declined what the Pell covered shrunk as well—with aid shifting from grants to loans. For example, at the dawn of the 1980s, Carter submitted his budget for the fiscal year with Pell grants

constituting 56 percent of total federal dollars allocated for student aid. By decade's end, when Reagan proposed his fiscal year budget for 1989, the numbers were almost reversed—with loans (50 percent) replacing grants (47 percent) as the largest source of total federal dollars available for student aid (Boren 1989, 12). Eligibility criteria for federal loans were changed as well. Low-cost, low-interest subsidized federal loans were limited to families with household incomes of less than $32,000—regardless of family size (Naegele 1983). The decline of aid, combined with the rising cost of college, compelled students to take out loans from both government and private lenders.

Some dispute that there was a decline in aid. They argue that, in overall dollars, federal grant assistance actually increased during this time. However, this argument obscures the fact that the biggest beneficiaries of aid were private corporations: independent for-profit, proprietary colleges. From a small base, Pell funds at for-profit schools skyrocketed 342 percent from 1978 to 1984. By 1984, proprietary students were using more Pell aid than were students at public community colleges. Only for-profit, proprietary colleges saw their total Pell dollars increase faster than inflation; traditional two- and four-year institutions, by contrast, failed to keep up with inflation.[5] This increase in aid for for-profit schools is explained partly by the growing number of proprietary colleges receiving accreditation. For many free-market conservatives, for-profit colleges were demonstration schools, out to prove that a profit-driven model could succeed even in the postsecondary education sector. However, these devotees to laissez-faire capitalism were heavily dependent on the federal government to make their case.

At least initially, starving the beast of government did not automatically mean an enlarged role for the private sector. In contrast to housing deregulation, bankers at first did relatively little lobbying for student loans. In fact, banks were quite skittish about lending to students—primarily teenagers with virtually no employment or credit history, no collateral, and no spouse and kids depending on the family breadwinner to behave responsibly by repaying the loan. Rather, when it came to student aid, deregulation and fiscal policies were designed less by and for the private financial sector, though they were obviously welcome. Instead, the architects of the rise of the student loan were cultural warriors like secretary of education William Bennett, who rolled back aid not simply to control spending but, as he frequently stated, "to restore the traditional role of parents and students in financing college costs" (Bennett 1985).

Command central for this radical shift was the Reagan White House. From the perspective of Education Secretary Bennett, Office of Management and Budget director David Stockman and others in the White House and D.C. think tanks, students receiving aid (whether subsidized loans or grants) were undeserving Americans (Saunders 1983; Thompson 1985; Bennett 1987). Branded "tax eaters" by the Administration and its allies, students were regarded almost no differently than people receiving food stamps or unemployment insurance, the indigent on Medicaid, or the elderly in need of Medicare. They were all fiscal parasites and a drain on the economy. "We were going to pull those leeches off the backs of decent, hardworking people," wrote Bennett's predecessor Terrel Bell, who oversaw the drastic cuts in the first Reagan Administration but was let go because hardliners thought him too soft on the aid question (Bell 1988, 75). (Tax-eater believers like William Bennett and OMB's David Stockman did not deny that education was a valuable investment. They just deemed it primarily a personal or private—not societal—investment.)

The tax-eater mindset would translate into a set of fiscal and education policies bent on restoring traditional family values by first making parents and their children financially accountable for their college education and less reliant on government assistance to defray tuition costs. What policymakers failed to anticipate, however, was the impact of wage stagnation on the American family. As wages froze, household debts rose, and

family savings dried up, more students were forced to turn to loans. According to a Federal Reserve Survey of Consumer Finances, between 1983 and 2001 student loans as a share of household debt increased from 28 to 58 percent (Dynan, Johnson, and Pence 2003).

Reagan Administration policies would also provide the private sector a roadmap to fees in student lending. Reagan's policies initiated the very first set of consumer fees on student loans: origination fees. Originally created to help offset the costs of tax cuts and reduce the national debt, the origination fee was an activation charge of 5 percent to set up each guaranteed student loan (Naegele 1983, 607). Origination fees increase the final loan amount because the fee is rolled into the principal and repaid with interest. Although introduced as a temporary measure, origination fees are now a permanent fixture for all student loans. As one onlooker bristled at the time, these dollars will never be "seen or available for expenses, yet it must be repaid with interest" (Ozer 1986, 26).

By the 1990s, the federal cuts would have a cascading effect nationally, as most states began following Reagan's budgetary template, reducing public expenditures on higher education in an effort to lower state costs (Mumper 1998; McLendon, Hearn, and Mokher 2009). With government doing less, the students' share of the cost of education spiked (Hossler, Lund, Ramin, Westfall, and Irish 1997). Students and universities had to pick up the tab in the form of ever-higher tuition and fees. Over the next three decades, high-cost, unsubsidized government and private student loans would increasingly fill the void left by the hemorrhaging of state and federally subsidized loan and grant programs.

Work

Like many other consumer expenses, numerous studies have shown that the cost of higher education has outpaced the average family income in recent decades (Mumper 2003; Rhodes 2006; Supiano 2008). The inability of incomes to keep up with expenses is symptomatic of a larger story: household debt, which has risen twice as fast as disposable income since 1981 (Schwartz 2010). By now it is a well-worn story: household debt is nine times what it was in 1981; household debt has risen twice as fast as disposable income since 1981 (Schwartz 2010). Meanwhile, the median wage has actually fallen since 2000—even though workers are laboring harder and better than ever before (Johnston 2011). This increased worker productivity could translate into working only about eleven hours per week; instead, the US worker works longer hours today than at any point in the twentieth century and the United States is the most overworked developed nation in the world. However, hard work has failed to translate into success. By 2007, according to data from the Bureau of Labor Statistics, the typical American worker was 400 percent more productive than in 1950 (Rauch 2000; Miller 2010).

Equally familiar are the strategies that individuals and families have used to make up the gap between income and expenses: working more hours, creating two-earner households as more women joined the workforce, and tapping home equity lines. Yet largely ignored is how the free market has responded to the crisis of middle-class wage stagnation. Perhaps the most ubiquitous response has been the proliferation of payday loan stores. Payday lending emerged to fill the unmet demands of American workers who watched their wages stagnate precisely as too-big-to-fail banks, which once offered retail services like low-interest, short-term loans, went after bigger institutional clients (Huckstep 2007; King and Parrish 2011; Pew Charitable Trusts 2012).

So how does a payday loan work? A cash-strapped customer goes to a local payday loan store and writes a postdated check to cover expenses until his or her next payday (usually in two weeks). The borrower immediately receives the amount in cash minus the so-called transaction fee. The loan has to be repaid in full out of the borrower's next paycheck, otherwise the borrower must assume another loan plus interest and the cost of the transaction

fee. Through the fees associated with payday loans, the free market has managed to trap the American worker further in debt (Peterson 2000; "Mayday for Payday Loans" 2007; Parrish and King 2009). It is not uncommon for a borrower to wind up paying as much as $800 for a $325 loan. Paying in full and on time is rare. As one 2009 study showed, 90 percent of borrowers rolled their loans over—not once but at least five times (Parrish and King 2009, 5). Payday lending is, by definition, more closely tethered to income than any other form of consumer credit. Payday borrowers must provide a paycheck stub to verify employment and income, unlike charge card borrowers, for example, where a stay-at-home spouse, a child, or even family pets have been known to have lines of credit.

How Payday Lenders Game the System

Nearly every state forbids usurious rates (Francis 2010). At the federal level, it is a crime to lend money at rates more than double the state's usury rates, which many states cap at 36 percent (Chin 2004). So how have payday lenders gotten away with charging exorbitant interest rates? Their success lies in the ability to game the system in four basic ways. First, payday lenders mask the true cost of their loans. In particular, unlike other lenders, they fail to disclose the annual percentage rate (APR) (Chin 2004). An APR is the total interest charged on principal to be paid in a year divided by the balance due. In other words, the APR is the agreed upon yearly rate of return on the money that is borrowed. By not disclosing the APR, payday lenders appear to be in blatant violation of the Truth in Lending Act (TILA), a law passed in 1968 to make loan pricing more transparent for the consumer by requiring the cost of all loans to be calculated on the same basis, the APR. A consumer not calculating the cost of a loan based on APR might assume a payday loan is less expensive than, say, a credit card cash advance.

Payday lenders have skirted disclosing APR for good reason: doing so would expose how expensive payday loans are compared to other short-term credit transactions such as a cash advance from credit cards (Center for Responsible Lending 2001). APR matters for a two-week loan. Let us say both the credit card company and payday lender are quoting an interest rate of 18 and 15 percent, respectively. If a payday loan is priced on a non-APR basis (calculated biweekly on payday), it would appear to be the cheaper option (15 percent) to a credit card (18 percent), which uses exclusively an APR. But when both disclose the APR, as required by TILA, the actual costs of the loans are clearer: The cost of the credit card cash advance remains 18 percent while the payday loan—after multiplying the 15 percent times twenty-six two-week terms—skyrockets to 390 percent (Center for Responsible Lending 2009).

Second, payday lenders successfully gamed the system through the so-called strategic alliances with banks. The Gramm–Leach–Bliley deregulatory law, passed in 1999, allowed federal insured depository institutions to enter into strategic alliances by contracting out their government-issued charters to payday lenders. Gramm–Leach–Bliley allowed retail banks to merge with other large-scale financial institutions like investment banks and insurance companies, something these institutions had been unable to do since 1933. The ability to merge also meant that government-backed banks could now enter into these alliances with high-risk financial entities such as payday lenders.[6] Banks entered into these business relationships despite payday loans' reputation as the most hazardous of all consumer financial products, with two out of three payday borrowers defaulting on their first loan (Skiba and Tobacman 2008). Two thirds of payday borrowers incur five or more payday loans per year (Ernst, Farris, and King 2003). For the payday lender, these strategic alliances or the so-called rent-a-bank charter agreements freed them from tougher state usury laws. That is because, under federal law, banks with national or state charters are empowered to preempt state usury laws and

thus could export interest rates using the bank's location regardless of the usury caps that may exist in the borrower's home state (FDIC Advisory Committee on Banking Policy 2009). In exchange for their charters, banks were often promised returns on their investments in payday loan companies above 20 percent, or about double the return on traditional investments (Check-N-Go 2001).[7]

Third, many payday lenders gamed the system through the risks associated with these strategic alliances. Strategic alliances posed a high risk for banks because it relied on borrowers who often went into default. Traditionally, banks lent money to borrowers who were expected to repay loans in full plus interest upon maturity. Payday lending turned traditional banking practice on its head, however—as the most profitable transactions came not from repaying the loan but, instead, rolling it over upon maturity; this triggered a whole new set of fees and expenses to be incurred by the borrower and created a highly profitable revenue stream for the creditor. While certainly profitable in the short run, these loans posed long-term problems. Finding themselves trapped in a spiral of debt, borrowers would be unable to pay their creditor (payday lender), which in turn would be unable to offer dividend payments to their investors (the bank). In part for this reason and alarmed at the spread of these strategic alliances, federal financial regulators admonished Congress and banks that the payday lenders' debt-based business model exercised anything but traditionally sound banking judgment.

These strategic relationships not only exposed banks to "risks associated with payday lending," as regulators warned the CEOs of all national banks (Comptroller of the Currency Administrator of National Banks 2000; Hodson, Owens, and Fritts 2003). Left undisturbed, regulators concluded, payday lenders would "pose a variety of safety and soundness, compliance, consumer protection, and other risks to banks" (Comptroller of the Currency Administrator of National Banks 2000). Ultimately, because these banks were federal insured institutions, they also posed a heavy risk to taxpayers. Such threats to our national economy were hiding in plain sight, especially since the debt-driven business model of payday lending had gone viral and now infected too-big-to-fail banks. Big banks would stop partnering with payday lenders on renting out their charters by the mid-2000s. Nevertheless, four of the nation's largest banks (Wells Fargo, Citigroup, Chase, and Bank of America), with assets controlling nearly 50 percent of US GDP, would continue exposing US taxpayers by extending billions of dollars of credit to high-risk payday lenders—an industry whose business model is predicated on their customers' inability to make payments.[8]

Fourth, it would have been impossible for the payday lending industry to trick the regulatory system, trap tens of millions of Americans in debt, and then have taxpayer bailed-out banks extend credit to publicly held payday lenders without the help of lawmakers. Since the problem was first introduced in the well of the House of Representatives in the late 1990s, Congress has tended to be more of a problem than the solution. For nearly a decade, a passive Congress preferred to look the other way despite repeated warnings from regulators, a growing number of consumer advocates, and even the Defense Department itself (Center for Responsible Lending 2001; US Department of Defense 2006). Clearly, money played some role. Payday lenders more than doubled their spending on lobbying and campaign contributions during mid-2002 to combat calls by the military, consumer advocates, and regulators for greater oversight. Within the financial service sector, payday lenders were second only to bankers in the amount spent on lobbying and campaign contributions (Salmon 2010; Citizens for Responsibility and Ethics in Washington 2012).

Thanks to policymakers, payday lenders were able to game the system—dodging and neutering antiusury laws dedicated to protecting consumers while passing deregulatory

legislation, like laws allowing rent-a-banks, that ensured the buck ultimately stopped with the American taxpayer.

Payday Loans and the Middle Class

America's middle class help to keep payday lenders in business. By 2008, there were over 24,000 payday lenders and similar high-cost check-cashing outlets, challenging the myth that these lenders cater solely to the American working poor and others living on the fringe of the nation's financial system. In 2011, the average approved online payday borrower earned above $50,000 annually, higher than the median household income ($46,242) for the entire United States (Pew Charitable Trusts 2012). Studies of payday lending conducted by university economists since the early 2000s have routinely showed that middle-class consumers are a critical part of the customer base, with three out of four borrowers possessing a high-school diploma or some college education (Moore 2001; "Claremont McKenna Professor Responds" 2005). A study of over 700,000 online payday loan applicants showed 45.2 percent of payday borrowers owned their own homes in 2010.[9] "The only common denominator is that our customers [have] steady sources of income and bank accounts," stated Darrin Anderson, president of the industry's largest trade association, the Community Financial Services Association (Schlein and Medsker 2008; "Community Financial Services Association" 2008). Consumer finance debt has become an inescapable part of daily life in America; nothing captures this better than the statistic that payday lending stores now outnumber Starbucks and McDonalds, establishments that our national business and political leaders once regarded as barometers of modern-day, middle-class consumption (Stegman 2007; Francis 2010; Martin and Longa 2012).

The Impact of Payday Lending

Despite the heavy demand for payday loans, this free-market cure proved at least as bad as the original cause. The average payday lender traps already financially strapped customers in a cycle of debt, largely by levying interest charges that range between 391 and 443 percent for a payday loan (King, Parrish, and Tanik 2006; Martin and Longa 2012). Such high-cost charges strip working- and middle-class households of hundreds of millions of dollars each year (Ernst, Farris, and King 2003; King, Parrish, and Tanik 2006). In the aggregate, these charges end up reducing the money retained and circulated in local economies. The above estimates of the net effects of payday lending even take into account the offsetting positive impacts the industry has on local spending, employment, and reinvestment in business. Not even the military has escaped the predatory practices of America's most ubiquitous usurious lenders. In fact, service personnel are three times as likely to assume a payday loan as the average consumer; such loans account for 70 percent of losses in security clearances for service members (Stegman 2007).

Payday lending offers a window into how deregulation has contributed to exposing the nation's entire financial system to unsafe banking practices and systemic risk. The difficulty was not simply that deregulatory laws like Gramm–Leach–Bliley opened the way for strategic alliances with banks, which exempted payday lending from state oversight. By providing the implicit federal guarantee that went with rent-a-bank deals between payday lenders and federally-insured banks, lawmakers (and D.C. regulators) also ensured that the American taxpayer would be the one held accountable for the reckless lending practices of too-big-to-fail lenders. The story of payday lending's proliferation may be the best place to start for those wishing to understand how reckless lending and unsound financial practices spread throughout the economy, from Main Street to Wall Street.[10]

Transportation

Despite the higher profile of other financial products, nowhere is a de facto, hidden consumer tax more commonly assessed but so little discussed than in the realm of auto insurance. For nearly 90 percent of American households, the vehicle linking the above three areas of consumer finance—housing, education, and employment—is, quite literally, the automobile (McGuckin and Srinivasan 2003).[11] The car is the most commonly held nonfinancial asset in America and, second only to a home, the most durable goods and necessity that consumers purchase. By law in almost every state, one's car must be insured.[12] Relatively speaking, then, in the world of financial services, policy makers should hardly consider lenders to be the most advantaged and promoted class. That privileged perch should logically be reserved for the auto insurance industry, which occupies a unique and protected status within the US economy: it offers a service that people are required by law to purchase, yet it is provided exclusively by the private sector on a for-profit basis. This public–private collusion resulted in skyrocketing premiums for insured motorists by the mid-1980s (Cummins and Tennyson 1992).

Auto insurance also serves as a useful reminder that when discussing the wealth gap it may be helpful to include "accumulated effects of repeating the same pattern" (Lynch 2011, Si–Sv). These patterns tend to have a "dramatic [impact] on a consumer's overall financial picture" (Lynch 2011, Sv), though they too often are overlooked in favor a big-ticket, single expenditures. "People drastically underestimate how much wealth they will amass" because of small (if repeated) household decisions (Lynch 2011, Sv). Patterns that exacerbate the wealth gap might be particularly instructive in the zero-sum world of auto insurance, where there is an active and on-going transfer of wealth in the form of discounted insurance rates from one pool of insured drivers to another.

Auto Insurance and Zip Codes

Because auto insurance rates are based on place of residence (zip code) rather than driving record (the so-called territorial rating system, or TRS), higher rates are often borne by those motorists least capable of paying them. For example, drivers with urban zip codes in the populous northeast and mid-Atlantic states may pay as much as $800 more each year than their fellow suburban drivers (Preston 1998; Levick 1999). Over the lifespan of a typical motorist, this can translate into a loss of more than $40,000. This estimate is relatively conservative; in California, postal code profiling is estimated to cost good drivers as much as $974 each year, the lifetime expenditure of the "deserving" motorist who has no accidents or tickets is even higher (Consumers Union 2005; Kristof 2012; Hirsch 2012). With many motorists simply priced out of the market, the result is a skyrocketing number of uninsured. The shrinking risk pool means higher premiums for the insured. This shifts a greater financial burden from the undeserving motorist (e.g., one with recent accidents and tickets) to the deserving motorist—further widening the wealth gap between insured urban motorists and insured upper-middle-class drivers in suburban areas, where insurance is considerably cheaper.

Unaffordable insurance "is the most common complaint that I hear from my constituents," said a Detroit state representative who served as the ranking member of Michigan's House Insurance Committee (Michigan Chronicle 2009). In the late 1990s, Motor City drivers paid on an average $1,200 more each year than wealthier, whiter suburban residents of the famous housing tract known as Eight Mile Road, just a few blocks north. Insurers contended that rates were legitimate because of auto thefts and risk assessments, but other studies released by the state attorney general's office, based on the review of sixty auto insurance quotes, demonstrated average disparities of up to

17 percent between cities with comparable populations and auto theft rates (Insurance Advocate 2002). Nor is the world's most recognizable zip code immune. Drivers in the world's most famous zip code, Beverly Hills 90210, paid approximately $500 less each year than South Central Los Angeles motorists until 2010, when California became the first and only state to abolish the use of postal codes as a primary factor in determining auto insurance rates (Savage 2006; Consumers Union, Public Advocates and the Foundation of Taxpayer and Consumer Rights, 2006).Changing these rates to reflect a merit-based system in auto insurance would end the current subsidy for insured upper-middle-class and rural drivers now being paid by insured drivers living in urban, working-class neighborhoods (Galster and Booza 2008; Ladika 2012; Patel 2012).

The TRS is anything but transparent. In fact, it is the quintessential example of a TNT fee. Because auto insurers obscure the actual pricing system, drivers often have little clue exactly how much zip codes factor into what they pay. Like the formula for Coca Cola, the insurance industry has jealously guarded their rating recipe, contending that these are industrial trade secrets even though their zeal to protect the formula has raised questions about the veracity of their methods (*Consumer Reports* 2012). Because the public–private partnership creates a captive market, drivers in working-class urban neighborhoods are legally trapped into paying higher rates while subsidizing their wealthier neighbors (Savage 2006; Consumers Union, Public Advocates and the Foundation of Taxpayer and Consumer Rights, 2006). Even after taking into account primary risk factors (moving violation tickets, claim and loss rates) and secondary risk factors (accident and crime location statistics)—both typically used by insurers—redlining (a practice in which a specific geographic area, usually an urban or minority neighborhood, is either excluded or charged higher rates for a loan, insurance, or another financial service) explains more of the gap than the above primary and secondary risk factors in auto insurance premiums between neighborhoods (Stoll and Ong 2008).

Why would the middle- and upper-middle classes back the abolition of postal code profiling in auto insurance? In the movement that launched the consumer revolt, California's Proposition 103, it was precisely this demographic group that backed abolishing the TRS as a primary factor in calculating rates. In particular, it was suburbanites, especially those living in or around larger cities like Los Angeles and San Francisco, who provided the crucial votes for the proposition's passage. Suburbanites backed TRS reform for two basic reasons. First, suburban voters believed that doing so would lead to reductions in their own insurance rates (Fergus forthcoming). Second, a merit-based system appealed to voters' sense of fairness (Fergus forthcoming). Thus, the promise of Prop 103 stemmed from its unifying consumer appeal. The proposition galvanized the average California consumer against moneyed interests in ways that previous initiatives, which often pitted whites and suburbia against racial minorities and the inner city, had failed to do.

Regulatory Capture as De Facto Deregulation

While Prop 103 passed in 1988, it took a generation for its most controversial stipulation, abolishing the territorial rating system as a primary factor in determining rates, to be implemented. Insurers blocked the full implementation of 103 for an entire generation. Their success in stymieing enforcement was due in large part because they waged a stealth campaign against regulation known as regulatory capture, which looked to render the rating system and much of 103 ineffective.

Regulatory capture may occur for a number of reasons, including having regulated firms influencing the appointments or elections of weak and underfunded oversight agencies.[13] The end result is often the absence of toughness in the actual enforcement practices on the markets or industries these regulators are charged with policing (Cooper 2009, 12). This is what unfolded during the 1990s, when Charles Quackenbush, heavily

financed by insurers, won election as state insurance commissioner. An underdog who pulled an upset victory largely because of heavy finance by insurers late in the campaign. As California's chief insurance regulator, Quackenbush enacted a series of measures that appeared more responsive to his financial benefactors than voters: giving insurers greater liberties to base rates on criteria primarily unrelated to driving safety records; rolling back consumer-friendly settlement arrangements; lifting the rate caps twice in three years; and all while actually tightening the tether of rates to where one lived, rather than how an individual drove, namely, by allowing geographical factors like an area's average wage and income levels to compute rates (Fergus forthcoming). Ultimately, even the laissez-faire minded *The Economist* expressed concern about such capture and urged more effective oversight: "Surely it is a little absurd to allow insurance commissioners to raise money from insurers" (The Economist 2000). The use of regulatory capture by which to deregulate may not have been responsible for creating the disparity in rate pricing, but they have certainly helped to perpetuate it by blocking implementation and enforcement of laws designed to make insurance based more on how one drives rather than where one lives.

New Developments

Some of the developments since 2011 have been in the areas of payday lending and student financial aid.[14] In the payday lending industry, perhaps the most significant change has been the rise of bank payday lending. Many of the largest banks have actually become directly involved with making high-interest short-term loans to their bank customers, where the APR is over 300 percent (Carnns 2012). Often called "direct deposit advance loans" by the bank, these loans are thought to contribute heavily to the indebtedness of the bank accountholder. In part because of they are charged usurious rate terms, these bank customers are in debt to their banks for 175 days per year or twice long as the maximum length of time the FDIC advises is appropriate (Center for Responsible Lending 2011). Yet, despite the growing industry practice, banks prefer to keep the practice out of the public and regulators' spotlight: "You're never going to walk into a store and see a poster about this product," Richelle Mesnick, a Wells Fargo spokeswoman told Main Street, an online personal finance publication (Skowronski 2011). Efforts to stay under the regulatory radar have apparently failed, as financial regulators (prompted by consumer groups) have agreed to launch examinations of this latest bank product (Floro 2012; Woodruff 2012). One thing seems clear, however: bank payday lending underscores how a once stigmatized financial good is fast becoming a product of necessity for banked, but cash-strapped, middle-class Americans who have not benefitted from real wage growth since the 1970s.

Remarkably, payday lenders and their supporters in Congress continue their efforts to bury their historic role in America's financial unraveling, evinced in their collective opposition first to Dodd–Frank finance reform law and now to the implementation and enforcement of the new Consumer Financial Protection Bureau (Roth 2012). Their efforts to block these regulatory reforms is an effort to protect its profits and continue to make money. Yet, burying their past (and current) business relationships with Wall Street is central to the payday lending industry's project of circumventing oversight.

The news appears a bit more sanguine regarding college financial aid. During its first term, the Obama Administration has signaled a new direction, most significantly pushing for and signing the Health Care and Education Reconciliation Act in March 2010. This act helps student borrowers in four important ways. First, it eliminates fees paid to the so-called middlemen private banks that used to act as intermediaries between the government and students receiving federally insured student loans. This change is expected to save student loan recipients an estimated $68 billion over the next 11 years.

Second, for those with federal student loans, the legislation lowers the loan repayment caps to 10 percent (down from 15 percent) of their monthly discretionary income. Third, it doubles funding for Pell grant awards by pegging it to inflation and adding 820,000 more grants by 2020. Fourth, the act provides loan debt forgiveness after 20 years for on-time borrowers (Baker and Herszenhorn 2010).

This act has been complemented by the work of the newly created Consumer Financial Bureau. The CFPB, in cooperation with relevant federal agencies like the Department of Education, has engaged a two-prong approach targeting consumers and lawmakers. For consumers, it launched a financial literacy campaign via a recently released report as means to raise greater awareness about student-borrower about the traps of private loans (United States Consumer Financial Protection Bureau and US Department of Education 2012). For lawmakers, the CFPB has issued recommendations to Congress, as charged by Dodd–Frank, about best regulatory practices to rein in private student loan abuses throughout the life of the loan, including fuller and less complicated initial contacts with prospective borrowers, improving underwriting and eligibility standards, and more flexible bankruptcy protections for private loan borrowers (Chopra 2012).

Conclusion

As Sherraden explained to a *Washington Post* staff writer in the spring of 1990, asset-building programs "are intended to help low-income Americans get what most Americans strive for: a college education or vocational training, a home, and a secure retirement [income]" (Spencer 1990). However, in recent decades, financial fracking has become more visible and pronounced in the very conveyances—homeownership, education, and employment, as well as the related expenses of transportation—Sherraden and other pioneers of asset building have shown are key to upward mobility. Central to this kind of wealth extraction has been the erosion of consumer protections—a casualty of financial deregulation since the 1980s. The loss of regulatory oversight has wrought profound change in the financial services marketplace, a sector that has become the lifeblood of the American economy over the last three decades. While a free-market economy produces a society of winners and losers, at no point in the memory of the vast majority of Americans has the wealth gap between the rich and the rest been so wide. To see a similar level of income disparity, one must return to 1917 (Saez 2012, 2). The financial elite, especially the so-called working rich (e.g., hedge fund managers, Wall Street CEOs, and financial entrepreneurs), have been among the biggest beneficiaries. This group has been abetted by financial deregulation as well as a kinder, gentler tax code, which has rolled back progressive taxation through lower marginal rates and a spate of tax loopholes and deductions. The take-home income gap has been especially pronounced since the 1980s. According to a Congressional Budget Office report, the share of income received by the top 1 percent grew from about 8 percent in 1979 to over 17 percent in 2007 (US Congressional Budget Office 2011).

These winners, ever in search of new markets, have forged new business models designed to extract wealth from the working poor and, increasingly, middle-income Americans.[15] Deregulating some businesses did yield cost-controlling benefits for consumers, if not necessarily workers, especially in such industries as airline, trucking, and telecommunications (Wilentz 2008, 194–200).[16] Yet the net result of financial deregulation has been a rising tide that has sunk most American boats. By the mid-2000s, the typical American earner had suffered a 72 percent drop in discretionary income compared to their counterpart in the early 1970s (Warren 2006). The discretionary income of today's families is being eaten away by a surfeit of fees and charges in areas central to upward mobility: housing, higher

education, transportation, and employment. For lower-income households, these fees further undermine the ability to build assets and so exacerbate the wealth gap.

Financial deregulation has had a big impact on consumer finance. Financial deregulation has been used by public–private partners to facilitate access, opening up markets, services, and products to heretofore excluded or under-served communities: women, racial minorities, lower-income, youth, and immigrants. However, inclusion has come at ever-higher costs of entry precisely to those consumers who are least able to afford to pay it. Deregulation and the rise of usurious fees suggest the brokenness of the broker state.[17] The contemporary broker state has lost its way over the last four decades, departing from its traditional course and role of serving as broker for the middle-class and working poor consumers to now entitling and advancing the wants and demands of the working rich. When the broker state did seek to check potentially predatory or abusive behavior of financial service elites, the state's preferred method of choice was almost always the carrot of enticements (tax credits or deferred interest, low-cost loans, etc.) over the stick of enforcement.

The crisis of the broker state, the growing complexity of the marketplace, and the decline of leisure time over the past generation have all put today's consumer at a distinct disadvantage in the financial marketplace. The newly created Consumer Financial Protection Bureau is a starting place to repair and modernize the broken broker state, so that it once again functions on behalf of working and middle-class consumers to end the fracking of wealth and assets that has come to define the financial services' relationship with the American consumer.

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Notes

1. The rich, bipartisan recent history of asset building for the poor tends to be overlooked (Seidman 2001). For example, HUD Secretary Jack Kemp actively promoted asset building by low-income households during the George H. W. Bush Administration. The first Individual Development Account (IDA) bill was introduced in the House by Tony Hall (D-OH) and the Senate by Bill Bradley (D-NJ). As a presidential candidate, Bill Clinton endorsed IDAs in 1992 and then included them in his early welfare reform proposal in 1994. Republicans in the House (John Kasich of Ohio) and Senate (Dan Coats of Indiana) were sponsors of IDA and have been credited for the inclusion of IDAs in the Welfare Reform Act of 1996. Thereafter, JC Watts (R-OK) and James Talents (R-MO) proposed family development accounts as part of the American Community Renewal Act. For more, see Laurence Seidman, "Assets and the Tax Code" in Thomas Shapiro and Edward Wolff, eds. *Assets for the Poor* (NY: Sage, 2001), 338.
2. This figure is based on a 2002 Association of American Medical Colleges Questionnaire; for a more recent argument, see Bach, Peter B., and Robert Kocher. "Why Medical School Should Be Free." *The New York Times* May 28, 2011; Ladapo, Joseph. "What's Debt Got to Do With It? Student Debt Seen as Nagging Influence on Residency Decisions." Harvard Medical School. May 2, 2008; Prep, Veritas. "Weigh Medical Student Debt, Specialty Choice." *US News and World Report* June 20, 2011.
3. For more on the case, see *Perdue v. Crocker National Bank,* 702 P.2d 503 (Cal. 1985).
4. This provision was confirmed by a 1996 unanimous Supreme Court decision in *Smiley v Citibank*—whereby the Rehnquist court ruled that fees were in essence interest rates and did not need to adhere to the consumer protection laws of the states where bank customers resided, effectively allowing rates to be exportable across state lines. Unfettered from the

various state usury laws, fee-based income (or simply fee income) began its rapid ascent in the consumer credit industry. Those affected first were bank credit card issuers. According to Robert Manning, thanks largely to *Smiley*, "Penalty fee revenue has climbed from $1.7 billion in 1996 to $7.3 billion in 2001. The average late fee has jumped from $13 in 1996 to $30 in 2002. Incredibly, combined penalty ($7.3 billion) and cash advance ($3.8 billion) fees equaled the after-tax profits of the entire credit card industry ($11.13 billion) in 2001." One regional bank's total, nonfinance-related revenues jumped from $28.98 million in 1994 to $31.57 million in 1996 (new fee structure imposed in second half of the year), then to $73.03 million in 1997 and then to $76.03 million in 1998 when it was acquired by FirstUSA credit card company (Bank One). During this period, for example, returned check fees for this regional bank jumped from $200,000 to $2.85 million. Statement by Robert D. Manning, "Hearing on 'Role of FCRA in the Credit Granting Process'" on Financial Institutions and Consumer Credit, House Financial Services Committee, June 12, 2003.

5. Inflation increased by 75 percent between 1978 and 1984. During the same period, total Pell dollars at traditional two- and four-year institutions increased by 52 percent and 69 percent, respectively. For more information, see Lee (1985).
6. See "Check-N-Go" Payday Lender Advertisement in the *American Banker* Newspaper March 21, 2001, p. 7.
7. For more information, see "An Update on Emerging Issues in Banking" from FDIC, January 2003.
8. For more information, see "Utilities and Payday Lenders: Convenient Payments, Killer Loans." A National Consumer Law Center Report, June 2007; "Choosing the Road to Prosperity: We Must End Too Big To Fail—Now." *2011 Annual Report*, Federal Reserve Bank of Dallas; and "An Update on Emerging Issues in Banking" from FDIC, January 2003.
9. Based on a study of 736,369 online applicants who applied between June 10 and July 11, 2010. Of those applying, the average annual salary was $41,753, and nearly 50 percent were homeowners. See "Payday Loan Industry Report 2010 Statistical Analysis of Pros and Cons." Prepared by PersonalMoneyStore.com, September 2010.
10. Not that the payday lending industry was vital to the lifeblood of America's financial economy. After all, borrowers receive only $38.5 billion in these short-term loans each year, an amount that barely registers a blip on the nation's financial radar. The idea that payday lenders have an impact on the larger economy and are partly responsible for the financial crisis has been listed by the group's trade association as one of the fifteen great myths told about the industry. However, payday lending—which even more than the subprime mortgage market has a debt-based business model at its core—reveals a story impossible to tell elsewhere: how the reckless and unsound financial practices of shadow banks have infected mainstream banks. For additional information, see Jessica Silver-Greenberg, "Payday Lenders Go Hunting." *Wall Street Journal* December 24, 2010; "About the Payday Advance Industry: Myth vs. Reality" at the trade association website.
11. This includes 87.9 percent of households that drove to work, see chapter 1. National Summary of "Journey to Work." Census Transportation Planning Products.
12. Within the United States, 47 of 50 states have compulsory vehicle insurance laws. De facto insurance liability coverage in the form of proof of indemnification—via the uninsured paying an additional motor vehicle fee (Virginia) or posting a special cash bond (Mississippi and New Hampshire)—must be demonstrated by motorists in the three states where it is legally permissible to drive without buying any auto insurance.
13. Other forms of regulatory capture are identification with the industry and sympathy with the particular problems of the firms efforts to meet standards, see Toni Makkaiand John Braithwaite, "In and Out of the Revolving Door: Making Sense of Regulatory Capture." *Journal of Public Policy* 12(January 1992): 61–78.
14. There have certainly been major developments in rulemaking regarding auto insurance and mortgage markets. However, space and time constraints prevent a fuller discussion of the latest changes in these two critical spheres.
15. For more discussion of equity stripping of today's middle class as well as some potential pitfalls of asset building, see Robert Hiltonsmith, "The Retirement Savings Drain: The Hidden and Excessive Costs of 401(k)s." Demos (2012). According to Hiltonsmith, the average 401(k) account holder loses $155,000 in fees and loss earnings over the life of the plan.

16. For a more critical view of deregulation in nonfinancial industries, see, for example, Phillip Longman and Lina Khan, "Terminal Sickness." *Washington Monthly* March/April 2012, and Leah Platt, "Predatory Pricing" *The American Prospect* December 19, 2001.
17. For an excellent primer on the rise and traditional role of the broker state, see Alan Brinkley, "Prosperity, Depression, and War" in Eric Foner, ed. *New American History* (Philadelphia: Temple University Press, 1997), 147–8.

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Part II
Pathways to Asset Building

Chapter Five
The Widening Racial Wealth Gap: Why Wealth Is Not Color Blind

Thomas Shapiro, Tatjana Meschede, and Sam Osoro

Researchers began to explore the wealth holdings of households by race in the mid-1980s, when data became available for the first time. The magnitude and implications of these early findings were shocking: most found that, on average, black households owned only a dime for each dollar of wealth owned by white households (Lui, Robles, and Leondar-Wright 2006). This difference was much larger than the prevailing income gap of 60 cents-to-the-dollar. More alarmingly, the racial wealth gap has increased further since it was first analyzed. Our analysis reveals an increase of $151,000 in the absolute racial wealth gap between 1984 and 2009. This chapter empirically examines the main reasons behind the rise in the racial wealth gap over the past 25 years, deepening the analytic and policy understanding and narrative required to effectively disrupt and reverse this trend.

It is critical, initially, to set forth the context for the racial wealth gap discussion: why it is important, what it tells us about the state of material racial inequality, and a brief conceptual detour exploring the difference between examining absolute gaps and analyzing the pattern of an increasing gap.

Existing Research on Wealth and the Racial Wealth Gap

A Paradigmatic Shift from Income to Assets

Information regarding household wealth and liabilities has been available for the United States only since the mid-1980s. Prior to the first reports analyzing household wealth in the late 1980s, family income provided the standard, taken-for-granted lens for understanding economic racial inequality. This severely skewed our understanding of the causes of racial inequality—and our efforts to redress it—toward labor market factors. Bringing family wealth into the picture changed the paradigmatic understanding of racial inequality for economics, history, sociology, public understanding, and policy. This change took place in an era in which great pride was taken about the fact that apartheid had been overcome legally and accompanied by changing individual attitudes. But from this point on, the traditional liberal narrative about race in America would never be the same.

The taken-for-granted benchmark for material racial inequality, income, tells us that the typical African American family earns between 54 and 61 cents of income (depending on the year) for every dollar of income earned by typical white families (Shapiro 2004).

By shifting the lens to family wealth, the first empirical analyses showed that, in 1984, the typical African American family possessed between five and ten cents of wealth (depending upon the measure of wealth) for every dollar of wealth owned by typical white families (Shapiro 2004). This vast wealth disparity has policy and historical implications beyond those raised by income alone and suggests more complex and nuanced prescriptions for achieving social and racial justice.

Including family wealth as a critical economic resource necessitated a qualitative shift in the pursuit of democracy and equality. The discussion now needed to focus not simply on addressing a much larger disparity but also on extending the analysis of what brought us to the starting points that were so vast. Traditional understanding and policy approaches had to push beyond market dynamics and human capital to a more comprehensive understanding of how history impacts the present, how state policy impacts the generation and growth of individual wealth, how wealth is accumulated differently by various population groups and in different historical eras, how family wealth is generated and used, and the enduring significance of contemporary institutional dynamics in American life.

The analytic and policy trajectories come from two directions. One trajectory springs from the groundbreaking work of Michael Sherraden's 1991 book, *Assets and the Poor*. Sherraden's legacy in the asset field, as all roads in the current asset field, leads from his scholarly work and his genius for demonstration projects and strategic research combined with tireless, tenacious, and gracious advocacy for asset building. The robust applied and policy agendas built from Sherraden's inspirational work center on poverty alleviation, social mobility, and well-being. Universal, inclusive, and progressive policy features are at the core of these bold and aspiring efforts. The second trajectory comes from an equity perspective and is anchored in sociology, economics, critical legal theory, social policy, and movements for social change. The work of Oliver and Shapiro in the late 1980s and culminating in 1995 with *Black Wealth/White Wealth* set the foundation for a new and challenging understanding of racial inequality in America in the post–Civil Rights era. Analyzing the racial wealth gap forced us to move beyond the uncritically accepted formulaic consideration that equal opportunity leads directly to equal results. It raised fundamental questions about rewards from and distribution of achievement: Was it possible for African Americans to earn their way out of the racial wealth gap? To educate their way out? Or marry their way out? Or thrift their way out? Or even save their way out?[1]

A paradigm shift of sorts has resulted from this body of work that conceptualizes wealth as a fundamental anchor both for sustaining inequality and enabling economic well-being. Today, no serious discussion of poverty, inequality, or racial inequality can take place without a thorough understanding of the role of family wealth. For example, in 1990, Oliver and Shapiro introduced the concept of "asset poverty," defined as the lack of economic resources to support one's household in the absence of income.[2] This helped transform the standard paradigm that equated poverty solely with an absence of sufficient income. We now turn to what we have learned about wealth and race since the mid-1980s.

Qualitative Studies of Wealth

The early studies of family wealth in the United States were quantitative and largely descriptive, documenting levels of wealth inequality. As we began to grasp the enormity of wealth inequality, something we had all "known" but could not quantify before these first studies, some scholars began to gather qualitative data, through in-depth interviews with families. Attention now turned to how families accumulate wealth, the meaning wealth has, and how families strategically employ wealth as emergency savings or to leverage mobility. Questions of class, race, life course, and gender differences spurred much

of this work. Qualitative studies began to reveal the dynamics driving advantage and disadvantage, and driving the racial wealth gap in particular.

Wealth provides a matrix of resources for families to plan residential, homeownership, career, and schooling decisions. The family interviews show that families with adequate resources can act on these decisions, which often are framed in terms of the advantages they provide for their children and family. Families hold similar aspirations about education for their children and similar desires to live in safe, healthy, and fostering neighborhoods, but wealth makes a substantial difference in families' ability to achieve these aspirations. The interviews clearly show how wealth provides different sets of resources to meet similar sets of aspirations. Those without adequate resources attempt to compensate and navigate opportunities through kin, community, credit cards, and creative means.

Interviews with families also highlight the way they use wealth to plan for economic and social mobility. Some young families are fortunate to have "transformative assets" (Shapiro 2004). These assets are transferred across generations through inheritances and family financial assistance and provide resources for social and economic mobility. For example, a young couple may receive money from their parents for a downpayment on a home that they otherwise could not afford. As a result, the couple may have access to better-resourced communities and richer educational environments for their children; transformative assets enable families to access resources or to achieve a status that they would otherwise be unable to achieve based on their income alone. In other words, this wealth assistance has the capacity to lift a family beyond its own achievements (Shapiro 2004). Families of color have little opportunity to receive these sort of transformative assets.

Quantitative Studies of Wealth and the Wealth Gap

Measuring Wealth and the Wealth Gap

Most quantitative analyses of the racial wealth gap measure wealth as total net worth, which includes the sum of all financial assets as well as equity in business and one's own home and deducts debt from this amount. Another approach deducts the value of home equity from total net worth. The argument for not including home equity relates to the different nature of the full extent of housing wealth that needs to be replaced when tapped into (Shapiro, Meschede, and Sullivan 2010). In constructing asset poverty, for example, some continue to include home equity in their calculations and some exclude it. The issue is about the liquidity of home equity, having to replace housing, and the debt entailed by tapping home equity.

The racial wealth gap has typically been measured in two ways. A common method is to compare the absolute difference, in dollars, between the median wealth holding of whites and the median wealth holding of blacks. This approach is called the absolute racial wealth gap. A different approach is to show the racial wealth gap in relative terms, with a ratio. For example, as noted above, in 1994 the median African American household owned 10 cents of wealth for each dollar owned by the median white household. Both the absolute and the relative approach may be used to show changes in the racial wealth gap over time.

Data and Analytic Techniques

Researchers examining the wealth holdings of US families have traditionally relied on three major national surveys that contain validated wealth measures: the Survey of Consumer Finances SCF conducted by the Federal Reserve Board, the Survey of Income and Program Participation SIPP conducted by the US Census Bureau, and the Panel Study of Income Dynamics (PSID) conducted by the University of Michigan. The SCF

is a cross-sectional survey that collects data from a representative US sample every three years. In contrast, both SIPP and PSID collect information from households over time: SIPP follows households up to four-years period, and PSID has followed the sample families, their children, and their grandchildren since 1968.

Much of the existing analysis is cross sectional.[3] That is, researchers examine family wealth at a single point in time. Cross-sectional data may be used to compute a dollar figure and a ratio illustrating the black–white wealth gap. The numbers vary somewhat, depending on the data set and measures used, but there is consistent evidence of a large black–white wealth gap. By using different samples of cross-sectional data, we can compare changes in the racial wealth gap over time.

Cross-sectional data may also be used in multivariate analysis attempting to explain the huge black–white difference. We can attempt to discern the relative importance of historical, demographic, ascriptive (inherited), institutional, policy, and achievement factors. In existing multivariate studies, although the significance levels on individual variables like income are quite compelling, the amount of the racial wealth difference explained is small. This pattern implies either that the social science models remain theoretically thin, that the survey data do not capture deeply embedded historical, institutional, or policy factors, or that the large unexplained variance is a residual attributed to race. We suspect that the second factor is particularly important, that is, the fact that the data do not adequately capture deeply historical, policy, and institutional dynamics.

Evidence of a Rising Racial Wealth Gap

A plethora of studies have documented the rising racial wealth gap. In 2010, the Institute on Assets and Social Policy released a research brief that tracked the wealth holdings of white and African American working-aged families between 1984 and 2007 (Shapiro, Meschede, and Sullivan 2010). During this 23-year time period, the absolute racial wealth gap increased fourfold, from $20,000 to $95,000. Moreover, high-income white households experienced significant gains in wealth over this time period, while high-income African American households gained less than middle-income white households. The latest SCF data also show a widening of the racial wealth gap in absolute terms: In 1998, the average net worth of white households was $100,700 higher than that of African Americans. By 2007, this gap had increased to $142,600 (Shapiro 2009).

The impact of the Great Recession on the racial wealth gap is most closely documented by the Pew Research Center study released in July 2011 (Kochhar, Fry, and Taylor 2011). Over the four years of the Great Recession (2005–2009), median net worth decreased by 16 percent for white households. African American households lost much more: 53 percent of their median net worth was gone after the Recession, and the white–black wealth ratio had increased from 12 in 1984 to 19 in 2009. Hispanic households lost even more, experiencing a 66 percent decline in median net worth. The Pew study further reports that between 2005 and 2009 homeownership rates remained at 74 percent for white households but dropped slightly for African Americans, from 47 percent to 46 percent, and dropped from 51 percent to 47 percent for Hispanics.[4]

State of the Art: Empirics and Narrative

Perhaps remarkably, the metrics of the racial wealth gap have not been challenged seriously. That is, we cannot find in the literature, and we have not experienced in public speaking and writing, any contestation regarding the choice of metrics. Certainly, the numbers vary depending upon the survey, the measure of wealth, and the year in which

the data are drawn. However, the pattern has been clearly established. For net worth (including housing wealth), the ratio hovers around 0.15; for a liquid definition of wealth that excludes housing wealth, the ratio hovers around 0.10.

While the empirical foundation of the racial wealth gap is apparently unassailable, the narrative interpretation is highly and provocatively contested. We often think of the racial wealth gap as a sort of racial Rorschach test where everyone ventures to "know" why the gap exists and then asserts his or her own theories. Indeed, $106,500 represents a large gap, and many claims about factors that contribute to it will have some level of accuracy. The challenge that remains is to connect the racial wealth gap to an evidence-based narrative that accounts for the largest drivers of the gap. Any of us who ventures into a public discourse regarding the racial wealth gap has, no doubt, been met with responses like, "I know how to close the gap, get married before having children"; "the gap will close when blacks stop buying designer sneakers at the mall and save"; or "the gap will close when blacks work hard"; and so forth. The task before us, and one this chapter begins, is to rigorously and analytically identify the largest drivers of the increasing gap, connect it to a compelling narrative, and begin impacting public understanding and policy development.

New Evidence of the Escalating Racial Wealth Gap

In this chapter, we adopt a longitudinal approach, examining the trajectory of the racial wealth gap by following the same set of families from 1984 to 2009. The data cover a quarter of a century and the course of a generation of American families moving through educational institutions, communities, work and family life, and policies—in short experiencing American life. This approach conceptually moves the research from an examination of different starting points to a critical look at the impact of American life on the racial wealth gap. To be clear, we believe that this approach also moves the balance of the analysis away from differential starting points of history toward contemporary institutions, policy, and community. This is not an either-or dichotomy; rather it allows us to better connect the historical legacy to contemporary dynamics.

In order to track the same households over time, we use PSID data from 1984, when wealth data were first collected, through 2009, the latest year data were available. Because we are interested in changes to wealth holdings over time, we limit our analyses to households of working age (25–55 years old) in 1984 who were also present in 2009, thereby eliminating any households lost due to attrition over the 25-year survey period.[5] The final study sample includes 1,188 white households and 486 African American households.[6] Because in the latter years of the study period these adults are older, on average, than a sample representative of the entire US population, their median wealth holdings are greater than those reported in studies using cross-sectional data sets. Despite these particularities, the data offer an extremely powerful means to track the experience of families over time, which can help us understand the specific impact of broader socioeconomic trends.

For the families in our sample, we present two measures of total wealth: net worth and net worth minus home equity. Net worth is the sum of the following seven components:

- home equity;
- other real estate, not including the primary home;
- vehicles, such as automobiles, motor homes, and boats;
- farm or business assets;
- stocks, mutual funds, investment trusts, and stocks held in Individual Retirement Accounts (beginning in 1999, IRAs are their own category of wealth);

- checking and savings accounts, and certificates of deposit (CDs), treasury bills and savings bonds; and
- trusts, life insurance, and valuable collections.

Noncollateralized debt (credit cards, student loans, medical loans, and loans from family members) is subtracted from the sum above to derive the total net worth variable. We use the Consumer Price Index to adjust all dollar amounts to 2009 values.

We begin our presentation with descriptive information depicting trends in median wealth for white and African American households between 1984 and 2009 (appendix 5.1 presents the data used to create figures 5.1–5.8). Figure 5.1 shows very different trends by race: In this time period, median net worth for white households increased from close to $100,000 in 1984 to more than $300,000 in 2007 just before the Great Recession. The median net worth of white families then declined to about $265,000, mostly due to the decline in stock values and housing prices. In the same time period, median net worth of African American households rose from close to $6,000 in 1984 to $36,000 in 2007 and fell to $28,500 in 2009. Thus, the absolute racial wealth gap grew from $85,000 in 1984 to $265,000 in 2007 before it narrowed to $236,500 in 2009.

Figure 5.2 presents median wealth excluding home equity (NW-HE) for the same time period. Again, the data show that the absolute racial wealth gap increased consistently between 1984 and the advent of the Great Recession, growing from $30,000 in 1984 to $123,000 in 1997, and then decreasing slightly to $106,500 in 2009. During the entire 25-year period, net worth excluding home equity grew by 244 percent for the median white households, while it grew only 110 percent for the average African American household.

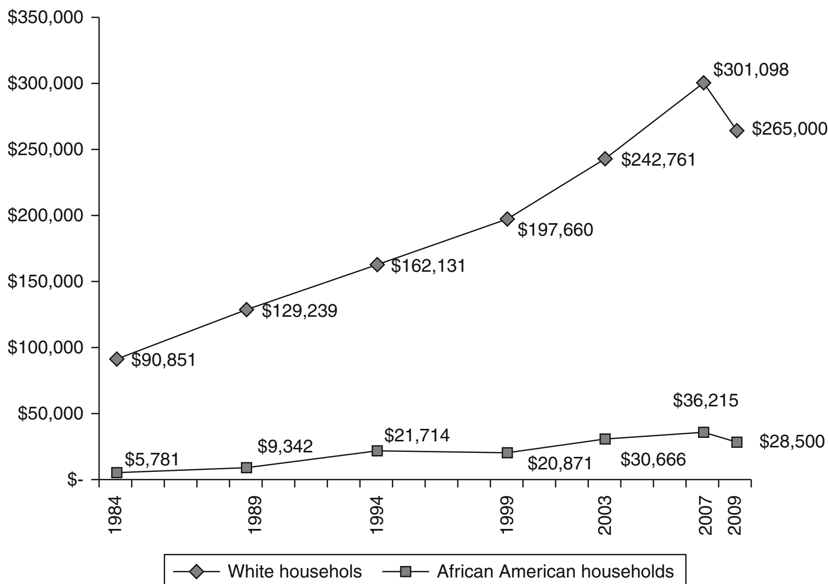

Figure 5.1 Median net worth of 1984 working-age households, by race, 1984–2009 (in 2009 dollars).

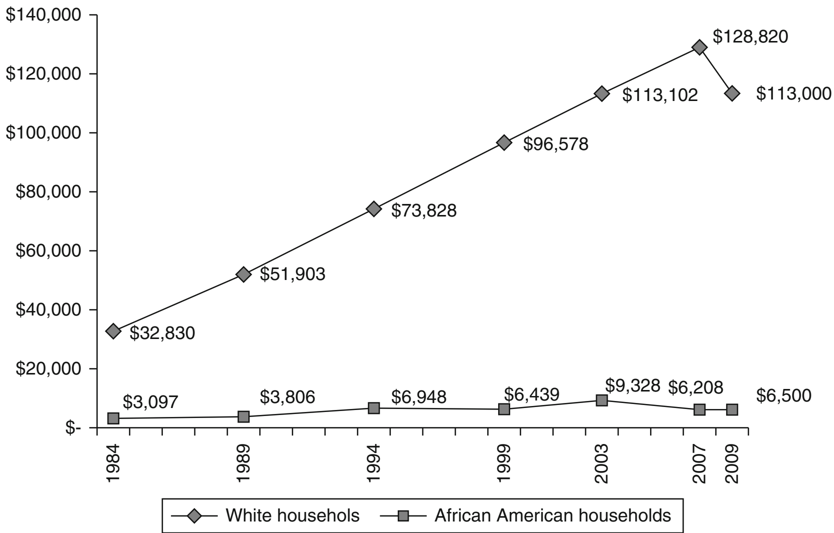

Figure 5.2 Median net worth excluding home equity of 1984 working-age households, by race, 1984–2009.

As shown in figures 5.1 and 5.2, differences in home equity contribute substantially to the racial wealth gap. While the absolute racial gap in 2009 amounts to $235,500 for total net worth, it is $106,500 for net worth minus home equity.

Housing wealth is a primary component of net worth for everyone, but it makes up a greater portion of assets for African American households than for white households. In 2009, housing wealth comprised 57 percent of total net worth for white and 77 percent of total net worth for African American households. In 2009, African American households had only $6,500 in nonhousing wealth, at the median, with 50 percent of them having less. The impact of housing wealth on total wealth will be further explored in the next section.

Income and Wealth

Our next analyses examine the role that income may play in explaining the widening racial wealth gap. As we know, the racial income gap has been about 0.6:1.0, that is, the average African American person earns 60 cents for every dollar earned by the average white individual. We also know that income is highly related to wealth for a number of reasons; for example, children of wealthy families have access to better education, thus higher incomes, and individuals with higher incomes have more money to set aside for investments, home purchase, and retirement savings.

We divided households into three income groups based on their average income over the 25-year study period, a technique that levels income fluctuations over the entire study period and reduces the impact of shocks such as unemployment. We then estimated median wealth holdings for each income group by race. Depicted in figures 5.3 and 5.4 are median net worth and median net worth excluding home equity for high- and middle-income white and African American households.[7]

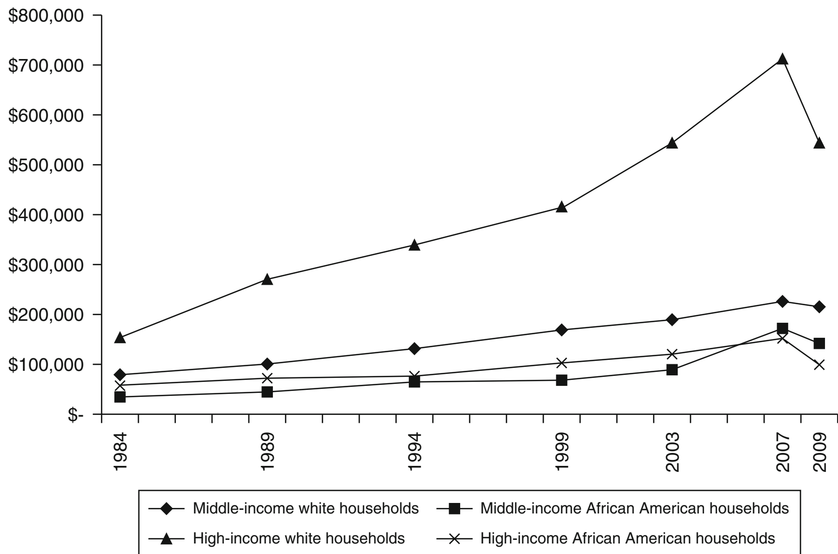

Figure 5.3 Median net worth of middle- and high-income White and African American households, 1984–2009.

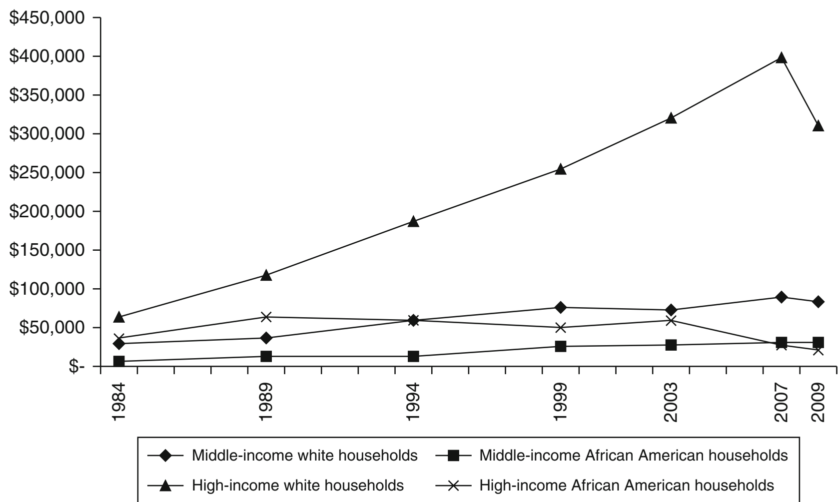

Figure 5.4 Median net worth excluding home equity of middle- and high-income White and African American households, 1984–2009.

In both figures, high-income white households show the greatest wealth accumulation over a quarter century, increasing their net worth from $155,000 to over $700,000 in 2007 and their net worth excluding home equity from $63,000 to close to $400,000. The Great Recession had an impact, decreasing their net worth sharply by 2009, to levels similar to those in 2003. A large portion of these declines is probably due to the dramatic fall of the stock market, and these losses may be temporary. In stark contrast, African American households accumulated very little wealth over the 25-year period, regardless of their income group. In fact, white middle-income households added more to their household wealth than high-income African American households, increasing their net worth from $77,000 in 1984 to $216,000 in 2009, and their net worth excluding home equity from $27,000 to $83,000 (appendix 5.1). Although high-income African Americans had, in 1984, more net worth excluding home equity than middle-income white households did, by 1999, they had more than $60,000 less than their middle-income white counterparts. By 2009, the average middle-income white household had more wealth than a high-income African American household.

Investigating the Major Drivers of the Widening Racial Wealth Gap

To further explore the factors that contribute to the widening racial wealth gap, we perform a series of multivariate regression analyses.[8] These analyses allow us to examine a number of predictors explaining the rise or decline of wealth for the median household and test the impact of race on wealth (see appendix 5.3 for more details).

We focus on the following predictors: household characteristics (age, marital status, and the number of children), employment characteristics (income, unemployment spells, and type of work), and wealth-related variables (homeownership and receipt of inheritance). Our work indicates that, over the 25-year study period, the most important predictors behind the rising racial wealth gap were as follows: (1) income, (2) homeownership and home equity, and (3) intra family transfers, such as inheritances. In the following, we examine these findings more closely.

The Role of Income

In many studies (e.g., Chang 2010; Conley 1999), income is more strongly correlated with wealth than any other observed variable. Clearly, those with higher incomes have the opportunities to set aside greater resources for investment in retirement, education of their children, and their homes. However, as shown in figures 5.3 and 5.4, higher income does not translate into the same wealth accumulation for African Americans as it does for white households. Our regression results tell a similar story: Each dollar increase in income translates into about five dollars of wealth for white households (at the median) and only about 70 cents for African Americans. Increased income (measured as average income over the 25-year period) is critically important to build wealth for both groups, yet the same earnings boost magnifies the racial wealth gap sevenfold. Another way to understand this magnitude is that simply to keep pace in terms of wealth, African Americans need income increases of seven dollars for every dollar increase in income for whites.

One of the biggest takeaways thus far is that increases in income do not build wealth the same for whites and blacks. Part of the reason for this disparity may be greater downward income mobility for initially high-income African Americans, compared to their white counterparts. Figure 5.5 shows income mobility by race, by plotting average income between 1984 and 2009 against income in 1984, for both races. A larger proportion of white households who were in the high-income category in 1984 remained high income

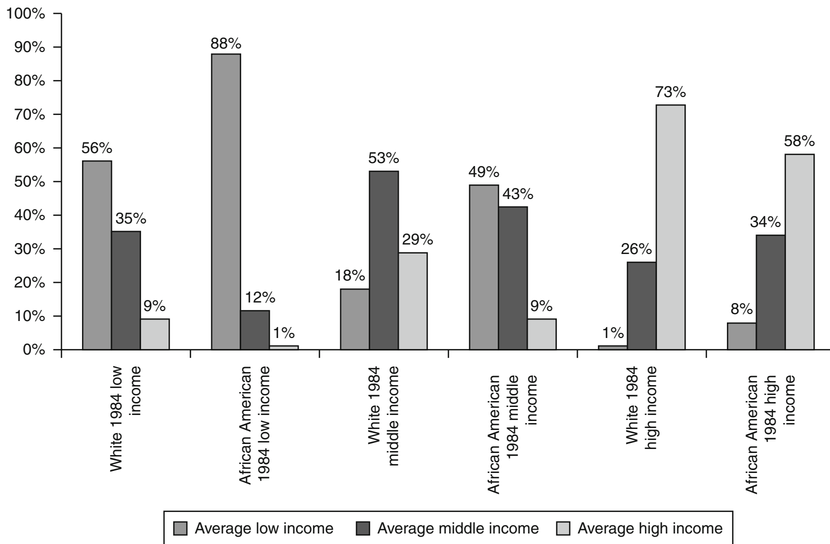

Figure 5.5 Movement between income categories, 1984–2009, by race and income in 1984.

on average over the 25-year study period (73 percent, compared to 58 percent of African American households). Conversely, 88 percent of African American households who were in the low-income category in 1984 remained low-income compared to 56 percent of low-income white households. This finding is wholly consistent with previous work showing the comparative inability of middle-class African Americans to sustain achieved status and pass it along to their adult children (Oliver and Shapiro 1994).

The Role of Homeownership

Homeownership is another major driver behind the racial wealth gap. Historically, homeownership rates have been much higher for white than African American households (Joint Center for Housing Studies 2012).The same patterns hold true for the households in our 25-year study. Homeownership rates were highest for both groups in 2003 when 88 percent of white households and 61 percent of African American households owned their home. By 2009, these rates had dropped, but they did not do so evenly. For whites, there was a one percentage-point decline to 87 percent, but for African Americans the homeownership rate fell 4 percentage points to 57 percent (figure 5.6). In addition, 51 percent of white households owned a home throughout the entire study period, and only 4 percent never owned a home. In comparison, 22 percent of African American households owned a home throughout the period, and 26 percent of African American households never owned a home.

During the same time period, the absolute racial gap in home equity also increased (figure 5.7). For most of the study period, home equity increased substantially, for both groups. Between 1984 and 2007, the median value of home equity for white households increased 109 percent from $74,500 to $156,000. For African Americans, median home equity rose 106 percent, from $33,000 to $68,000. With the recession, however, home equity declined, decreasing 11 percent between 2007 and 2009 for white households and 17 percent for African American households. As a result, the racial home equity gap grew from $41,000 in

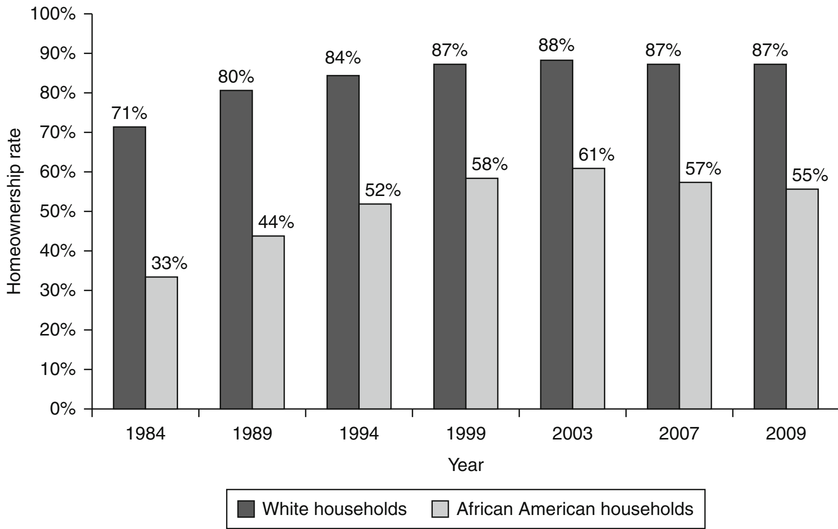

Figure 5.6 Homeownership rates by race, 1984–2009.

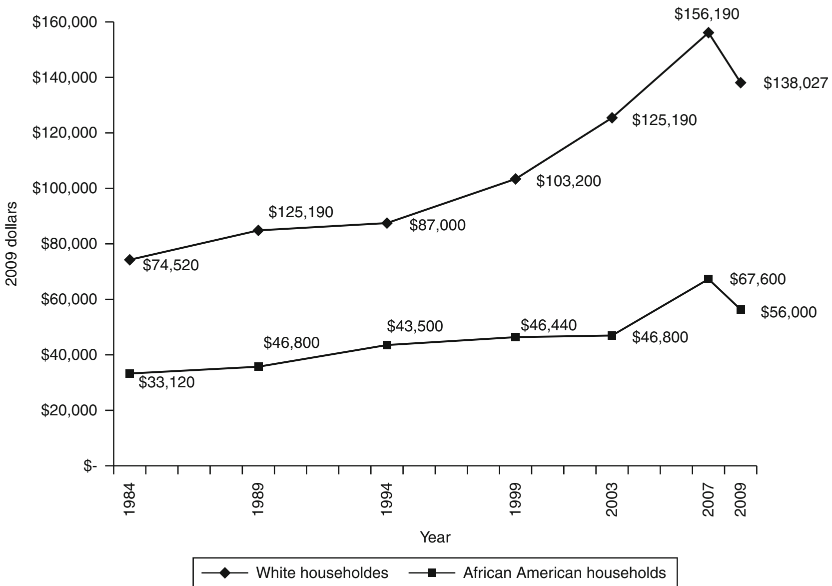

Figure 5.7 Median home equity by race.

1984 to $82,000 in 2009. Part of the differential increase in home equity is caused by residential segregation intersecting with the growth of home values. We know that many more white households live in more racially homogeneous neighborhoods in which many saw a rapid increase of their home values before the 2008 downturn (Shapiro 2004). There is also ample evidence that many more households of color faced foreclosures of their homes, resulting in a tremendous loss of wealth (Center for Responsible Lending 2012).

We examined changes in wealth for families who moved from renting to owning, and from owning to renting, over the study period, in the quantile regression analyses (see appendix 5.2 for more details). Results of this analysis are different for white and black households. Black households experienced substantial gains in overall wealth when they purchased a home at some point during the 25-year study period; the wealth of white households did not significantly increase due to the switch from renting to homeownership, and this reveals the important role of home purchase and successful homeownership in building economic security for African Americans. For African Americans, the number of years of homeownership is also statistically significant at the median, while it is not for white households. Both groups experienced statistically significant wealth losses when they sold their home at some point during the 25-year study period.

The Role of Inheritance

Intergenerational transmission of wealth contributes greatly to growing wealth for those who are fortunate to be at the receiving end. Inheritances are a significant driver in the growth of the racial wealth gap. Among white households, who tend to have more wealth

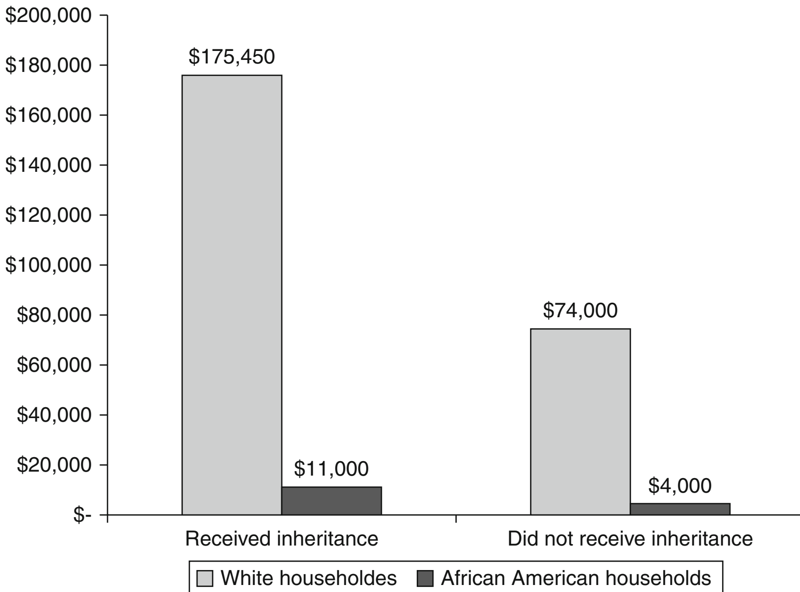

Figure 5.8 Median net worth (in 2009) (excluding home equity) for households receiving any inheritance or monetary support (1984–2009) by race.

to share with their relatives, close to two in five reported receiving monetary supports or an inheritance during the 25-year study period. Slightly less than one in ten African American households reported any form of inheritance or monetary support. Such monetary supports or inheritances increase the wealth holdings of the beneficiaries. It is not surprising then to find that white households who have received any inheritance have far greater wealth than African American households who received an inheritance and all households who did not receive any inheritance or monetary support (figure 5.8).

The multiple regressions reveal additional complexities. Intergenerational transfers (gifts that are $10,000 and above) in form of inheritances or monetary supports are highly significant for whites; every dollar of inheritance is associated with a 90 cent increase in wealth. For African Americans, these transfers are statistically insignificant contributors to wealth. However, ongoing smaller gifts (below $10,000) are important contributors to wealth growth at the median for both groups.

Income, homeownership, and large monetary gifts are large drivers of the widening racial wealth gap. We also tested the impacts of often discussed causes of the differential wealth growth for whites and African Americans, including family composition and number of children and found that these have little, if any, effect at all. In fact, getting married over the 25-year study period improves median wealth for white households (by about $75,000 over 25 years), while it has no significant effect for African Americans.

Moving from Analysis to Narrative and Policy Development

The march toward democracy in United States history has incorporated civil rights and legal equality for people of color; however, the great challenge of achieving economic equity has been far more difficult. Because of a long history of slavery and Jim Crow laws—and currently, as our data demonstrate, different rewards for similar achievements—the racial wealth gap has been structured through policy, practice, and institutional arrangements. It has always been with us, yet in an era of legal equality and supposed equal economic opportunity, the gap has grown significantly. The threefold increase in the gap has been overall further exacerbated by the Great Recession, which highlights both the need for households to have assets and the vulnerability of people of color. The widening of the racial wealth gap is ironic perhaps given the belated recognition of family financial assets as a prime means for family well-being, economic security, poverty alleviation, and social mobility. The assets perspective and movement are new and are still developing a robust policy agenda. The irony is that the gap has widened in the context of important asset policy advances such as IDAs, FSS, more progressive asset exemptions, and greater public awareness of current reverse Robin Hood tax code and policy.

Closing the racial wealth gap is critical for the economic, political, and moral health of the nation. The benefits would be manifold, especially if the gap can be closed, in the context of increasing family wealth and security for all. However, there should be no illusion about the challenges involved in closing the racial wealth gap. We are convinced that it is indeed possible to make significant strides in closing the gap and that our analysis might serve as a guide for sustained policy development, organizational practices, and institutional reform needed to address the harm of an increasing gap and begin the long-term project of closing it.

This work helps us identify the levers required to close the racial wealth gap and assure growing prosperity for all. Following the same households for 25 years and identifying the largest drivers of the increasing wealth gap highlight the importance and complexities of labor markets, institutional arenas, policy, and inheritance. Increasing incomes contribute to wealth accumulation, yet the dynamics operate so differently that the returns to wealth are far greater for whites than African Americans.

As we seek to identify the critical next steps in narrative and policy development, our work must be informed by empirical analysis. However, specific policy choices should also be informed by many voices and considerations. Three primary empirical findings from our work carry large implications for narrative and policy development. First, income may be the most complicated driver to fashion policy around. Clearly, rising incomes is a powerful generator of family wealth. However, the finding that each dollar increase in income translates into about five dollars of wealth for white households (at the median), but only about 70 cents for African Americans means that we must dig much deeper than earnings and the context of African American labor force participation.

Second, homeownership and the home equity that results clearly is a major generator of wealth for both groups. However, perhaps because the starting point for black wealth is so low and home equity is a larger part of their portfolio, it is significant for blacks and not for whites. While not a vindication of all policies attempting to spread homeownership, it seems evident that making homeownership affordable needs to remain at the center of policy development. Just as clearly, though, the housing and foreclosure crisis contains many lessons and cautions, and we need to be smarter in fashioning future policies promoting homeownership.

Third, in many ways the most uncomplicated finding concerns inheritance and family support. Among whites fortunate enough to receive family wealth, the reward is nearly one-to-one; a dollar inherited is a dollar of additional wealth. For African American wealth generation, the prevalence of intergenerational transfer is small, and family support (smaller, annual giving) plays a critical role. Family wealth is critical to enable first-time homeownership and this sort of intergeneration transfer is more common among whites than blacks. There are clear policy implications to promote transformative asset building opportunities for all through mechanisms like matched savings, pension variations, or other strategies. The significance of inheritance and intergenerational transfers for white wealth accumulation and stability is strong enough to warrant a careful look at how policy structures can provide similar opportunities for wealth accumulation for households who do not receive much intergenerational support.

There are a few small policies that can significantly impact the distribution of wealth. However, our current federal tax code includes a number of policies that subsidize individual wealth creation and maintenance. Recent estimates put the "asset-building budget" of the US government at roughly $400 billion a year, with the largest tax expenditures spent subsidizing homeownership (through the mortgage interest deduction) and retirement contributions. These public transfers largely benefit households with higher incomes and greater assets. For example, the wealthiest 5 percent receives 53 percent of the $500 billion asset-building package—$265 billion—while the bottom 60 percent receives only 4 percent (CFED 2010). This is a major way the government redistributes wealth every year to the top of the wealth pyramid. Viewed from a longer time horizon, the federal government spends $5 trillion over ten years to subsidize asset building—and the wealthiest 5 percent receive $2.6 trillion over a decade.

A compelling case can be fashioned for policies that direct resources toward low-and moderate-income households and households of color in particular. It would be more equitable if African Americans, who constitute about 13 percent of the population but receive only 3.5 percent of the asset-building tax expenditures (IASP calculation), received a larger share. If the African American community received a proportional share of these tax expenditure resources, they would be able to access $47.5 billion each year, and almost half a trillion dollars over a decade.

The case for policies that lead to this level of allocation must be evidence driven, highlighting both the main drivers of the increase in the racial wealth gap and holding

ideological and cultural explanations accountable to the data. In conjunction with initiatives and advocacy, and vetted through constituencies, we can weave a common-sense strategic narrative grounded in evidence that explains the racial wealth gap. Policy development then can coalesce and frame a sustained movement for racial justice.

Notes

1. This line of thought and research was developed further by scholars and activists such as Edward Wolff, Mariko Chang, Meizhu Lui, Sandy Darity, Darrick Hamilton, Dalton Conley, Barbara Robles, Betsy Leondar-Wright, Rose Brewer, Rebecca Adamson, Jessica Nembhard, Chiteji Ngina, and others who advance the research and bring a critical wealth perspective to racial and ethnic inequality, wealth inequality, gender inequality, senior economic security, and more.
2. Oliver, Melvin L., and Thomas M. Shapiro. 1990. *Wealth of a Nation: At Least One Third of Households Are Asset-Poor*.
3. In fact, even though the SIPP is a panel in which families are interviewed at several points for up to four years, most SIPP users examine the family wealth data in a cross-sectional manner.
4. The same study highlights the increase in wealth disparities within racial groups: In 2009, 51 percent of total wealth owned by white households was owned by the wealthiest 10 percent of households (up from 49 percent in 2005). In the same year, 67 percent of the total wealth owned by black households was owned by the wealthiest 10 percent (up from 59 percent in 2005).
5. Wealth data were available for 1984, 1989, 1994, 1999, 2001, 2003, 2005, 2007, and 2009.
6. Families are not required to provide data for all waves between 1984 and 2009.
7. When income is averaged across the twenty-five-year study period, the middle-income category includes incomes between $53,461 and $91,150 (2009 dollars); this range is higher than the middle-income range for 2009 ($35,000–75,000) due to older age of this cohort that was of working age in 1984.
8. Due to the uneven distribution of wealth, we ran a series of quantile regressions at the median of the wealth distribution separately for white and African American households.

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Appendix 5.1

Detailed Data Tables for Figures 5.1–5.8

Table A5.1 Median net worth (1984–2009) (figure 5.1)

	1984 ($)	*1989 ($)*	*1994 ($)*	*1999 ($)*	*2003 ($)*	*2007 ($)*	*2009 ($)*
White households	90,851	129,239	162,131	197,660	242,761	301,098	265,000
African American households	5,781	9,342	21,714	20,871	30,666	36,215	28,500

Table A5.2 Median net worth (1984–2009), excluding home equity (figure 5.2)

	1984 ($)	*1989 ($)*	*1994 ($)*	*1999 ($)*	*2003 ($)*	*2007 ($)*	*2009 ($)*
White households	32,830	51,903	73,828	96,578	113,102	128,820	113,000
African American households	3,097	3,806	6,948	6,439	9,328	6,208	6,500

Table A5.3 Median net worth (1984–2009), by income level (figure 5.3)

	1984 ($)	*1989 ($)*	*1994 ($)*	*1999 ($)*	*2003 ($)*	*2007 ($)*	*2009 ($)*
Middle-income White households	77,017	98,616	128,836	169,976	188,309	224,530	215,500
Middle-income African American households	33,037	41,263	65,142	67,991	86,984	170,208	140,000
High-income White households	154,447	269,550	340,186	414,639	542,190	712,908	544,000
High-income African American households	53,685	69,204	71,222	100,441	117,766	151,894	97,500

Table A5.4 Median net worth (1984–2009), excluding home equity, by income level (figure 5.4)

	1984 *($)*	*1989* *($)*	*1994* *($)*	*1999* *($)*	*2003* *($)*	*2007* *($)*	*2009* *($)*
Middle-income White households	26,842	36,678	58,628	75,330	72,292	88,467	82,500
Middle-income African American households	7,020	13,495	14,476	25,239	26,818	31,389	30,000
High-income White households	62,770	117,647	186,017	253,677	319,484	398,360	309,000
High-income African American households	35,102	62,284	57,904	48,933	58,300	27,730	21,000

Table A5.5 Income mobility (1984–2009), by race (figure 5.5)

	Low-income average (percent)	*Middle-income average (percent)*	*High-income average (percent)*
1984 Low-income White families	55	36	8
1984 Low-income African American families	88	11	30
1984 Middle-income White families	18	52	30
1984 Middle-income African American families	49	42	9
1984 High-income White families	1	26	73
1984 High-income African American families	8	35	57

Table A5.6 Percent homeownership 1984–2009, by race (figure 5.6)

Percent of households with home equity	*1984 (percent)*	*1989 (percent)*	*1994 (percent)*	*1999 (percent)*	*2003 (percent)*	*2007 (percent)*	*2009 (percent)*
White families	71	80	84	87	88	87	87
African American families	33	44	52	58	61	57	55

Table A5.7 Median home equity 1984–2009, by race (figure 5.7)

	1984 *($)*	*1989* *($)*	*1994* *($)*	*1999* *($)*	*2003* *($)*	*2007* *($)*	*2009* *($)*
White families	74,520	84,770	87,000	103,200	125,190	156,000	138,027
African American families	33,120	35,465	43,500	46,440	46,800	67,600	56,000

Table A5.8 2009 median net worth (excluding home equity) of families receiving any inheritance or monetary support, by race (figure 5.7)

	Received inheritance *($)*	*Did not receive inheritance* *($)*
White families	175,450	74,000
African American families	11,000	4,000

Appendix 5.2

Regression Results: Quantile Regression of Change in Net Worth 1984–2009, by Race

Table A5.9 Quantile regression of change in net worth 1984–2009, by race

	White families				*African American families*			
	Coeff.	*Standard error*	*T-Stat*	*p-Value*	*Coeff.*	*Standard error*	*T-Stat*	*p-Value*
Years of homeownership	1,681.43	1,041.00	1.62	0.107	**1,447.49**	**214.51**	**6.75**	**0.000**
Rent to own	−1,062.65	17,035.30	−0.06	0.950	**2,7340.64**	**4,152.32**	**6.58**	**0.000**
Own to rent	**−97,513.26**	**30,672.11**	**−3.18**	**0.002**	**−39,158.08**	**8,090.91**	**–4.84**	**0.000**
Large transfers	**0.91**	**0.05**	**16.72**	**0.000**	0.20	0.11	1.83	0.069
Support	**0.35**	**0.09**	**4.05**	**0.000**	**0.51**	**0.15**	**3.31**	**0.001**
Average income	**5.19**	**0.09**	**55.17**	**0.000**	**0.69**	**0.08**	**8.69**	**0.000**
College in 1984	16,233.26	14,508.47	1.12	0.263	−2,838.01	7,388.50	–0.38	0.701
Unemployed	−-181.97	219.44	−0.83	0.407	15.41	36.13	0.43	0.670
Age of head	146.40	972.64	0.15	0.880	−7.23	264.42	−0.03	0.978
Children in 1984	−4,916.20	5,758.52	−0.85	0.393	−135.33	1,290.71	−0.10	0.917
Single to married	**75,635.21**	**18,396.43**	**4.11**	**0.000**	4,368.66	4,324.02	1.01	0.313
Married to single	16,289.04	17,472.11	0.93	0.351	−2,497.12	4,453.51	−0.56	0.575
Retired by 2009	4,015.38	15,912.34	0.25	0.801	502.31	4,554.33	0.11	0.912
Constant	-253,399.50	43,107.17	−5.88	0.000	−13,657.01	11,492.56	−1.19	0.235
Pseudo *R*-square				0.1345				0.1437
Number of observations				1188				496

Source: Panel Study of Income Dynamics.

Appendix 5.3
Regression Variables

Table A5.10 Regression variables

Dependent variable	*Description*
Change of net worth, 1984–2009	Difference 1984 and 2009 net worth in 2009 dollars
Independent variable	*Description*
Years of homeownership	Number of years of homeownership 1984–2009
Rent to own	Dummy variable if household rented a home in 1984 and owned a home in 2009
Own to rent	Dummy variable if household owned a home in 1984 and rented a home in 2009
Transfers (1984–2009)	Total amount of large gifts and inheritances transferred to household over $10,000 between 1984 and 2009
Support (1988–2009)	Total amount of cash transferred, of any amount to household between 1988 and 2009
Average income (1984–2009)	Average household income between 1984 and 2009, in 2009 dollars
College in 1984	Dummy variable if head of household had a college degree in 1984
Unemployed (1984–2009)	Number of weeks unemployed between 1984 and 2009
Age of head in 1984	Age of head of household between 25and 55 years old in 1984
Children in 1984	Number of children in family unit under the age of 18 in 1984
Single to married	Dummy variable if head of household was single, divorced or separated in 1984 and married in 2009
Married to single	Dummy variable if head of household was married in 1984 and single, divorced or separated in 2009
Retired by 2009	Dummy variable if head of household was retired any time before 2009

Chapter Six
The Promises and Pitfalls of Homeownership

Carolina Reid

In 1990, as Michael Sherraden was writing *Assets for the Poor*, the homeownership rate in the United States hovered around 64 percent, and concerns about the vitality of the US housing sector were growing. The 1980s had seen a drop in overall homeownership rates, in part due to stagnant incomes and declining affordability, and the Savings and Loan banking crisis had shaken the public's and policymakers' confidence in the financial stability of home mortgage lending institutions. Racial and ethnic gaps in homeownership also loomed large; in 1989, only 42 percent of African Americans and 40 percent of Latinos owned their own home, compared with nearly 70 percent of non-Hispanic whites (Wolff 2001). Thus, the 1990s ushered in a renewed attention to homeownership policy, one that produced a wide range of initiatives designed to expand access to credit, and, in particular, to promote homeownership among lower-income and minority families.

Today, many suggest that these efforts were a failure. After reaching a high of 69 percent in 2004, the US homeownership rate had fallen back to 66.1 percent by the end of 2011, eroding much of the gains achieved during the 1990s. Between three and five million families have already lost their homes to foreclosure, and defaults remain at historically high levels (Bocian et al. 2011). Collectively, US households have suffered an estimated $10 trillion decline in wealth, and the wealth gap between African Americans and whites is larger than it has been on record (Pew Research Center 2011; Shapiro, Meschede, and Osoro, chapter 5, this volume). The lesson that some want to take from these trends is that promoting homeownership was a flawed policy goal; indeed, a small number of voices have led a loud chorus that government efforts to expand homeownership among historically underserved groups were, in fact, the cause of the crisis. This "zombie narrative" has held remarkable purchase in the contemporary debate over the future of the US housing finance system, despite the fact that there is no credible evidence to support it (Immergluck 2011).

Yet there are lessons to be learned from the crisis that can inform how to support sustainable homeownership. Rather than focus exclusively on the failures of the last five years, we should consider more fully the promises and pitfalls of homeownership for lower-income families. A great deal of knowledge has emerged over the last 21 years about what it takes to do homeownership right. The assets field, in particular, has shown that government policies and subsidies shape how families save and acquire assets, and has demonstrated that

when these policies are targeted effectively, the benefits can extend to even those with the lowest incomes. However, the persistent widening of wealth inequality suggests that much more needs to be done if the end goal of homeownership policy is to help lower-income and minority families build assets. In many ways, efforts to close the homeownership gap have had to "swim against the tide"[1] of much larger private market forces and public policy reforms. From the deregulation of financial markets to the shrinking of the social safety net, these trends have increased the vulnerability of lower-income and minority families to economic shocks and have mediated the potential returns to homeownership.

This chapter begins by reviewing trends in homeownership for lower-income and minority families over the past two decades, distinguishing between the "boom" experienced between 1990 and 2004 and the "bust" period after 2005. The second section looks at the evolution of low-income homeownership policy, focusing specifically on the efforts in the 1990s to expand access to credit and how that created new opportunities for families to become owners and subsequently build wealth. The third section summarizes the research on the benefits of homeownership for lower-income families, and outlines what has been learned about the components of sustainable homeownership. In the final section, the chapter explores the pitfalls of the dual mortgage market and raises questions about how to help families better manage the risks associated with homeownership and create a more inclusive housing finance system capable of promoting responsible and sustainable homeownership in the years ahead.

Trends in Homeownership Rates

Over the last century, the US homeownership rate has seen two significant periods of growth (figure 6.1). The greatest expansion of homeownership occurred after World War II, prompted by rising prosperity, changing demographics, as well as a host of government policies in the 1930s and 1940s designed to stimulate the housing sector.

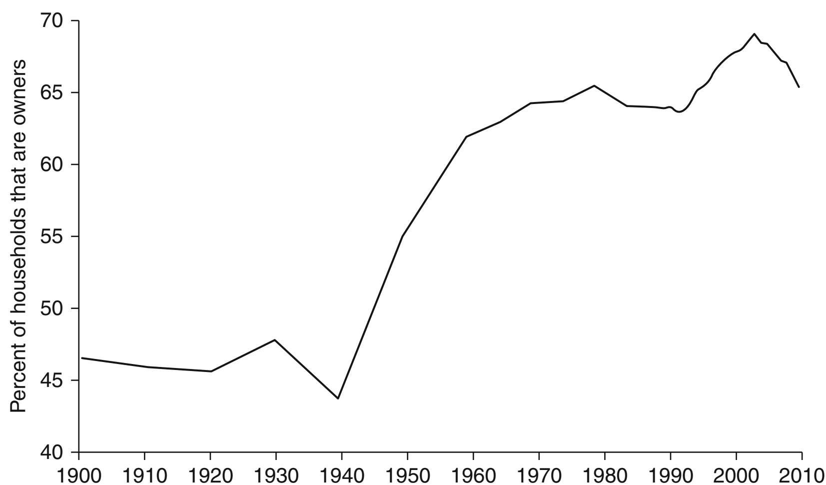

Figure 6.1 The US homeownership rate, 1900–2012.

Source: Data from 1965 to 2012 come from Current Population Survey/Housing Vacancy Survey, Series H-111 Reports, Bureau of the Census, Washington, DC 20233. Data for 1960 and earlier are from the Historical Census of Housing Tables.

Importantly, the establishment of the Federal Housing Administration and the emergence of fully amortized, government-insured long-term mortgages greatly expanded access to credit, and the US homeownership rate grew from 44 to 60 percent in just two decades. Between 1970 and 1990, however, the homeownership rate remained fairly constant, fluctuating between about 63 and 65 percent for almost a quarter century.[2] Starting in the early 1990s, the rate started to rise again, climbing from 64 percent in 1994 to a peak of 69.2 percent just a decade later. Although smaller than the boom in the 1940s, the growth was quite remarkable from an historical point of view, adding nearly six million additional new homeowners.

Equally remarkable was that, during the 1994–2004 time period, families that had historically been excluded from broad access to homeownership experienced large gains. African Americans saw their homeownership rate rise by 16.1 percent between 1994 and 2004 (from 42.3 to 49.1 percent), compared to only 8.6 percent for non-Hispanic whites. Asians and Latinos also saw significant gains, rising 16.7 and 16.6 percent, respectively (table 6.1). As a result, the homeownership gap between whites and members of other demographic groups narrowed, although not coming anywhere close to parity (figure 6.2).

Table 6.1 The homeownership rate by household race/ethnicity and income, 1994–2012

	Household race/ethnicity				*Household income quintile*				
	Non-Hispanic White	*Black/ African American*	*Hispanic/ Latino*	*Asian/ native Hawaiian*	*Lowest fifth*	*Second fifth*	*Middle fifth*	*Fourth fifth*	*Highest fifth*
1994	70.0	42.3	41.2	51.3	NA	NA	NA	NA	NA
1995	70.9	42.7	42.1	50.8	44.0	56.0	64.3	76.5	86.1
1996	71.7	44.1	42.8	50.8	44.3	56.1	64.9	76.9	86.4
1997	72.0	44.8	43.3	52.8	44.0	57.3	65.5	77.1	87.1
1998	72.6	45.6	44.7	52.6	44.5	56.9	67.1	77.7	87.2
1999	73.2	46.3	45.5	53.1	46.2	57.6	67.1	77.9	87.3
2000	73.8	47.2	46.3	52.8	48.1	58.0	67.6	77.9	87.0
2001	74.3	47.7	47.3	53.9	49.0	58.6	67.4	78.1	87.3
2002	74.7	47.4	47.0	54.6	48.1	58.8	67.2	78.8	88.2
2003	75.4	48.1	46.7	56.3	47.8	58.6	68.1	80.5	89.1
2004	76.0	49.1	48.1	59.8	49.0	58.8	68.9	80.5	90.0
2005	75.8	48.2	49.5	60.1	46.1	58.2	68.8	80.0	89.3
2006	75.8	47.9	49.7	60.8	45.6	59.2	68.2	79.7	88.9
2007	75.2	47.2	49.7	60.0	46.3	58.1	67.3	79.2	88.7
2008	75.0	47.4	49.1	59.5	45.2	57.5	67.2	78.6	87.8
2009	74.8	46.2	48.4	59.3	44.1	57.8	66.5	78.7	88.0
2010	74.4	45.4	47.5	58.9	43.6	55.9	66.8	77.4	87.4
2011	73.8	44.9	46.9	58.0	NA	NA	NA	NA	NA
2012	73.5	43.5	46.4	55.1					

Sources: Data on household race and ethnicity come from the US Census Bureau, Housing Vacancies and Homeownership (CPS/HVS)—Historical Tables, Table 16. Quarterly data are averaged to provide an estimate of the homeownership rate for the year (2012 has only 2 quarters of data). Data from 2002 are revised based on the 2000 Census. Data on household income come from the US Census Bureau's Current Population Survey, Annual Social and Economic (ASEC) Supplement HINC-05.

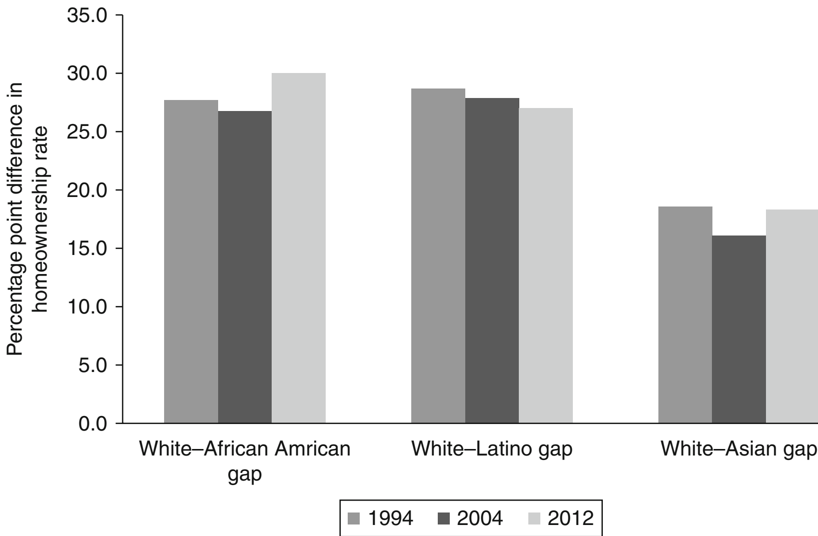

Figure 6.2 The homeownership gap by race/ethnicity.
Source: US Census Bureau, Housing Vacancies and Homeownership (CPS/HVS)—Historical Tables, Table 16.

Lower-income families similarly benefited, with the greatest percentage gains in homeownership accruing to families in the lowest quintiles of the income distribution (table 6.1).

Multiple factors contributed to this sustained growth in homeownership in the 1990s. The period between 1994 and 2004 was characterized by strong economic growth and low unemployment, as well as relatively low interest rates.[3] In addition, the changing demographic composition of the US population contributed to greater household formation and increased demand for homeownership (Chambers et al. 2007). However, research suggests that innovations in mortgage finance (including automated underwriting and other technological advances) were the proximate causes of the rise in homeownership over this time period. In particular, relaxed underwriting criteria expanded access to credit for minority and low-income families (Chambers et al. 2007; Garriga et al. 2006; Retsinas and Belsky 2002).[4] Between 1990 and 2003, home mortgage lending for these groups expanded significantly (table 6.2). While home purchase lending to whites doubled over this time period, for blacks it more than tripled, and for Hispanics it grew fivefold, from just 100,000 loans in 1990 to more than 528,000 loans in 2003. Low-income families (those earning less than 80 percent of area median income) saw a fourfold increase in the number of home purchase loans, compared with just over a doubling of loans for upper-income families (those earning above 120 percent of area median income).

This expansion of mortgage lending for homeownership happened well before the subprime boom of the 2000s, which was characterized by the origination of loans with increasingly exotic product features (such as adjustable rate mortgages [ARMs] with low, "teaser" interest rates and interest-only and negative amortization payment schedules) and the retreat from "tried and true" underwriting practices (including the proliferation of no documentation loans and a lack of attention on the part of mortgage brokers as to whether or not borrowers had the ability to repay the loan). Indeed, the subprime boom did little to increase the homeownership rate among lower-income or minority

Table 6.2 Home purchase loans by borrower race/ethnicity and income, 1990–2003

	Borrower race/ethnicity				*Borrower income*			
	White	*Black*	*Hispanic*	*Asian*	*Low income*	*Moderate income*	*Middle income*	*Upper income*
1990	1,733,981	94,624	100,022	78,345	315,623	231,405	224,897	931,017
1991	1,751,767	95,399	98,529	73,804	376,859	249,722	241,772	882,727
1992	2,022,875	106,581	101,807	76,943	436,459	290,432	273,802	944,572
1993	2,577,772	162,379	157,434	91,369	667,446	397,365	357,115	115,708
1994	2,804,382	218,310	201,456	104,981	767,532	435,902	385,442	1,215,959
1995	2,718,058	240,268	216,049	97,384	738,015	425,398	373,993	1,205,131
1996	2,937,986	247,692	245,026	105,344	868,950	484,434	417,944	1,346,164
1997	2,997,069	257,233	254,382	118,190	920,924	496,160	424,718	1,415,990
1998	3,382,196	279,093	294,639	133,700	1,093,295	565,784	489,784	1,620,469
1999	3,440,868	310,064	348,520	155,442	1,242,787	604,434	512,789	1,684,488
2000	3,225,538	306,672	374,314	168,443	1,191,787	587,010	503,347	1,742,574
2001	3,257,542	285,243	405,809	175,151	1,216,836	606,575	522,344	1,781,596
2002	3,341,732	291,491	449,893	206,909	1,272,024	624,536	540,590	1,855,244
2003	3,717,880	334,658	528,529	240,407	1,347,858	674,030	593,538	2,094,594

Note: Low income equals less than 80 percent of area median income (AMI). Moderate income equals 80–99 percent of AMI. Middle income equals 100–119 percent of AMI. Upper income equals 120 percent or more of AMI.

Source: FFIEC Reports—Nationwide Summary Statistics of Home Mortgage Disclosure Act, 1990–2003 LAR Reports. Data are limited to home purchase loans (not refinance loans) and include both conventional and government insured loans.

households. The largest gains for blacks and Hispanics in the purchase market were in the mid-1990s; by 2000, the growth in purchase loan originations for these groups dropped off significantly. Despite the expanded availability of mortgage credit and the relaxing of underwriting standards between 2004 and 2007, the overall homeownership rate remained flat, and for African American households, it actually declined nearly 2 percentage points, even though this was the period when the volume of subprime lending and Alt-A[5] lending grew substantially (figure 6.3).

Unfortunately, despite many warnings at the local level that there was a link between subprime lending, particularly in the refinance market, and rising borrower distress, the strong performance of the housing sector in 2004 meant that the warnings fell on deaf ears (the Financial Crisis Inquiry Commission 2011). The consequences of not listening have been dire. In the first quarter of 2012, the overall homeownership rate had dropped back to 65.4 percent, where it last stood in 1997. While estimates of the cumulative impact of the crisis vary significantly, some suggest that between eight and thirteen million homeowners will lose their homes to foreclosure (The Financial Crisis Inquiry Commission 2011). A study published by the Center for Responsible Lending found that for loans originated between 2004 and 2008—the peak years of subprime lending—6.4 percent, or more than 2.7 million loans, had ended in foreclosure as of February 2011. Another 8.3 percent of these loans, or 3.6 million households, were 60 or more days delinquent on their mortgage or in some stage of the foreclosure process, and at serious risk of losing their homes (Bocian et al. 2011).

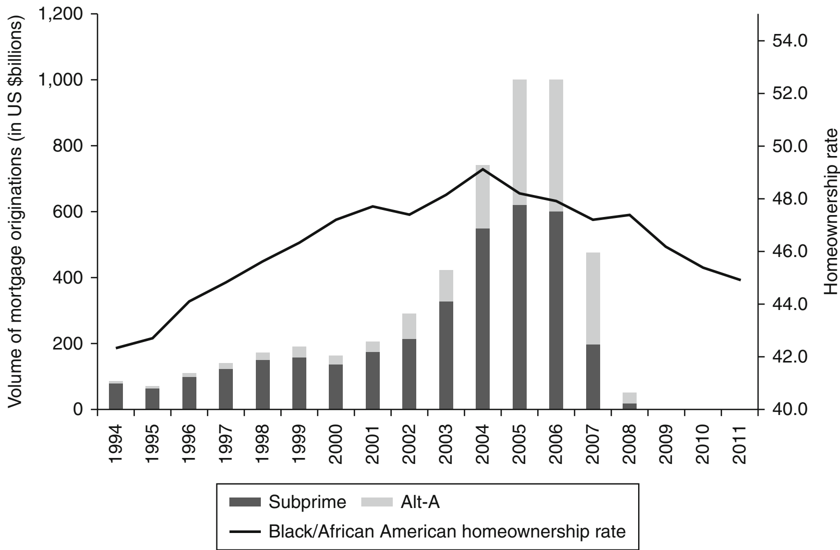

Figure 6.3 The growth in subprime lending and African American homeownership.

Note: Inside Mortgage Finance defines subprime as mortgages that back mortgage-backed securities (MBS) that are marketed as subprime, and Alt-A loans as those that are in an MBS that is marketed as Alt-A.

Source: Data on the volume of subprime and Alt-A mortgage originations come from Inside Mortgage Finance (http://www.insidemortgagefinance.com/). Data on the Black homeownership rate come from the US Census Bureau, Housing Vacancies and Homeownership (CPS/HVS)—Historical Tables, Table 16.

While the crisis has extended into virtually every community, African American and Latino borrowers and communities have been hardest hit. As of February 2011, among African American and Latino borrowers who received loans between 2004 and 2008, 9.8 and 11.9 percent had lost their home to foreclosure, and an additional 14 percent of loans were seriously delinquent (Bocian et al. 2011). This suggests that nearly 25 percent of African American and Latino borrowers who bought or refinanced their homes during the subprime crisis could lose their homes. Lower-income households have also experienced the highest delinquency and foreclosure rates, although the differences by income are less significant than are the differences by race and ethnicity. In large part this is due to who received loans with the riskiest loan product features; in states like Arizona, California, Florida, and Nevada, middle- and upper-income minority borrowers were prime targets for subprime ARMs, and have therefore experienced the highest rates of default (Bocian et al. 2011).

The disparate impact of foreclosures on communities of color has had marked consequences for the homeownership and wealth gaps. Overall, African American households have seen the greatest impacts. At the start of 2012, the African American homeownership rate stood at 43.5 percent, 5.6 percentage points lower than in 2004 before the subprime boom began (figure 6.2). Latinos, who saw a strong increase in homeownership beginning in 1994, have also lost ground since 2004, but their overall homeownership rate of 46.4 percent in the first half of 2012 still represents a significant improvement over the 41.2 rate in 1994. Still, the gap between Hispanics and non-Hispanic whites remains high, at 27.1 percentage points. Asian and Native Hawaiian homeowners seem

to have been less affected by the crisis, although understanding the impact of foreclosures on this demographic group is difficult due to the lack of data that distinguished among different Asian populations. Local evidence suggests that certain Asian and Pacific Islander groups were hard hit. The Asian homeownership rate also dropped quite substantially between 2011 and the first half of 2012, increasing the gap between Asians and non-Hispanic whites (figure 6.2).

While more research is needed to understand how the crisis will play out for different demographic and income groups, an initial analysis of US Census microdata[6] provides some insights. Figure 6.4 examines the intersection of race/ethnicity and income. Lower-income African Americans experienced a 12.5 percent decrease in their homeownership rate between 2004 and 2010, compared to a 5.8 percent decrease for lower-income Latinos and a 6.6 percent decrease for lower-income whites. In contrast, higher-income Latinos saw a 3.6 percent decrease, compared with 1.5 percent for higher-income whites. The data also suggest that the combined impact of the foreclosure crisis and the resulting recession is having the greatest impact on younger households; for all races and ethnicities, the homeownership rate has dropped most for those between 25 and 40 years of age. Strikingly, among African Americans under 35, the homeownership rate dropped 21 percent, from 26 percent in 2004 to just 20 percent in 2010. Younger white households also experienced a considerable drop, but still had a homeownership rate of around 50 percent in 2010.

These trends are troubling, and suggest that the foreclosure crisis could result in a "lost generation" of homeowners of color, with attendant implications for wealth and asset building. Because home equity is such a large component of household wealth for these populations, the foreclosure crisis is likely to exacerbate already wide gaps in wealth. Evidence for

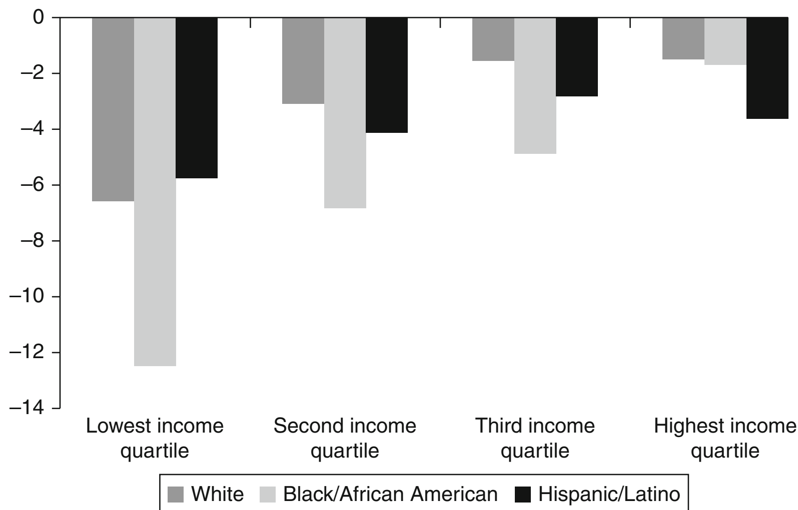

Figure 6.4 Percent change in the homeownership rate by race/ethnicity and income, 2004–2010.

Source: Author calculations using IPUMS Data. Steven Ruggles, J. Trent Alexander, Katie Genadek, Ronald Goeken, Matthew B. Schroeder, and Matthew Sobek. Integrated Public Use Microdata Series: Version 5.0. Minneapolis: University of Minnesota, 2010.

this is already making its way into the data. A study released by the Pew Foundation in 2011 found that the (inflation-adjusted) median wealth of black and Hispanic households has declined by one-half to two-thirds. From 2005 to 2009, median wealth fell by 66 percent among Hispanic households and 53 percent among black households, compared with just 16 percent among white households. In 2009, the typical black household had just $5,677 in wealth; the typical Hispanic household had $6,325 in wealth; and the typical white household had $113,149 (Pew Research Center 2011). While whites were still able to build wealth over this time period, the foreclosure crisis and subsequent recession eroded all the previous wealth gains for Hispanics and blacks.

The Role of Government in Expanding Low-income Homeownership

There is no doubt that the foreclosure crisis has shaken the foundations of "The American Dream"; it is hard to look at these statistics and not feel a real sense of loss and failure. However, it is a mistake to place the blame for the reversal of fortunes on specific efforts to expand homeownership or on assets-based policies more generally. Rather, many of the initiatives and policies in the 1990s designed to reduce credit barriers for lower-income and minority households were largely successful. The 1995 revisions to the Community Reinvestment Act (CRA), the establishment of affordable housing goals for Fannie Mae and Freddie Mac (also known as the Government Sponsored Enterprises or GSEs[7]), as well as innovations such as the Self-Help Community Advantage Program (CAP), the Department of Housing and Urban Development's Family Self-Sufficiency (FSS) Program, and the growing experience of Individual Development Accounts (IDAs) offer lessons that can inform how future homeownership policy can work for families with lower incomes and fewer resources.

In thinking about the government's role in homeownership, it is useful to distinguish between the different ways government has promoted homeownership through public policy. For instance, the federal government has long used its bully pulpit to promote homeownership. Presidents from Hoover to Obama have linked homeownership to the American Dream and to deeply held values such as access to opportunity, freedom, and community.[8] In addition, as Vale (2007) has shown, there has been a long history of campaigns, sanctioned by the government and supported by the real estate industry, that extol the virtues of homeownership. As a result, there has been a strong cultural preference for homeownership in this country, a preference that continues to this day.[9]

Despite this great rhetorical support for homeownership and its transformative potential, actual efforts to expand homeownership have often been driven by other goals such as supporting job creation or stimulating the banking industry; expanding homeownership has been something of a "rationale of convenience" (Collins 2007). Nevertheless, the government has long supported homeownership more broadly, through subsidies such as the mortgage interest tax deduction and/or grants and loans for the production of affordable units or downpayment assistance, through credit enhancements offered through the Federal Housing Administration and the GSEs, and through regulations and oversight (including the CRA and the enforcement of fair lending laws).

Beginning in the 1990s, at the same time that an assets-based approach to policy making was gaining attention, efforts to expand all of these government policy mechanisms increased significantly. This new push to promote homeownership, particularly for lower-income and minority households, was driven by a number of sometimes intersecting, sometimes competing motivations.

First, the early 1990s saw increased disenchantment with the welfare state and the crystallization of a neoliberal policy agenda that emphasized small government, including the privatization of public services and deregulation. The belief in the efficacy

of government interventions was replaced by a belief in bureaucratic failures. The Department of Housing and Urban Development (HUD) was not immune to these trends; throughout the 1980s, the agency had been plagued by inefficiency and scandal, greatly weakening public and political confidence in its mission and opening the door for a dismantling of rental housing subsidies (Wolf 1990). Jack Kemp, the secretary of HUD under George H. Bush, seized the moment to promote "HOPE" (Homeownership and Opportunity for People Everywhere). Inspired by the privatization of social housing in Great Britain under Margaret Thatcher, HOPE represented a direct effort to transform "dependent" public housing renters into "deserving" homeowners by converting public housing into owner-occupied housing. Kemp's rhetoric played off this narrative, arguing that HOPE would quite literally end public dependency and transform lives; it would "tear down the walls that come between people and their self-respect . . . [and] prevent people from exercising their talents and reaching their potential" (Kinnaird 1994).

Homeownership thus fit in nicely with the prevailing beliefs in civic obligation, private sector provision of public goods, and the use of tax and credit mechanisms to deliver social welfare transfers, particularly since public subsidies for homeownership were largely hidden (e.g., through the mortgage interest tax deduction). While driven largely by a Republican agenda, the left was not immune to the sentiment that public policies had failed to address social problems, and academics and policymakers were looking for new solutions.[10] Sherraden's book, *Assets and the Poor*, reflected this concern with the failure of past social welfare policies, and put forth the bold idea that an asset-based welfare policy would contribute to a more equal society, socially, economically, and politically (Sherraden 1991).

Second, there was increased awareness of the challenges facing poor neighborhoods. Concentrated poverty had risen substantially in the 1980s, and the Los Angeles riots in 1992 reinforced the need to address the lack of investment in the inner city. In a hearing on GSE reform, then Senator Riegle of Michigan argued for the affordable housing goals this way: "We know from the problems we saw in Los Angeles and problems we see in other cities that there is an urgent need to facilitate the proper flow of credit on a nondiscriminatory basis to people in those areas who properly can and should have the financing available to them to buy their own homes. It is one of the ways that we strengthen the fabric of neighborhood life; that we give people some sense we are responding to the problems in those areas."[11] If public housing had served to concentrate poverty and distress, then access to credit and homeownership offered an opportunity to promote reinvestment in distressed neighborhoods, increase civic participation, and reduce violence and crime.

Third, despite the civil rights and fair lending reforms of the 1960s and 1970s, the early 1990s saw a spate of news articles and research that highlighted continuing disparities in access to credit and mortgage lending. In 1988, the *Atlanta Journal* ran a series of articles titled "The Color of Money," which exposed racial disparities in home mortgage lending in Atlanta, Georgia. Despite quotes from bank officials denying charges of racism, the stories of prominent black leaders in Atlanta who were unable to obtain loans were jarring, and revealed the extent to which credit was determined as much by neighborhood and race than by borrower creditworthiness (Dedman 1988).[12] In 1992, the Federal Reserve Bank of Boston published a landmark study of mortgages, which showed that minority mortgage applicants in the Boston area were 56 percent more likely to be turned down than were equivalent white applicants (Munnell et al. 1996).

Thus, the 1990s saw a significant increase in governmental and nongovernmental initiatives designed to promote homeownership among lower-income and minority households. Collins (2007) provides an excellent review of all the government programs that existed over this time period to support homeownership. The largest government

subsidy for homeownership is the mortgage interest deduction; while not a direct product of the 1990s, the mortgage interest deduction had emerged from the 1986 Tax Reform Act as the only retained interest deduction. In 2012, the mortgage interest deduction will cost the federal Treasury an estimated $131 billion, more than ten times HUD's spending on homeownership initiatives (around $11 billion). [13] The mortgage interest deduction largely benefits higher-income households, however, leading some to suggest that a refundable tax credit available to all taxpayers—not just itemizers or those with positive tax liability—would be more effective at increasing homeownership, especially among lower-income households (Toder et al. 2010).

Both the Clinton and Bush Administrations also used their bully pulpit in support of homeownership. In 1994, Clinton released *The National Homeownership Strategy*, which set a national homeownership target of 67.5 percent.[14] In 2002, Bush followed suit with *Blueprint for the American Dream*, which promised to help close the homeownership gap by increasing minority homeownership by 5.5 million families before the end of the decade. Both of these strategies sought to leverage existing public and private actors in the housing industry to reduce the barriers and frictions in housing and credit markets; however, neither directly appropriated any funds toward these goals. In addition, direct subsidies to expand access to homeownership were relatively limited, coming largely from the funds available from HUD programs, such as HOME, CDBG, and SHOP, as well as funds allocated for housing counseling and homebuyer education (Collins 2007). Overall, the impact of these programs on the homeownership rate is likely to have been small; although data are hard to come by, these programs appear to have assisted only between 15,000 and 20,000 households a year.

Expanding Access to Credit: The GSEs and CRA

So why the ire over government attempts to support low-income homeownership? Most of the critiques have focused on two policies: the affordable housing goals established for Fannie Mae and Freddie Mac (the GSEs), and the CRA, which requires that banks meet the credit needs of communities in which they have branches, including low- and moderate-income (LMI) areas. Both of these policies relied on regulatory and legislative tools to encourage the private sector to provide increased access to credit.

In 1992, Congress passed the Federal Housing Enterprises Financial Safety and Soundness Act, which established three targets for the GSEs, requiring that they expand their purchase of loans to (1) lower-income borrowers (the "low-moderate-income" goal), (2) borrowers residing in lower-income communities and borrowers in certain "high-minority" neighborhoods (jointly, the "geographically targeted" or "underserved areas" goal), and (3) the very low-income borrowers and low-income borrowers living in low-income areas (the "special affordable" goal). These goals were deemed necessary because the GSEs had lagged the primary mortgage market in funding loans in these three areas, and because they had been slow to finance mortgage on rental properties (both single-family and multifamily rentals), which are a major source of low-income housing. HUD increased the goals four times between 1996 and 2005, with an eye toward moving the GSEs closer to the private market.[15]

Before the mortgage market collapse, research evaluating the effect of the GSE affordable housing goals was mostly favorable, finding that the goals had helped to expand GSE purchases in targeted communities and improve access to less expensive conventional, conforming loans (Ambrose and Thibodeau 2004; An et al. 2007; Bunce and Scheessele 1996). In addition, the research suggested that the GSEs may have reduced information externalities in target areas, thereby expanding the overall supply of credit even if those loans were not eventually purchased by the GSEs (Harrison et al.

2002).[16] Nevertheless, the overall effect of the GSEs was likely small, and some studies found only a limited link between the GSE goals and the supply of mortgage credit or volume of sales (Herbert and Kaul 2005). Importantly, the share of GSE business going to lower-income borrowers and underserved neighborhoods typically fell short of the corresponding shares of other market participants (Bunce and Scheessele 1996; Canner et al. 1994; Case et al. 2002).

A second policy that influences the flow of credit to lower-income communities is the CRA. Originally passed in 1977,[17] the CRA established a "continuing and affirmative obligation" that federally insured banks and thrifts meet the credit needs of the communities that they serve, including LMI areas, consistent with safe and sound banking practices. A key component of the CRA is the lending test (accounting for 50 percent of a large bank's CRA rating), which evaluates the bank's home mortgage, small-business, small-farm, and community-development lending activity. In assigning the rating for mortgage lending, examiners consider the number and dollar amount of loans to LMI borrowers and areas, and whether or not they demonstrate "innovative or flexible lending practices."[18] In 1995, President Clinton directed the regulatory agencies to review and revise the CRA regulations to make them more performance-based, and to make examinations more consistent, clarify performance standards, and reduce cost and compliance burden.

As with the research on the GSEs, studies conducted through the early 2000s all found that the CRA did improve access to credit in lower-income areas (Avery et al. 1996; Barr 2005; Belsky et al. 2001; Evanoff and Siegal 1996; Litan 2001). In a detailed review, William Apgar and Mark Duda concluded that "CRA-regulated lenders originate a higher proportion of loans to lower-income people and communities than they would if CRA did not exist" (Apgar and Duda 2003, 176). The research also showed that, overall, lending that fulfills a CRA obligation was not inherently more risky or less profitable than banks' other lending activities. In 2000, a report issued by the Federal Reserve Board concluded that mortgage loans to lower-income borrowers proved to be at least marginally profitable for most institutions, and that CRA lending performed no differently than other lending (Essene and Apgar 2009).

While the "pitfall" of subprime lending is discussed in more detail below, it is a mistake to conflate the subprime boom between 2004 and 2008 with the GSE affordable housing targets or the revisions to the CRA. The rampant growth in subprime lending between 2004 and 2008 was not driven by either the GSEs or by the CRA; indeed, most of the riskiest loans originated over this time period were ineligible for credit under either the GSE goals or the CRA (Belsky and Richardson 2010). While the GSEs did purchase subprime mortgage-backed securities as investments and did receive affordable housing goal credits for those purchases, their share of such purchases was a fraction of that of the private sector (Thomas and Order 2011; Weicher 2010). In addition, the GSE's losses were greatest among "nontraditional" loans that did not qualify for goal credits. At the end of 2010, among loans acquired by the GSEs between 2005 and 2008, affordable housing targeted purchases comprised less than 8 percent of their ninety-days delinquent portfolio, only a small share of overall troubled assets held by the GSEs (Seiler, 2010). Similarly, approximately 75 percent of subprime loans were originated by nonbank lenders and bought by investment banks not subject to CRA (Avery et al. 2007). Research conducted by the Federal Reserve Board of Governors found that only 6 percent of subprime loans were subject to CRA review, meaning that they were extended by CRA-obligated lenders to lower-income borrowers within their CRA assessment areas (Kroszner 2008).

In fact, the CRA, in particular, seems to have had the opposite impact that its critics claim, protecting borrowers from the risky lending practices that were dominant in the

marketplace over this time period. Research has shown that LMI borrowers who received their loan through CRA lenders within their assessment area were significantly less likely to receive a subprime loan or loan with a risky product feature, even after controlling for borrower and neighborhood risk characteristics (Laderman and Reid 2009; Reid and Laderman 2011). In fact, other studies using different data and methods have confirmed this "stewardship" effect of the CRA (Avery and Brevoort 2011; Hernández-Murillo et al. 2012; Nelson et al. 2011). In other words, the CRA actually promoted responsible lending and the origination of good loans—especially to LMI borrowers within a bank's assessment area—even as overall mortgage lending standards deteriorated.

The private flow of capital is critical to expanding access to homeownership for historically disadvantaged groups, and the experience of the 1990s makes it clear that government policies can help to promote that flow of capital through subsidies, guarantees, and regulations. For example, the experience of Self-Help's CAP provides a very clear example of how banks' CRA obligations can be leveraged to expand sustainable homeownership, even for very low-income families (Quercia et al. 2011). Launched in 1998, CAP is a partnership among Self-Help, a large community development financial institution (CDFI) located in Durham, North Carolina, the Ford Foundation, and Fannie Mae. Under CAP, Self-Help purchases mortgages originated through the CRA-related lending activities of participating lenders. Self-Help then sells those loans to Fannie Mae; because the loans do not meet Fannie's underwriting guidelines, Self-Help retains the risk of the loans, using a $50 million grant from the Ford Foundation as recourse against loans that fail. Since its inception, the CAP program has enabled 46,000 low-income families to buy homes,[19] significantly more than had the grant been used solely to make mortgages (Quercia et al. 2011). In addition, fewer than 4 percent of the loans have ended in foreclosure, despite the fact that CAP borrowers tend to have subprime credit scores and often put less than 10 percent toward a downpayment. Evaluations of the CAP program conducted by researchers at the University of North Carolina have demonstrated that when done right, homeownership for lower-income and minority families can not only be sustainable, but also result in broad benefits, including increased wealth and residential stability and satisfaction (see Freeman and Ratcliffe, chapter 7, this volume).

The Emergence of Asset-based Strategies for Homeownership

In addition to efforts to improve the flow of private capital for mortgage loans in lower-income communities, a second set of innovations that emerged during the 1990s were focused more on working with borrowers, and expanding their ability to save or overcome the downpayment constraints to buying a home (Galster and Santiago 2008). These programs included efforts such as HUD's FSS Program and IDAs, both of which targeted institutional constraints that have historically limited savings among lower-income families.

The FSS program was enacted in 1990 with the goal of helping families in subsidized housing reduce their reliance on public assistance and eliminating the "disincentive" to work that was inherent in public housing rent calculations (Ficke and Piesse 2004). Residents in public housing, or those who hold Section 8 vouchers, pay 30 percent of their income for rent and utilities; if their incomes increase, so do their rents, reducing the returns to work. The FSS program created a structure to eliminate this disincentive by putting the difference between their increased rent and their previous rent into an escrow account. In addition, families in the FSS program work with a case manager to define savings goals and to help link the family to other support services, such as employment training, childcare, and financial education. An evaluation of FSS found that, compared to public housing residents not in the program, participants experienced greater increases

in median income and received a greater share of their income from earnings rather than transfer payments (Ficke and Piesse 2004). In addition, families participating in FSS had saved an average of $3,350 in their escrow accounts (Ficke and Piesse 2004). Local data from public housing authorities have shown that approximately 30–40 percent of participants were able use these funds to help purchase a home (Cramer 2004).

IDA programs, an idea that emerged directly out of Sherraden's *Assets and the Poor*, similarly focused on using incentives to encourage lower-income families to save toward an "asset" purchase, including homeownership.[20] Nationwide, the number of IDA programs has grown from three programs in 1995 to more than 500 programs in 2002. While global numbers are lacking, estimates suggest that well over 50,000 low-income households have opened accounts (Reid 2005). Even though calculating the impact of IDAs on overall homeownership attainment is difficult, an evaluation of the federal Assets for Independence[21] program found that the program increased the homeownership rate among participants by 10.9 percentage points above the rate that would be expected based on the comparison group (Mills et al. 2008). In addition, a recent study found that IDA participants who purchased a home were less likely to receive a subprime loan than other low-income homeowners in the same communities, and that their foreclosure rates were significantly lower (McKernan et al. 2011).

The Promise of Homeownership

One of the reasons why the government has promoted homeownership among LMI families (as well as more broadly) is due to the economic, social, and civic benefits that are associated with homeownership (Mallach 2011). This section briefly reviews the literature on the benefits of homeownership for lower-income households, and also highlights the components of affordable homeownership programs that can help to ensure that these positive benefits are realized.

The Benefits of Homeownership for Lower-income and Minority Households

In addition to program innovation, the 1990s also spurred a large body of research on the effects of homeownership for lower-income and minority households. In 1991, the benefits of homeownership were mostly taken for granted, with few studies bothering to tease out if the better financial circumstances of homeowners were due to tenure choice or to existing income and wealth endowments. In part due to the homeownership boom of the 1990s, many more researchers began to study the effects of home-owning and grapple with issues of endogeneity and selection bias. Today, there is a much richer literature on the benefits (and risks) of homeownership for different types of households (see Herbert and Belsky 2008; Mallach 2011; McKernan and Sherraden 2008; Retsinas and Belsky 2002; Rohe and Watson 2007).

Overall, the research literature shows that homeownership does confer important financial benefits, both for homeowners in general and for lower-income and minority families as well. Importantly, the research has shown that homeowners do accumulate more assets than their renter counterparts, particularly when homeownership is sustained over time (Boehm and Schlottmann 2004; Carasso and McKernan 2008; Case and Shiller 1990; Di et al. 2007; Goetzmann 1993; Reid 2004; Rossi and Weber 1996). Recent evidence from the CAP program shows that even during the most recent period, homeowners in the CAP program accumulated nearly $17,000 in wealth, equivalent to an annualized return on equity of 24 percent (Freeman and Ratcliffe, chapter 7, this volume). These benefits are derived from both house price appreciation and through the forced savings associated with paying down outstanding mortgage principal. Moreover,

many studies that measure the returns to homeownership fail to account for the mortgage interest and property tax deductions, exemptions on capital gains on selling a home, as well as the value of implicit rents (net of maintenance and property taxes), all of which also contribute to financial gains for homeowners (Nichols 2005).

In addition to the financial benefits, homeownership is also associated with a host of positive social outcomes, including better health and well-being, higher residential satisfaction, and increased civic engagement and political participation (Rohe et al. 2002). However, the strength of these associations vary, and is often significantly muted when the effects of selection bias are taken into account (Herbert and Belsky 2008). In contrast, the positive effects on children are more robust and compelling. Research has found that homeownership improves child's educational attainment (Aaronson 2000; Green and White 1997; Harkness and Newman 2002, 2003; Haurin et al. 2002), labor market outcomes (Boehm and Schlottmann 1999; Harkness and Newman 2003), and reduces teenage pregnancy and other behavioral problems (Green and White 1997; Haurin et al. 2002).

Yet, the research has also shown that the benefits are not guaranteed, and that the returns to homeownership for lower-income and minority household may not be as great as for white or higher-income households (Herbert and Belsky 2008; Mallach 2011; Nichols 2005; Reid 2004; Rohe et al. 2002; Shlay 2006). The disparities in financial returns can result from differences in neighborhood-level appreciation rates as well as the condition and maintenance of the property. Moreover, as with any investment, the timing of purchase and resale, and the market in which the house is located, can have a significant impact on home equity (Case and Marynchenko 2002; Shlay 2006; Belsky, Retsinas, and Duda 2005). There are also concerns that homeownership for lower-income and minority household may not confer the same access to neighborhood benefits as for higher income and higher wealth households. Although evidence for the strength of "neighborhood effects" is mixed, if lower-income and/or lower-wealth household are only able to purchase homes in neighborhoods with high rates of poverty, not only might appreciation rates be lower but also the attendant benefits that homeownership is thought to provide—for example, access to better schools—may not be realized (Herbert and Belsky 2008; Oliver and Shapiro 2006; Reid 2004; Zandt 2007).

Perhaps most importantly, studies have shown that low-income and minority families may be particularly vulnerable to shocks that lead to homeownership exits, suggesting that entering and sustaining homeownership are two different things (Haurin and Rosenthal 2005; Herbert and Belsky 2008; Reid 2004). The next section reviews research on the elements that need to be in place to ensure that homeownership is not only attainable, but also sustainable.

Lessons Learned: The Components of Good Stewardship

Families that became owners through participation in a wide range of affordable homeownership initiatives—from CRA to IDAs as well as local downpayment assistance programs—have performed significantly better than their counterparts, with fewer foreclosures during a period of high default rates in the overall housing market. What about these experiences that lead to these positive outcomes? While more research is needed to understand the most important components of what comprises good stewardship—the elements of affordable homeownership programs that ensure that homeownership is not just attainable but also sustainable—there are some important lessons to be learned from all of these programs.

First, in direct contrast to the lax underwriting standards and risky loan product features that were prevalent during the subprime boom, well-designed affordable homeownership programs—whether administered as part of an IDA program or as part

of a bank's CRA lending commitment—ensure that the household has the ability to repay the loan. One hallmark of all these programs is that borrowers generally receive a 30-year, fixed rate mortgage, and do not rely on riskier loan products such as teaser rates to make the loans "affordable." Research has shown that loan product features contributed to the recent high rates of mortgage default. For example, using propensity score matching to create a sample of borrowers with similar risk profiles, Ding and his colleagues (2011) assessed the performance of CAP loans against subprime loans. Among borrowers with similar characteristics (e.g., low credit scores and high loan-to-value ratios), the estimated default risk was about 70 percent lower with a CAP loan than with a subprime mortgage that included risky features, such as adjustable interest rates and prepayment penalties. In addition, research has consistently demonstrated higher default risks for loans with adjustable and hybrid interest rates, prepayment penalties, and balloon payments (Pennington-Cross and Ho 2010; Quercia et al. 2005).

Second, the servicing process can have a profound impact on the disposition of delinquent loans (Cutts and Green 2004; Levitin and Twomey 2011; Stegman et al. 2007). Because lower-income borrowers tend to have less of a financial cushion to fall back on in the event of an economic setback, postpurchase support can help to ensure sustainable homeownership. Servicing practices that help to reach borrowers in the earliest stages of delinquency are often the most effective. For example, in a 2001 review of Federal Housing Administration (FHA) loans, one servicer had a success rate that exceeded 45 percent for workouts processed within the first two months of delinquency, but only a 10 percent success rate if the workout was processed after seven months (HUD 2002). Recent research on loan modifications has similarly found strong servicing effects (Cordell et al. 2008). In addition, while funds have historically been limited, some local programs offer bridge or emergency loans to help borrowers cover unexpected expenses; evidence suggests that this can greatly increase a borrower's ability to successfully resolve a serious delinquency (Quercia, Cowan, and Moreno 2005). Some programs also offer lower-cost rehab loans, which can help lower-income families to address problems like a broken water heater or a leaky roof, especially if the property has deferred maintenance issues.

Third, many of the programs also include a financial education component. Overall, the research on the benefits of financial education has been limited by the heterogeneity of programs and populations served, selection bias, and the challenges in tracking clients over time. Nevertheless, the majority of studies that have evaluated prepurchase and postpurchase counseling homeownership programs have found improvements in loan outcomes and consumer behavior as a result of counseling (Collins and O'Rourke 2010). One of the benefits of prepurchase counseling may actually be in helping families recognize when they are not ready to buy a home; a review of city-based affordable homeownership programs found that the screening process often helps to identify families who need to work on credit repair and debt reduction before they can qualify for a mortgage (Reid 2009).

Finally, one interesting finding emerging out of current research is the importance of local social relationships and networks shaping who gets capital and at what cost (Uzzi 1999; Pittman 2008; Moulton 2008; Reid 2010). While these networks do not always lead to positive outcomes (Reid 2010; Granovetter 2005), research has shown that participating in a community-based lending or affordable homeownership program or having a loan originated by a "local" bank leads to fewer defaults and more sustainable loan terms. As bank consolidation and technological advancements push lending away from a "Main Street" banking model, it may be important to think about how to encourage more socially embedded connections between underserved communities and mainstream lending institutions. For example, CDFIs already serve that function in some LMI neighborhoods; providing CDFIs with additional capital to play an expanded role

in mortgage lending and reach more borrowers could be one way to create a network of local intermediaries that could respond to local conditions and social processes and help to expand access to responsible credit for lower-income families.

The Pitfalls of Homeownership

While the last 21 years have revealed important lessons about the benefits of homeownership, the recent subprime crisis also reveals significant pitfalls that can undermine efforts to help lower-income and minority families build wealth through homeownership. This section explores three key pitfalls: the risks associated with deregulation and a lack of consumer protections in mortgage lending, the costs associated with a "dual" mortgage market and disparities in the cost of credit, and the changing nature of risks that households face as the result of the erosion of the safety net. While there are certainly other pitfalls that can influence the returns to homeownership—including the timing of purchase and geographic variations in house price appreciation—these three areas should be a priority for the asset building field.

Deregulation and the Lack of Consumer Protection

As Fergus argues in his chapter, efforts to expand homeownership arose at the same time that there was an unprecedented push for the deregulation of financial markets and a lack of attention to consumer protection. As a result, efforts to expand homeownership were greatly undermined by the proliferation of risky products and an uneven regulatory landscape that allowed many institutions to escape oversight. In the 1980s, a suite of federal legislation transformed the context for mortgage lending by facilitating the expansion of the secondary mortgage market, securitization, and the use of increasingly complex securities and derivatives (Newman 2008).[22] This new system of mortgage securitization paved the way for the subprime boom, yet despite fundamental changes to the mortgage market industry, federal policymakers did little to adapt supervisory systems to protect consumers (Immergluck 2009). For example, the Federal Reserve failed to use its authority under the Home Ownership and Equity Protection Act (HOEPA) to expand protections for consumers taking out subprime loans until July 2008 (McCoy and Renuart 2008), and the Office of the Comptroller of the Currency and the Office of Thrift Supervision both preempted the lenders they regulated from stronger state antipredatory lending laws (Ding et al. 2012). In addition, subprime mortgage loans were frequently originated by independent mortgage companies or affiliates and subsidiaries of financial institutions, which were not subject to the same level of regulatory or legal scrutiny and review.[23] The dominance of broker originations in the subprime market further placed borrowers at risk, as brokers had a financial incentive to charge borrowers higher rates for their mortgage. Without adequate consumer protections in place, borrowers in underserved communities—especially those with inadequate information or knowledge of the mortgage lending market—were more vulnerable to poor underwriting and other predatory practices.[24]

The crisis has taught us that the federal government has an important role in mediating and regulating the flow of mortgage credit. The Consumer Financial Protection Bureau (CFPB) and the reforms enacted by the Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd–Frank) provide a very important first step in restoring regulatory oversight to the financial markets, and will greatly expand consumer protections while limiting the ability of financial institutions to engage in predatory lending practices. Most important are the policies that will limit the origination of loans with risky product features, and that close the regulatory loopholes that allowed mortgage companies to operate outside of many consumer protections.

The Dual Mortgage Market and Disparities in the Cost of Credit

For most of the twentieth century, mortgage discrimination was overt and easy to spot: the presence of racial discrimination throughout American society was, to use the words of Samuel Johnson, a fact "too evident for detection and too gross for aggravation" (Arrow 1998). Both the private sector and the federal government were complicit in these practices (Stuart 2003). For example, restrictive covenants were widely used in the first half of the century to bar various racial groups from living in certain neighborhoods; title to almost all new homes built during the construction boom of the 1920s contained covenants prohibiting black occupancy. The FHA and the Home Owner's Loan Corporation (HOLC) perpetuated racial discrimination by explicitly advising real estate appraisers to note "adverse influences," which included "inharmonious racial groups" (LaCour-Little 1999). In addition, in 1935, HOLC created "residential security maps" of major cities in the United States to indicate the perceived security of real-estate investments. The maps, which outlined minority neighborhoods in red, identified areas that were deemed "too risky" to receive financing. It was not until November 1965 that the FHA commissioner announced that the agency would no longer "redline" black and other minority neighborhoods (Stuart 2003).

In the 1960s and 1970s, a series of historically significant federal laws were passed to address these inequalities, including the Fair Housing Act (Title VIII of the Civil Rights Act of 1968) and the Equal Credit Opportunity Act of 1974, the Home Mortgage Disclosure Act in 1975, and the CRA in 1977. As a result, the gross evidence of discrimination available before 1964 is no longer present (Arrow 1998). Yet, more than three decades after the enactment of these laws, race and ethnicity continue to play an important role in shaping access to credit, and the persistence of a "dual mortgage market" has contributed to consistent inequalities in the credit markets, even as overall access to credit has expanded (Apgar and Calder 2005). Studies have consistently found racial and ethnic disparities in mortgage lending denial rates (Munnell et al. 1996; Ross and Yinger 2002), the costs of credit (Bocian et al. 2008; Courchane, 2007), and in the prevalence of subprime loans or loans with risky product features (Bocian et al. 2011). For example, for loans originated between 2004 and 2008, African American and Latino borrowers with prime credit scores (above 660) were still much more likely than non-Hispanic whites to receive higher-priced loans or loans with risky product features, such as hybrid ARMs and prepayment penalties (figure 6.5). While there is likely to be an ongoing debate as to how much of these disparities can be attributed to racial discrimination per se and how much are due to income, wealth, and other observable and unobservable differences between demographic groups, the continued inequalities in the mortgage market represent one of the greatest pitfalls for lower-income and minority homeowners.

Current efforts to restructure the housing finance system need to ensure that policy decisions do not unintentionally create a new "dual mortgage market."[25] In their efforts to prevent another subprime crisis, regulators must avoid setting lending criteria that unduly restrict access to credit, especially for borrowers with lower credit scores or wealth. Looking at the past six years provides an unfair test of how subprime borrowers would have fared under "normal" circumstances. As Belsky and Richardson (2010) point out, the deterioration of lending standards, loans layered with multiple risky features, and the housing bubble created a recipe for disaster; had there been strong regulations in place, the performance of subprime loans might have been much better. Data from the CAP program, as well as other affordable homeownership programs, provide solid evidence for the ability of lower-income families to buy homes and sustain them, even with minimal downpayments, poorer credit scores, and higher debt-to-income ratios. There is a real risk that setting thresholds for downpayment requirements, credit

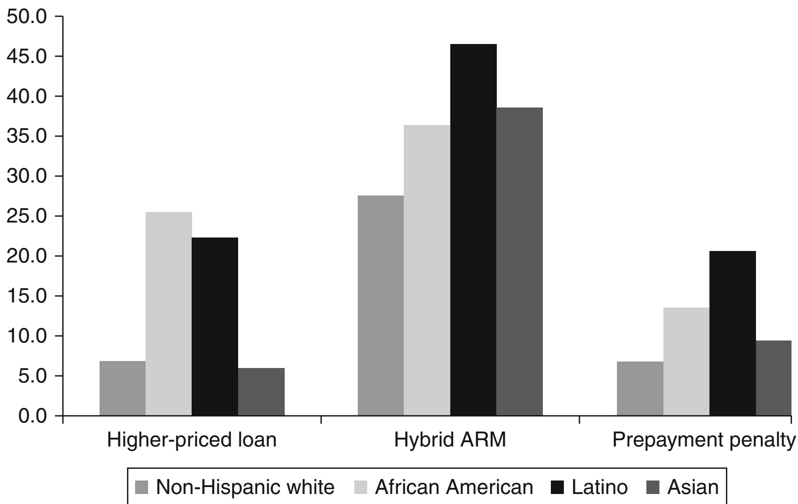

Figure 6.5 Percent of borrowers with a FICO score above 660 who received a loan with a risky feature.

Note: ARM, adjustable rate mortgage. Data are for loans originated between 2004 and 2008.

Source: Bocian, D., et al., Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures. The Center for Responsible Lending, Durham, NC, 2011.

scores, or debt-to-income ratios too high will create a new dual mortgage market, one that relegates lower-wealth households yet again to a market segment with the highest costs and smallest protections. While FHA currently plays an important role in providing access to credit for underserved borrowers, it is unclear what FHA's role will be in the future. Tightened underwriting standards at FHA, coupled with loan limits that may not reflect the costs of housing in some regions, will make it harder for moderate-income—especially minority—households to purchase homes, particularly in better neighborhoods (Immergluck 2011).

In addition, there also needs to be greater attention to how disparities in the cost of credit affect the financial returns to homeownership for lower-income families. The default risks of higher-priced loans are well documented, but there has been significantly less research on the long-term equity implications of risk-based pricing. An analysis of loans originated between 2004 and 2008 shows that of 27.3 percent of African American and 20.5 percent of Latino homeowners who were current on their mortgage in February 2011 were paying off "higher-priced" loans, compared with just 6.6 percent of Asian and 9.9 percent of non-Hispanic white homeowners. African American and Latino homeowners with higher-priced loans are also paying more on average for that credit—an average of 4.9 and 4.7 percentage points above the rate on Treasury securities of comparable maturity when the loan was originated. These differences can lead to significant differences in asset accumulation over the long term.

While some of these differences are likely due to inequalities in the mortgage market, it is also important to understand how different consumers make decisions about debt and credit after they become homeowners. For example, research has shown that African Americans and Latinos are less likely to refinance their homes to take advantage of lower interest rates (Herbert and Belsky 2008). Between 2008 and 2010, the number

of refinance applications dropped by 45 percent for African Americans and 34 percent for Latinos, but increased by 72 percent for Asians and 31 percent for non-Hispanic whites. Given today's historically low interest rates, this too could have considerable implications for the amount of equity African Americans and Latinos are able to build up in their homes. On the flip side, the risk factors for "cash-out" refinance products may also vary by borrower income and race/ethnicity. Within the CAP program, among borrowers who refinanced, 34 percent extracted equity from their homes. These borrowers were more likely to move from the CAP fixed-rate mortgage into a subprime ARM product (Spader and Quercia 2009a). In some cases, cash-out refinancing may be the right financial decision for a household, but the risk is that households lose the ability to sustain their mortgage payments or build equity over the long-term.

Finally, disparities in access to credit—and the higher cost of lending—are directly tied to disparities in credit scores. Research by the Federal Reserve Board of Governors has shown that African Americans and Latinos have, on average, lower credit scores than other demographic groups (Bostic et al. 2005; Federal Reserve Board of Governors 2007). Numerous concerns have been raised about the reasons these differences in credit scores persist, including the length of borrowers' credit histories, the lack of transparency in how credit scores are calculated, and the potential for feedback effects as credit scores affect individuals' credit options and vice versa (Spader and Quercia 2009b). At the same time, one recent study did not find any evidence that the credit characteristics used in credit history scoring models disadvantage minority borrowers (Avery et al. 2010). More research is needed to understand the interactions among individuals' economic characteristics, intergenerational resources, credit scores, and the pathways through which households are channeled toward high- and low-cost credit markets. In addition, the fact that payday lenders, check cashers, tax preparers offering refund anticipation loans, debt settlement companies, and yoyo auto lenders all concentrate their services in lower-income and minority communities may compound the risk that these households take on asset-stripping debt, which can indirectly affect homeownership and wealth accumulation.

The Changing Nature of Household Risks

The third key pitfall is related less to issues of mortgage lending, and more to the context in which families become homeowners. Compared with the golden age of homeownership after World War II, today's households face a significantly different constellation of risks due to changes in work, family, and public policy (Katz 2001; Skocpol 2000). While the expansion of homeownership during the 1950s and 1960s did translate into real wealth gains for families who were able to access this time period, the stability of employment and the presence of a relatively strong safety net allowed homeowners to take on mortgages that are premised on households being able to make steady, monthly payments. Today, rising levels of earnings inequality, the growing volatility of income over time, and the increase in part-time and contingent work all increase the vulnerability of lower-income families. From 2000 to 2007, incomes for the bottom 90 percent of earners rose only about 4 percent; for the top 0.1 percent, incomes nearly doubled. High divorce and separation rates and the increasing prevalence of single-parent families also can augment risk, especially when two incomes are needed to support higher mortgage costs (Warren and Tyagi 2003). At the same time, social policies designed to mitigate income risks have not adjusted to reflect these new realities, and contemporary tax policies largely benefit the rich (Hacker 2004; Moffitt and Gottschalk 2002; Saez 2012).

The ability of lower-income and lower-wealth families to sustain homeownership in the face of these changes is unclear. Thus, if the benefits of homeownership are to

be realized, a broader range of interventions, both pre- and postpurchase, needs to be considered. For example, lessons from saving programs could point the way toward larger-scale efforts to increase incentives and remove institutional barriers to promote savings—not only for a downpayment but also to increase a household's financial stability and resilience in the face of unexpected income shocks. As Mallach (2011) has argued, creating a support system for lower-income homeowners may be as important as creating a responsible process by which they become homeowners in the first place.

Conclusion

The recent crisis is a stark reminder that efforts to expand homeownership among lower-income and minority families do not operate in a vacuum: There is a need to pay attention to how socioeconomic inequalities are reproduced in housing and mortgage markets, and to recognize that these patterns of inequality can greatly undermine the end goals of sustainable homeownership and wealth accumulation. Indeed, virtually all the factors that shape the success of the homeownership decision are likely to be influenced by a household's income, race, and ethnicity (Herbert and Belsky 2008). For these reasons, homeownership is not a panacea, and expanding access to homeownership alone is unlikely to close the wealth gap.

However, that is not sufficient reason to give up on the goal of reducing disparities in access to homeownership and ensuring fair and equal access to credit. In fact, there is a strong case to be made for a greater governmental role in targeting supports for low-income homeownership. Absent government action, it is likely that the private sector will pull back from lending to lower-income households and communities—and in a way that will especially impact minorities (Belsky and Richardson 2010). Rather than retreating from the goal of promoting homeownership, we can draw on the lessons from the last 21 years of asset building strategies to build the foundation for a more equal credit system. Not doing so would be, in the words of Michael Sherraden in his book *Assets and the Poor*, a "failure of national vision," and would certainly guarantee even greater wealth disparities for future generations.

Notes

1. Alice O'Connor (1999) first used the analogy of "swimming against the tide" to emphasize how community development and affordable housing efforts have continually been undermined by broader economic and political trends.
2. The one exception is in the late 1970s, when the homeownership rate edged upward. These gains were driven largely by households seeking to hedge against inflation over this time period; when inflation came under control in the 1980s, the homeownership rate returned to around 64 percent.
3. Between 1995 and 2005, nominal mortgage interest rates fell about 2 percentage points to about 5.8 percent, reaching their lowest levels since the 1960s.
4. The growth in mortgages to low- and moderate-income households was supported by the introduction of mortgage products featuring flexible underwriting—including low downpayments, higher debt ratios, and reduced cash reserves—combined with the use of nontraditional means of verifying creditworthiness.
5. There is not a clear, universally accepted definition for either subprime or Alt-A mortgages. In general, however, subprime refers to loans made to borrowers with lower credit scores, although it is also often used to refer to (1) loans with interest rates above a given threshold; (2) as loans from lenders that have been classified as specializing in subprime loans; or (3) as mortgages that back mortgage-backed securities (MBS) that are marketed as subprime. Alt-A loans are those

made to borrowers whose credit scores are often between prime and subprime, but the mortgage itself may also be deemed riskier due to characteristics such as limited or no documentation of income or assets and/or higher loan-to-value or debt-to-income ratios. Typically, loans are identified as being alt-A by virtue of being in an MBS that is marketed as alt-A.

6. Author calculations of 2004 and 2010 Census microdata extracts. Steven Ruggles, J. Trent Alexander, Katie Genadek, Ronald Goeken, Matthew B. Schroeder, and Matthew Sobek. *Integrated Public Use Microdata Series: Version 5.0*. Minneapolis: University of Minnesota, 2010.
7. GSE is a general term that refers to quasi-governmental organizations that are "chartered" by the federal government but are privately owned (as evidenced by capital stock owned by private entities or individuals). While there are other GSEs, the term GSE is often used as a shorthand reference for Fannie Mae and Freddie Mac, which provide liquidity to the mortgage market by securitizing home mortgage loans. For a good overview of the functions of Fannie Mae and Freddie Mac, see Frame and White (2005).
8. The term "American Dream" was first coined in 1931 by James Truslow Adams in his book, *The Epic of America*. The product of Depression-era politics, the original formulation flowed from the idea of American exceptionalism, stressing individual freedom and the possibility of significant upward social mobility through ingenuity and hard work. It promised, too, that successive generations would enjoy steadily improving economic and social conditions (Knox 2007).
9. Fannie Mae conducts a survey to assess the degree to which Americans wish to own their own home. The survey has consistently found that the desire to own a home is strong across all socioeconomic groups. Even with the recent crisis, more than 90 percent of homeowners and 70 percent of renters say that owning makes more sense than renting.
10. A Pulitzer Prize-winning series in *The Washington Post* about a welfare mother, Rosa Lee Cunningham, and her eight children and thirty-two grandchildren, generated tremendous attention in Washington. The series, which included eight days of front-page lengthy articles about "a three-generational family of welfare-dependent petty criminals" (Dash, 1994, p. C1), was particularly powerful because it was a sympathetic portrayal by a liberal newspaper, and yet the underlying message was the failure of the welfare system.
11. Senator Riegle, Comments at a hearing on Government Sponsored Enterprises Legislation, US Senate, June 18, 1992.
12. Shortly thereafter, the US Department of Justice began investigating lending practices at 64 institutions, and charged Decatur Federal Savings and Loan Association with a "pattern and practice" of racial discrimination in lending (Goldstein and Urevick-Ackelsberg, ND).
13. Homeowners also benefit from other federal tax preferences, including deductibility of residential property taxes on owner-occupied homes ($31 billion), and exclusion of tax on the first $250,000 ($500,000 for joint returns) of capital gains on housing ($50 billion).
14. According to Craig Nickerson, who served as executive director of the National Homeownership Strategy, this target was not pulled out of thin air. Researchers at HUD had carefully analyzed demographic and economic data, and saw this is a viable target that would help to close the racial and income homeownership gaps. (Nickerson, personal communication)
15. In 2004, recognizing that the GSEs still lagged the market, HUD raised the affordable housing targets "so that by 2008 [GSE purchases] would equal the projected shares of goal-qualifying units financed in the primary mortgage market." (Thomas and Van Order 2011).
16. The prevalence of information externalities are considered to be a primary factor influencing the flow of credit in lower-income communities. Mortgage applications in "thin" neighborhoods—those with few mortgage transactions—will be deemed riskier than applications from neighborhoods with high transaction volumes. If the GSEs help to elevate the number of transactions in thin markets, they can enhance the overall flow of credit by reducing these information externalities, regardless of whether the mortgage is subsequently purchased by a GSE or not.
17. The CRA is one of several laws passed in the 1960s and 1970s intended to reduce credit-related discrimination and expand access to credit. The Equal Credit Opportunity Act

(1974) and the Fair Housing Act (1968) explicitly prohibit discrimination on the bases of race, sex, or other personal characteristics. In addition, the Home Mortgage Disclosure Act (1975), which requires the disclosure of mortgage lending and application data, was enacted to increase transparency and to support public and private investment activity.

18. As part of their CRA exam, large banks are also evaluated on their investments and services. Under the investment test, which accounts for 25 percent of the bank's CRA grade, the agency evaluates the amount of the bank's investments, its innovation, and its responsiveness to community needs. Under the service test, which makes up the remaining 25 percent of the bank's evaluation, the agency analyzes "the availability and effectiveness of a bank's systems for delivering retail banking services and the extent and innovativeness of its community development services." Different rules apply for "small" and "intermediate small" institutions. For more complete details on the CRA regulations, visit the Federal Financial Institutions Examination Council website for text of the regulations and Interagency Q&A.
19. The median borrower in the CAP program earned $33,000; about 40 percent of the mortgages are to single female-headed households, and about 40 percent are to minority borrowers.
20. Although specific program features vary, IDAs help low-income people save for a specified asset building purpose, most commonly purchasing a home, starting a small business, or paying for continued education. Accountholders make monthly contributions to an account, usually over a one- to four-year period, and their savings are matched at a predetermined rate, typically at a rate of 1:1 to 3:1. Accountholders also take mandatory classes in budgeting and financial management, and receive specialized training in their asset area (e.g., homebuyer education). Matching and operating funds come from both public and private sources, and match deposits are usually capped to control program costs.
21. Assets for independence (AFI) is a federal program that provides grants to enable community-based nonprofits and state, local, and tribal government agencies to implement IDA programs.
22. These included the 1980 Depository Institutions Deregulation and Monetary Control Act, the 1982 Alternative Mortgage Transaction Parity Act, the 1984 Secondary Mortgage Market Enhancement Act, the 1989 Financial Institutions Reform, Recovery, and Enforcement Act, and the Tax Reform Act of 1986.
23. In the case of affiliates and subsidiaries, the federal bank regulators did have examination responsibilities, but these institutions were subject to less rigorous review. Independent mortgage companies unaffiliated with a depository fell under the purview of various state financial agencies; however, their capacity to review and enforce lending regulations was much more limited.
24. In a detailed survey, Courchane and her colleagues (2004) found that subprime borrowers were less knowledgeable about the mortgage process and were less likely to search "a lot" for the best rates. "Borrowers who do not search for the best interest rates or who do not have the opportunity to make choices about their mortgage options disproportionately end up with subprime loans, as do borrowers whose search emphasized affordable monthly payments."
25. This issue is particularly salient given the current debate over how to define qualified mortgages (QM) and qualified residential mortgages (QRM)—two related statutory provisions in Dodd–Frank that will govern the origination of residential mortgages. The QM definition will determine the underwriting criteria that will help to ensure that a borrower has a "reasonable ability to repay the obligation," and will restrict the origination of loans with features associated with higher default rates, such as lack of income documentation, prepayment penalties, and loans with interest-only, negatively amortizing or balloon payments. QRM will define which loans will be exempt from requirements that at least 5 percent of the credit risk be retained by the securitizer. While the QM "ability to repay" obligation will apply to all residential mortgages, the QRM definition will apply only to mortgages that are privately securitized.

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Chapter Seven
Setting the Record Straight on Affordable Homeownership

Allison Freeman and Janneke Ratcliffe

In his 1991 groundbreaking work *Assets and the Poor: A New American Welfare Policy*, Michael Sherraden permanently shifted the discussion about welfare policy in the United States. Sherraden argued for a focus on the promotion of savings and wealth generation rather than the then-current emphasis on income and consumption. He advanced the use of Individual Development Accounts (IDAs) in order to push welfare policy beyond addressing immediate needs and instead to the support of long-term economic well-being for lower-income households. Sherraden's groundbreaking work argued that low-resource households can build financial security if given access to the proper tools and systems.

This chapter takes as its central focus one of the constituent elements of economic well-being that Sherraden proposed IDAs should enable: homeownership. Our position is that affordable, sustainable homeownership is one of the surest ways to help lower-income households build long-term wealth. The home can be used for all of the purposes Sherraden designated for IDAs, that is, to finance postsecondary education, to provide capital for self-employment, and to provide security during one's retirement years. However, a home has the added benefit of being a consumption good: essentially a home provides its owner with a place to live while simultaneously forcing the owner to save, and hopefully build wealth, through principal reduction and equity accumulation.

In the wake of the foreclosure crisis, some argue that homeownership was pushed too far (Kiviat 2010). The implication is that this well-traveled route to economic security should be closed off to certain families. While homeownership is not appropriate for everyone (e.g., it will not work well for the income poor), it is extremely well suited for working families who are asset-poor. How do we know this? For ten years, we at the University of North Carolina's (UNC) Center for Community Capital (CCC) have tracked borrowers in the Community Advantage Program (CAP), a portfolio of over 46,000 home-purchase mortgages made to lower-income households. We speak annually with more than 2,000 of these CAP homeowners as well as with a comparison group of renters. The data from these annual and detailed telephone interviews have informed a series of empirical papers by CCC researchers, which provide the content for the chapter.

There is ample debate over the merits of homeownership for low- and moderate-income people, much of it centered on financial matters, that is, whether homeownership is a reliable wealth-building mechanism and whether it is less costly, all things

considered, than renting. While some see homeownership as an important contributor to household wealth in the United States (Hollaway 1991; Turner and Luea 2009), others believe that renting is less risky and less costly than owning (Smith and Smith 2007).

In a detailed review of the literature concerning lower-income homeownership, Herbert and Belsky (2008) point out that one's likelihood of realizing any of the benefits associated with homeownership will depend upon a number of factors, including timing of purchase, location of purchase, age and condition of the home, maintenance costs, if or when the owner taps into equity, eligibility for the tax benefits associated with housing, the return to alternative investments, the cost of renting, and the household's frequency of moving. Duda and Belsky (2001) note that timing and location (i.e., neighborhood-based price movement) are not the only things that affect the returns to housing for lower-income owners; the willingness and ability of these owners to hold onto their homes during market fluctuations also affect overall wealth gains.

The chapter, relying on extensive analysis of the rich, unique, real-time CAP data, challenges five suppositions about homeownership that have risen to prominence since the mortgage lending crisis began. Critics of efforts to ensure that homeownership opportunities are available to families with low and moderate incomes (LMI) often rely on one or more of these assertions: homeownership is not a reliable wealth-building strategy for lower-income families; homeownership crowds out other investments for lower-income borrowers; lower-income borrowers erode their equity through excessive borrowing; renting is a more affordable option for lower-income individuals; and homeownership should be restricted to those who can afford a 20 percent downpayment.

Our analysis of the CAP panel data compels us to refute each of these claims, and we conclude that while no one, low or high income, should receive an unsound loan for a home they cannot afford, qualified lower-income households, when provided with the right tools and structures, can be successful homeowners and can realize the lasting benefits of homeownership.

The Evidence

All of the evidence presented in this chapter comes from analysis of CAP data. Self-Help Ventures Fund (Self-Help) launched CAP in 1998, with a $50 million grant from the Ford Foundation and institutional capacity provided by Fannie Mae. CAP is essentially a risk-sharing mechanism: under the program, Self-Help purchased community reinvestment loans from lenders around the country and sold them to Fannie Mae, while retaining the associated risk. The goal of CAP was twofold: to increase the flow of efficient, secondary-market capital to lower-income and minority borrowers, and to demonstrate that making mortgages to these borrowers could be profitable for the lenders. In the early 2000s, the Ford Foundation engaged CCC to conduct a long-term study of the program's impacts on the participating institutions and households.[1]

Who are CAP's borrowers? At the time they bought their homes, borrower households had a median annual income of just $30,792.[2] The median borrower age at origination was 32 years old. Some 41 percent of CAP borrower households are headed by a woman, and approximately 40 percent of CAP's borrowers are minorities. The median loan balance at origination for CAP's borrowers was $79,000, issued at a median interest rate of 7 percent, which was consistent with prevailing prime, conforming mortgage rates at the time of origination. Fifty-three percent of CAP's borrowers had credit scores less than or equal to 680 when their mortgages were originated, and 72 percent of borrowers made a downpayment of less than 5 percent on their homes.

Despite the ostensibly risky profile of CAP's homeowners and the turmoil experienced within housing markets since 2008, the CAP portfolio has performed well. Through the third quarter of 2011, the portfolio of currently active CAP loans had a serious delinquency rate of 9 percent. This is lower than the rate of serious delinquency for prime adjustable rate mortgages (15 percent), subprime fixed rate mortgages (20 percent), and subprime adjustable rate mortgages (36 percent) through the same quarter.[3] CAP has enabled a group of creditworthy, though nontraditional, borrowers to obtain homes with 30-year, fixed-rate, self-amortizing mortgages, underwritten for the ability to repay. The lenders involved in CAP took these creditworthy borrowers and helped get them into homes they could afford with mortgages they could manage.

Our evidence shows that lower-income families can succeed as homeowners and can receive the benefits traditionally associated with this form of tenure. Yet, critics of affordable homeownership initiatives want to shut out of the mainstream homeownership finance market households matching the profile of those served by CAP lenders, effectively shutting off a valuable pathway to economic security and well-being. Here we offer evidence to contradict five of their justifications for doing so.

Supposition #1: Homeownership Is Not a Reliable Wealth-building Strategy for Lower-income Families

While there is understandable and valuable debate about the wealth-building effects of homeownership for lower-income people, the CAP data show that when LMI families purchase homes they can afford with mortgages that are sustainable, wealth happens. A look at how CAP's rates of equity appreciation have fared relative to other investments into which these LMI owners could have put their downpayments illustrates the point.[4] From loan origination through the second quarter of 2011, CAP's homeowners saw a median annualized return on their equity of 27 percent. In comparison, during that same period, the Dow Jones Industrial Average increased by a median of 2.4 percent on an annualized basis, and the median annualized return on the ten-year Treasury bill was 5.4 percent. The gains experienced by CAP's owners led to a median increase in equity of close to $18,000, so that by the end of the third quarter of 2011, CAP's owners held $21,000 in home equity (at the median).[5]

When comparing the balance sheets of owners to comparable renters, home equity gains appear to have been a primary factor leading to wealth building from 2005 to 2008. Grinstein-Weiss et al. (2011) find that over that period, as the crisis was just beginning to unfold, homeowners saw an average gain in net worth of more than $11,000, while the matched sample of renters only gained $742 on average. Interestingly, they found that nonhousing wealth grew faster for owners than for renters over this period, and they also found no significant increase in liabilities for the owners relative to the renters.[6]

Our research reveals that homeownership does not just generate wealth for lower-income owners during good economic times, but that it can also act as a buffer against losing wealth in difficult economic times. The analysis examines how owners and renters who were financially similar to one another before the crisis have fared since the crisis. First, we look at the fate of owners and renters who were initially in the same income categories; this shows us how households with similar income levels, but different types of tenure, fared between 2005 and 2010—essentially from near the peak of the housing market to deep into the recession.

As expected, both owners and renters in all income categories lost wealth at the median over that five-year period (see figure 7.1). Yet, within each income group, owners ended the period with significantly higher net worth than their renter counterparts. In only one instance did any group of renters' median net worth exceed $1,000 in 2010; in

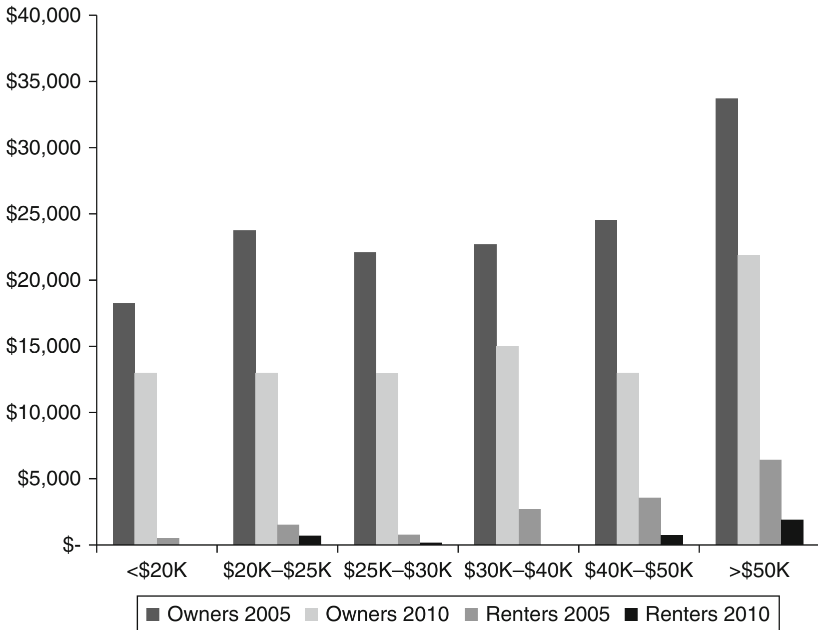

Figure 7.1 Median net worth of owners and renters, by income group (2010 dollars). Owners (*N* = 998) and Renters (*N* = 849).

Note: Our samples include all original owners and renters, regardless of subsequent tenure changes, who provided all three years of wealth information.

contrast, most groups of owners ended the period with a median net worth of around $13,000. What is clear from this comparison is that before the crisis, in 2005, owners held far more wealth than renters with similar incomes. Although the owners lost more than the renters through 2010, they had much more to lose, and they were therefore able to retain greater net worth through the crisis.

A second comparison of changes to owners' and renters' wealth over time is derived by matching owners' and renters' by net worth in 2005 and seeing how they fared between 2008 and 2010 (see figure 7.2). The data reveal that, even though they started with comparable net worth in 2005, owners' and renters' net worth diverged greatly by 2010. By that year, all groups of renters who had positive net worth at the beginning of the period saw their net worth fall precipitately. For example, the renters who had net worth in excess of $30,000 in 2005 had a median net worth of only $1,200 by 2010, and only one group of renters had median net worth in excess of $2,000 by 2010. While all groups of owners also lost wealth at the median, each group of owners ended with median net worth between $4,456 and $22,559. These shifts suggest that homeownership and the housing investment helped buffer CAP's owners from financial devastation during the crisis, whereas the wealth of comparably situated renters was more vulnerable to the financial turmoil.

Related to the argument that homeownership is not a reliable wealth-building mechanism for LMI families is the assertion that homeownership is too stressful for lower-income families to bear. Manturuk et al. (2011) consider this line of thinking as they analyze the financial and psychological stress associated with homeownership during

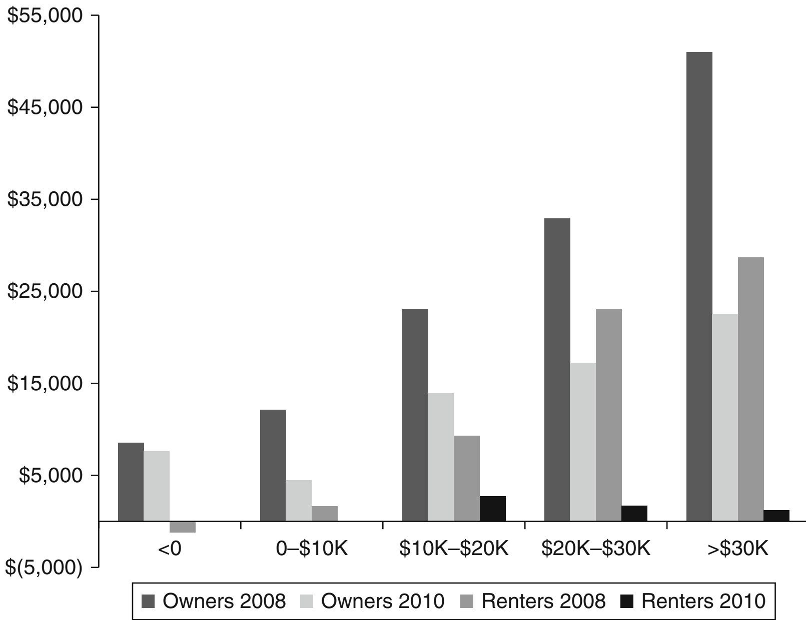

Figure 7.2 Median net worth of owners and renters, by net worth in 2005 (2010 dollars). Owners (*N* = 998) and Renters (*N* = 849).

the housing bust. The financial crisis that started in 2008 served as a reminder that the value of housing, like that of any investment, is subject to market fluctuations. Given this, and given the extent to which lower-income homeowners are potentially under-diversified in their portfolios (examined later in the chapter), it is reasonable to suspect that homeownership might increase the financial and psychological stress that LMI homeowners experience when housing values are falling.

Manturuk et al.'s (2011) analysis looks at the impact of homeownership on three dependent variables: financial stress (a measure of the extent to which actual financial difficulties in paying for housing, managing money, carrying debt loads, and saving for retirement are causing people stress), satisfaction with one's financial situation, and overall stress (based on a four-item measure of how much people felt in control of their lives). After adjusting for observable differences between the owners and renters,[7] the authors measure the impact of tenure on the three outcomes of interest (financial stress, financial satisfaction, and general stress); they control for age, relative income, net worth, geographic region, and two measures of financial hardship. Every model includes the 2008 measure of general stress to control for respondents' baseline stress levels.

The analyses uncover no significant difference between renters' and owners' actual reported financial stressors, yet they showed homeownership to have a persistent significant beneficial effect on financial satisfaction and overall stress. Specifically, homeownership is associated with an increase of between 27 and 37 percent in the odds of a higher financial satisfaction score.[8] In other words, the owners reported lower psychological stress than comparable renters, despite facing a similar level of financial pressure. The fact that, despite comparable economic experiences, CAP's homeowners

reported significantly lower levels of financial stress and significantly greater levels of financial satisfaction indicates that the benefits of homeownership go beyond those that can be measured in financial terms.

In conclusion, whether considered against alternative investments or against the financial stress experienced by comparable renters, homeownership appears to be working well for CAP study participants. Of course, not all households fared equally well: some of the owners who bought late in the cycle in more volatile markets have lost wealth. However, the evidence shows that on the whole, renters who missed out on the opportunity to build home equity-related wealth before the onset of the financial crisis were badly buffeted in the recent economic imbroglio.

We cannot emphasize strongly enough that we believe the main reason that CAP's owners have fared well, both financially and psychologically, is that they bought their homes with affordable, sustainable mortgages. All of the owners in the CAP portfolio received fixed-rate, fixed-payment, standardized, competitively priced, and long-term mortgages. This instrument, when carefully underwritten and well serviced, has stable and predictable payments, and it can enable homeownership for the long term. It is largely due to the durability of their affordable mortgages that CAP's owners have enjoyed the benefits traditionally associated with homeownership and that they have found it to be an effective means of long-term wealth building, even in the mid of economic upheaval.

Supposition #2: Homeownership Crowds Out Other Investments, While Renting Allows Households to Diversify Their Investments

One criticism of the home as an investment is that it crowds out other investments, leaving households with under-diversified and, therefore, riskier portfolios. This is a potentially serious concern for lower-income individuals, who invest a greater share of their net worth in housing than higher-income individuals do. However, is this concern warranted? In other words, absent housing, would lower-income households have well-diversified, low-risk portfolios?

To assess whether or not the accrual of home equity leads to the crowding out of other investments for lower-income individuals, Freeman and Desmarais (2011) examined whether or not CAP's homeowners restrict their investments in other financial instruments as a result of having concentrated their investing activities in the home. The goal of Freeman and Desmarais' analysis was to identify any possible effect of equity accumulation on the rest of the respondents' financial portfolios.[9]

The authors analyzed respondents' adjustments in asset distribution in response to changes in home equity.[10] Asset-based outcome variables included transaction account balances and CDs, investments (stocks, bonds, and retirement), and equity in nonprimary residences and major durables. Control variables included age, income, education, number of children, race, and home equity level. The model simulated how the portfolios of LMI renters would respond to the equity levels held by their matched owners. The model was run for cross-sectional amounts in 2008 and for the change between 2005 and 2008.

What did Freeman and Desmarais find concerning the relationship between home equity and other assets? In the cross-sectional analysis, the effect is significant but miniscule: when renters were given the equity amounts of their matched owners in 2008, the simulated effect on their investment portfolios was a shift of less than one cent. In the analysis measuring change over time, there does seem to be a negative relationship between change in home equity and change in investments, but again the effect is significant but very small, with a $120,000 increase in home equity corresponding

to a $100 reduction in investments (stocks, bonds, and retirement). Equity in property other than a primary residence does seem to exhibit a relationship with home equity: the change-over-time analysis indicates that the accumulation of home equity is associated with a decline of approximately $5,000–$15,000 in nonprimary residence equity. This might imply that there is a trade-off between homeownership and investment in other real estate, that is, that once LMI households purchase their own home, they no longer invest in land or timeshares, for example, but concentrate their resources in their housing.

In conclusion, Freeman and Desmarais (2011) do not find evidence of significant asset-related opportunity costs to home equity accumulation for the CAP borrowers. They find little evidence that other investments or savings suffer from the resources tied up in the generation of equity. They conclude that affordable lending for homeownership "serves as an effective means for promoting stable wealth-building for LMI households through the forced-savings mechanism of equity accumulation" (155).

Supposition #3: Lower-income Homeowners Erode Their Equity Gains Through Excessive Borrowing

Another criticism of the home as an investment vehicle is that homeowners, particularly those who are income constrained, might be tempted to diminish their wealth gains through excessive borrowing. While the accrual of equity can be beneficial for LMI households, in order for owners to realize this benefit, they must resist the temptation to borrow that money back for other uses. In response to these concerns, Freeman and Desmarais's (2011) analysis (detailed in the preceding section) also considered the important question of whether or not CAP's LMI homeowners increase their levels of borrowing in response to the accumulation of home equity.

The authors looked specifically at the relationship between the accumulation of equity and three types of debt: credit and charge card debt, student loan debt, and borrowing against the home in the form of home equity lines of credit, cash-out refinances, and second mortgages. Again, the fixed variables included age, income, education, number of children, race, and home equity level.

Freeman and Desmarais (2011) found that when renters are given (through simulation) the level of equity held by matched owners in 2008, there is a moderate positive relationship between home equity and credit card debt, particularly for those with higher levels of home equity. Specifically, home equity of more than $150,000 corresponds to an *average* predicted increase of $1,000 or more in credit card debt. However, the accumulation of equity over time shows a smaller relationship to the accumulation of credit card debt, with the analysis revealing a *maximum* upper bound in the confidence interval of approximately $700 increase in credit card debt as a result of home equity accumulation.[11] The relationship between student loan debt and home equity is small, with extremely high or low values of equity in 2008 corresponding to an increase of approximately $600 in student loan debt; the change-in-time effect of home equity on student loan debt is negligible. As for the amount of equity and borrowing against the home, notable borrowing against home equity only occurs where equity levels are $100,000 or more, and such borrowing never reaches a scale that would decimate equity-based wealth.

Freeman and Desmarais conclude that while there appears to be some association between the accumulation of large amounts of equity ($150,000 or greater) and increased indebtedness, there is no evidence that debt accumulation by CAP homeowners offsets the wealth-building effect of home equity.

Supposition #4: It Is Cheaper to Rent Than to Own, So Renting Is a Better Option for Low- and Moderate-income People

The long-standing debate over whether it makes more sense for lower-income people to rent rather than own a home has been especially heated since the mortgage finance crisis began in 2007. Renting is said to be better for lower-income households because, all things considered, it is thought to be less expensive than owning. The user costs of owning versus renting have been analyzed extensively, but seldom for lower-income households. Riley and Ru (2011) use the CAP data to fill this gap in the literature.

Riley and Ru assess whether CAP's owners would have been better off renting over the period 2003 –2010. The authors calculate owners' ex-post user costs and equivalent rents from the CAP survey data based on property attributes. The construction of owners' user costs components include mortgage payments (including property taxes and insurance); the opportunity cost of holding equity in the house[12]; mortgage closing costs and origination fees; homeowners association fees; maintenance expenditures; annual depreciation; the observed net property appreciation as of the third quarter of each year; and the tax benefit received in each year from claiming the mortgage interest tax deduction.[13]

The authors calculate that the median owners' user cost was $36,000 for the period 2003–2010, less than the estimated median cumulative equivalent rent of $41,000. When they decompose their results by year, they discover that median annual user costs were generally lower than median equivalent rents before 2007 and were higher thereafter. However, Riley and Ru determine that the initial period of house price appreciation was sufficient to offset the subsequent higher owners' user costs as a whole. The authors estimate that annual house price appreciation of about 2 percent at the median was necessary to ensure that owning was no more costly for CAP's owners than renting would have been between 2003 and 2010.

In the analysis described above, house price appreciation rates drive the comparison, but there are two key variables not tested in the CAP experience that also affect the overall costs of owning versus renting. The first of these is the type and cost of financing used. CAP borrowers all received similar mortgages: fixed-rate, fixed-payment, and competitively priced. Changes in interest rates and different fee structures would yield different results. The second critical factor is the cost of renting, which has recently been on the rise (Lazo 2012). Therefore, if home prices stabilize, homeownership may gain relative financial advantage over renting.

Supposition #5: Homeownership Should Be Restricted to Those Who Can Put 20 Percent Down

Finally, we turn from the effects of homeownership to the topic of how access to homeownership should be enabled or restricted. As Sherraden (1991) notes, one of the constraints on homeownership as a wealth building vehicle for LMI households "is institutional barriers to credit. Studies have shown that owning a home is, on the average, less expensive than renting, but many of the working poor are not able to accumulate a downpayment to make home ownership possible… [L]iquidity constraints, stemming from the uncertainty of lenders, prevent the extension of credit even when the working poor might be a good risk" (128).

Since the mortgage lending crisis began in 2007, downpayment requirements have loomed large as part of the discussion over what led to the crisis and how to prevent another one. In May 2011, in an effort to develop underwriting guidelines for qualified residential mortgages (QRM)—which are exempt from risk retention requirements

for privately securitized mortgages under the Dodd–Frank Wall Street Reform and Consumer Protection Act—the FDIC and Federal Reserve proposed the institution of a 20 percent downpayment requirement. QRMs would not be required to purchase homes, but presumably would be less expensive than the alternative financing. While the uproar that followed has kept regulators from actually settling on this amount, downpayment requirements continue to loom in the ongoing debate over mortgage finance in the United States.

The loans in the CAP portfolio run contrary to this "new normal." CAP's loans are notable for their high loan-to-value ratios. Among the programs from which CAP loans have been purchased, 97 percent is the typical maximum loan-to-value ratio, though some programs issue loans all the way up to 103 percent of house value. A downpayment of 1–3 percent of the home price is not uncommon, nor is a minimum borrower contribution of $500.

Cloaked within the debates over downpayment requirements is the belief that all downpayment money must come from the borrower, that is, that homeowners must have a significant financial stake in their homes in order not to be tempted to default. It might surprise some readers, therefore, to learn that a substantial portion of CAP's borrowers had help meeting their modest downpayment requirements and closing costs. Analysis of 3,684 CAP owners responding to the baseline survey yielded some interesting results concerning sources of downpayment and closing costs. Some 38 percent of CAP owners relied on some form of assistance beyond their own savings and assets to get into their homes. From what sources did borrowers obtain this help? Sellers and real-estate agents were the source of assistance most frequently cited by CAP's owners: 20 percent of all owners received a contribution from these sources.[14] Thirteen percent of owners received help from family and friends, while 8 percent relied on a grant from a community group, government agency, or other organization. Two percent of owners used a second mortgage to help meet their downpayment and closing costs, while 2 percent used help from another source altogether. Eighty-four percent of those using external assistance relied on only one source of help, 15 percent combined two types of help, and the final 1 percent used three types of help.

Analysis of which factors affect the use of different types of nonbank assistance toward one's downpayment and closing costs reveals the following (Freeman and Harden 2012).[15] Among CAP borrowers, African Americans are significantly less likely than whites to receive downpayment assistance from their parents (by 14 percentage points), and are significantly more likely than whites to use a community grant toward their home purchase (by 10 percentage points). Older respondents, not surprisingly, are less likely overall to receive assistance, as are those who learned financial skills from their parents. Women are more likely than men to use nonbank assistance toward downpayment and closing costs (by 8 percentage points), and the analysis reveals that the predominant source of assistance for women is help from parents.

Analysis of the CAP data reveals which categories of borrowers were more likely to get help with their downpayment and closing costs, but an important question remains. Are homeowners who used help toward their downpayment and closing costs more likely to become delinquent or even default? To answer this question, Freeman and Harden used data from 2003 through 2011 to estimate a multilevel multinomial logistic regression model with random state intercepts (to account for geographic variation).[16] Controlling for a rich array of variables, the authors modeled the likelihood of delinquency and default.[17] They found that having received assistance toward one's downpayment and closing costs has no significant effect on CAP homeowners' mortgage performance. Thus, there is no evidence that homeownership should be restricted to those who can put 20 percent down.

Policy Implications

Sherraden challenged all of us to shift our focus from short-term, consumption-based welfare for lower-income people to the promotion of long-term, asset-supported economic well-being. For many families, homeownership is an important component of a long-term asset-building strategy. It may begin with the process of saving for the home purchase, continue as the self-amortizing mortgage builds equity, and extend all the way through the retirement years.

The collective evidence presented here refutes a number of commonly held but poorly substantiated claims about the pitfalls of homeownership for lower-income, lower-wealth families. There are real risks associated with homeownership, but by examining the real-life experiences of participants in the CAP program, we find that homeownership has been a beneficial proposition on the whole for these households. These findings are particularly noteworthy because they persist through recent market turmoil that has negatively affected comparable renter households.

There are important caveats to these findings. First, not all the CAP borrowers and renters had identical experiences; in particular, homeowners who bought at the wrong time and in volatile markets fared worse. Second, the experience of the CAP homeowners cannot be generalized to all lower-income borrowers over this same period, because the type of financing used is a key determinant of the financial trajectory of investing in a home. Borrowers who used more costly, riskier products were not as fortunate as CAP borrowers, and many have lost their homes as a result. We are not proposing that owning a home is a fail-safe solution to economic turmoil. Owning a home is no substitute for good jobs, affordable health care, a strong economy, and a comprehensive social safety net. Many households are better off renting, some households prefer to rent, and renting offers advantages that homeownership does not, chief among them ease of geographic mobility.

However, when homeownership works well, it can enable lower-income families to remain in their homes over the long term and begin to accrue wealth, and it can do so even in turbulent economic times. What factors allow this to happen? Certainly appropriately structured mortgages are crucial. Our research demonstrates that fixed rate mortgages that are carefully underwritten to ensure affordability over time are the most likely to lead to enduring homeownership (Ding et al. 2008). Importantly, these mortgages do not require a 20 percent downpayment; within CAP, the median loan-to-value ratio at origination is 97 percent, meaning that half of CAP's owners put down 3 percent or less when they purchased their homes.

Will an emphasis on carefully originated mortgages require major changes on the part of banks? No: in order for banks to lend sustainably to LMI families, they only have to return to practices from their recent past. Banks already know how to underwrite loans for borrowers' ability to repay; they did so for decades before the subprime lending crisis. Things went wrong only when lenders stopped doing this: when they began issuing low-documentation or no-documentation loans, when they began approving loans whose monthly payments would explode after a few affordable years, and when they began issuing loans in which borrowers did not pay down principal each month and loans that stripped borrowers of wealth outright.

As we redesign a housing finance system for the future, we must do so with a focus on its being both inclusive and sustainable. What will enable this? The mortgages in the CAP portfolio were issued in order for banks to meet their requirements under the Community Reinvestment Act, which states that banks make credit available throughout their entire service area, consistent with safety and soundness. Access to credit by LMI households is entirely compatible with safety and soundness for banks; these things are not at odds, but rather support one another. How?

Safety will be promoted for both banks and households when banks issue credit that is designed to remain affordable over the long term. By providing access to mortgages that endure over the long term, lenders can foster a robust market in which people can buy and sell homes. Mechanisms such as the credit enhancement that the CAP program provides can help financial institutions renew sound lending in affordable markets. The CAP program has facilitated billions of dollars in mortgage lending to LMI households by bridging the gap between banks and the secondary market. Because of the $50 million that Self-Help provided to mitigate any losses associated with the underlying loans, more than 46,000 loans were moved off of banks' balance sheets and into the secondary market. This freed up capital for additional loans to be made to LMI families. CAP is a model for a national credit enhancement fund that could bring the wealth-building effects associated with affordable homeownership to scale.

Yet trends in mortgage lending rules and regulations threaten to close off access to homeownership by the very types of households whose successes we document in the chapter. Deciding that such families should not have access to homeownership has major implications. For the US housing market, it means stripping off a growing demographic that could be the key to a sustained recovery and long-term vitality. For lower-income households, it means denying them the wealth-building opportunities that the CAP owners have experienced and that Americans have relied upon for decades for their economic betterment.

Curtailing access to homeownership would be particularly detrimental to the long-term economic prospects of minority households in this country. The racial wealth gap (blacks hold an estimated $5 for every $100 of net worth held by whites[18]) is due in large part to racial gaps in homeownership rates: currently 74 percent of non-Hispanic whites own their homes, while only 45 percent of blacks enjoy this same privilege (US Census Bureau 2011). The ongoing mortgage finance crisis will only exacerbate wealth inequality in America, owing to the high incidence of subprime lending in predominately black neighborhoods (see Immergluck 2009 and Rugh and Massey 2010). Between 2004 and 2008, blacks were close to three times as likely as whites to receive higher-rate loans (Bocian et al. 2011).[19] The result is that approximately 25 percent of black borrowers are now seriously delinquent or in foreclosure, compared with 12 percent of white borrowers (ibid.). The unequal impact of the housing finance crisis will have ramifications for generations to come as blacks lose the opportunity to build wealth through their homes.

Without access to homeownership—the classic pathway to the American middle class—how else will low-resource households begin to build an economic base? The real-life experiences of the CAP participants demonstrate that homeownership is still a viable route to building assets for working LMI families who are ready to take on the responsibility of owning a home. The lessons learned from the practices of the lenders who participated in the CAP program—who issued carefully underwritten, fixed-rate loans that are well serviced—offer a model for how to help households and the housing market begin to recover from the financial crisis.

Notes

1. Between 1998 and 2009, CAP purchased more than 46,000 loans made to lower-income households, funding an estimated $4.06 billion in purchase money mortgages. CCC has tracked these home loans since origination. In 2003, we began our series of annual phone interviews with a sample of over 2,000 of these homeowners. In 2004, we began annual interviews with a panel of renters matched to the homeowners by income and geography.
2. All statistics in this section of the chapter come from the CAP generalizability sample.

3. Rates of serious delinquency come from Mortgage Bankers Association, *National Delinquency Survey* (2011) (Moody's Analytics' Databuffet.com). Figures are from the third quarter of 2011.
4. CAP home values are calculated using a zip code-level house price index that is proprietary to Fannie Mae. The Fannie Mae index provides a more accurate estimate of home value than do publicly available house price indices (such as the FHFA index, formerly OFHEO) because it relies on information at the zip code, rather than MSA or state, level.
5. This figure is the latest Fannie Mae value minus the last unpaid principal balance. It is biased downward (i.e., it is conservative) because some loans are inactive and therefore "stopped in time" at a lower level of equity.
6. All of the papers relying on the CAP data confront a similar problem, namely, bias in sample selection. Because random assignment into homeownership is unrealistic, there is inevitable bias in the studies comparing CAP's owners and renters. When comparing owners and renters, it is difficult to say whether the changes in wealth we observe result from homeownership or from particular individual, social, economic, and demographic factors that are associated with homeownership and likely increases in wealth. Therefore, each of the papers underlying the chapter uses advanced statistical techniques to address selection bias. Interested parties should refer to these papers for extensive detail on the various analyses conducted.
7. Tenure status (owner/renter), which is the main independent variable, is potentially endogenous, because individuals choose whether to own or rent. Therefore, the authors use four different methods, namely, propensity score matching, propensity score weighting, coarsened exact matching, and instrumental variable regression, to make sure that the measured effect of homeownership cannot simply be attributed to the fact that homeowners are systematically different from renters. The predictors of homeownership that the authors consider are age, gender, marital status, race/ethnicity, relative income, the presence of children in the home, and dwelling type.
8. For a description of how this score was calculated, see Manturuk and Ratcliffe (2011).
9. This analysis draws on the two years of CAP data, 2005 and 2008, in which the panel survey included an extensive module related to participants' wealth. Sample sizes are 982 owners and 595 renters matched to owners.
10. In fact, the authors used the joint distribution generated from the copula function to derive the adjustment of each element of the financial portfolio in response to a shift in home equity. They tested all portfolio variables (both asset and debt) at the same time. These variables included the following: transaction account balances and CDs, investments (stocks, bonds, and retirement), equity in nonprimary residences and major durables, credit/charge card debt, student loan debt, and borrowing against the home (i.e., the combined value of home equity lines of credit, second mortgages, and cash-out refinance amounts). Asset and debt variables are discussed separately here for ease of discussion.
11. In the interest of conservative inference, Freeman and Desmarais place 99 percent confidence intervals from the simulation around the estimates.
12. The authors set this equal to the return on a six-month treasury bill, reduced by the taxes that the household would have paid on such interest.
13. Some argue that LMI households do not benefit from the mortgage interest tax deduction. However, of the 2,701 CAP owners who completed the 2005 phone interview, 60 percent filed for the mortgage interest tax deduction.
14. While most of this assistance likely came from sellers rather than real estate agents, it was not possible to disaggregate this response further due to the wording of the survey question.
15. Analysis in progress; contact allison_freeman@unc.edu for details. This research employs multilevel logistic regression analysis with random state intercepts to account for unobserved heterogeneity at the state level. The dependent variables, which were measured in 2003, include whether a respondent (1) received assistance in any form; (2) received parental assistance; (3) took out a second mortgage; (4) received assistance from a community grant; and (5) received assistance from a real-estate agent. Separate logistic regression models are used (instead of a multinomial model) because the outcomes are not mutually exclusive (i.e., some people received more than one kind of help). Independent variables, also measured in 2003,

include respondent race, gender, age, education, marital status, number of minors living in the home, employment status, and income (scaled by Metropolitan Statistical Area-level median income). Several financial literacy variables are also included: whether respondents' parents had a checking account, whether respondents' parents taught financial skills, and whether respondents prefer to save or spend. Finally, the analysis controls for loan-to-value ratio at origination, respondents' credit scores at origination, and debt-to-income ratio at origination.

16. Analysis in progress; see previous footnote and contact allison_freeman@unc.edu for details.
17. Control variables include age, race/ethnicity, sex, marital status at baseline, education at baseline, relative income at baseline, number of minors in the home at baseline, respondent's employment status at baseline, being a two-income household at baseline, origination loan-to-value ratio, credit score at origination, debt-to-income ratio, whether or not one received assistance toward one's downpayment and closing costs, whether or not the respondent's parents held bank accounts when the respondent was young, respondent's assessment of how much his/her parents imparted about managing money, and respondents attitudes toward spending versus saving money.
18. This figure is calculated from 2009 data. For details, see Taylor et al. (2011).
19. "Higher-rate" is defined as first-lien loans for which the APR spread was 300 basis points or more above Treasuries of comparable maturity.

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Chapter Eight
A Behavioral Economics Perspective on Innovations in Savings Programs

Piyush Tantia, Shannon White, and Josh Wright

Many programs designed to increase saving behavior among low-income households fail to attract and retain the expected numbers of participants, and thus have only limited large-scale impact. These disappointing results have led to debates about the cost effectiveness and general merit of funding such efforts. At the root of these debates are some more fundamental questions about why people find it so hard to save, and routinely make poor saving decisions. Why, for example, do even those who have the capacity to put some money aside for emergencies routinely fail to do so, resulting in their incurring expensive debt or late fees when an emergency does occur? And why do people underutilize savings programs and products that would help them stabilize their finances and accumulate savings when these are made available to them?

It is routine to attribute the failure of such programs to the values or capacities of those they target. For instance, some argue that those with low and moderate incomes fail to save because they do not fully understand or appreciate the importance of thrift, while others suggest that those with lower incomes lack the capacity to make adequately thought-out, long-term financial calculations. However, research in the applied behavioral sciences makes it clear that wealthy, middle-class, and lower-income individuals all exhibit a number of frailties and quirks in their decision making. Across the income spectrum, people are frequently impatient and prone to poor planning. The difference is that the stakes are higher, and the decisions harder, for those living under precarious financial conditions.

Policies and programs aimed at improving saving behavior have traditionally been built on a set of standard assumptions about human behavior, for example, that preferences are consistent, that all information is processed accurately, and that decision making is not influenced by extraneous information. As a result, savings policies and programs have focused primarily on a two-pronged approach involving increasing incentives and offering more information. Incentives usually take the form of matching contributions, while information often includes educational sessions and pamphlets about things like the cost of living during retirement, the increasing cost of college education, and so on. While successful to a degree, these methods have repeatedly failed to bring about the expected and desired magnitude of behavioral change. Low participation rates

in 401(k) plans with matching contributions have been compared to passing up "$100 bills on the sidewalk" (Choi, Laibson, and Madrian 2005). Tax deductions for retirement plan contributions have appeared not to improve savings contributions among low- and moderate-income families very significantly (Duflo et al. 2007). Moreover, such programs are often costly, both administratively and because they rely primarily on financial incentives (e.g., matching contributions) to motivate saving behavior. Even excluding the cost of matches, Individual Development Accounts (IDAs) cost about $64 per participant per month (Boshara 2005).

By contrast, applied behavioral economics demonstrates that large impacts do not necessarily require either large administrative investments or large financial incentives. Significant improvements in participation, retention, and use can be achieved through slight tweaks in a program's structure or communications. Historically, policymakers and program designers have paid little attention to the impact of design on behavior, and may thus have inadvertently discouraged participation and retention. For example, enrollment and participation procedures are often demanding, unpleasant, or opaque—all of which have been shown to significantly decrease the take-up of programs. Conversely, integrating behavioral principles into policies and program design offers a range of low-cost solutions to improve saving behaviors, leveraging small "nudges" to achieve large impacts.

This chapter outlines some key principles of behavioral economics, examples of interventions that have incorporated these insights, and future directions for the development of savings programs and policies. The behavioral principles underlying saving decisions are too numerous for an exhaustive description in this chapter. Instead, we present what we believe to be the most important behavioral principles in four simplified categories useful for the design phase of a policy or program: suboptimal decision making, intention-action gaps, depletion, and scarcity. The discussion of recent behavioral interventions will reveal that some concepts and principles of decision making overlap; a single intervention can improve saving by addressing multiple causes of low engagement levels in a program. However, because many distinct psychologies also contribute to similar behaviors, the effectiveness of interventions can vary between contexts and target populations. In the final section, we provide examples of new ways to increase saving through behavioral interventions, explain why rigorous testing is an important part of program development, and suggest that behavioral interventions in particular can help develop scalable and sustainable savings programs. As with the behavioral perspectives, our discussions of existing interventions and future recommendations are not intended to be exhaustive; rather, we will highlight a few, high-potential ideas to begin a dialogue on further developing policies and savings programs.

Principles of Behavioral Economics Underlying Savings (and Many Other) Behaviors

While people with low incomes face unique challenges to saving, many of the behaviors that can inform savings program design are common to all individuals. An individual's decisions and actions in many aspects of life—from saving and spending to health care and education—are driven by similar kinds of mental short-cuts, situational influences, and fatigue.

Behavioral economists have devised "dual-self" models to account both for "rational" behaviors aligned with standard economic models and for behaviors deviating from

such models' predictions. In Richard Thaler and Hersh Shefrin's account (1981), one half of this dual-self is the "Planner": deliberate, slow, logical, self-aware, and effortful. Psychologists use the umbrella term "executive functioning" to describe activities at which the planner excels, such as problem solving, reasoning, planning, sustaining attention, and exerting self-control (Chan et al. 2008). In contrast, the "Doer" is impulsive, fast, intuitive, and error prone, and his actions involve neither effort nor much voluntary control.

Since humans could not possibly attend to and actively process all of the information they encounter, the Doer is quite useful for navigating a complex world. Automatic and intuitive thinking helps one complete hundreds of tasks without conscious effort (eating, grooming, skimming an article for key words, etc.). However, a foundational principle of behavioral economics is that people do not always engage these different modes of decision making at the appropriate times. For example, people tend to eat mindlessly, even to the point of eating more if their serving containers are large (Wansink and Park 2001; Wansink and Kim 2005; Wansink and Payne 2008). Conversely, the dinner companion who takes thirty minutes to choose an entrée might have enjoyed the evening more had he deliberated less.

Furthermore, one's capacity to act as the Planner is limited. Researchers have described our exhaustible capacity for executive functioning with metaphors, such as a muscle that can be fatigued with use (Muraven and Baumeister 2000; Baumeister 2002; Gailliot 2008; Schmeichel, Bohs, and Baumeister 2003), or a "mental bandwidth" that is not only limited but also functions more poorly as it is more heavily used (Laury and Mullainathan 2010). As a consequence of such limits, making the right decisions about saving, following through with plans to save, and engaging repeatedly in behaviors necessary for saving are all more difficult than standard models—even those that incorporate transaction costs—would predict. Financial constraints compound these difficulties; because managing a tighter budget is intrinsically more mentally taxing, those who have the least room for error, indulgence, or fatigue have the most depleted capacity to manage their lives, financial and otherwise.

Suboptimal Decision Making

In some versions of standard economic theory, individuals who have properly aligned incentives and access to all relevant information will make optimal decisions. However, research shows that our decision making can be biased, based on rules of thumb, swayed by social influences, or even self-undermining. While a number of decision-making tendencies contribute to saving behaviors, the following are particularly common.

Financial decisions are often influenced by reference points. One consequence of this is that losses tend to loom much larger than gains. Such loss aversion leads people to prefer the status quo and to value current possessions disproportionately (Tversky and Kahneman 1991; Kahneman, Knetch, and Thaler 1991). Saving, often felt as an immediate loss, may be significantly more unpleasant than the perceived benefit of gaining that same amount of money. Another consequence of reference points is anchoring, or clustering decisions around a number that serves as a reference point. For example, the asking price for a house may influence how much one is willing to pay for it (Thaler and Sunstein 2009, 23–4). This also affects saving and spending: employee savings in a 401(k) plan tend to be influenced by suggested contribution rates (Madrian and Shea 2011).

Violating standard assumptions of fungibility, people also tend to adjust spending within different budget categories (rent, food, and shopping) and mental accounts. Current income, assets, and future income are treated differently, with the highest propensity to spend current income (Thaler 1985). Similarly, because paying with cash makes the "pain of payment" salient, one may spend less freely when paying with cash than when using a credit card, which offers immediate consumption and delays the "painful" moment of payment (Prelec and Loewenstein 1998). The opposite holds in the case of saving: the saver experiences the pain of paying in the moment, but the increased consumption that savings makes possible lies well in the future.

Furthermore, people often have inaccurate beliefs or preferences about probabilities. They may be overconfident about their ability to manage finances, just as the vast majority of people tend to think they have superior intelligence, health habits, driving habits, immunity to cognitive biases, and chances of succeeding in a start-up business (Hoorens and Harris 1998; Svenson 1981; Pronin, Lin, and Ross 2002; Cooper, Woo, and Dunkelberg 1988). People also tend to be risk-seeking for low-probability gains or high-probability losses (Tversky and Kahneman 1992). Both tendencies can explain behaviors that appear myopic or foolish, such as chasing ill-fated get-rich-quick schemes or purchasing lottery tickets, while neglecting the slow and steady accumulation of savings.

A broad class of social influences, such as a tendency toward conformity and a fear of shame or reproach, can also impact saving behavior. For example, individuals' participation in their employer's retirement program, as well as their vendor selection, tended to conform to their peer group's behavior (Duflo and Saez 2002). Personal relationships can affect whether or not borrowers remain current on their payments (Drexler and Schoar 2011), and groups built on mutual accountability have been used as integral components of savings commitments, as with Rotating Savings and Credit Associations (ROSCAs) (Basu 2008) and microcredit programs (Gine and Karlan 2008).

Without a status quo, anchor, or social norm to serve as a reference point or standard, making any decision at all can be difficult. In a set of studies on choice overload, subjects were more likely to make a selection when offered fewer options, such as a smaller assortment of jams, chocolates, or mutual funds in a retirement account (Iyengar and Lepper 2000; Iyengar, Huberman, and Jiang 2004). Without a simple way to make a selection, the very process of making a choice, such as which bank to begin a relationship with if one is unbanked, can be daunting enough to delay or even prevent a person from making the decision at all.

Intention-action Gaps

A failure to follow through on one's best intentions is a pervasive feature of our decision making. People have a tendency to overestimate the significance of their intentions and underestimate the importance of situational or contextual factors when making predictions about their future behaviors (Koehler and Poon 2006). As a result, goals can be sabotaged by temptations or the chaos of daily life in spite of one's strongest convictions.

Choices about saving or spending right now are qualitatively different from—and inherently more susceptible to temptations than—choices about saving or spending in the future. People display a tendency toward selecting "shoulds" when pay-offs are in the more distant future (like beginning a jogging routine tomorrow—and really sticking to

it this time) and "wants" when pay-offs are in the near future (like watching *Mad Men* instead of jogging—but just for today). In one experiment, people were more willing to commit to a savings plan when they would be enrolled in the distant future instead of the near future (Rogers and Bazerman 2008). In fact, completely different neural systems are activated for choices that involve present pay-offs versus choices that involve only future pay-offs (Loewenstein and Prelec 1992; McClure et al. 2004).

In addition to want/should conflicts, people face struggles to navigate unexpected hassles, to attend to and remember important details, and to cope with unexpected set-backs that contribute to a range of planning failures. A common example in time management is called the planning fallacy, or the tendency of individuals and organizations to take significantly longer to complete a task than planned, even when similar planning mistakes have been made before (Kahneman and Tversky 1979). A correlate can be seen in budgeting: giving up on a long line at the bank delays opening an IRA, failing to notice the fine print leads to an expensive mortgage, and so on. It is easy for savers and program designers alike to underappreciate just how complex saving can be. It requires several small, repeated choices, some of which may involve an elaborate series of coordinated steps. Obstructions at any point could derail the whole plan to save.

Depletion

Even if individuals manage to avoid or overcome a host of proclivities, temptations, and hassles long enough to make difficult but prudent savings choices, their capacity for making such choices is subsequently diminished. Acting as a Planner today—for example, by attending to important information and acting appropriately on it—actually depletes one's ability to act as a Planner tomorrow.

When mental bandwidth is exhausted, people are less able to perform tasks and self-regulate in all aspects of life. One set of researchers observing air traffic controllers in their homes found that they were more likely to exhibit anger toward their spouses on days that a different set of researchers marked as high-traffic days (Repetti 2006). Some theorize that self-regulation breaks down specifically when individuals are mentally exhausted (Baumeister and Heatherton 2009). For example, people tend to choose chocolate cake over fruit salad immediately after performing difficult cognitive tasks (Shiv and Fedorkhin 1999), suggesting that self-control and cognitive performance rely on the same mental resources. Saving money, or even trying to take steps to save money, can paradoxically undermine one's immediate ability to save.

Many of the interventions that address more specific behavioral problems are effective because they relieve the tax on mental bandwidth and prevent depletion. In one experiment, providing information about Free Application for Federal Student Aid (FAFSA) forms had no effect on filing, while offering assistance and prepopulating the maze-like forms increased rates not only of filings but also of college attendance (Bettinger et al. 2009). Precommitment, such as cutting up credit cards, secures a "should" choice, reducing the effort needed to resist temptations in the present. Reminders outsource one's need to retain and recall information at appropriate times. Structuring some options to engage the doer—such as providing an anchor or a social norm, quickly directing behavior that otherwise has no reference point—frees mental bandwidth for the planner to attend to more difficult decisions and resist temptations. Interventions to relieve taxes on mental bandwidth may change behavior most significantly among those who are already struggling to manage their lives.

Scarcity: How a Lack of Slack Creates Vicious Cycles

Saving behaviors (or lack thereof) have consequences as trivial or as dire as the constraints facing the individual in question. Traditionally, explanations of the behaviors of poor people have been driven, implicitly or explicitly, by two dominant views. Either poor individuals are thought to be making optimal choices under harsh constraints, or they are thought to be succumbing to a culture with deviant values. Poor people are thus seen in one of two extreme situations: they are either calculating (though perhaps unlucky) individuals and need little or no help with their goals, or they are people whose principles are so flawed that they need heavy-handed assistance.

A third view paints a picture of dynamic interaction between person and environment: People with low incomes have the same decision-making tendencies and imperfections as everyone else, but they have less room for error, rendering suboptimal choices and behaviors more consequential (Bertrand, Mullainathan, and Shafir 2004; Mullainathan and Shafir 2009). For poor families, a lack of slack in their finances and a lack of slack in their mental bandwidth can easily snowball. Scarce financial resources require significant attention and energy to manage, but depleted attention and energy increases the propensity toward mismanagement. Not only do relatively volatile and unstructured lives present logistical challenges to saving, but ever-present financial problems further diminish the capacity of low-income people to manage both their finances and other aspects of life.

The majority of expenses for lower-income households are very basic; indulgences, errors, or shocks can lead to more severe hardships that reverberate in every aspect of their lives. For example, a nationally representative survey found that food stamp recipients consume fewer calories toward the end of the month than the beginning of the month, when they receive food stamps (Shapiro 2004). A complementary study shows that the children of food stamp recipients in Chicago were more likely to have disciplinary problems in school toward the end of the month (Gennetian and Winn, forthcoming). A failure to smooth consumption did not, as it would for the wealthier classes, merely result in an irksome credit card balance or a resolution to avoid Starbucks for a year; rather, small indulgences or planning errors early in the month led to enough hardship that children were struggling in school. Financial shocks can have similar ripple effects: an emergency car repair may lead to work tardiness, an inability to pay for other bills, and skimping on important but unnecessary items such as school supplies. The financial problems of low-income families are rarely confined to their finances.

Not only are shocks more consequential, but they are also more common. The lives of low-income families are relatively volatile. Working hours fluctuate, jobs are less stable, and home and auto repairs are needed more frequently. In one study, within a 12-month period, 90 percent of low- to moderate-income households in the Detroit area experienced a major illness or medical expense, eviction, utility shutoff, or a bankruptcy filing, and 35 percent reported being unable to meet their living expenses during more than six months of the year (Barr 2009). Worse, many of the structures and institutions available to help smooth income and make saving easier are currently unavailable to, or underutilized by, poorer individuals. Moderate- and high-income individuals have relatively easy access to direct deposit, automatic bill payments, low-interest-rate loans, "no fee" accounts, advisers, flexible employers, and systems that send reminders of financial obligations to help manage and stabilize their finances (Mullainathan and Shafir 2009). Many of the lower-income individuals who do manage to save are unbanked or underbanked, leaving their savings more vulnerable to theft, impulse spending, or use by

family members (Berry 2004; Bertrand et al. 2004). Hence, along with smaller budgets, poor families have more hassles, emergencies, and distractions that make managing needs—independent of mental bandwidth constraints—intrinsically both more difficult and more important.

Such struggles occupy mental bandwidth that could otherwise be used for other important tasks. In a telling study, researchers approached people in a mall and randomly asked some of them to imagine their car breaking down and incurring a few thousand dollars in expenses. Low-income subjects (but not high-income subjects) subsequently performed worse on cognitive tests, while there was no significant difference in test results between low- and high-income individuals who had not been asked to imagine the financial shock (Mullainathan and Shafir 2010). When there is no slack to cover expenses, the problem becomes so intractable and so consuming of a low-income person's mental energy that even a hypothetical scenario causes their observed cognitive levels to be lower.

The constant difficulty of managing needs, especially when one's future may be uncertain or unclear, can cause poor people to focus too much on information relevant to present but not future needs (Mullainathan and Shafir 2009). A well-known correlate in time management literature is called "urgency addition," or a compulsive attending to urgent but not necessarily important matters (Covey, Merrill, and Merrill 1994; Koch and Kleinmann 2002). Without slack, such tunnel-vision impacts decision sets down the road. For example, taking out a payday loan for car repairs reduces cash flow even more in the next pay cycle, when later financial shocks may require still more creative cash flow solutions (Bertrand, Mullainathan, and Shafir 2004). Because the financial and cognitive constraints faced by poor individuals produce such ripple effects, policies and interventions that are very successful for moderate- and high-income individuals may be ineffective (or even problematic) for lower-income individuals. Despite these groups' shared behavioral tendencies, situational constraints add a layer of complexity to saving for lower-income individuals.

Innovations in Savings Programs

The last decade has seen many new behavioral applications to savings programs. The resources available to moderate- and higher-income individuals—such as direct deposit of paychecks and Vanguard's tax refund splitting services—have often served as models. Program designers have not needed to reinvent the wheel or request exorbitantly large increases in their budget in order to see improvements. Two major types of savings programs—tax refund savings accounts and savings accounts designed for regular deposits—exhibit behavioral elements in both their structures and their outreach efforts. While a variety of behavioral interventions have been tested, a key component of most changes is a shifting of constraints: making enrollment and saving behaviors easier while simultaneously making withdrawals harder.

A description and analysis follows of how specific savings programs have been informed by behavioral features. The challenges presented by recent savings programs offer useful lessons for refining program designs. Not all behavioral interventions will work as planned. An intervention to improve one behavior may exacerbate another. It may be necessary to balance different program goals in order to optimize overall saving behavior in target populations. While not every feature will fit all programs, the efforts and challenges of different programs can be mutually informative and inspire further policy developments and program design.

Defaults and Automating Processes

Just over a decade ago, Brigitte Madrian and Dennis Shea (2001) discovered one of the most powerful remedies for low participation and savings contribution rates: defaults. In their seminal study, 80 percent of employees remained in their company's 401(k) plan when automatically enrolled, compared to only 13 percent of those who needed to opt in actively in order to participate. Furthermore, most participants stuck with the default allocation and contribution rate. Default enrollment meant that the choice that most employees were too busy, unmotivated, or distracted to make, even though they expressed interest when surveyed, was already made for them. A number of behavioral bottlenecks to saving were resolved using one sweeping intervention. In another example, SEED OK (Save, Earn, Enjoy Deposits for Oklahoma Kids), a Child Development Account program, had nearly 100 percent uptake with automatic enrollment; opting out was possible, but hardly anyone did (Sherraden and Stevens 2010; Nam et al. 2012).

Like automatic enrollment, direct deposit bypasses the pain of lost income, the hassles of physically making deposits, and the mental tax of remembering to do so. Both IDAs and AutoSave, an employer-based savings account, offer this option. In one study, those who used direct deposit for IDAs saved more and were 22 percentage points less likely to drop out of the program compared to those who did not opt to use direct deposit (Grinstein-Weiss, Wagner, and Ssewamala 2005; Schreiner, Clancy, and Sherraden 2002). AutoSave, an employer-based savings account, has sought to entice participants to enroll in direct deposit with catchy slogans such as "Save it and forget it!" (Lopez-Fernandini and Schultz 2010).

To address both loss aversion and inertia, the Save More Tomorrow (SMarT) program uses a particularly effective automatic enrollment feature: paycheck deductions toward retirement plans are initially set at a comfortably low percentage of income but automatically increase with each pay raise. Employees are only signing up for lower future gains, rather than suffering a loss of current income. The pilot was remarkably successful: 98 percent of participants remained in the program after two pay raises, leading to average savings rates of 13.6 percent among those who joined SMarT (up from 3.5 percent) (Thaler and Benartzi 2004).

Unfortunately, defaults and automating processes—two of the most powerful interventions in the behavioral toolbox—are often not logistically possible, legal, popular, or even effective. For example, policies wherein a default is possible, such as automatically opening a college savings account for all school children, may face political resistance nationally. Even when there are no logistical or legal barriers, defaults simply may not work. In a recent study of lower-income filers at eight Volunteer Income Tax Assistance (VITA) sites, tax refunds were automatically diverted to savings bonds, unless filers opted out. Those with an adjusted gross income of less than $18,000 opted out of the savings program at such high rates that the default was found to produce no statistically significant increase in savings (Bronchetti et al. 2011). Participants in the savings bond study may have had plans for their tax credit already, whereas not every dollar necessarily has a specific purpose in the typical moderate-income budget.

Other efforts to automate saving may have limited success because low-income families might fear being unable to manage volatile cash flows. A savings program called SEED (Save, Earn, Enjoy Deposits) in the Philippines had 202 participants, and only 2 opted for automatic transfers into their savings accounts (Ashraf, Karlan, and Yin 2005). While defaults may bypass a range of issues that could hinder saving behaviors, they may not in themselves convince individuals to save money already earmarked for other purposes.

Convenience and Simplicity

While defaults and automating processes may not always be possible or even preferable, program designs can still bypass most causes of intention-action gaps and reduce choice overload by making enrollment convenient. Two programs that promote saving out of tax refunds, Refunds to Assets (R2A) and $aveNYC, had staff working at tax preparation sites to sign up clients onsite (Beverly, Schneider, and Tufano 2006; Black and Cramer 2011). The AutoSave program enrolls people while at work so that no trips to the bank are required; its designers also hope to make it part of the orientation process for new employees (Lopez-Fernandini and Guge 2010; Lopez-Fernandini and Schultz 2010). From the perspective of potential participants, having the enrollment process streamlined and options simplified also reduces hassles and the tax on mental bandwidth. AutoSave also attempts to increase uptake by minimizing paperwork and prepopulating form fields (Lopez-Fernandini and Guge 2010; Lopez-Fernandini and Schultz 2010). Both AutoSave and $aveNYC are designed to prevent choice overload by keeping options, such as available financial institutions and account options, to a minimum (Schultz et al. 2010; Cramer 2011). H&R Block created a simple and transparent structure for their tax refund savings program, which they explained in a straightforward manner (Duflo et al. 2006).

However, increasing convenience and simplicity can have two negative consequences. First, oversimplification may lead to attractive features of a program being removed. For example, program designers of AutoSave attempted to make the enrollment process easier by limiting options, such as offering only one available financial institution. While the simplified process may have made the program attractive to many participants, it was also listed as one of the top five reasons for not participating, as some individuals already had primary accounts at other institutions and did not want to juggle multiple relationships (Schultz 2010). Second, streamlining and simplifying processes requires a lot of effort upfront. These types of burdens may dampen support for a program if they require those implementing programs to invest a large amount of time and energy.

In addition, an inability to implement a program as planned may reduce its effectiveness. For example, 62 percent of one site's employees enrolled in AutoSave, while only 2 percent of employees at another site did. Sites with the highest take-up rates tended to have managers very dedicated to ensuring participation through small group sessions and follow-up communications (Schultz 2010). Employers with lower uptake rates may not have been convinced of the value of the program or may have lacked the bandwidth to accept additional responsibilities. Where possible, reducing hassles and simplifying structures for the implementation, staff could encourage participation both among participants and among partners.

Channeling Mental Accounting

The structures of some savings programs have also been designed to channel savers' natural mental accounting tendencies. AutoSave keeps savings segregated from participants' primary account (Lopez-Fernandini and Schultz 2010), from which participants would have a high propensity to spend. Participants listed this feature as a primary reason for signing up, saying it helped in "hiding money from myself" (Schultz 2010). Earmarking and labeling savings accounts may also motivate saving. For example, the SEED program in the Philippines involved labeling the savings account for a specific purpose, such as saving for a wedding, so that the savings goal was concrete (Ashraf, Karlan, and Yin 2005).

The basic idea behind the tax refund savings programs is that people are more likely to put irregular income, such as the Earned Income Tax Credit (EITC), into savings than their regular income. In a moment of high liquidity after receiving a lump sum, people may feel more comfortable committing to saving in the future. In one study, the ability to use tax refunds as an opening deposit was cited as the second most important reason for opening an Extra Credit Savings Program (ECSP) account (Beverly et al. 2001). Receiving a refund or another similar windfall may even offer a brief mental "reset moment" (Gennetian, Mullainathan, and Shafir, forthcoming), briefly clearing individuals' minds of their financial struggles, freeing them to think of the future. A small but significant portion of surveyed R2A participants said that they opened an account to "try something new" (Beverly, Schneider, and Tufano 2006), and it would be interesting to see if this openness is more prevalent among EITC recipients around tax time.

The issue with this strategy, however, is that many EITC recipients make plans to spend this "windfall" income long before tax time, often in a ritualistic manner. In one survey, families reported either plans to indulge (e.g., going out to dinner "to all the places they could never normally afford") or regular plans to purchase goods (e.g., "I always buy furniture with my tax money") (Romich and Weisner 2000). One of the top reasons individuals cited in surveys for not participating in the R2A program was that they already had plans for the refund (Beverly, Schneider, and Tufano 2006). In contrast to moderate- and high-income individuals, who might not have immediate plans for windfall income, the lack of slack in low-income individuals' budgets makes spending the EITC either more necessary or more tempting. After a year of careful planning and conscientious spending—perhaps even foregoing basic necessities to get by—the tax refund offers a moment of relief from regular financial struggles; giving up this luxury may be felt as a particularly painful loss.

Increasing Access to Institutions

Because many lower-income individuals have had negative experiences with financial institutions, it is important to restore participants' comfort level and trust by making the program as accessible as possible. Increasing accessibility appears to have encouraged uptake of savings programs: a lack of fees or minimum balances were cited as top reasons for opening an ECSP account and an R2A account (Beverly et al. 2001; Beverly, Schneider, and Tufano 2006).

Easy access to the financial institution itself may influence uptake. One telephone survey respondent from the ECSP program said,

> Where I work at there is a [ShoreBank] on 31st and Kings Drive so I'm walking distance [of] that, so I go there basically all the time now (Beverly et al. 2001).

Furthermore, while rent-to-own stores, payday lenders, and other expensive alternative financial services advertise that they accept customers with bad credit, most banks would deny access to financial products to those with poor or no credit history. However, the AutoSave team and H&R Block piloted products that accepted clients with a history of bad credit management (Lopez-Fernadini and Schultz 2010; Duflo et al. 2006), potentially helping to restore a sense of good rapport or reducing the fear of shame for past financial mismanagement. In contrast to the federal Saver's Credit, which has extensive rules limiting the eligibility of a tax credit for savings contributions, H&R Block offered matching contributions for tax refund splitting to all tax filers at sites in low-income

areas (Duflo et al. 2006). Of course, the main complication with increasing accessibility is resistance from stakeholders and financial institutions, since supporting higher-risk individuals who maintain smaller account balances may not be profitable. To overcome behavioral risk problems, increased accessibility might be coupled with features that decrease risks and costs in other ways.

Decreasing Access to Funds

Decreasing access to funds can help participants maintain balances. While simply having money in a bank rather than in one's pocket can curb temptations, extra restrictions on withdrawals can help prevent the depletion of savings for nonemergency purposes. Some R2A participants said that they opened an account specifically to avoid spending all of their refund (Beverly, Schneider, and Tufano 2006). $aveNYC goes a step further: account holders can withdraw funds only from a teller, not from an ATM. This strategic hassle was cited by 59 percent of surveyed participants as a reason for signing up for the program, in which 80 percent of 2,200 participants saved their refund for the full term of the study (Cramer 2011). In the SEED program in the Philippines, 83 percent of participants opted to use a simple "ganansiya" box, like a piggy bank, for which only the bank had a key, and this group was more successful in maintaining savings balances (Ashraf, Karlan, and Yin 2005).

Different types of withdrawal restrictions have varying degrees of effectiveness and popularity, sometimes in ways that require balancing participation rates with saving rates. Lighter restrictions on withdrawals, such as allowing AutoSave participants to access funds from an ATM, might make the program more attractive while also making it easier to succumb to temptations; 27 percent of AutoSave participants made frequent withdrawals from their accounts (Schultz 2010). One-year retention was high in $aveNYC, where withdrawals were more difficult, but only 30 percent of participants chose to use the program again the following year (OFE 2010). Similarly, decreased access to funds in a 401(k) plan is associated with decreased participation rates (Munnell, Sunden, and Taylor 2001/2002).

Surveys and focus groups reveal significant demand among low-income populations for limits on the number of unrestricted withdrawals. Limiting withdrawals to a specific purpose or goal (perhaps with allowances for emergencies) or limiting the number of withdrawals per year (perhaps using payday lending behaviors and data on the frequency of emergencies as benchmarks) are two strategies that may curb temptations to tap into savings while allowing enough access to encourage participation (Chan 2011). The former type of limit in particular may both incentivize increased savings contributions and prevent depletion of savings from periodic indulgences each time withdrawal limits are renewed; however, it may also be less appealing than time-based limits. In the SEED savings account in the Philippines, which had the option to restrict withdrawals to a specific date in the future or to a specific financial goal, the former option was about twice as popular (Ashraf, Karlan, and Yin 2005). While there is not necessarily a trade-off between the attractiveness and effectiveness of withdrawal restrictions, the potential of a restriction to improve one outcome while hampering another should be considered in the design phase.

Prize-linked Savings

In 2009, the Doorways to Dreams Fund (D2D), the Filene Research Institute, and the Michigan Credit Union League began a pilot program called "Save to Win," a

prize-linked savings account that channels the natural tendency to overestimate the possibility of small gains, as well as the "thrill" of gambling, into a savings program. Participants earned a chance to win a $100,000 grand prize at the end of the year for every $25 deposited into the account. While those who were more able to save had a greater chance of earning the prize, take up of the product was highest among those with little to no savings (and, less surprisingly, those with a history of gambling and lottery participation) (Kearney et al. 2010). A full 40 percent of 2011 participants had incomes below $40,000. The program was very popular and had quick success: by the end of 2010, almost 17,000 program participants had accumulated a total of over $28 million in savings (Doorways to Dreams Fund, "Prize Linked Savings"). The regulation of lotteries is currently the largest obstacle to implementing the program in other states. However, the success of the D2D pilots has encouraged several states to pass saving promotion raffle bills (Doorways to Dreams Fund, "Legislative Success"). The mandate that state lotteries are meant to generate state revenue may lead to slow adoption from some states, as such programs would compete with state lotteries while generating significantly less revenue, but the idea is gaining momentum.

Future Directions

The potential of behavioral economics to revolutionize savings programs is still largely untapped. Behavioral economic principles can suggest simple but often overlooked techniques, as well as more nuanced intervention designs. Since program designs can involve trade-offs, such as weighing the cost of a program against its effectiveness, rigorous testing of different interventions is important for identifying the most significant levers in a design. By increasing the benefits of a program while only minimally increasing or even reducing costs, behaviorally informed program designs and policies can be particularly attractive to stakeholders and financial institutions whose partnerships offer opportunities for scale.

Underutilized Tools in the Box

There are still plenty of behavioral tools with potentially high returns that are not often incorporated into program designs. Interventions embedded into communications, such as framing decision sets and increasing the salience of motivating factors, are nearly costless but underutilized ways to improve saving behavior. Only a few programs use loss aversion (e.g., "Don't lose your matched deposit!") (Ratcliffe et al. 2010), social norms (e.g., framing participation as a standard employee benefit) (Lopez-Fernandini and Schultz 2010), or clear anchors (e.g., explicitly suggested contribution rates) (Lopez 2010b; Schultz 2010).

Identity priming is another way simply to tweak existing materials in order to increase saving behavior. In a recent study, mailers asking how important it is "to be a voter," compared to asking how important it is "to vote," significantly increased voter turnout (Bryan et al. 2011). People have a plurality of identities—for example, a female, a parent, a housecleaner, a Chinese immigrant, a chocolate-lover, a liberal, a continuing education student, and so on—even though those identities may be associated with opposing actions in some contexts. Increasing the salience of savings-oriented identities—for example, by conveying that, "as a loving parent," one should save for one's children—may be useful for improving saving behaviors.

Other interventions with particularly significant potential for high returns focus on closing intention-action gaps. Most programs have treated saving as a premeditated decision; however, people may also have impulses to save, just as they have impulses to spend. Today, it takes several mouse clicks along with a properly set-up mobile or online banking account, or even a trip to the bank, to act on an impulse to save. Mobile applications being developed for "impulse saving" reduce the delay between the decision to save and the act of saving to a few seconds, the time it takes to hit a button on one's phone.

Saving could also be automated by linking accounts to debit or prepaid debit cards, such as with Bank of America's Keep the Change program or Wells Fargo's Ways2Save program, coupling each purchase with a barely noticeable transfer to savings. When direct transfers are not feasible or popular, automation could be replaced with text message reminders to save. Explicit implementation intentions can also be effective; having individuals write down the date and time of a planned action has increased both voter turnout (Nickerson and Rogers 2010) and vaccination rates for influenza (Milkman et al. 2011). A savings program, or even tax return forms, could ask for a written commitment to a ritual deposit of $10 every other Friday after work.

The precommitment strategy employed by SMarT might be particularly instructive both for tax-time and employer-based savings programs. People are less likely to save an imminent tax credit or current income because of loss aversion. As previously discussed, many EITC recipients know how they plan to use their refunds long before tax time. However, using the tax-time "reset" moment to inspire savings contributions from next year's return would allow individuals to select both the "should" choice of saving and the "want" choice of spending this year's return. Similarly, employer-based savings accounts could increase contributions with each raise, and the tax return filing process itself could include an opportunity to divert a portion of each paycheck toward the purchase of savings bonds.

Finally, linking overdraft fees to saving can channel bad habits into good outcomes. Some populations have money management issues but may still have enough slack in their budget to absorb higher overdraft fees in the short term. Diverting a portion of this overdraft fee to savings, and limiting access to this savings account either with time-based or reason-based withdrawal restrictions, can increase savings while also incentivizing better money management. Even if the withdrawal restrictions are light, such as allowing any reason to be sufficient for accessing funds, the hassle of having to go to the teller and provide a reason might limit access enough to change behavior.

Importance of Rigorous Testing

Behavioral economics has demonstrated that the drivers of behavior are often counter-intuitive. Without rigorous testing, common sense approaches would prevail, and the shortcomings of some savings programs would remain a mystery. An intervention's effectiveness may even vary counter-intuitively with minor details in its structure. Testing different program designs, especially with randomization techniques, can help identify which interventions have the most significant impact.

Experimentation can reveal findings that surveys and focus groups do not. When participants respond to survey questions, such as why they did or did not participate in a program, they are prone to the confirmation bias, or the tendency to fabricate rational (and often inaccurate) explanations of events that align with preexisting beliefs (Oswald and Grosjean 2004), making survey data informative only to a limit. Furthermore,

experimentation can reveal the ineffectiveness of designs that few would otherwise question. For example, messages meant to convey that littering is terrible and unfortunately common actually increased littering in high-litter areas. The message's subtext, "lots of people do this," established a norm that licensed people to litter (Cialdini 2003). Contrary to early expectations, increasing salience of the female identity in messages about breast cancer, such as using the color pink, appeared to trigger defensive behaviors, with participants minimizing their perceived risk and being less likely to donate to a breast cancer charity (Puntoni, Sweldens, and Tavassoli 2010). Any intervention could affect a person in different ways, either beneficial or detrimental to savings goals, and testing is the only way to find out what those effects will be.

An intervention's effectiveness may even depend on slight variations in its structure. The results of the H&R Block experiment even suggest that, holding a policy's funds constant, offering a match for savings contributions would be significantly more effective than an equivalent tax credit (Duflo et al. 2006). The mere presence of matches, and potentially the match rate, may increase participation rates in savings programs while having a small or negative impact on contribution rates, presumably because participants can more easily meet savings goals with higher matches (Huberman, Iyengar, and Jiang 2007; Duflo et al. 2006; Grinstein-Weiss, Wagner, and Ssewamala 2005; Munnell, Sunden, and Taylor 2001/2002). By comparison, a couple of studies have found that higher match caps are associated with increased participation and contribution rates, perhaps by turning the match cap into a goal, or an anchor for savings (Boshara 2010/2011; Schreiner, Clancy, and Sherraden 2002). In yet another variation on incentive structure, offering a small bag of lentils to Indian villagers doubled vaccination rates (Banerjee et al. 2010). A prize-linked savings program piloted by D2D and the Central Credit Union of Indiana uses the same idea, offering relatively frequent, small prizes, such as mp3 players, gift cards, and laptops (Doorways to Dreams Fund). Tangible, immediate rewards add a salient "want" component to an otherwise purely "should" choice, coupling the immediate loss of cash with immediate consumption. While there are insufficient data to declare definitively that one incentive structure is superior to the others, experiments that randomly offer different caps, rates, or nonfinancial incentives can help calibrate the relative effects of each.

How Behaviorally Informed Programs Can Create Pathways to Scale

The scalability and sustainability of a policy or program depend to an extent on the balance of its costs and benefits. Very often, scaling a program also depends on viable partnerships between financial institutions and program designers. By increasing participation and retention rates, behavioral interventions can help boost the benefits of policies and programs while decreasing or barely increasing costs, making policies more sustainable and programs more attractive to the partners who could bring them to scale.

Historically, policies have focused on incentives and penalties to influence behavior, which can be particularly costly if those are a policy's only tools. For example, the Saver's Credit, a federal tax credit for contributions to retirement plans, has had very little success in increasing participation by increasing the size of the incentives. A change in the effective match rate from 25 to 100 percent increased participation by only 1.3 percentage points (Duflo et al. 2007). Instead of increasing the match rate, policymakers might achieve the same or a larger increase in participation with conscientiously designed communications materials, well-timed outreach efforts, or much cheaper prize incentives.

An increase in cost effectiveness could also help otherwise small-scale, short-term, or local policies gain support and potentially be adopted on a larger scale.

In the case of savings programs, behavioral interventions can do more than improve the balance of costs and benefits; they can help inform a financial institution's long-term development goals. Servicing mainstream accounts can cost between $15 and $70 per year, and since institutions often assume that poor individuals cannot save significantly more than that, small-dollar savings accounts can appear to be unsustainable (Chan 2011). However, the net benefit of savings programs to financial institutions may be low in part because they consider such savings accounts as stand-alone products. Instead, they could consider a savings account that is attractive to lower-income individuals as the gateway to longer-lasting relationships between otherwise unbanked individuals and the financial institution. Furthermore, testing products that incorporate insights about a new customer base can inform the design and development of other products for those customers. Project managers of AutoSave noted that the appeal of a new, broader customer base most strongly enticed financial institutions to sponsor the program (Schultz 2010). Presenting the value of additional business can encourage financial institutions to test a program pilot as a candidate for a scalable product.

This chapter is not meant to be exhaustive in its analysis or to offer ideas that are entirely new. Rather, it is intended to be the beginning of a discussion about how best to facilitate saving by those with low and moderate incomes. The examples of real-world applications of behavioral insights applied to saving efforts that we cite here only begin to scratch the surface of all possible uses of behavioral science in this area. Policies and programs in all phases of development, sponsored by any source, can immediately start testing behavioral interventions on the pathway to scale. Program designers might rephrase marketing messages, experiment with different incentive structures, and consider different ways to channel natural behavioral tendencies while requiring few if any additional resources.

The incorporation of innovative ideas that traditional or straightforward approaches would overlook could make policies or programs much more effective. Rigorous testing of behavioral interventions, along with a thorough consideration for the unique challenges of low-income families, can help move savings programs from modest beginnings to impact, scale, and sustainability.

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Chapter Nine

Solving the Paradox of High College Expectations: The Role of Children's Savings Accounts

William Elliott III

Given the well-documented disparities in college attendance and completion rates by socioeconomic class, and the increasingly critical role that education plays in employment and economic mobility, a primary question for the twenty-first century is, "How do we achieve greater access to college and higher college completion rates for more of America's children?" The federal government's response to this challenge has been primarily to make college loans more accessible. However, this trend has led to very high levels of student debt for students leaving college that may undermine their belief that education is a path for achieving the American Dream. Historically, perhaps no institution has been more important in sustaining the American Dream than public education, including colleges and universities. Education in America has been called the "great equalizer," evoking the widespread belief that disparities among groups of people can be narrowed through effort in school and the pursuit of higher education. As such, the entire nation has a stake in making sure that all citizens continue to see college attendance and graduation as a viable way to achieve the American Dream.

This chapter presents evidence of the links between savings and children's college progress. College progress is conceptualized here as students being "on course" for achieving the American Dream via the education path. Furthermore, this chapter offers evidence of the role children's savings plays in reducing what experts have termed "wilt."[1] Children "wilt" due to lack of resources much in the same way a growing plant loses vitality due to lack of sun and water. If children who expect to graduate from college are less likely to actually attend college when they do not have savings, we can consider financial barriers rather than a lack of desire as a critical barrier in the path to a college degree.

In a very basic way, having savings changes the way children think about college. Using the identity-based motivation (IBM) theory developed by Oyserman (2007, 2009) and applying it to assets (Elliott et al. 2011; Elliott and Nam, under review), this chapter suggests that children who have positive college expectations and who have

a savings account in which they have mentally designated some of the money in the account for college (i.e., the college-saver identity) are more likely to attend college than if they have positive college expectations alone (i.e., the college-bound identity). When children form a college-saver identity, it makes college feel more secure and certain, and outcomes related to school appear to them to be more clearly linked to their own efforts.

Can Savings Help Children Progress to and through College on Their Way to Achieving the American Dream?

Low- and moderate-income (LMI) students continue to believe in the *idea* of education as a means to achieving the American Dream. With limited opportunities for accumulating savings for college, however, a lot of college-qualified, LMI students do not believe that college is within reach. They learn this at a very young age. How might this be changed? Policies that encourage and facilitate college savings may help LMI students think about college as within reach.

"On course" is operationalized as being enrolled in or having graduated from a two- or four-year college by age 23 (Elliott and Beverly 2011a). Data from the Panel Study of Income Dynamics (PSID) reveal large disparities in college progress (i.e., being on course) by race, gender, householder's marital status and education, and household income and net worth (first column of table 9.1).[2] Whites, females, those living with married householders and householders who have at least a four-year college degree, and those who live in high-income and high-net worth households are far more likely to be on course than peers with other demographic characteristics. For example, 88 percent of high-income children are on course, compared to 37 percent of low-income children, a gap of 51 percentage points. Eight-six percent of children with parents who have at least a four-year college degree are on course, compared to 47 percent of children with parents who have a high school degree or less, a gap of 39 percentage points. And 71 percent of children in high-net worth households are on course, compared to 45 percent of those in negative net worth households.

Of particular interest here is the relationship between children's savings and college progress: 74 percent of children with savings accounts and some savings designated for college are on course, compared to 59 percent of children with savings accounts but with no savings designated for college and 41 percent of children with no savings account at all.

The finding that children who have savings accounts and have designated a portion of their savings for college are more likely to be on course than other children holds true even when controlling for the influence of other important factors. A recent study to be published in the *American Journal of Education* finds that, when controlling for factors including race, gender, academic achievement, parent's education, household income and net worth, children with savings designated for college are almost twice as likely to be on course as children without savings designated for college (Elliott and Beverly 2011a).

Desire, Ability, and Effort Are Not Enough

Some researchers attribute gaps in college attendance and completion to low levels of desire, ability, and effort among low-income or minority children. Below are summaries of several popular theories which consider how these attributes explain the educational outcomes of lower-income children.

Desire

Aspirations are one way that researchers measure children's desire to attend college. Aspirations are sometimes expressed by people as a desire or a hope. They are not formed through experience or by making judgments, but instead are acquired through socialization. Aspirations are relatively stable beliefs that are often maintained even in the face of contradictory evidence. Aspirations have been shown to be predictive of children's educational outcomes (Marjoribanks 1984; Mau 1995).

Ability

Human capital is commonly defined as the skills, capabilities, knowledge, and adaptive behaviors that an individual accumulates through education, work, and other life experiences (Sunstein 1997). Stratton, O'Toole, and Wetzel (2007) state that one of the most effective pieces of information young adults have when assessing whether the benefits of attending college outweigh the costs is their record of academic performance as reflected by high-school grades or standardized test scores. Furthermore, research consistently finds that academic ability is a strong predictor of whether children enroll in college or not (Braddock II and Dawkins 1981; Noble and Sawyer 2002).[3]

Effort

Self-efficacy is an example of a theory that attempts to explain children's academic achievement based on the level of effort they put forth. Self-efficacy is believed to be predictive of how hard a child will work in school and whether the child will persist when faced with difficult school-related activities (Pajares 2002). Bandura (1994) defined self-efficacy as "people's beliefs about their capabilities to produce designated levels of performance that exercise influence over events that affect their lives" (ibid., 71). A simple definition of self-efficacy is children's "I Can Do" beliefs. The basic principle of self-efficacy theory is that children who believe they can do well at a particular task in school (like doing a math problem) put forth more effort and in turn are more likely to be successful. For a review of research on this topic, see Pajares (1996).

Although desire, ability, and effort are clearly important factors for understanding why there are gaps, these factors do not sufficiently explain why the education path fails to lift high-achieving, low-income, and minority children out of poverty, while simultaneously charting a path to prosperity for low-achieving, high-income, and nonminority children (Advisory Committee on Student Financial Assistance [ACSFA] 2002; Ingles et al. 2002). In other words, arguments that focus on college attendance and completion gaps often overlook the fact that the lowest-achieving children from high-income families attend college at a much higher rate than the lowest-achieving children from low-income families (77 percent versus 36 percent). In comparison, 97 percent of the highest-achieving children from high-income families attend college, while only 78 percent of the highest-achieving children from low-income families attend college (ACSFA 2001). This suggests that not all children have the same access to college even after desire, ability, and effort are considered.

Wilt: The Paradox of High College Expectations, Low College Attendance

According to theACSFA, a group charged by Congress with enhancing access to postsecondary education for low-income children, educational decision making by low-income

Table 9.1 College progress and wilt, by demographic and economic characteristics, 2007

	Percent of all children on course	*Percent of all children who were certain*	*Percent of certain children on course*	*Percent of certain children not on course ("wilt")*
Full sample	61	86	68	32
White	66	86	72	28
Black	38	75	47	53
Female	64	86	71	29
Male	58	85	64	36
Head is married	68	88	74	26
Head is not married	40	79	48	52
Head has four-year degree or more	86	94	90	10
Head has some college	59	89	64	36
Head has high-school degree or less	47	80	54	46
High income	88	94	89	11
Moderate income	59	86	66	34
Low income	37	77	45	55
High net worth	71	90	76	24
Moderate net worth	38	76	48	52
Negative net worth	45	81	53	47
Has savings for college in savings account	74	93	77	23
Has savings account	59	84	66	44
Has no savings account	41	76	51	49

Notes: Table results are rounded to the nearest percent. Children who are "on course" are enrolled in or have graduated from a two- or four-year college by age 23. Children who are "certain" said, in 2002, that they were "pretty likely" to graduate from a four-year college or responded "it will happen." Those who were certain in 2002 but who are not on course in 2007 have experienced "wilt." Full sample, N=729; certain sample, n=626. For more information on data and methods, see appendix 9.1.
Source: Weighted longitudinal data from the Panel Study of Income Dynamics and its supplements, the 2002 Child Development Supplement, and the 2007 Transition into Adulthood.

children is not the result of choice or academic preparation but reflects an inability to pay for college (ACSFA 2001, 18). The majority of high-achieving, poor children desire to attend college and recognize the value of college for future economic success, but many do not attend (ACSFA 2006). According to ACSFA (2006), 70 percent of low-

income children in tenth grade plan to go to college, but only 54 percent actually enroll in college upon graduating from high school. The paradox of positive college expectations and low college attendance among low-income children is one reason why some analysts suggest that the ability of education to act as the "great equalizer" in society is at risk (ACSFA 2002; Haycock 2006; Hertz 2006; Lee and Burkham 2002). This suggests that even with high levels of effort and ability, along with a strong desire to attend college, many poor and minority children perceive college as out of reach.

As noted above, "wilt" occurs when high-school students who expect to attend and graduate from college sometime in the future are not enrolled in college shortly following high school. The concept of "college progress" has been used to discuss the paradox of high college expectations but low college attendance (Elliott and Beverly 2011b). College progress refers to children who were either enrolled in a two- or four-year college in 2007 or who had already graduated. Data presented in this chapter on wilt build on Elliott and Beverly (2011b) by examining college progress data from 2007 and by looking at college progress rather than college enrollment by itself. Wilt is examined in table 9.1, using PSID data.[4] First, the sample is limited to children who, in high school, said they expected to graduate from a four-year college. For brevity, these children are referred to as "certain."[5]

The second column of table 9.1 shows the percentage of children who, in 2002, were certain. It is noteworthy that advantaged children were more likely than disadvantaged children to be certain. All else equal, we would expect class differences in wilt to be smaller than class differences in college progress because class differences in expectations are factored out of wilt.[6] The third column shows the percentage of certain children who were on course five years later, and the fourth column shows the converse, the percentage of children who had experienced wilt.

In the full sample, 32 percent of certain children had experienced wilt. As expected, large disparities exist across subgroups. Blacks, males, those living with unmarried and less-educated parents, and those living in low-income households and moderate or negative net worth households were much more likely than others to experience wilt. In addition, children without a savings account and children with a savings account but no savings designated for college were much more likely than children with designated college savings to experience wilt. Finding ways to explain and ultimately resolve this paradox will have a lot to do with whether or not the education system can fairly be said to be the "great equalizer" in American society or not.

The College Saver Identity

In simple terms, building savings over a period of years may raise children's educational expectations. Higher expectations may lead to increased academic effort and achievement (see appendix 9.2 for more on this theorized relationship). In other words, if children grow up knowing they have financial resources to help pay for current and future schooling, they may be more likely to have more positive college expectations, which may in turn foster educational engagement. Greater engagement may lead to better academic preparation and achievement. These attitudinal and behavioral effects of savings could be at least as important as the money itself in the transition from high school to college. But how do they occur?

Elliott et al. (2011), Oyserman (2012), and Elliott and Nam (under review) have applied IBM theory as a way of understanding how assets might help resolve the paradox of positive college expectations and low college attendance. IBM is a theory about how identities are formed and which identities people will act on (Oyserman and

Destin 2010). It focuses on visions students have of themselves in a future state (or a possible self). Theorists suggest that three principal components explain the relationship between conceptions of the self like a college-bound identity and motivation while lending significant attention to how context (social and cultural) drives the process. The three core principles of IBM are (1) identity salience—is it on the forefront of the mind; (2) congruence with group identity—when an image of the self feels tied to ideas about relevant social groups such as friends, classmates, family, and cultural groups; and (3) interpretation of difficulty as normal—when identities feel important to work on as opposed to impossible to attain. These principles have been found to be important predictors of students' school behaviors (ibid.).

When using IBM to explain the assets/expectation relationship college expectations serve as a proxy for what IBM researchers refer to as a college-bound identity. However, as stated, research has shown that while children's college expectations are a strong predictor of educational outcomes, many children who expect to graduate from college end up not attending college. This raises the question of why college-bound identities are not an even stronger predictor of college attainment than they are. Or, equally if not more importantly, what can be done to help children who expect to attend college actually get to college? It is suggested here that an important reason that the college-bound identity or positive expectations are not better predictors of college attendance than they are, is because they are not necessarily linked to strategies for getting to and through college. IBM suggests that students are more likely to act on an identity when the identity is salient (i.e., on the mind) and students have a strategy for interpreting difficulty as normal (Oyserman and Destin 2010).

Although a student who expects to attend college but has not identified the strategy of saving has identified college as an important goal in the future that requires action now, she may not know how to move forward—to act with respect to paying for college. As a result, the student may see college as a closed path for her. While a strategy for paying for college is certainly not the only type of strategy needed for the college-bound identity to be actionable, it is a required strategy for viewing college as an open path in a society where children have to pay high tuition fees to attend college.

Destin and Oyserman (2010) provide some evidence of how this might work. They propose that students with fewer assets may lower their expectations for school success and plan to engage less in school if they felt that there was a closed path to attain the desired self (i.e., a college-bound self). They tested this proposition by experimentally manipulating mind-set about college as either closed or open. They did this by randomly assigning classrooms to a closed-path (college is expensive) or an open-path (college can be covered with need-based financial aid). Students in the closed-path were read a simple text that indicated that the average college tuition costs $31,160–$126,792, while the open-path group was read a text that did not discuss the cost of college but instead informed them of the availability of need-based financial aid opportunities. They found that students assigned to the open-path condition were significantly more likely to expect higher grades and planned to spend more time on homework than those assigned to the closed-path condition.

This example illustrates the link between educational engagement and students' perceptions about their ability to access money to pay for college. It also illustrates how a college-bound identity linked to strategies for paying for college is likely to be a better predictor of students' educational outcomes than when it is not. When the college-bound identity is linked to the strategy of saving to pay for college, Elliott and Nam (under review) refer to it as the college-saver identity. They find evidence to suggest

when the college-bound identity is linked to saving for college, it is a better predictor of college graduation than when it is not.

Policy Considerations

One type of asset accumulation strategy that is gaining increasing support is Children's Development Accounts (CDAs). In their simplest form, CDAs can be thought of as savings accounts for students. However, CDAs have the potential to serve as a policy vehicle to allocate resources (intellectual and material) to LMI students so that they can compete in the twenty-first century. This is because, unlike a basic savings account, CDAs leverage investments by individuals, their families, and in some cases third parties with investments from the federal government (e.g., initial deposits, incentives, and matches). An example of such a policy can be found in the proposal by the U.S. Department of Education (DOE) to conduct a College Savings Account Demonstration Project within the GEAR UP program (Gaining Early Awareness and Readiness for Undergraduate Programs).

GEAR UP is a federally funded grant program designed to increase the number of low-income students who enroll in college. Under the proposal, the DOE would allocate $8.7 million worth of funds to support the demonstration and provide an account to participating students with an initial deposit of $200. Students would be eligible for a one-to-one match totaling $1,600. The demonstration is designed to test the effectiveness of pairing federally supported college savings accounts with GEAR UP activities against GEAR UP activities alone. When the US Department of Education announced the savings demonstration, a news reporter asked whether $1,600 would be enough savings to make a meaningful difference in a child's life. In large part the answer to this question depends on whether or not savings produce the types of psychological effects described in this chapter. Research by Elliott and colleagues suggests that even small amounts of savings (less than $1, $1–$499, or $500 or more) can have meaningful psychological effects (Elliott, under review).

Research cited here also suggests that, in the case of children, positive outcomes include more than changes in saving behavior, for example, how much children save for college. As discussed in this chapter, a likely part of the effect of having assets is making salient aspects of their identity, such as being college bound, and providing them with a strategy (i.e., savings) for overcoming difficulties they perceive during their educational pursuits.

The policy implication is that it may be an important start by giving young children accounts with an initial deposit and to encourage them to designate a portion of this savings for college. When children are given a savings account as proposed in the GEAR UP research demonstration, and when some portion of that account is designated for college, the account *may* serve as a regular cue to children that college is in their future; however, more research is needed (Elliott and Nam, under review). It also provides them with a strategy for overcoming difficulty related to paying for college. Finally, a federally funded program such as GEAR UP that is run out of schools conveys the message to children that "We save, we go to college." That is, it creates a sense of group congruence.

Some simple theoretical propositions that can be drawn from this are as follows: (1) Children who have an account with an initial deposit know that there are resources available to help them finance college—brings college to the forefront of the mind; (2) children who have a college savings account know that someone expects them to go

to college—group congruence; and (3) children who have an account with an initial deposit might be more likely to see savings as a strategy to pay for college—normalizes difficulty related to paying for college.

While savings has the potential for multiple effects that can help children be better prepared for college, at some point children do have to pay for college, and this should not be ignored or undervalued. So, in addition to providing children with an account, we also need to find new and innovative ways to help them accumulate enough savings to pay for college. One way to help children accumulate savings for college might be to reallocate money that is currently being spent on loans, scholarships, and grants. For example, low-income children are eligible for Federal Pell Grants when they reach college age. Pell Grants do not have to be paid back like a loan. The Pell Grant program is a need-based grant for low-income undergraduate and certain post-baccalaureate students. During the 2012–2013 school year, students can receive up to $5,550. What if the money allocated to the Pell Grant program was instead allocated, or some portion of it, to a restricted savings account, at birth, for all children born into low-income families? Low-income children, in particular, would gain the added advantage of saving, be able to build on the $5,550 over the course of their childhood years, and ultimately have power over a meaningful amount of money to help pay for college.

In writing about what he calls "early commitment" financial programs, Schwartz (2008) states, "The children of high-income parents have a strong early commitment in that they can usually assume, from an early age, that their parents will pay their college expenses" (ibid., 118). In other words, high-income students have internalized a strategy for paying for college similar to that most aptly espoused by presidential candidate Mitt Romney during the 2012 presidential election. When talking to students about how they should pay for college, he said they should borrow money from their parents.[7] Higher-income children from a young age learn that borrowing from their parents is a real and viable strategy for obtaining the things they want in life. Whether it be from their parents' paying for private school or providing them with costly tutoring, the message is clear. Low-income children receive a very different but equally clear message about the ability of their parents to afford day-to-day necessities, let alone big-ticket items like college. Needless to say, this strategy is not available for lower-income students, and as a result they do not grow up with the same assurance that college is a viable path for them that their higher-income counterparts grow up with. This might really matter as the research in this chapter begins to point out.

Some might argue that low-income students do not need to rely on their parents: they can borrow from the federal government. However, high student loan debt does little to encourage students to engage in school prior to reaching college age (research shows that low-income and minority students are averse to taking out student loans; Campaign and Hossler 1998); it reduces the chances that students enroll in college or graduate from college (Dynarski 2003; Kim 2007; Perna 2008), and it often destroys their credit after they graduate from college or at the very least results in students having to delay achieving milestones typically associated with the American Dream like buying a car or a home (Mishory and O'Sullivan 2012). Unlike student loans, asset accumulation strategies, especially in the form of account ownership, might assist students in preparing for and affording college, and leading to increased college expectations, greater educational engagement, and better academic achievement. That is, LMI students might be more likely to seek a college education if—from a very young age—they perceive they have a way to pay for it. Greater perceived control by LMI students over financing college should lead to more students viewing college as within reach. Furthermore,

asset accumulation policies hold promise for helping students to enter their adult lives without the burden of a weak credit history because they either have too much debt or because they are struggling to make their payments.

Additional theoretical positions that can be drawn from this are as follows: (1) Children who have college savings have less need for student loans and so may be more willing to incur college expenses; (2) the effects of having an account are likely to be stronger when the account is in the child's name; and (3) the earlier children are given an account, the earlier they are likely to develop an assurance that college is affordable.

Conclusion

The belief that an ordinary citizen can turn the American Dream into reality through effort and ability is embedded in the history and culture of America. Higher education has been and continues to be viewed as a key instrument for making the American Dream a reality. However, in a highly technical global economy, realizing the American Dream often requires a college education. Findings from the studies discussed in this chapter suggest that if high-school children have savings of their own, and especially when they have designated some of their savings for education, they are more likely to be on course five years later than if they do not have their own savings. The importance of children's savings on college progress holds when controlling for such things as children's academic achievement, parent's education level, and family income, and suggests that children who have designated a portion of their savings for college are about two times more likely to be on course than if they did not have any savings at all (Elliott and Beverly 2011a).

Unfortunately, disparities between children who have their own savings accounts are associated with race, gender, parental marital status, and socioeconomic class. It is not surprising that children with socioeconomic advantages are more likely than their less-fortunate peers to have savings accounts and to graduate from college. The research discussed here also asks, "Does owning savings matter for low-income children?" The answer appears to be yes. The suggestion from recent research is that ownership of children's savings accounts may be playing a role in current educational disparities. Given this, an important part of any strategy for promoting college attendance and graduation (and for helping to ensure that education as the "great equalizer" in society remains such) may be to assure that all children own a savings account early in life that is seeded with publicly funded deposits.

Furthermore, access to college in America is commonly believed to be based on merit. From this perspective, whether a child is on course is not a matter of financial resources, including savings, but rather of desire and preparation. Tests of "wilt" help determine how factors other than desire play a significant role in determining whether college attendance and graduation is more than a dream for many children. Findings suggest that wilt is largely due to socioeconomic factors such as parental education and income. While not typically included in studies as a socioeconomic factor, children's savings are also a key financial factor influencing wilt. Children who have college savings experience less wilt than their peers without savings. Further, when controlling for such things as children's academic achievement, parent's education, and family income, children who expect to graduate from a four-year college and have savings are about six times more likely to attend college than their peers (Elliott and Beverly 2011b). It is also worth noting that family income remains a significant predictor of college attendance in these tests. However, children's academic achievement and parent's education do not remain significant in their effects on college progress when controlling for these other

factors. These findings parallel the results of ACSFA's research, and suggest that college attendance and graduation is not solely about desire or academic achievement, but that tangible financial resources are also critical to college success.

In conclusion, LMI children continue to believe in the idea of education as a means to achieving the American Dream. With limited opportunities for accumulating savings for college, however, many LMI children do not believe that college is within their reach from a very young age. Asset accumulation, especially in the form of savings, can assist children in preparing for and affording college, leading to a salient college-bound identity and greater educational engagement and academic achievement. In other words, LMI children may be more likely to seek a college education if—from a very young age—they have a way to help pay for it. Greater control by LMI children over financing college should lead to more children viewing college as within reach.

Notes

1. Michael Sherraden is given credit for coining this term (Elliott and Beverly 2011a).
2. See appendix 9.1 for more information on data and methods used in table 9.1.
3. An extreme form of the explanation that ability determines academic outcomes is found in *The Bell Curve* by Richard Herrnstein and Charles Murray (1994). Herrnstein and Murray suggest that black children are intellectually inferior to white children due to genetic differences and are therefore predetermined to fail in school. From this perspective, investments in education programs that seek to reduce the achievement gap or raise college enrollment are a waste of taxpayer dollars. As Murray (2007) writes, "There is no reason to believe that raising intelligence significantly and permanently is a current policy option, no matter how much money we are willing to spend" (ibid., 1).
4. The analysis of wilt summarized in table 9.1 extends Elliott and Beverly (2011b) by examining data through 2007.
5. Children were asked about their chances of graduating from a four-year college. They could respond by saying no chance, some chance (about 50–50), pretty likely, or "it will happen." Those who chose either of the latter two categories are defined as expecting to graduate or "certain."
6. Children with college savings were more likely than others to expect to finish college, but the causality probably moves in both directions: Children who do not expect to go to college are unlikely to designate any of their savings for college. At the same time, children with college savings are probably more likely to perceive themselves as "college-bound" (for the reasons discussed below).
7. See Heather's blog (2012).

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Appendix 9.1
Methods for Table 9.1

Data

This study uses longitudinal data from the Panel Study of Income Dynamics (PSID) and its supplements, the Child Development Supplement (CDS) and the Transition into Adulthood supplement (TA). The PSID is a nationally representative longitudinal survey of US individuals and families that began in 1968. The PSID collects data on things such as employment, income, and assets. The CDS was administered to 3,563 PSID respondents in 1997 to collect a wide range of data on parents and their children, aged birth to twelve years. Questions covered a broad range of developmental outcomes across the domains of health, psychological well-being, social relationships, cognitive development, achievement, motivation, and education. Follow-up surveys were administered in 2002 and 2007. The TA supplement, administered in 2005 and 2007, measures outcomes for young adults who participated in earlier waves of the CDS and were no longer in high school.

The three data sets are linked using PSID, CDS, and TA map files containing family and personal ID numbers. The linked data sets provide a rich opportunity for analyses in which data collected at one point in time can be used to predict outcomes at a later point in time, and stable background characteristics can be used as covariates. Because the PSID initially oversampled low-income families, descriptive analyses are weighted using the last observed weight variable as recommended by the PSID manual (Gouskova 2001).

Children's Savings

Children were asked in 2002 whether they had savings in a bank account held by a financial institution with the child named as owner. If they had an account, they were also asked whether they were saving some of this money for future school, like college. The children's savings variable divides children into three categories: those who in 2002 had an account but had not designated a portion of the savings in the account for school (children's savings), those who had an account and had designated a portion of the savings in the account for school (children's college savings), and those with no account (the reference group).

Demographic and Economic Characteristics

Children are divided into subgroups according to several demographic and economic characteristics. Child race (black/white) comes from the 1997 wave of the CDS. Child

gender (male/female) comes from the 2002 wave of the CDS. Head's marital status (married/not married) comes from the 2001 wave of the PSID.

Household head's education level is a continuous variable ranging from one to sixteen and comes from the 2003 wave of the PSID. Each number represents a year of completed schooling, so those who have twelve years of education, for example, are assumed to have graduated from high school. Head's education is changed into a categorical variable, dividing heads into three groups: those with a high school degree or less, those with some college, and those with a four-year degree or more.

Household income is calculated by averaging self-reported income for 1993, 1997, and 2002. (Income values were adjusted to 2007 price levels using the consumer price index.) Income averaged over multiple years provides the best estimate of permanent income (Blau 1999; Mayer 1997). Next, household income is changed into a variable with three groups: low income (<$33,377), modest income ($33,377–$84, 015), and high income ($84,016 or more).[1]

Net worth in the PSID is a continuous variable that sums separate household values for a business, checking or savings accounts, real estate, stocks, and other assets, and subtracts out credit card and other debt. In this analysis, net worth does not include home equity. Net worth is averaged for 1994, 1999, and 2001. (Values were adjusted to 2007 price levels using the consumer price index.) Net worth is then changed into a variable with three groups: negative net worth (< $0), modest net worth ($0–$10,000), and high net worth (>$10,000) (Nam and Huang 2009).

Analysis

In the first stage of the analysis, missing data are replaced using multiple imputations. Missing data might result in limitations related to generalizability of the findings and model comparisons as well as reduced power (Rubin 1976). Multiple imputation has been recognized as a preferred method for estimating and completing missing data (Little and Rubin 2002). This method assumes that missing data occur randomly. To complete missing data, the multiple imputation method uses information from the observed variables as well as the missing data. The Markov Chain Monte Carlo method is performed to create five completed, or imputed, data sets with no missing data (Saunders et al. 2006; Schafer and Graham 2002). In the second stage of the analysis, the data are pooled across the five imputed data sets to reduce bias in the estimations of parametric statistics (Saunders et al. 2006). In third and final stage, basic frequencies and means are estimated.

Note

1. Category amounts are based on those used in the US Census Bureau's Current Population Report Income in the United States: 2002 (De Navas-Walt, Cleveland, and Webster 2002). De Navas-Walt et al. used five income categories; we recoded into three categories to increase the sample size within each group.

Appendix 9.2

Research that Includes Children's Savings and College Expectations

Study	*Asset variables*	*Methods/data*	*Outcome*	*Findings*
Staying on course: the effects of savings and assets on the college progress of young adults				
Elliott and Beverly (2011a)	Net worth; children's school savings; parents' school savings for young people	Methods: Logistic regressions Data sets: Panel Study of Income Dynamics (PSID) and Child Development Supplement (CDS) and Transition to Adulthood (TA) Longitudinal: Baseline measured at mean age of 17 in 2002; outcome measured mean age of 20 in 2007; *N* = 1,003	Expectations	Baron and Kenny findings: Net worth/college attendance is not mediated by children's college expectations; parents' school savings/college attendance is not mediated by college expectations; children's school savings/college attendance is partially mediated by children's college expectations Bootstrap findings: Net worth has no indirect effect; parental savings has an indirect effect on college attendance; children's school saving has an indirect effect on college attendance
The age old question, which comes first? a simultaneous test of children's savings and children's college-bound identity				
Elliott et al. (2011)	Children's savings	Methods: Path analysis using (SEM); the sample is restricted to children who have graduated high school or completed a GED and are not attending a four-year college and have not graduated from a four-year college by 2007. The reason for these restrictions is because college-bound identity as measured in this study has no meaning for children who are currently attending a four-year college or have already graduated from a four-year college. Data sets: PSID and CDS and Transition into Adulthood Longitudinal: Baseline measured at ages 12–17 in 2002; outcomes measured at ages 17–23 in 2007; *N* = 592	Expectations	Simultaneously tests whether savings leads to higher expectations or higher expectations lead to owning savings; children's savings has a modest effects on college expectations and vice versa
Asset holding and educational attainment among African American youth				
Elliott et al. (2010)	Net worth; children's school savings	Methods: Path analytic technique using structural equation modeling (SEM); bootstrapping (Bollen and Stine 1992); data sets: PSID and its CDS;	Expectations	Children's school savings are significantly related to children's college expectations for both blacks and whites; net worth is not significantly related to college expectations for either blacks or whites Bootstrap findings:

		cross sectional: measured at ages 12–18 in 2002; N = 1,063		the relationship between white children's school savings and their math scores are partially mediated by college expectations but not with blacks or in the case of reading w/whites or blacks; the relationship between homeownership and white children's math scores are fully mediated by college expectations but not with blacks or in the case of reading w/ whites or blacks
Math achievement and children's savings: implications for child development accounts				
Elliott, Jung, and Friedline (2010)	Net worth; children's savings account; children's savings amount	Methods: hierarchical linear modeling (HLM) Data sets: PSID and its CDS Cross sectional: measured at ages 12–18 in 2002; N = 1,063	Expectations	Children's basic savings is not significant w/ their college expectations; children's school savings is significant w/ their college expectations; parent's school savings for their child is significant w/ their child's college expectations; net worth is not significant w/ young people college expectations; head's education level and marital status interact with children's savings in predicting children's college expectations
Children's college aspirations and expectations: the potential role of college development accounts				
Elliott (2009)	Net worth; categorical net worth (1) < $4,564; (2) $4,564–$47,742; (3) $47,743–$153,700; and (4) > $153,700; children's school savings; children's school savings amount	Methods: logistic regression; multiple regression; Baron and Kenny 1986 tests; Sobel test (1982); and Bootstrapping (Bollen and Stine 1992) Data sets: PSID and its CDS Cross sectional: Measured at ages 12 to 18 in 2002; N = 1,071	Expectations	Baron and Kenny findings: Net worth is not significant with children's college expectations; children's school savings is significantly associated with children's college expectations. The effect of children's savings on math achievement is significantly reduced when college expectations are included in the model (i.e., college expectation acts as a mediator) Sobel test findings: Total effect of children's school savings on math scores is significantly reduced Bootstrap findings: Children's school savings is indirectly related to math achievement through their college expectations

Chapter Ten

Extending Savings Accounts to Young People: Lessons from Two Decades of Asset Building

Terri Friedline

Over the last two decades, a growing number of researchers and policy makers have endorsed asset building as a strategy for improving young people's well-being, specifically by extending savings accounts early in life. There are several reasons why extending savings accounts to young people, such as children, adolescents, and young adults, might prove beneficial. First, extending savings accounts to young people lays the foundation for connecting them to mainstream banking institutions and teaching them about saving. It is hoped that young people can build upon this foundation by remaining connected to mainstream banking institutions, diversifying their asset portfolios, and making informed decisions about savings. Second, the greatest benefits may occur when young people begin saving early in life (Sherraden 1991; Sherraden et al. 2012). This is because the effects of saving are believed to compound over time. If the savings goal is several years away, people have a longer time to develop a habit of saving, to become educated and savvy financial consumers, and to invest emotionally and financially into their accounts. For example, a young person who has a savings account from birth has 18 years to benefit from the account, ranging from gaining entrée into banking institutions to accumulating savings for college. Third, young people are already prepared to begin saving early in life because they affirm saving as a socially desirable behavior around ages five and six (Ward, Wackman, and Wartella 1977). When young people have savings accounts and participate in saving, the experience may reinforce their perceived social norms and capitalize on a key moment in their development (Elliott et al. 2010). Fourth, research links young people's savings accounts with financial and educational outcomes (Elliott, Destin, and Friedline 2011; Elliott et al. 2012; Friedline, Elliott, and Nam 2012a). The linkage between savings accounts and college graduation, for example, gives insight into young people's ability to develop their human capital. Ultimately, savings accounts may help young people lead productive and satisfying lives.

Notably, not all young people have savings accounts. Young people from lower-income households—households that by definition have fewer resources to extend savings and other asset building opportunities to their young people—may be at a disadvantage for experiencing effects on well-being. A growing array of programs and policies has been developed to redress barriers in access to savings accounts and balance the scales of

opportunity so that young people from lower-income households have a better chance of experiencing improved well-being.

This chapter aims at placing young people's savings within the broader context of two decades of development in asset building and to review the current state of affairs.[1] It will do so by presenting a review of the theory and research on young people's savings and explore a contemporary set of policy implications. While programs and policies to support young people's savings have advanced by leaps and bounds in the international arena, this chapter focuses mainly on the United States. This is because the theories developed, research undertaken, and policies proposed are context specific—rooted in language, culture, economies, and politics. Despite differing contexts even within the United States, this focus provides a more homogeneous context for understanding young people's savings without making cross-national comparisons.

Extending Two Decades of Asset Building to Young People

New directions for theory, research, and policy emerged with the introduction of Michael Sherraden's seminal book *Assets and the Poor*, which distinguished the effects of assets (wealth) from income for improved well-being and introduced the concept of asset-based social welfare policies (Sherraden1991). The introduction of asset building into the social sciences set off a firestorm of development over the last 20 years, leading to the documentation of the promising effects of assets and subsequent enactment of policy. Initially, much of this development focused on families' and households' asset building and well-being. The American Dream Demonstration (ADD) began in 1998 to test whether lower-income families could save in subsidized savings accounts, referred to as Individual Development Accounts (IDAs). The five-year demonstration concluded with promising results, and the long-term effectiveness of IDAs is still being tested (Birkenmaier, Curley, and Kelly 2012; Grinstein-Weiss et al. 2011; Richards and Thyer 2011). During that same year, the Assets for Independence (AFI) Act was passed into public law, establishing a federal grant program to provide nonprofits and government agencies with funds to offer IDAs to lower-income families. As a result, there are over 200 AFI-supported IDA programs nationwide (US Department of Health and Human Services 2012).

IDAs were originally proposed as accounts that would be available to every citizen in the United States, accrue interest, and limit or restrict usage to preapproved expenses such as homeownership, microenterprise, or education (Schreiner and Sherraden 2007). Account holders whose annual incomes fell below certain thresholds would be eligible to receive subsidies to incentivize and support their saving. Michael Sherraden initially proposed that IDAs would be opened early in life to promote asset building and well-being across the life course: "Because asset-based welfare is a long-term concept, some of the best applications of IDAs would be for young people. Young people would be given specific information about their IDA accounts from a very early age, would be encouraged to participate in investment decisions for the accounts, and would begin planning for use of the accounts in the years ahead" (Sherraden 1991, 222). As implemented, however, IDAs are short-term asset building programs to temporarily assist families toward establishing and maintaining self-sufficiency.

The gap between IDAs as proposed versus implemented created an opening for another savings vehicle that could be accessed by young people, often called Child Development Accounts (CDAs).[2] In addition to retaining the same features of IDAs, such as universal availability and subsidies for young people whose families and households meet income eligibility guidelines, CDAs were proposed to be automatically opened at birth. In this way, young people could experience improved well-being as a

result of this long-term approach. CDAs were tested in the field beginning in 2003 with the Saving for Education, Entrepreneurship, and Downpayment (SEED) initiative, a national demonstration project that operated in 12 locations across the country (Mason et al. 2010; Sherraden and Stevens 2010). Shortly thereafter, the America Saving for Personal Investment, Retirement, and Education (ASPIRE) Act was introduced into the US Congress. The ASPIRE Act proposed to establish a national CDA policy that would automatically open savings accounts for all young people at birth.

As a concept, CDAs represent a turn in the road for asset building for young people. This is because CDAs provide savings accounts directly to young people instead of intervening at the family or household level. In addition, because the CDA policy vision includes universal and automatic access, young people from lower-income households would have equal access to accounts. During the last two decades, a concerted, nationwide effort has aimed to extend accounts to young people with particular emphasis on access for those from lower-income households. Key features of CDA program and policy design such as universal and automatic access enhance the impact on this target population by distributing accounts in a way that is equitable and less dependent on households' financial resources. This means that access to savings accounts would not be dependent on whether a savings program is offered by a local bank or whether families are motivated and able to open accounts for their young people.

Appendix 10.1 summarizes the growing number of policies and proposals in the last two decades geared toward young people's savings. They vary in terms of key features, such as universality and availability of financial incentives, but collectively they demonstrate widespread interest in young people's savings at local, state, and national levels.

What Is Savings?

Before moving forward, it is necessary to define exactly what is meant by the term "savings." The following definitions have relevance to the presentation of theory and research and are discussed here to provide background and establish a common understanding. While this may seem like an unwarranted question, savings is defined in many ways. As a result, the term savings may convey different meanings depending on how it is used. Neoclassical economists define savings as the remainder of money left over after consumption is subtracted from income, whereas social scientists more recently define savings as accumulated assets (Katona 1975; Keynes 1936; Modigliani and Brumberg 1954; Sonuga-Barke and Webley 1993). Specifically, social scientists have defined savings as money in an interest-bearing account that is "kept through time" (Schreiner and Sherraden 2007, 19). These latter definitions suggest that savings is the result of purposeful agency. Rather than simply the difference between income and consumption, savings is the intended product of saving behaviors—a behavior resulting in increased assets over time. That is, savings is accumulated money that is kept in an interest-bearing account and results from saving behaviors.[3]

These definitions of savings suggest that the term is sometimes used interchangeably to refer to savings account ownership, savings accumulation, or behaviors that affect whether savings is set aside and maintained for future use. These concepts, albeit related, are distinct dimensions of savings. The distinctions between the concepts are noteworthy because theory and research on young people's savings test account ownership, accumulation, and behaviors all under the umbrella term of savings—yet each may have distinct effects on outcomes. Without distinguishing between these concepts, we may unintentionally overlook nuances in the relationships between savings and young people's outcomes.

Savings account ownership refers to the product or vehicle in which savings can be accumulated. There are even variations in how savings accounts are defined. Sometimes theory and research refer to savings accounts held at mainstream banking institutions and other times they refer to savings accounts via CDAs or 529 plans. These nuances of account ownership are important because, on the one hand, savings accounts at mainstream banking institutions are products in the financial marketplace in which account holders can save for any expense and make withdrawals at any time. Savings accounts at mainstream banking institutions have very few institutional supports like automatic account opening or initial deposits that help account holders save. On the other hand, CDA savings accounts are intended to be universally available; restricted to preapproved expenses such as homeownership, microenterprise, or education; and designed with match incentives and subsidies to help account holders accumulate savings. CDA savings accounts are explicitly designed with institutional supports to help account holders save. Savings accounts in 529 plans are restricted to educational expenses, and in some cases, states offer incentives and subsidies for lower-income account holders (CFED 2012). Savings account ownership is also at times referred to as the amount saved—a snapshot of how much savings young people have accumulated in their accounts.

Savings accumulation refers to a process of building assets and increasing savings. In other words, savings accumulation measures families' or young people's increasing savings rather than simply measuring whether or not families or young people own savings. This also means that savings accumulation is more than the static amount saved at any one point in time—it is a process that can be thought of along a continuum. This distinction between savings account ownership and accumulation is relevant because some social scientists have found relationships between savings accumulation and young people's financial and educational outcomes (Friedline, Elliott, and Chowa 2012; Friedline, Masa, and Chowa 2012; Loke 2012). Saving behavior refers to a range of behaviors that affect whether or not funds are set aside and maintained for future use. Behaviors can include making deposits into savings accounts, signing up for direct payroll deposit, or managing income and expenses by budgeting. For instance, young people's saving behavior is sometimes referred to as whether or not they designate a portion of their allowance for savings or talk with their parents about savings (Furnham 1999; Kim, LaTaillade, and Kim 2011).

For the purposes of this chapter, savings is used to refer to account ownership, savings accumulation, and saving behaviors. Distinctions are made so that the reader can identify the dimension of savings to which discussions are referring.

Lessons from Theory

Asset building and IDAs emerged from theory on families' and households' savings, and it is equally important to establish theoretical grounding regarding young people's savings. Research that tests theoretical explanations can inform how and why people save and how and why their savings effects well-being—information that can be used to streamline and strengthen savings programs and policies for young people. Until recently, little attention has been devoted to explaining young people's savings. This oversight may be due to the guiding theoretical principles of the life-cycle hypothesis within neoclassical economics, which suggests there is little reason to believe that young people are capable of accumulating savings because they are involved in accumulating debt (Modigliani and Brumberg 1954). In other words, their incomes are low and their consumption needs are high.

Recent theoretical research suggests that young people's savings is quite complex and deserves attention (Lunt and Furnham 1996; Sonuga-Barke and Webley 1993). Several

theoretical perspectives focus on young people's savings, meaning that they develop and test their explanations using samples of young people. These include economic psychology theory, financial socialization theory, the institutional model of saving, and college-bound identity theory based on Identity-Based Motivation (IBM), which respectively examine the roles of development, family, institutions, and identity. Notably, behavioral economics and the theory of asset effects are absent from this list, as very few studies test behavioral economic and asset effects explanations of young people's savings.[4] Much of the work on economic psychology and financial socialization theories predates asset building from the last two decades; however, their perspectives are discussed as pillars that provide explanations for young people's savings. Findings from each perspective offer lessons that can shape our understanding of how and why young people's savings may affect well-being.

The Role of Development

The developmental approach to savings tends to focus on savings behavior and theorizes that young people are socialized into the world of money and finances at a young age. Their comprehension of money and finances is initially made up of separate and incomplete pieces of information that become integrated over time (Jahoda and France 1979; Leiser 1983). Young people begin by differentiating between coins and other objects and learning that money is related to purchasing; however, they do not yet grasp the complexities of monetary transactions (Berti and Bombi 1981a, 1981b; Strauss 1952). For instance, they may insist on using exact change to purchase an item or have preferences for certain coins based on their shape or color. Eventually, as young people mature, their comprehension of money and finances becomes integrated, and they behave accordingly. As a result, young people understand complex monetary concepts and can carry out advanced financial behaviors by approximately age 12. Young people closer to and older than twelve have the capabilities to use banks to regulate and invest their money, whereas young people prior to age 12 conceptualize banks as a place for storage or may even consider putting money in a bank as synonymous with *losing* money (Ng 1983, 1985; Sonuga-Barke and Webley 1993).

This should not be taken to mean that young people prior to age 12 are not ready to engage in saving behaviors (see, e.g., Elliott et al. 2010; Sherraden et al. 2012). In fact, young people already make notable gains in their capabilities to save around ages eight and nine and may move through developmental stages more quickly when they have early experiences with money management (Ng 1983, 1985). Early opportunities to save make use of an important time in young people's development by influencing them when their capabilities to save may be most impressionable (for more information about the impressionability of young children, see, e.g., Bruck and Ceci 1999; Scullin and Ceci 2001). If given early opportunities to save, it appears that young people may use the bank as a saving strategy sooner.

The Role of the Family

Financial socialization focuses on the role of the family in teaching young people about money and finances (Lunt and Furnham 1996). Financial socialization tends to focus on explanations for saving behaviors and has more recently been extended to explain savings account ownership and savings accumulation. Families may directly and intentionally provide financial socialization to young people, as well as indirectly and passively based on cues and context. For example, families may give allowances to young people to teach them about money and finances, but young people also receive financial socialization when they overhear conversations about bills or witness how families juggle finances to afford emergency expenses.

As the primary providers of financial socialization, families offer experiences like giving allowances, helping young people open savings accounts, or teaching them the importance of saving (Ashby, Schoon, and Webley 2011; Kim, LaTaillade, and Kim 2011; Mandell 2010; Ward et al. 1977; Williams et al. 2010). Research suggests socialization endeavors may be more successful when parents display greater degrees of warmth and involvement with young people and provide allowances contingent upon chores or other responsibilities. Greater displays of warmth and involvement may significantly improve young people's future orientation, a variable commonly linked with savings. From this viewpoint, young people's financial socialization is determined by their families' ability to provide and deliver endeavors like giving allowances, teaching about savings, and opening accounts. Unequally distributed household financial resources may play a role in families' ability to provide financial socialization, potentially resulting in unequal payouts like disparities in account ownership (Elliott 2012b; Friedline 2012; Friedline, Elliott, and Chowa 2012).

The Role of Institutions

The institutional model of saving was proposed by Michael Sherraden as a way of incorporating institutions in explanations of asset building. Here, institutions refer to intentionally designed "policies, programs, products, and services" that shape financial behavior (Beverly et al. 2008, 90). Savings is one example of asset building, and theory and research on the institutional model has referred to savings as account ownership, accumulation, and behavior. In part, the institutional model is designed to influence each of these savings dimensions through seven institutional mechanisms: access, information, facilitation, incentives, expectations, restrictions, and security. Furthermore, savings and asset building may be made easier when mechanisms are bundled. This means accounts are automatically opened, paired with financial education, facilitated by features like direct deposit, incentivized by providing matches (e.g., every dollar saved in the account is matched with an additional dollar), designed to identify expected savings goals (e.g., a minimum threshold for monthly savings), and penalized for making unapproved withdrawals. Presumably, people are less likely to have savings accounts and have less money saved in the absence of these mechanisms. A number of studies support the relationship between institutional mechanisms and savings and asset building (see, e.g., Grinstein-Weiss et al. 2010; Johnson, Adams, and Kim 2010; Loibl et al. 2010).

While institutional mechanisms were identified with families in mind, they may be relevant for explaining young people's savings and asset building. The design of existing CDA initiatives has relied heavily on institutional theory. For example, one large CDA program (the SEED national initiative) incorporates financial incentives and withdrawal restrictions and encourages direct deposit. Evidence suggests that these mechanisms have varying associations with young people's participation in a CDA program, savings, and total asset accumulation (Mason et al. 2010; Scanlon, Buford, and Dawn 2009; Wheeler-Brooks and Scanlon 2009). While the right design and bundling of mechanisms are still being discerned, institutional mechanisms may indeed shape young people's savings and asset building.

The Role of Identity

College-bound identity theory has recently been used to explain savings and educational outcomes (Elliott, Nam, and Johnson 2011; Elliott 2012b), a perspective that is grounded in IBM (Oyserman and Destin 2010). Here, savings most often refers to account ownership. Given that a separate chapter by William Elliott discusses the role of identity in

greater detail, only a brief discussion is presented here. Readers are encouraged to refer to chapter nine for an in-depth understanding regarding the role of identity.

William Elliott and colleagues have extended IBM for application to savings and educational outcomes and propose three central components. These components include identity salience, interpretation of difficulty, and congruence with group identity. Imagine, for instance, that a young person is working toward attending college. Her college-bound identity is salient when she is thinking about attending college (on the mind), has strategies (savings) for overcoming difficulty (affording college costs), and therefore is empowered to reach her goal. In order for her to sustain effort and work toward the image of herself as college-bound, she must have a way to address obstacles along the path toward attending college. These obstacles might include affording costs such as college entrance exams, admissions fees, books, room/board, and tuition. Savings provides her with a strategy for overcoming these difficulties and perhaps helps her to interpret the difficulties as surmountable—able to be overcome. Her family may share her college-bound identity, meaning that they also expect her to attend college. When this occurs, the young person's college-bound identity is congruent with the group identity, and her college-bound identity is reinforced.

In sum, young people may be developmentally ready to save early in life; however, families typically determine when and how young people begin saving. Families may have different ideas about or abilities to extend savings accounts to young people. Therefore, the financial socialization experiences of young people vary widely; some young people save early in life and accelerate their developmental capabilities to save, whereas other young people do not. Some young people may miss important milestones in their development completely by starting to save too late. When young people do engage in savings, they may benefit from institutional mechanisms that structure their savings and make saving behaviors automatic. When young people have savings accounts and engage in related behaviors, they may be more likely to think about and plan for their futures. Especially if savings are labeled "for college," they may think about the possibilities of attending college and be more likely to enroll and graduate when the time comes. The lessons learned from these theoretical perspectives begin to shape our understanding regarding how and why young people's savings may influence their well-being.

Lessons from Research

Extending savings accounts to young people may improve well-being outcomes in a number of ways. For example, young people who have savings accounts at one point in time have been found to have savings accounts at a later point in time and more money saved. In this case, young people's savings accounts appear to be linked to financial outcomes (Ashby et al. 2011; Elliott et al. 2012; Friedline, Elliott, and Chowa 2012). The same holds true for educational, physical, and emotional outcomes—young people's savings accounts have been linked to a greater likelihood of college attendance and graduation and a lower likelihood of being depressed (Elliott and Beverly 2011a; Ssewamala et al. 2009, 2010, 2011). The research presented in this section distills findings from studies that include a savings measure for young people at baseline for improving financial and educational outcomes (based on 12 and 14 studies, respectively).[5] By including only studies that measure young people's savings at baseline, the review hones in on lessons encompassing a key hypothesis of young people's savings programs and policies: having savings accounts at an earlier point in time has effects on outcomes at a later point in time. Moreover, the research in this section is presented as an overview of the main findings rather than a detailed review.

Notably, this research refers to savings as account ownership and amount saved. However, as mentioned in the definitions of savings, savings account ownership in and of itself has different meanings. In most cases, this research refers to savings as accounts or amounts held at mainstream banking institutions. As previously mentioned, these accounts are in the financial marketplace and do not have in place the same institutional features incorporated into CDAs. Savings accounts at mainstream banking institutions do not automatically open accounts, provide initial deposits, incentivize savings, limit deposits and withdrawals, or restrict usage to specific expenses like education or homeownership. A growing number of research studies test savings as CDA or 529 savings accounts that do include institutional features like automatic account opening and initial deposits.

Savings accounts in this research are most often accounts held at mainstream banking institutions. As opposed to CDA savings accounts that are universally available and automatically opened, some young people have savings accounts at mainstream banking institutions and others do not. This means that young people with savings accounts at baseline may look very different compared to young people without savings accounts at baseline. As mentioned in the introduction, young people from lower-income households may be at a disadvantage for accessing savings accounts. If young people's savings account ownership at baseline is determined by their households' income, it becomes challenging to rule out the possibility that household income (and not young people's savings accounts) produces the effects on young people's financial and educational outcomes. Researchers attempt to minimize this limitation using advanced methodological techniques.[6] However, the reader should keep this limitation in mind.

Financial Outcomes

Financial outcomes in this context refer to the types and values of savings accounts owned by young people.[7] The underlying assumptions that young people's savings speak to their financial well-being and give insight into their ability to afford expected and unexpected expenses (e.g., paying for college and weathering shocks to income) drive this research. Findings are relevant, then, because they offer beginning evidence on the degree to which young people have the financial resources needed to lead productive and satisfying lives. Currently, this research limits the scope to savings and will eventually expand to encompass other assets, such as homeownership, 401(k) participation, stocks/bonds, and other assets. Findings tell us that young people who have savings accounts at one point in time, compared to those who do not, (1) are more likely to have savings accounts at another point in time; (2) have higher amounts saved at another point in time; and (3) still depend on their families and households for savings despite their own account ownership. These findings hold true whether the account is held at a mainstream banking institution or in a CDA.

Studies find evidence that young people's savings at baseline relates to or predicts young people's savings at outcome.[8] For example, a longitudinal study of British young people by Julie Ashby et al. find that savings accounts at mainstream banking institutions at age 16 was directly and significantly related to their savings at age 34 (Ashby et al. 2011). Using a combined sample of lower-income and higher-income young people from US households with data from the Panel Study of Income Dynamics (PSID), researchers find that young people age 17–23 in 2007 were significantly more likely to own savings accounts at mainstream banking institutions and to accumulate savings when they had savings accounts five years earlier at age 12–17 in 2002 (Friedline, Elliott, and Nam 2011). Another study with PSID data restricts the sample to only young people from lower-income households

and finds that young people age 18–22 in 2007 were significantly more likely to own savings accounts and to accumulate more savings when they had accounts at banking institutions five years earlier (Friedline, Elliott, and Chowa 2012).

Despite the inclusion of young people's own savings accounts, studies continue to find that families' and households' characteristics matter. Young people appear to have better savings outcomes when their households have more assets and their heads of households have higher levels of education. For example, lower-income young people accumulate more savings in accounts at mainstream banking institutions when their households have higher net worth (Friedline, Elliott, and Chowa 2012). Notably, the strength of the relationships between household characteristics and young people's savings outcomes tends to be weaker when compared with young people's own savings. That is, while research cannot rule out the importance of households' characteristics to young people's savings (e.g., education levels, household net worth, and parents' savings), extending savings accounts to young people at baseline may be the more direct route to affecting their savings outcomes.[9]

Educational Outcomes

Educational outcomes refer to young people's academic achievement (specifically, reading and math scores), educational expectations, and college attendance and/or graduation.[10] These measures of educational outcomes are assumed to indicate the degree to which young people achieve important indicators of the American Dream—most notably college attendance and graduation. Findings tell us that young people who have savings accounts at an earlier point in time, compared to those who do not, (1) have higher academic achievement at a later point in time; (2) develop educational expectations for their futures at a later point in time[11]; and (3) are more likely to enroll in or graduate from college at a later point in time.[12] The majority of research on young people's educational outcomes refers to accounts held at a mainstream banking institutions.

A number of studies find a significant relationship between young people's savings and their educational outcomes, even after taking into consideration households' financial resources like income and assets. For example, young people's savings accounts at mainstream banking institutions are associated with higher math scores, controlling for assets like homeownership and household net worth (Elliott et al. 2010). As mentioned, young people's savings accounts at mainstream banking institutions measured at baseline are also linked to their educational expectations—what William Elliott refers to as "college-bound identity." This research explores whether savings accounts promote young people's expectations for college. It appears that young people with savings accounts at mainstream banking institutions also expect to go to college, and their college expectations are linked to educational outcomes like higher college attendance rates. Young people with savings accounts are also more likely to be enrolled in or to have graduated from college—benefits that appear to transcend race and class differences (see, e.g., Elliott, Constance-Huggins, and Song 2011; Elliott and Nam 2012). The significant relationship between savings and educational outcomes also holds true when their savings is designated specifically for school purposes, like college (Elliott and Beverly 2011a; Elliott et al. 2010).

In addition to young people's savings, studies continue to find that families' characteristics are related to educational outcomes (see, e.g., Elliott and Beverly 2011a; Elliott, Jung, and Friedline 2010; Elliott and Nam 2012). However, when simultaneously considering families' characteristics and young people's savings with educational outcomes, young people's savings accounts have the stronger relationship. That is, young people's

savings accounts may be the more direct route for relating to their educational outcomes, in part because it develops their expectations for college. These findings validate programs and policies that extend savings accounts to young people as a strategy for improving educational outcomes as opposed to intervening only at the family or household level.

It should be mentioned that this research tests the effects of savings account *ownership* at baseline on educational outcomes, meaning that simply owning a savings account may produce the desired effects and the amounts accumulated or the process of accumulation may be less important. However, some rightly question whether savings account ownership can realistically improve young people's likelihood of college attendance and graduation, given the gap between high college costs and the small amounts of money young people save. A series of research studies suggests that young people's savings accounts at mainstream banking institutions with money designated for school are significantly related to their college attendance and graduation, even when small amounts of money are saved ($0 or $1–$499; Elliott 2012a; Elliott, Song, and Nam 2012a, 2012b; Friedline, Elliott, and Nam 2012b). The findings from this series provide some indication that account ownership may still have effects on educational outcomes even when the amounts saved are small.

Overall, lessons from research suggest that young people are more likely to have savings accounts and more money saved, have higher math scores, and attend and graduate from college at higher rates when they have savings accounts early in life. While families' and households' characteristics are still related to financial and educational outcomes, extending savings accounts to young people at baseline may be the more direct intervention for improving their outcomes. It is important to note that no one study provides a definitive test of the relationships between young people's savings and financial and educational outcomes. Rather, attention should be directed to the complete body of research on young people's savings, which consistently confirms that savings is linked to their financial and educational outcomes. Implications for policy can be gleaned from the lessons learned from theory and research and are discussed in the following section.

Considerations for Policy

Recognizing the potentially transformative role of extending savings accounts to young people, many programs and policies have been proposed or implemented to support young people's savings. Several states have relaxed requirements for and incentivized 529 savings accounts so those from lower-income households can more easily open and use the accounts to save for college. The Harold Alfond Challenge in Maine is one example of how states have encouraged families to open 529 accounts. Programs and policies have also experimented with default-enrollment, or automatic, savings accounts. The ASPIRE Act, one of the most comprehensive pieces of legislation on young people's savings, proposes to automatically open savings accounts for every newborn at birth with an initial deposit and incentivize saving for income-eligible young people by matching dollar for dollar the deposits up to $500 annually. The SEED for Oklahoma Kids (SEED OK) experiment—one of the first tests of an automatic, universal, and incentivized savings policy—automatically opened accounts across the state of Oklahoma in 2007. Moreover, the SEED OK experiment uses Oklahoma's 529 structure as a vehicle for distributing savings accounts.

Many of the aforementioned programs and policies were proposed or implemented when theory and research on young people's savings was nascent. Theory and research

have expanded in the last two decades, with recent developments confirming early hypotheses and augmenting implications that can be drawn for program and policy development. Other scholars and advocates have provided well-articulated and comprehensive discussions regarding the specifics of asset building and savings policies for young people (see, e.g., Cramer 2010; Elliott 2012b; Elliott et al. 2011; Goldberg, Friedman, and Boshara 2010). The discussion here is more narrowly focused on policy considerations that (1) stem from theory and research, and (2) relate to a national CDA policy (like the ASPIRE Act) that aims to provide a comprehensive approach to asset building by young people. Theory and research point to considerations that can inform policy with regard to account enrollment, account design, and linkages with family and educational systems.

Account Design

In order to move from policy concept into public law, the first design consideration includes determining the best vehicle for rolling out young people's savings accounts. As mentioned, a majority of research on young people's savings uses savings accounts like those found at mainstream banks. These accounts are not automatically opened for young people. Instead, their families play a role in helping them to open accounts. Young people do not receive an initial deposit at account opening, nor is their savings incentivized with match deposits. They can freely make deposits and withdrawals and there are no restrictions on the types of expenses for which their savings can be used. However, this research tests accounts at mainstream banks as proxies for CDA savings accounts. Comparatively, the SEED national initiative tested a form of CDA savings accounts by inviting young people to open accounts, providing initial deposits, and incentivizing their savings by matching deposits. Accounts from SEED were restricted for use toward education, homeownership, retirement, or small-business start-up. Still other research considers the usefulness of section 529 accounts for delivering a national CDA policy. Proponents of 529s contend that statewide college investing accounts would be ideal given that the existing structure would ease the burden of rolling out a CDA policy at the national level. Research that compares the potential vehicles for extending savings accounts to young people—savings accounts like those found at mainstream banking institutions versus CDA savings accounts—would go a long way toward informing young people's savings account design.

Even though most research tests savings accounts at mainstream banks, CDA savings accounts are likely the better design. This is because CDAs incorporate institutional features like automatic account opening, incentives on deposits, and restrictions on withdrawals that have been found to shape savings for young people and families. Importantly, the features of CDAs would likely help to redress barriers in access to savings accounts and to give young people from lower-income households the opportunity to save.

Moreover, we can still expect effects on young people's outcomes when research tests savings accounts with CDAs. The relationship between CDAs and financial and educational outcomes may even be stronger and not weaker given the proposed design of the account. This is because every young person with a CDA account is connected to a larger movement that encourages asset building and makes the savings-education link explicit. By design, the purposes of a CDA account are to build assets and to save for the future. Should a national CDA policy like the ASPIRE Act be enacted, every child would save toward their college education or another preapproved future goal like homeownership or retirement. In the current SEED OK experiment, every child

assigned to the treatment group has a CDA-type of an account. We might expect the relationships between young people's savings and their outcomes to be stronger with CDA accounts based on their intentional and institutional design compared with savings accounts at mainstream banking institutions. The remaining considerations for policy are based on the assumption that CDA savings accounts are the better vehicle for young people's savings compared with accounts at mainstream banking institutions.

A second consideration speaks to savings account design and encompasses the institutional mechanisms built into account design and vehicles for rolling out savings accounts. Aside from automatic and universal enrollment at birth, other institutional mechanisms may be embedded into savings account design. These mechanisms, which have been found to shape adults' saving behaviors, include initial deposits to jumpstart saving in the accounts, incentives like matches on deposits or rewards for achieving milestones, arrangements to facilitate easy and convenient deposits like direct deposit plans, expectations for minimum regular deposits, and restrictions against frequent withdrawals. Conversations with young people in the SEED national initiative revealed that the institutional mechanisms that have been endorsed for shaping adults' saving behaviors may be productive for young people, as well (Scanlon et al. 2009; Sherraden et al. 2012; Wheeler-Brooks and Scanlon 2009). For instance, young people in the Juma Ventures program in San Francisco reportedly approved of incentives for saving and restrictions against withdrawing their savings impulsively (Wheeler-Brooks and Scanlon 2009). However, some institutional mechanisms may be less suitable for shaping young people's saving behaviors. Young people who experienced transient employment reportedly did not benefit from facilitation mechanisms like direct deposit. Interruptions in employment translated into interruptions in direct deposit and, ultimately, inconsistent savings. Some mechanisms may need to be redefined or re-envisioned to apply to young people's circumstances. Exploring the mechanisms suitable for young people may ultimately lead to better account design and implementation. More research is needed in this area.

Along these lines, institutional mechanisms may also be tailored to improve savings for young people from lower-income backgrounds. Savings programs and policies primarily intend to benefit young people from lower-income backgrounds. Given this, research should explore which institutional mechanisms shape the saving behavior for these young people. One question that holds particular relevance for those from lower-income households is where young people will get the money to save? Young people from higher-income households are likely in a better position to receive money from their families; however, young people from lower-income households may be at a disadvantage. Incentives may prove particularly useful because they would subsidize savings for income-eligible young people and help them accumulate savings.

Institutional mechanisms are commonly proposed to be bundled. People may save more often and greater amounts when multiple mechanisms are available at once rather than having one mechanism in isolation. As such, savings programs for adults and young people often combine incentives, facilitation mechanisms, and restrictions (Mason et al. 2010; Schreiner and Sherraden 2007). However, the individual contributions of each mechanism for improving outcomes are unknown. This could mean, for instance, that the effects of institutional mechanisms on financial and educational outcomes are driven by incentives and facilitation whereas restrictions play a lesser role, or vice versa. Determining the value added by each institutional mechanism would go a long way toward designing young people's savings accounts and would help create a streamlined and cost-effective national CDA policy. More research on institutional mechanisms is needed. A CDA policy that has effects on young people's outcomes while

simultaneously considering cost-effectiveness may be more likely to pass into public law and to be brought to scale at a national level. Caution is warranted, however, because a CDA policy should not sacrifice effectiveness for cost, especially when the well-being of young people from lower-income households is on the line.

Some have suggested that savings accounts may be more productive for young people from lower-income households when restrictions on accounts are flexible. Young people may benefit from a flexible savings account that allows early withdrawals so they can meet needed expenses along their path to college as opposed to an account that prohibits any withdrawals. For instance, a young person whose household cannot afford a school uniform in middle school likely would benefit from using their savings in the short term so they can stay on track to attend college in the long term. The goal is for young people to be able to use their savings to finance educational expenses and to overcome financial obstacles along the path toward college attendance. William Elliott recommends a three-in-one design that includes a "short-term account, an intermediate account, and a long-term account" (Elliott 2012b, 3). Research is needed that compares restricted and flexible accounts in order to determine which design produces the desired effects on young people's outcomes.

Account Enrollment

Another consideration speaks to account enrollment in terms of the age at which savings accounts can be introduced to young people and the way in which young people are enrolled. Both theory and research support an "earlier is better" approach and point to extending savings accounts to young people perhaps even as early as birth (although the effects of account opening at birth are still being tested in the SEED OK experiment). Account enrollment at birth may be wise for two reasons. First, it encourages savings in concert with young people's developmental capabilities. Young people as early as ages five and six believe that saving is a good thing, are excited about savings, and can learn to do so when given the right supports. When young people are enrolled into accounts at birth, the accounts precede and possibly accelerate developmental capabilities to save. Second, savings accounts early in life have been linked to improved financial and educational outcomes later in life. By extending savings accounts at birth, young people have a longer time to benefit from the cumulative effects of account ownership on outcomes.

Given that young people's savings account ownership is still dependent upon families' and households' characteristics, some young people have savings and others do not—differences that are evidenced along lines of race and class. A universal and automatic approach may work best to enroll these young people who might otherwise be excluded. If all young people were enrolled automatically, then household characteristics would have much less of an impact. For example, young people would not have to rely on their parents' financial resources or their willingness to open an account.[13] Evidence confirms that enrollment rates vary significantly between programs with and without automatic enrollment. Consider, for example, the Harold Alfond Challenge program, which deposits $500 into the 529 account of every newborn in Maine, as long as the account is opened by the child's first birthday. Between 2008 and 2010, only 21 percent of eligible newborns in Maine had a 529 account by their first birthday, and account opening was related to household characteristics like education, income, and assets (Huang et al. 2011). In contrast, in SEED OK, when accounts were automatically opened for newborns, only one of the 1,340 eligible families chose to opt-out, so enrollment was nearly 100 percent (Nam et al. 2011).

Linkages with Family and Educational Systems

The final consideration points to opportunities to link young people's savings accounts with existing family and educational systems. Research findings suggest that young people may benefit from engaging in savings and asset building alongside their families and households. For instance, young people's savings may be enhanced when their families and households simultaneously engage in asset building, perhaps improving financial outcomes in the long run for everyone involved. This is not to say that asset building for families and households takes precedence over young people's savings.[14] Rather, this is to recognize that lower-income households typically have fewer assets and may benefit from building assets themselves. Meanwhile, young people may benefit from sharing a common goal with their families and households who are simultaneously engaged in saving and accumulating assets. Programs and policies like IDAs that are geared toward families and households may consider expanding to include young people's savings. Pairing CDAs with IDAs, for instance, may leverage the savings families and households to improve young people's own savings.

Similarly, young people may benefit when savings accounts are linked to educational systems in order to increase the effects on educational outcomes and leverage college-bound identities. First, given the relationship between savings and educational outcomes, it may be natural to make this relationship explicit by embedding savings accounts within educational systems. Moreover, it may be efficient to pair savings accounts with educational systems because all young people are connected to schools, making schools a natural place to intervene in young people's lives. San Francisco's Kindergarten to College (K2C) savings program exemplifies this linkage by automatically extending savings accounts to all kindergarteners in the San Francisco Unified School District.

Second, linking accounts with educational systems may leverage college-bound identities. Most young people expect to attend college regardless of their families' ability to pay college costs; however, fewer young people enroll in or graduate from college soon after high school despite high expectations—an experience that is amplified for young people from lower-income households (Advisory Committee on Student Financial Assistance [ACSFA] 2006). This experience has been called "wilt" by William Elliott and Sondra Beverly (2011b). This means that leveraging young people's already-high college-bound identities, rather than attempting to raise them, may be the most advantageous. Linking savings accounts to educational systems may provide the context needed to leverage college-bound identities and improve educational outcomes.

Crossing the Bridge from Policy Concept to Public Law

Despite growing theoretical and research support for young people's savings, a national CDA policy has not been implemented. In addition to lack of political will or partisanship, one reason a national CDA policy might not have been implemented is perhaps due to limited evidence regarding the specifics of savings account and policy design. Policies, including asset-based social welfare policies, often consist of a comprehensive set of provisions that are intended to address social issues by identifying priorities, describing activities and protocols, and implementing the policy. Prior to becoming public law, policy makers render judgment on proposed policies and determine their fate by examining each individual provision within the broader, comprehensive set of provisions. When policy makers have limited knowledge about the value added by individual provisions, they have limited evidence on which to evaluate the validity of proposed policies and make informed decisions. Ultimately, proposed policies may not pass into public

law. Policy makers may have especially limited knowledge to make informed decisions regarding young people's savings policies, which is perhaps indicated by the fact that these policies have been proposed into the US Congress since 1995 but have not passed into public law at the national level. To assist in crossing the bridge from policy concept to public law, continued theory and research on young people's savings is needed.

There are many remaining questions: Is there a cutoff for the age at which young people should be enrolled into savings accounts to improve outcomes, and if so, when is it? Which institutional mechanisms improve which outcomes? Are there thresholds for the levels of initial deposits and incentives and if so, where should the thresholds be set? Do thresholds differ depending on families' and households' characteristics like income and assets? Should incentives be geared toward match contributions or rewards for milestones? Are there distinct effects when young people manage and control their savings accounts versus having savings accounts in their own names? Should young people transition into the role of account managers after a certain age? If so, when and how should this transition take place? Do young people's savings accounts matter most for improved outcomes, or are there thresholds of savings amounts that are also beneficial? For example, is there a certain level of savings that is linked to college attendance or graduation, such as an amount that allows young people to purchase books or afford registration fees? Do the effects of savings accounts persist across the life course and if so, how? Are the effects passed on to future generations? If these questions are tested in future research, there will be additional evidence on which to evaluate young people's savings policies.

Asset building during the last two decades has endorsed extending savings accounts to young people and mounting evidence from theory and research supports this strategy. This chapter hopefully provides a compelling presentation for why extending savings accounts to young people may be beneficial for improving financial and educational outcomes. Many valid questions remain about how extending savings accounts to young people will work. Researchers and policy makers alike should welcome dialogue around such questions that can help move us toward a national policy solution that provides savings opportunities for all young people.

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Notes

1. It should be noted that "asset building" is an umbrella term for account ownership, saving behaviors, savings, and asset accumulation. As such, asset building can be applied to owning stocks and bonds, accumulating net worth, or depositing money into savings accounts at a local bank. A narrower term, savings, is adopted for use in this chapter. This is because most theory and research have focused on young people's savings—not other types of assets like stocks, bonds, or net worth.
2. These accounts are also referred to as Children's Savings Accounts (CSAs).
3. It is worth noting that this narrow definition of savings—accumulated money that is kept in an interest bearing account and results from purposeful saving behaviors—does not capture other ways in which people save. For instance, lower-income families may save at home without the benefit of an interest bearing account. Higher-income families may save passively

when they automatically invest their capital gains. While this narrow definition is consistent with how theory and research has defined young people's savings (purposeful savings in an interest bearing account), it would be inadequate to always define savings in this way. As a reviewer has kindly pointed out, such a narrow definition could unintentionally perpetuate the misconception that lower-income families or young people do not save since they have interest bearing accounts less often than their higher income counterparts.

4. This is not to say that behavioral economics has not been applied to young people generally speaking. Rather, behavioral economics has been applied infrequently to the context of their saving behaviors. For two exceptions, see Lahav, Benzion, and Shavit (2010) and Marshall, Chuan, and Woonbong (2002). We will know more about the role of choice architecture (heuristics, time horizons/discount rates, rules of thumb, and loss aversion) as behavioral economics is increasingly applied to young people's saving behaviors.
5. Each of these studies measure young people's savings as savings in an account at a mainstream banking institution or savings in a CDA program. Earlier research measures young people's savings more broadly such as saving a portion of their allowance or agreeing saving is a good thing (see, e.g., Jahoda and France 1979; Lunt and Furnham 1996; Ward et al. 1977). However, this chapter narrowly discusses findings that measure savings in an account at a mainstream banking institution or savings in a CDA program.
6. Studies statistically control for potential confounding variables such as heads of households' education level, household income, and household assets. In some cases, studies use propensity score analysis to balance the samples based on observed characteristics, which is one way to replicate an experimental design in secondary data. However, the reader should be cautioned that propensity score analysis is not the same as an experimental design.
7. Findings for financial outcomes come from 12 studies: Ashby, Schoon, and Webley (2011); Elliott et al. (2011); Elliott et al. (2012); Friedline and Elliott (2011); Friedline, Elliott, and Chowa (2012); Friedline, Elliott, and Nam (2011); Huang et al. (2011); Huang, Nam, and Sherraden (2012); Mason et al. (2010); Nam et al. (2011); Scanlon, Buford, and Dawn (2009); Sherraden et al. (20070; and Sherraden et al. (2012).
8. It is worth noting that these findings are consistent across studies. For example, eleven of twelve studies find that savings at baseline is related to or predicts savings accounts at outcome in both cross-sectional and longitudinal data. Among eight studies that examine savings amounts at outcome, all find some evidence to suggest having a savings account at baseline relates to the amount of savings accumulated at outcome. Among the twelve studies, all find some evidence to suggest that families' and households' characteristics relate to young people's savings outcomes. See, for example, Friedline, Elliott, and Chowa (2012) and Mason et al. (2010).
9. Most findings come from regression-based research where all variables are added at once to the models, meaning that the effects of one variable (young people's savings at baseline) on an outcome (young people's savings at outcome) exist when all other things (education level and household net worth) are held constant. Researchers may find differences in influences when time order is considered, meaning that variables are introduced chronologically relative to one another (education level may temporally precede household net worth, both of which may precede young people's savings at baseline). It may be that young people's savings at baseline mediates the effects of household net worth on their savings at outcome, a finding more easily examined when time order is taken into consideration and similar to that proposed by Elliott, Jung, and Friedline (2010) with regard to math achievement at outcome.
10. Findings for educational outcomes come from fourteen studies: Elliott (2009); Elliott and Beverly (2012a, 2012b); Elliott, Chowa, and Loke (2011); Elliott, Jung, and Friedline (2010, 2011); Elliott et al. (2010); Elliott et al. (2010); Elliott and Nam (2012); Elliott, Nam, and Johnson (2011); Elliott et al. (2010); Elliott and Song (2011); Ssewamala and Ismayilova (2009); and Ssewamala et al. (2010).
11. Findings for educational expectations (separate from outcomes such as math achievement, college attendance, and college graduation) come from nine studies: Elliott (2009); Elliott and Beverly (2011a); Elliott et al. (2011); Elliott et al. (2010); Elliott et al. (2010); Elliott, Nam, and Johnson (2011); Elliott et al. (2010); Sherraden et al. (2012); and Ssewamala and Ismayilova (2009).

12. It is worth noting that these findings are consistent across studies. For example, fourteen studies examine savings at baseline for young people's academic achievement (seven studies) and college attendance and/or graduation (seven studies). Among the fourteen studies, all find some evidence to suggest that families' and households' characteristics relate to young people's educational outcomes. See, for example, Elliott and Beverly (2011a, 2011b) and Elliott Destin et al. (2011). Ten studies examine savings at baseline and young people's educational expectations (college-bound identity).
13. Of course, families could opt out of automatic accounts, but early evidence from SEED OK suggests that few families would (Nam et al. 2012).
14. Note that based on theory and research, the more direct route for improving young people's well-being may be through extending savings accounts to them directly without families and households as intermediaries. Linking families' and households' savings and young people's savings may be an alternate, albeit indirect, route for improving their well-being.

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Appendix 10.1

Progression of Asset-building Programs and Proposals for Young People in the United States

Year	*Asset-building programs and policies*	*Description*
1995	KidSave accounts[1]	Proposes to amend the Old Age, Survivors, and Disability Insurance program of the Social Security Act to create a new Part B, which would automatically open KidSave Accounts at birth with an initial deposit of $2,000 and allow contributions of $500 per year, to be managed by the Thrift Savings Plan.
1996	Small Business Job Protection Act 26 U.S.C. § 529	Creates state-run qualified tuition programs in Section 529 of the Federal tax code, otherwise referred to as Section 529 plans. Savings can accrue tax free and is restricted for use toward educational purposes. Section 529 plans were expanded upon by the Taxpayer Relief Act of 1997, the Economic Growth and Tax Reconciliation Act of 2001, and the Pension Protection Act of 2006.
1999	The Harold Alfond College Challenge Program	Provides $500 to all Maine newborns who have a Maine 529 plan account by their first birthday with an additional $200 for all accounts opened with an initial deposit of at least $50, along with other incentives.
2003	SEED national initiative	Demonstration and research initiative in 12 communities across the United States and in Puerto Rico. Offered incentivized and restricted-access savings accounts to low- and moderate-income young people ages birth to 23.
2004	ASPIRE Act[1]	Proposes to establish a universal nationwide CDA policy. Savings accounts would be automatically opened at birth with an initial deposit of $500. Deposits into accounts held by income-eligible young people would be matched.
2007	401Kids accounts	Changes name of Coverdell education savings accounts to 401Kids Savings Accounts. Allows tax-free deductions from a 401Kids Savings Account for first-time homebuyers and rollovers into Roth IRAs.
	Baby bonds[1]	Proposes to provide a $500 savings bond at birth and another at age 10. Funds could be used for postsecondary education or training, homeownership, and retirement.

	PLUS accounts[1]	Proposes to automatically open a savings account at birth for every newborn citizen, with an initial deposit of $1,000. Workers could arrange to have 1% of every paycheck automatically deposited and employers would be encouraged to provide a 1 percent match.
	SEED for Oklahoma kids	Randomized CDA experiment using a probability sample of newborns in Oklahoma. Automatically opened a 529 account for every newborn in the treatment group, with a $1,000 initial deposit.
	Young savers accounts[1]	Proposes an opt-in Roth IRA that is maintained by families for young people under the age of 26, with contributions subject to limits and annual income-based tax deductions allowable up to $5,000.
2010	Kindergarten to college	Automatically opens a 529 college savings account with a $50 initial deposit for every kindergartener in the San Francisco Unified School District. Income-eligible children receive an additional $50. Includes financial incentives and financial education.
2011	Department of Education's GEAR UP invitational priority	Includes an invitational priority that invited grant applicants to incorporate college savings accounts and financial education as part of the Gaining Early Awareness and Readiness for Undergraduate Programs (GEAR UP) discretionary grant program. GEAR UP was authorized in 1998 to improve postsecondary education outcomes for young people from lower-income households.
2012	Department of Education GEAR UP college savings demonstration	Allocated $8.7 million to implement a college savings account research demonstration using a randomized experimental design within GEAR UP. Assigns college savings accounts to a treatment group of 10,000 young people and designates a control group of 10,000 young people. Designed to test the potential impact of pairing savings accounts with GEAR UP activities, there is uncertainty as to whether this demonstration project will in fact be implemented in the field due to funding restraints.

Notes: "Section 529" programs are tax-advantaged education investment plans (also known as "529 plans") that are governed by Section 529 of the Internal Revenue Code. Individual banks and financial institutions often have savings programs designed for young people; however, this table does not include programs and/or policies of individual banks.

[1] Indicates programs or policies that have been proposed but have not been implemented.

Source: Information from this table was compiled from CFED 2012, Cramer 2010, and Lassar Clancy and McClure 2010, and from information available through Thomas.gov and Govtrack.us.

Chapter Eleven

Making Tax Time the Financial Management Moment

David Rothstein and Rachel Black

The delivery of social policy has significantly transformed over the past two decades. This is most evident in changes to the tax code, which is used increasingly to distribute resources and incentivize behavior. The creation and subsequent expansions of the Earned Income Tax Credit (EITC), combined with dramatic reductions in welfare cash assistance programs, embody this shift. Historically, the primary objective of tax policy was to raise sufficient revenue to fund the cost of government. Today, the tax filing process not only collects funds but also triggers a process of delivering benefits to households. Consequently, filing taxes has become the gateway for millions of families to access billions of dollars of support (Holt 2011; Tufano 2010).

A series of policy changes has increased the resources available to families at tax time. For many families, their tax refund is now the largest single influx of income they will receive all year, frequently equivalent to three months of pay (LaLumia 2010). As the size of refunds has grown, a network of not-for-profit organizations with varying degrees of capacity has emerged to connect low-income families with opportunities to leverage their refunds and accumulate assets. These organizations provide free or very low cost assistance to families filing tax returns. The unrestricted nature of the tax refund also provides households with much more flexibility in how to allocate these resources than in-kind benefits such as housing vouchers or the Supplemental Nutrition Assistance Program (SNAP, formerly food stamps). As a result, tax filing now allows families to pursue a range of financial objectives, including increasing their savings and managing their finances in ways previously unavailable through traditional public assistance programs.

The largest network of organizations to assist low-income tax filers is a network of Volunteer Income Tax Assistance (VITA) providers and sites. The VITA program has grown both in scale and in scope, reaching more clients and providing these clients with a diverse menu of services to meet their financial needs, from help filling out financial aid forms for college to applying for public benefits (Holt 2011). VITA sites are often existing nonprofits or libraries, or are run through local municipalities.

The extensive infrastructure of this network and its role as the conduit through which many families receive what is often the largest financial transaction of the year has positioned VITAs on the front line of the delivery of asset-building opportunities to low-income households. In addition to connecting individual clients with asset-building

tools, such as basic checking or savings accounts, VITA sites have been the testing ground for programs and policies that could take promising practices to a national scale. These include emergency savings accounts, Individual Development Accounts (IDAs), and financial education courses. Diversification of services beyond its core mission of free tax preparation has allowed the VITA network to provide clients with additional strategies to address their financial security, though there is still opportunity to offer a more comprehensive set of options to a greater number of people. However, organizations face considerable constraints on their capacity to fill this space.

This chapter explores the emergence of the free tax preparation movement, the expansion of VITA providers into the asset-building field, and challenges that VITA sites will need to resolve in order to continue evolving in their financial management role. It will provide an analysis of how policy changes, such as the expansion of the EITC, transformed and magnified the significance of tax filing; describe the emergence and evolution of the network of organizations focused on providing free filing and other services; and identify challenges that exist both in policy and infrastructural capacity that limit the asset development, consumer protection, and financial education services these sites are able to provide at tax time. Finally, it will close with a discussion of ways to make tax time a more effective financial management opportunity for families.

The Transformation of Tax Time

Asset building at tax time cannot be divorced from the distribution of federal and state tax refunds. The numerous credits and deductions in the income tax system, which have grown considerably in the last 50 years, provide many tax filers with a refund. The progressive income tax structure makes this especially true for low-income families who pay a larger share of their income toward sales, social security, and usage taxes (Marr and Huang 2012) but receive some relief in the federal income tax. Deductions for student loan interest, mortgage interest, and property tax deductions reduce the tax liability of millions of families. Yet the largest development in tax-time refunds and savings policy are tax credits, some of which are refundable. Refundable credits are powerful because if the credit exceeds the filer's liability, the Internal Revenue Service (IRS) refunds the difference. Through these refunds, the tax code is now the primary method of delivering social welfare policy, which influences families' ability to save.

The largest refundable tax credit, the EITC, benefits low- to moderate-income families by providing an offset to payroll and social security taxes, though it is more recently seen as an income supplement to lower wage workers. The benefit is structured to increase as earnings increase in order to encourage work effort as well as to provide a larger benefit for families with children. The EITC boosts the value of earnings for low-wage workers by providing an additional subsidy for every dollar in earned income. The impacts on families and communities are plentiful. Nationally, the EITC lifted an estimated 6.3 million children above the federal poverty line in 2010, dwarfing other poverty prevention programs (Center on Budget and Policy Priorities 2012). It also helps the near-poor to get a little further above the poverty line, which can be crucial to greater long-term stability. The EITC is lauded for its "multiplier effect" because families use their refunds for purchases in the community, generating business and jobs that otherwise might not be leveraged (see National Community Tax Coalition [2012] for an overview of this literature).

Created by President Nixon and enacted under President Ford, the EITC's growth has been remarkable. The maximum credit in 1975 was $400. Major expansions of the credit were enacted in 1986, 1990, 1993, and a temporary expansion in 2009, which increased coverage and benefit size. These were bipartisan changes made to increase the assistance

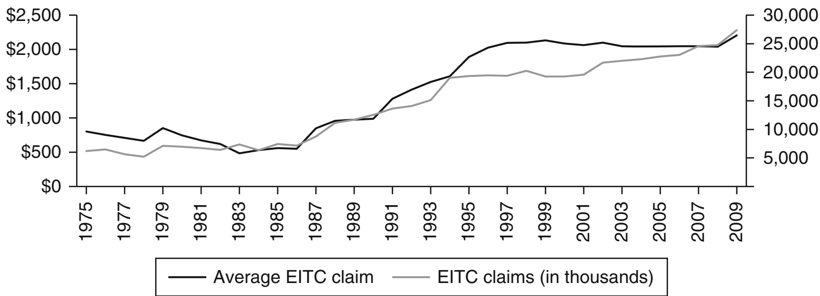

Figure 11.1 Growth of the EITC: average claim amounts and number of claims.
Source: Tax Policy Center. Average EITC claim data is adjusted for inflation.

provided by the EITC to cover more workers and children. These changes in the EITC took the maximum credit from $400 to $5,600. The credit varies by the number of children and amount of earned income, where married families with three children earning between $20,000 and $30,000 receive the maximum credit value.

Figure 11.1 illustrates the growth in the number of EITC claims and the average amount claimed. In the 2011 tax season, almost 27 million households filed for the EITC, bringing more than $59 billion to families at tax time. The average value of the EITC in the 2011 tax season was $2,240 per household, but some families were eligible to receive the maximum benefit of $5,666 (Internal Revenue Service 2010).

As part of the American Recovery and Reinvestment Act (the "Stimulus Bill"), passed in 2009, both the EITC and Child Tax Credit (CTC) were made more generous for families claiming those benefits. A parent working full time at minimum wage with two children, for example, would see a boost of around $1,500 in her tax refund. These expansions were extended through 2017 by the American Taxpayer Relief Act of 2012. Households with children could also be eligible to receive an additional $1,000 per child through the CTC.

For many households, their tax refund may be the largest lump sum of cash they receive all year. Households view their tax refund in a unique way, often different than income from public benefits and employment. While many families use their tax refund to pay down debt or pay on utility bills, others want to save portions of it (Grinstein-Weiss 2012). This mind-set has made tax time an ideal moment for intervention and planning in saving and asset building.

While the importance of EITC at tax time cannot be understated, the delivery mechanism through the tax code is far from perfect, and this limits the credit's potential to boost savings consistently over time. Claiming the EITC is a complex process for many low-income families. The printed EITC instructions, for instance, consists of 68 pages detailing the multiple conditions that have to be met in order to receive the benefit, from what constitutes earned versus unearned income to who can be claimed as a qualifying child. Presumably, this complexity contributes to the fact that nearly one in every five eligible filers does not claim the credit (Holt 2011).

The EITC also presents a challenge for saving because families are rarely eligible to claim the credit every year. In fact, through 2009, 42 percent claimed the credit for only one year at a time, and only one in five claimed it for five or more consecutive years (Dowd and Horowitz 2011). The EITC is only available for families that have earned income, so Social Security, unemployment compensation, and disability payments do not count. In times of high unemployment, the EITC becomes less effective

for many families who do not possess earned income. Thus, long-term asset building that leverages the EITC can be challenging for families whose income changes from year to year.

Cash infusions from the EITC and total tax refund can be used in a variety of ways, such as meeting immediate needs, paying down debt, or making purchases that have been deferred over the course of the year in anticipation of receiving the refund. These uses have perhaps become more common in recent years as other forms of public assistance, such as Temporary Assistance for Needy Families (TANF, also known as cash assistance), have declined relative to the value of the EITC and other tax benefits. The growth in the value of the refund, however, and implementation of the split refund option, which allows filers to receive their refund in up to three accounts as opposed to just one lump sum payment, have created opportunities for families to pursue provided a broader set of objectives, including saving and asset building.

The Rise of Community Tax Programs

Claiming the EITC can be difficult. Consequently, most EITC filers seek assistance when preparing their return. For-profit preparers largely serve this market, processing over 70 percent of all EITC returns at average costs of $250 to the customers, which can deplete around 10 percent of the value of the average EITC amount (Wu and Fox 2012; Berube et al. 2002). Not only does this cost function as an access fee for families who have earned benefits, it also acts as a public subsidy to the paid tax preparation industry.

Since before the creation of the EITC, community groups prepared taxes for low-income families and seniors for low or no cost. These tax clinics, referred to generally as community tax programs, were typically products of individual initiative, often run by an individual at a college or religious institution. Over time, several legislative changes have increased demand for free tax preparation and provided funding for infrastructure. As a result, the localized approach that was common a few decades ago has expanded into a national network with a centralized organizational structure. One network is the National Community Tax Coalition, a nonprofit coalition of volunteer tax preparers and advocates who focus on leveraging free tax preparation for asset building. A second network is coordinated by the National Disability Institute, focusing on merging the importance of claiming public benefits and tax credits for disabled individuals.

The growth of VITA, the largest sector of the community tax preparation field, was fueled by legislation that increased both the supply and demand for these services. In 1969, with the passage of the Volunteer Income Tax Assistance Act, the IRS formalized free tax assistance and invested public resources in tax clinics. Shortly thereafter, in 1975, the EITC was created. While this and other benefits have increased the financial resources available to low-income families, the process of administering this benefit through the tax code, rather than through a traditional direct delivery system, effectively required that filers actively seek out assistance in order to receive these benefits. Consequently, the newly established VITA network became integrated into receipt and management of what would grow to become the largest antipoverty program for working families in the country.

Community groups that provide free tax preparation are diverse in size, mission, and services. Most groups are nonprofits that provide a range of services for low-income families and include free tax preparation from late January to April. The groups rely on volunteer preparers who are trained and certified through the IRS. Most free tax locations are part of a larger city- or county-wide coalition of sites that share marketing, client appointments, and volunteer recruitment. These groups typically offer services

in addition to tax preparation, including financial education classes, homeownership counseling, and public benefits enrollment.

Clients using these services are equally diverse. Demographic characteristics vary based on the location and region of the tax site. Most clients are women with children, and the majority has a high-school degree or GED with some college education (NCTC 2012). According to the National Community Tax Coalition (2012), in tax year 2011, the median adjusted gross income of filers was $15,000. Most filers (86 percent) claimed a federal refund, and the median refund amount was just over $1,000.

Community tax preparation coalitions and sites are funded through several mechanisms. Many began as existing nonprofits that provided direct services related to financial education, housing counseling, or community action. Funding traditionally came from community block grants, private and public foundations, and redefined TANF dollars. In 2008, the VITA program received specific federal funding for tax preparation from the IRS. Some 177 organizations received $11 million in funding for tax year 2011 (Internal Revenue Service 2010).

In 2004, community tax preparers and committed funders created the National Community Tax Coalition (NCTC) in order to significantly expand free tax preparation and asset building services to low- and moderate-income (LMI) workers. The community tax preparation field formalized membership, best practices, and advocacy through NCTC. Other national groups in this movement (including the National League of Cities, Wal-Mart Foundation, and Goodwill) have made it a priority to provide volunteers and resources to the field. VITA programs filed EITC returns for more than 700,000 families in 2011, netting more than $1 billion in total EITC dollars (National Community Tax Coalition 2011). Not all VITA clients are EITC filers, so the total number of returns filed by VITA programs is even larger, increasing from 674,000 in 2001 to more than 1.3 million in 2008 (Holt 2011). This means that the free tax preparation community now serves two percent of EITC recipients, which ultimately ranks them as the number three network of tax preparers in the country serving lower-income families, behind H&R Block and Jackson Hewitt (Dornbrook 2012; Greenblatt 2011). The gap between the VITA network and these commercial preparers remains large, however, and it is unlikely that the VITA sites can substantially increase their capacity without additional public resources or changes in policy, both of which may be necessary if the full potential of the tax-time moment as an asset-building opportunity is to be realized.

Integrating Tax Preparation with Other Financial Management Tools

In recent years, a more holistic set of financial management tools, including asset building opportunities, have been integrated into the services provided by free tax preparation site. NCTC developed a working group solely focused on asset-building curriculum and connections at tax time, which included financial education, opening bank accounts, and leveraging the split refund option on the tax form. In the mid-2000s, the Annie E. Casey Foundation led the charge for free tax coalitions to integrate strategies to help clients save portions of their tax refund. In recent years, a number of practices have spread among community tax programs that seek to use the tax-time moment to connect their clients with a range of other services designed to help them manage their personal finances more effectively.

Opening Accounts

Nationally, in 2011, approximately two-thirds of free tax clients were banked in some manner (NCTC 2012). This means they already owned savings or checking accounts and had a relationship with a financial institution. In some cities, the figure approached

90 percent of clients (Rothstein 2012). However, many of the clients could be considered underbanked because they used expensive alternative financial products even though they had checking accounts (FDIC 2012). Free tax coalitions responded by asking for increased partnerships with financial institutions. At the same time, financial institutions realized that there was a large market of unbanked and underbanked households with serious financial needs. Thus, in partnership with financial institutions, free tax sites began opening bank accounts.

Account opening at free tax sites varies by program and location. Usually a financial institution has a presence at a free tax site, perhaps sponsoring it, and opening basic or second chance checking for clients. The near instant opening of an account allows free tax clients to direct deposit their refund into the new account, saving time and money for the client.

Encouraging Saving and Refund Splitting

In addition to connecting clients with basic bank accounts to facilitate the receipt of their tax refunds and minimize costs, there has been an aggressive effort to help clients save a portion of their refund. Due to their skilled force of volunteers and direct engagement with low-income clients in the tax filing process, VITA sites have become an attractive platform from which to launch savings initiatives. Perhaps the largest success involved the ability to split a tax refund into three accounts, which VITA sites piloted and still utilize for asset-building programs (Beverly, Tufano, and Schneider 2006; Cramer 2005).

One new savings account pilot in Columbus, Ohio, focused on using refunds to create emergency savings accounts at tax time. In 2012, free tax clients were offered $150 in incentives and an end-of-the-year bonus for the purpose of opening an emergency savings account with some of their tax refund. This program provided incentives to deposit funds throughout the year and utilized a state program that provided a three percent interest bonus on the average daily balance after the twelfth month (table 11.1). The tiered approach was designed to encourage savings throughout the year by offering participants the opportunity to earn additional bonus for deposits made after the initial account opening. They were also given access to free budget counseling and a monthly email with tips and resources to save. Participants were able to withdraw money from the savings account at any time, since the goal was to create an emergency savings account. Of the 400 free tax clients who were offered the program, 78 entered the pilot. Of those who chose not to open the account, most responded that they might have considered it if they could use an existing account or if it were already created before tax time (Rothstein 2012).

Table 11.1 Savings account pilot in Columbus, Ohio: sample year growth

Franklin County EITC Coalition (United Way of Central Ohio) SaveNOW Plus Account							
Initial savings deposit examples	*Enrollment bonus ($)*	*Additional deposits between February and June, 2012 ($)*	*Savings bonus ($)*	*Additional deposits between June and September 2012 ($)*	*Savings bonus ($)*	*State of Ohio 3% bonus (12th month) ($)*	*Total balance ($)*
500	50	20	25	20	75	22.50	772.50

In addition to meeting the proximate objective of enhancing each client's financial well-being, saving initiatives have also been used as demonstration projects to establish proof of concept for a more universal policy. In 2009, for example, the Doorways to Dreams Fund launched a campaign to promote the purchase of a US Savings Bond at tax time. Utilizing the ability to split a refund, tax clients at certain free tax sites and H&R Block locations were able to use some of their refund to purchase a Bond. The success of the effort was sufficient to persuade the Treasury Department to reinstate the option to purchase a bond on the tax form itself. In 2011, only the second year in which it was offered on the form, around 45,000 returns purchased a Bond, generating $11 million in saving, most by low-income filers (Doorway to Dreams Fund 2011).

Similarly, in 2008, the City of New York launched a pilot through its VITA network to test the potential of a savings account offered at tax time with a direct match incentive. Unlike other initiatives, $aveNYC allowed participants to save for the short term in an unrestricted account, consistent with the stated needs of many low-income households. By the end of the third year, 2,200 people with very-low incomes had saved an average of $560 before the match, and evidence suggests that saving was becoming a habit: almost three quarters of participants continued making deposits one year after opening their account (Black and Cramer 2011; Ratcliffe et al. 2010). Three more cities, Newark, New Jersey, Tulsa, Oklahoma, and San Antonio, Texas, are currently replicating the program under the name Save USA with federal dollars. Senator Robert Menendez (D-NJ) introduced legislation to take this model to scale in a previous Congress and is expected to do so again.

Enrolling in Public Assistance Programs

Just as foundations, nonprofits, and communities invested in free tax preparation coalitions and services, there was a similar push in the latter half of the 2000s for combining free tax assistance with other public benefit enrollment programs. The overlap in client's eligible for both refundable tax credits and public assistance programs, as well as technological changes that allowed simultaneous evaluation of benefit eligibility, made integrating this process attractive for both clients and the organizations administering these programs.

The concept of these one-stop shops, embraced by both governments and funders, involved at least three main components. First, community groups needed to expand their impact and operations with limited resources. Enrolling families in multiple programs at one location made strategic sense, prompting funders to push this mission expansion. Second, 23 states and the District of Columbia enacted state EITC programs as a supplement to the federal program. Other states funded EITC and free tax preparation outreach, including large-claiming states like Michigan and Illinois. By allocating state and local resources, including regrants of TANF funds, there was an emphasis on developing more holistic direct services for economies of scale. Finally, practitioners in the field revealed that families were eligible but not receiving public benefits and/or free tax preparation. Specifically, because programs for supplemental food, free or reduced price school lunch, and utility assistance have similar income criteria as the EITC, families could access these benefits all at once.

Challenges to Continued Growth

As the network of VITA and free tax coalitions has grown, the focus of their work has evolved to include asset building and public benefits enrollment. Even as community

tax programs increasingly have recognized tax time as a moment to connect families to an array of other opportunities, a number of challenges remain that limit the effectiveness of the network. Some of these challenges relate to organizations' internal capacity to train volunteers or to identify appropriate programming to serve clients' needs, while others relate to policy impediments that can complicate tax filing for clients or restrict the funding needed to expand coverage or services. Competition from the expansive and well-funded paid preparer industry presents yet another challenge. This section discusses challenges community tax programs need to overcome in order to establish a sustainable set of practices that provide a diverse set of financial management tools for low-income clients.

Organizational Capacity

Ultimately, the success of a coalition depends upon leadership and training inside the coalition. Perhaps the largest challenge for growth and asset building is that the free tax field relies on volunteers for tax preparation and services. Some 88,000 volunteers were certified by the IRS in 2010, providing service at more than 12,000 sites around the country (National Community Tax Coalition 2011). Providing training, certification, and incentives to volunteers is a costly endeavor for most coalitions. It also leaves little time for adding financial education, budget counseling, and asset-building programs at tax time.

There are also structural issues in designing an asset-building program that involve financial institutions, technology, and economies of scale. Specifically, a financial institution may want to facilitate the opening of new bank accounts at a tax site, but may find that it is not cost effective to design a new product for only 200 participants. There are also challenges in prearranging bank accounts for clients stemming from privacy issues.

VITA sites can also struggle to find a delivery model that provides the financial services that their clients seek. One-stop shops often sound like the silver bullet for reducing poverty and helping families claim assets. However, combining free tax preparation with public benefits enrollment proves to be a tricky puzzle. First, due to the stigma still attached to public assistance, many clients who visit a free tax-preparation site are not interested in claiming public benefits or report that they are not eligible. Some Benefit Bank sites, which provide eligibility screening for a range of public assistance programs, noted that they use free tax preparation to get clients in the door and then offer public benefits enrollment (Ohio Association of Foodbanks 2011). Second, the IRS voices concerns over volunteers who help clients with tax preparation but are not trained and certified through the VITA process. This debate about the credentials for preparing taxes versus enrolling people in public benefit programs has not helped to grow the field, but, rather, has divided efforts.

Third, many families are uncomfortable with a process that ties public benefits to their tax return. This is exacerbated by prevailing misconceptions around the impact of savings on eligibility for public assistance programs (Sprague and Black 2012). While tax refunds can exceed the asset threshold in some public assistance programs, these resources are often excluded from the calculation of benefits. Finally, many volunteers indicate that they are interested in preparing taxes but are not interested in doing benefits screening.

Funding and Service Constraints

The current federal funding that exists for VITA sites is insufficient to meet current costs or support expansion. For the 2011 tax season, 374 organizations made requests

Table 11.2 Funding of VITA sites through the community volunteer income tax assistance matching grant program, 2009–2011

Filing year	*Organizations requesting funds*	*Organizations receiving funds*	*Total funds requested ($)*	*Total funds allocated ($)*	*Average grant amount ($)*
2009	379	111	30 million	8 million	72,072
2010	260	147	30 million	8 million	54,421
2011	374	177	33 million	11 million	62,146

Source: IRS 2011.

for VITA grants, requesting more than $33 million in funds (table 11.2). Less than half of these organizations received grants, and only $11 million was allocated (IRS 2011). Additionally, the grant process requires a match from another funder—a barrier for new coalitions.

Other funding issues constrict free tax preparation operations and their expansion. First, many community tax preparation sites and coalitions are strapped for funding for basic operations. Free tax preparation is free for the clients but comes with a cost for the sites and organizations providing it. For example, marketing and outreach, key components of offering tax preparation services, are costly. The most common and effective method for advertising is word of mouth from family and friends currently using the service (Rothstein 2012). Additionally, many coalitions utilize ads on public transportation vehicles, free advertisements on the radio and television, and press conferences to market, but these efforts have difficulty competing with the robustly funded outreach of tax software and preparation companies. Second, asset-building programs that use an incentive, while effective, are difficult to bring to scale. Offering $100 or $200 per household creates funding challenges if the VITA population is 5,000 people, as in the Columbus pilot.

Second, funding for tax preparation is often restricted to preparation and not allowed to go toward additional services. Many grants, including the IRS VITA Grant and the regrant of TANF dollars at regional levels, place these types of restrictions or guidance on fund usage. While many groups would like to offer additional asset-building services, the costs of adding a new program element are prohibitive.

Although community tax programs are run by local coalitions, they work under the umbrella of the IRS Stakeholder Partnerships, Education and Communication (SPEC) team. This arrangement has some significant advantages, including free tax software and some technical assistance from the IRS. However, embedding social policy inside the IRS presents distinct challenges. The IRS is concerned first and foremost with accuracy and compliance; thus, there is little financial support for direct outreach to EITC and CTC eligible families. The SPEC division is responsible for the outreach and asset-building aspects of tax filing but for the last five years faced budget cuts and reductions in staff. Given the complexity of tax time, the lack of direct government outreach to clients regarding asset building opportunities is problematic.

Third, filers are often unaware of asset-building options at free tax sites until they arrive at the location. Marketing budgets for free tax coalitions are tight and year round advertising and outreach is often not possible. Even if there is an incentive or match, clients may be unable to process this information or plan during the tax preparation process. Many clients are thinking specifically about their taxes and not about their overall budget and financial situation. The additional time and steps to participate in

an asset building option are problematic. The ability to purchase Bonds at tax time showed the effectiveness of integrating asset building directly into the structure of the tax process, which helped mitigate this problem.

Competition from Commercial Tax Preparers

As coalitions grapple with balancing their budgets and determining which services to provide and the best way to deliver them, their efforts to promote sound financial management at tax time are undermined by the dominance of paid tax preparers in this market. In conjunction with the large increase in refundable credits like the EITC, the number of paid preparation stores spiked in the 1990s and into the 2000s. The business went to scale when paid preparers partnered with banks to sell refund anticipation loans (RALs, also known as "quickie loans" or "money now loans"). These loans advanced portions of or the entire refund to the filer after deducting a series of fees for the paid preparer and bank. During the height of RALs, more than 12.7 billion sold, netting more than $1 billion in fees (Wu and Fox 2011). Businesses lent the money because the IRS virtually guaranteed the refund by providing a free service known as the debt indicator. The debt indicator allowed preparers to see if the refund would be intercepted due to back taxes, late child support, or other factors. If the debt indicator did not indicate any problems with the refund, there was extremely low risk for the loan.

RALs came under serious scrutiny in the mid-2000s for being sold at triple digit interest rates. Ultimately, the fees were seen as exorbitant and unnecessary when IRS technology made e-filing and direct deposit widely available. The IRS, after a series of meetings with a stakeholder panel and careful review, terminated the debt indicator beginning in the 2011 tax season. RALs became less available as federal regulators clamped down on the safety and soundness of the product without use of the debt indicator (figure 11.2). Most banks have either voluntarily left or been regulated out of the RAL market.

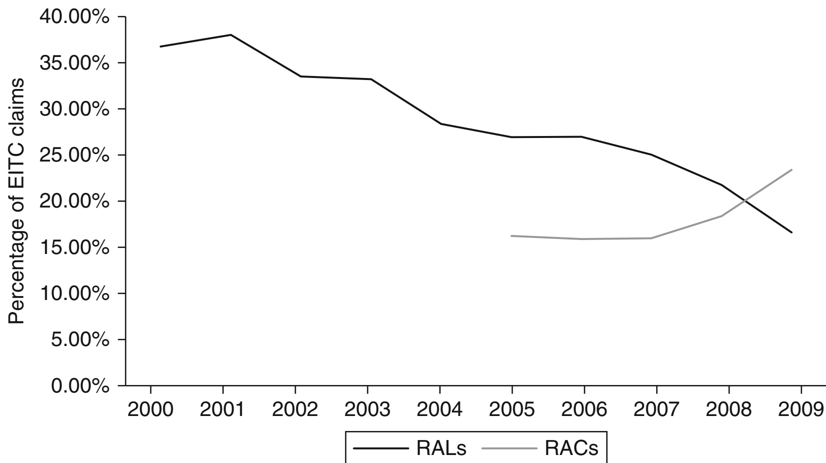

Figure 11.2 Refund products for EITC recipients.

Note: Tax Year 2009 data is from 80% of returns
Source: IRS SPEC Database

In the last several years, paid preparation chains have adjusted to the changes in the RAL market. These adjustments include issues of price, partnerships, and products. Jackson Hewitt, one of the nation's largest tax preparation chains, filed for bankruptcy in 2010 partly because of the lack of revenue from the RAL product. Other paid preparers raised the cost of preparing specific forms including the Schedule EIC. Filers who traditionally purchased RALs were routed to refund anticipation checks (RACs), a paper check that deducts the costs of preparation and arrives weeks later. As RALs have plummeted in volume, RACs have seen a steady increase (figure 11.2). Other paid preparers sell prepaid debit cards and charge for e-filing, administrative procedures, and audit protection. Prepaid debit cards tend to have few consumer protections and have a number of fees, including cash withdrawal, over-the-counter purchases, and balance inquiry fees. As with all banking products, the prepaid card market for refunds varies in quality.

Since the for-profit paid preparation market does the bulk of low-income and EITC returns, it is imperative to gauge their involvement in asset building. Unfortunately, much of the involvement of paid tax preparation involves the inverse of asset building, by way of charging fees or brokering loans that siphon parts of the tax refund.

Looking Forward

This section identifies specific ways to make tax time a more effective financial management moment for families. Tax time presents a unique opportunity for asset building, but LMI-income working families still face substantial barriers to saving. VITA and other free tax programs can be a powerful force in surmounting those barriers but will require significant reforms to increase both the capacity of these organizations to provide these services and demand for these services from clients. Below, a number of specific changes are described that would make service delivery more effective and increase the impact of asset-building programs and credits.

Tax Credit Policy Reform

As this chapter indicates, there are several changes in tax policy that would result in a more efficient delivery system and increase coverage to low-income households. Enhancing coverage would increase the opportunity to build assets at tax time and involve more households in the process. Restructuring savings credits would also incentivize saving for millions of working families.

Make Recent EITC and CTC Expansions Permanent

The value of the tax refund is nexus to which opportunities to leverage the tax-time moment are attached. For many low-income families, the refund is wholly or in part comprised of the EITC and the CTC. The expansions made in the American Recovery and Reinvestment Act and extended in the American Taxpayer Relief Act should be made permanent.

Increase EITC Benefit for Childless Workers

Since the value of the EITC is based on income and family composition, heavily favoring households with children, childless workers receive very little benefit (a maximum of $457). However, many childless workers support children through part-time custody, child-care payments, alimony, and other indirect arrangements that do not qualify

children as dependents on the tax return. Policymakers should double the childless worker portion of the EITC.

Replace the Saver's Credit

Most of the federal resources devoted to promoting saving and asset building are allocated through the tax code; however, few of these resources benefit low-income families (Cramer, Black, and King 2012). The Saver's Credit is the only incentive currently targeted toward LMI households; however, it is structured in such a way that most of these families would receive a modest benefit if any. It is nonrefundable, providing little benefit to LMI families already receiving a tax refund. Additionally, the Saver's Credit only covers retirement savings vehicles.

The Asset Building Program at the New America Foundation developed an idea called the Financial Security Credit, which would allow families to choose the savings vehicle that is most consistent with their needs (King 2012). That is, LMI working families could receive a refundable tax credit for saving for retirement, their children's college costs, or for emergencies. The credit could be claimed through a single line on federal tax forms.

Building a More Effective Tax Filing Infrastructure

As this chapter discusses, the tax filing process is an imperfect delivery system for social policy. It is crucial to improve access and precision for claiming tax credits and access to tax-time asset-building initiatives. This means rethinking outreach strategies, improving infrastructure, and protecting refunds for participating households.

Improve Delivery of the EITC and Tax Refunds for Low-income Families

Low-income families can experience significant fluctuations in their income and benefits. This volatility complicates their ability to manage their finances. Most recipients of the EITC receive this benefit for only a year or two before their incomes exceed the eligibility threshold (Dowd and Horowitz 2011). Having greater flexibility in how the credit is received so that it more closely coincides with the timing of expenses and coupling its receipt with access to a savings product could allow families to meet immediate needs as well as smooth consumption in the face of future changes in their income and expenses. This periodic payment structure could take a portion of the expected refund and divide it up quarterly for working families so that when tax time does come around, families will not be paying down as much debt and covering expenses so they will be more likely to save a portion of their refund (Holt 2008). Importantly, tax time would still provide the bulk of the EITC, which fosters asset-building at tax time.

Allow Families to Open Savings Accounts with Their Refund

Since filers already have the ability to split their tax refunds among different accounts using Form 8888, there should be an option to create a new savings account through the tax process. The Financial Security Credit shows the merit of this approach. The account could function like a prepaid debit card or default savings account with limited fees and easy accessibility. Converting the Savings Bond into a portable, more liquid savings product could also function as a tax-time savings account.

Continued Regulation of RALs and RACs

Policymakers should continue to regulate curtail RALs and RACs because they reduce the value of the EITC and limit the effectiveness of tax-time asset-building programs.

Developing low or no-cost options for not only receiving a refund but also paying a tax preparer through a refund are important projects. The Consumer Financial Protection Bureau could work with the private sector to create such a product given their mandate to work on tax time savings issues. Increased disclosure and transparency in the paid preparer sector would also help working families plan how to use and save portions of their refunds.

Expansion of Capacities

Free-tax preparation and tax-time asset-building services for low-income households are growing in size and scope but are nowhere near scale or covering the majority of eligible families. It is important to expand organizational capacity and the tools available to organizations so that more LMI families have access to free tax preparation and asset-building programs.

Increase Funding for Free Tax Preparation and Tax-time Asset-building Programs
Funding of operations for free tax clinics is a necessity to help families claim the EITC and secure their full return. VITA is underfunded, making it challenging to provide free tax services—let alone expand services into public benefits, banking, and savings policy. A conservative estimate of $35 million would provide base funding for at least 300 coalitions to continue to prepare taxes for free; however, asset-building programs would require additional financial support. This type of investment is necessary if free tax programs are the providers of current and piloted asset-building programs.

Facilitate More One-stop Shops
States and local governments should expand capacity for public benefits enrollment and tax compliance through one-stop shop approaches, which facilitate access to the full range of public benefits a family is eligible to receive. Direct service providers involved in public assistance programs should encourage clients to utilize all available public benefits and free tax preparation services. Many of these organizations could also serve as a free-tax center. One-stop shops, based in the heart of communities, are in the perfect position to implement asset-building programs including opening bank accounts, developing emergency savings accounts, benefits enrollment, opening Individual Development Accounts, and recruiting for foreclosure prevention and financial education classes.

Conclusion

The expansion of community tax preparers into broader set of financial services has provided clients with a greater set of tools with which to manage what can be the largest check they receive all year. Continuing to meet this need with in a shifting landscape of funding and mission will require changes along multiple fronts. The public policies that dictate the value of refunds and by extension the options for applying those resources in ways that best align with the needs of the families that are receiving them are in constant political battle. The trajectory of successes over the last several decades, however, has demonstrated the potential for this network to play a more comprehensive role in supporting the financial well-being of the clients they serve. Establishing a sustainable model for delivering those services will allow the tax-time moment to be a financial management moment for a greater number of families.

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Part III

Directions for the Future

Chapter Twelve

Foundations of an Asset-based Social Policy Agenda

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Income has historically been a standard measure of welfare because it serves as a proxy for consumption at a particular moment in time. Yet the factors that shape a person's economic well-being unfold over time, and may be better observed from a panoramic view rather than a simple snapshot. Beyond the consideration of a person's ability to produce income, their welfare is affected by the extent they are able to access other tangible resources that can make a difference in their lives and social development. These resources will vary in form and structure but, as a set, can be described as "assets." One of the central insights of Michael Sherraden's 1991 book, *Assets and the Poor*, is that the ability to accumulate assets—whether they are composed of human, social, or financial capital—is a key determinant of long-term social outcomes. In other words, assets matter.

Sherraden's aim was to offer a critique of the prevailing approach to mitigating the pernicious effects of poverty. Instead of a focus on income maintenance to facilitate immediate consumption, Sherraden envisioned an asset-based welfare policy that would integrate social policy and economic development. This approach, which considered the condition of poverty over an extended period of time, was additionally useful in considering how people build up and strategically deploy resources to move up the economic ladder. As the twenty-first century unfolds, it is clear that the path to future economic security will require access to both income and assets.

Sherraden's critique of existing welfare policy sparked interest in identifying policies and designing effective interventions that complement income maintenance by promoting saving, investment, and asset-building activities. Several policy ideas were initially articulated in *Assets and the Poor*. These included policies to promote matched savings accounts to facilitate asset purchases (called Individual Development Accounts) and programs to jumpstart the saving process by connecting children with accounts as early as birth (Sherraden 1991). In the intervening years, a fuller policy agenda has blossomed along with a community of practitioners, researchers, and policymakers who find value in using the "assets perspective" to inform how they think about social policy. This chapter presents a rationale for an expansion of asset-based social policy, identifies a set of informative policy guideposts that can shape effective policy formulation, and describes a specific set of policy proposals that have emerged as key components of an

asset-based policy agenda. A robust "assets agenda" does not displace social-insurance or safety-net programs, but instead offers ways to help more families build up their asset base on the path to economic success.

The Rationale for Asset-based Social Policy

The United States has been particularly effective at generating wealth for its middle class, and policies have repeatedly supported asset-building and wealth-creation activities. Previous efforts to democratize access to property, capital, and credit have had notable effects. Early large-scale initiatives, while highly flawed in their explicit exclusion of people of color, women, immigrants and other groups, were admittedly successful in creating economic opportunity for millions of Americans. Policies such as the Homestead Act, the GI Bill, and the establishment of the Federal Housing Administration historically benefited large numbers of families (Shanks 2005).

The role of public policy in encouraging asset building continues to this day; our prevailing policy framework identifies wealth creation as a central objective. Yet a persistent problem with our current policy paradigm is how many it excludes. Through targeted tax breaks and access to tax-preferred accounts, affluent families are given a full menu of choices to incentivize saving and ownership, while those with fewer resources are paradoxically offered fewer ways to build wealth. Tax expenditure programs in the form of deductions, credits, preferential rates, deferrals, or income exclusions are used to subsidize a broad range of asset-building activities. The value of these asset-oriented tax expenditures exceeds $500 billion in Fiscal Year 2013 (Cramer, Black, and King 2012). All told, the federal government offers over $199 billion in FY 2013 to support homeownership and over $165 billion to subsidize retirement savings, but 90 percent of these benefits go to households with incomes above $50,000 a year, roughly the top half of the income distribution (US Congress Joint Committee on Taxation 2012).

The cost of these asset policies has grown rapidly over the last ten years, reinforcing a pronounced shift toward social policy that distributes benefits through tax-preferred individual accounts while simultaneously creating new inequities. This is especially true in retirement policy, where there has been a transition from defined-benefit pensions to defined contribution 401(k)-style accounts. With half of America's workforce not employed by firms that offer these plans, millions of families do not benefit from these tax-based policies and are therefore not accumulating meaningful personal retirement savings (Cramer et al. 2009). This phenomenon is emblematic of an approach that has historically discouraged asset building among households with lower incomes. Not only are families with fewer resources less likely to own homes, have investments, or own retirement accounts that receive tax preferences, but also their limited tax liability diminishes any tax incentive that holding these assets may provide. While some tax expenditure programs may subsidize worthy activities and generate sizeable social and economic returns, they are not accessible to a large number of citizens that would benefit from them the most.

Families with lower incomes are often ill-served by the array of social safety net policies that focus on facilitating immediate consumption without paying attention to charting a path forward. Asset limits and other eligibility rules for public assistance programs reflect this phenomenon. The unintended consequence of this approach is that it creates a disincentive to engage in the types of activities that can help a family move up and out of poverty, namely, building up savings and a stock of assets

(Chen and Lerman 2005). This, in turn, contributes to pushing families outside the mainstream of financial services. Recent research estimates 28 percent of low-income families (with incomes under $15,000) do not have a basic bank account, and another 22 percent are classified by the FDIC as underbanked, since they regularly use more expensive alternative financial services in addition to their bank accounts (Burhouse and Osaki 2012). Without access to the basic tools of personal finance, these families are more likely to face additional barriers to saving and asset building because they pay more to manage their finances and increase their exposure to debt traps when they access short-term credit (Fergus, chapter 4, this volume). Being unbanked is not just an obstacle to financial security, but it can be a source of financial insecurity in its own right.

Expanding savings and asset ownership is especially consequential for families with lower incomes and limited resources. This is because assets can be held as savings or in other financial forms that can be readily converted to cash or tapped strategically for a variety of purposes. As such, assets are an essential component of a safety net that can stabilize a family experiencing an economic shock and a springboard that allows them to move up the economic ladder by taking advantage of opportunities as they arise. Households with higher incomes can more readily cover unexpected expenses and make investments as a matter of course. But for families with lower incomes, low savings makes long-term financial planning difficult and can compromise household stability (McKernan, Ratcliffe, and Vinopal 2009).

Recent research has confirmed the potential connections between savings and mobility, strengthening the case for asset-based welfare policies. One study from Pew's Economic Mobility Project looked at intergenerational mobility and found that children of low-income, but high-saving parents are more likely to experience upward mobility over time when compared to those with low-income, low-saving parents. Specifically, when looking at families with incomes in the bottom quartile, 71 percent of children with high-saving parents moved up from the bottom of the income ladder over a generation; in contrast, only 50 percent of children raised by low-saving parents moved up from the bottom a generation later (Cramer et al. 2009). Regardless of income, savings can provide a means to facilitate upward mobility and has the potential to exert impact across generations and over time.

Furthermore, the presence of savings on a family's balance sheet can reduce the need to borrow, either informally or from high-cost creditors, thus preserving long-term financial health. A growing body of research has also shown that asset ownership has behavioral effects that can change how people think about and plan for the future (Lerman and McKernan 2008). For all these reasons, expanding asset ownership, whether through savings that can be accessed in times of need or investment that can be deployed strategically, has the potential to meaningfully connect economic opportunity with economic security and ensure that every member of society is afforded a stake in the commonwealth.

The case for incorporating an inclusive asset-building approach has been strengthened by the experience of the Great Recession, which has made the distribution of wealth more unequal, especially when compared to income. For a number of years, median incomes have stagnated even as there were income gains at the very top, and this reconcentration of wealth is an emerging phenomenon. In 2010, the Federal Reserve reported that the top 10 percent of households had 45 percent of the nation's income but 77 percent of the nation's wealth, the highest concentration of wealth recorded since the early 1960s (Wolff 2012). Moreover, the median household net worth fell to

$97,000, a decline of 39 percent since 2007 (Bricker et al. 2012). In 2010, 43 percent of US households had less than $4,632 in assets, an amount that represents the amount of savings needed for a family of four to live at the federal poverty line for three months in the absence of income (CFED 2012).

The recession was severe, but the magnitude of its impact was not distributed equally. The median net worth of families in the top 10 percent rose by almost 2 percent. Those in the bottom quartile had the value of their assets drop to zero, and those in the next quartile had their net worth decline 43 percent from $56,800 to $32,200 (Bricker et al. 2012). These trends are even more pronounced for different racial and ethnic groups. For whites, median household wealth declined almost 36 percent between 2007 and 2010, but median wealth dropped almost 50 percent for African American households and 86 percent for Hispanic households (Wolff 2012). By 2010, African American and Latino households saw their median household wealth decline to $4,890 and $1,310 respectively, wiping out all of the wealth gains these groups had accumulated over the past 20 years (Wolff 2012).

The erosion of the gains made to the household balance sheet is one of the most debilitating aspects of the recent recession, stripping away assets and leaving many families cowering under an overhang of debt. A slow recovery characterized by wage stagnation and income volatility reflects the challenges of relying exclusively on a steady income as a foundation for financial security and economic opportunity. Assets can play a constructive role. If asset building is how individuals and families, develop, then a sensible public policy would promote asset building for all, because a more inclusive policy approach would have a greater payoff in social and economic development.

Policy Guideposts

To realize the promise of a prosperous society, all families should be afforded the opportunity to accumulate assets. A wide range of policy options can be pursued to support this goal. In developing an assets-based policy agenda, a set of policy guideposts can be used to inform the design and implementation of social policy efforts. These guideposts include employing a life course perspective that identifies key moments for policy intervention, recognizing the complexity of human behavior and decision making, and attending to the role of incentives, infrastructure, and institutions.

The Life Course Perspective

One of the primary contributions of the asset-building field to social policy has been the emphasis on an extended time horizon. Social development, economic security, and general welfare unfold over the life course. By its nature, asset building is a long-term process. It takes time to accumulate financial resources and to realize the social and economic benefits of asset holdings. Some benefits may compound within a person's lifetime, and some may be passed to family members and across generations. Regardless of whether the asset is a college degree, a home, or retirement savings, the impact of obtaining that asset can take years and even decades to have an effect. Measuring the discrete effects of owning a particular asset requires looking beyond when it was initially acquired.

A life-course perspective underscores the reality that people have multiple savings needs, which manifest at different moments in time or stages of life. This hierarchy

of motives for saving takes shape and evolves as a person ages (DeVaney, Anong, and Whirl 2007). A longer planning horizon can motivate people to save for retirement but does not eliminate the need to have resources available for intermediate and short-term needs as well. When households lack sufficient levels of savings that can be tapped without restrictions, they may be forced into costly economic choices. Households without flexible assets may forgo necessary purchases, borrow from their employer or social network, or take on a high-cost loan. Similarly, there is a different process required to build up savings to facilitate a home purchase than there is for retirement savings, reflecting the need to build up resources for different purposes simultaneously.

Children, young adults, workers in their prime earning years, and those nearing retirement all have different needs and abilities, which, in turn, are associated with various levels of asset accumulation. Younger couples and single workers have lower amounts of assets than near retirees or people in the prime of their working years. In this respect, it is useful to consider wealth building more holistically for each of these cohorts and recognize the distinct role assets play at different stages of life (Boshara 2010).

Furthermore, people's ability to acquire different types of assets changes over time (McKernan, Steuerle, and Lei 2010). With this perspective in mind, key moments for asset building can be identified when there is a greater motivation and potential to acquire, accumulate, and access a range of assets. These are often linked to major or transitional life events, such as the birth of a child, entering the workforce, or buying a home. There is value in designing policy mechanisms that work in tandem with the trajectory of the life course.

Behavioral Economics and Decision Making

For a policy to be effective, it should be responsive to how individuals act and behave in the world. Recent insights from the field of behavioral economics can help explain why many individuals fail to save or save enough, as well as ways to improve savings outcomes (Barr, Mullainathan, and Shafir 2008). Behavioral economics offers a contrast to the dominant, neo-classical economic model of saving, which presumes rational individual choice and complete information about markets, products, and possible outcomes. The behavioral model focuses instead on the complexity of how people act, manage their money, and make financial decisions.

Consumer preferences and demand inform behavior and help to explain the fate of many products offered in the financial services marketplace. These preferences are not set in stone, but can change over time. Yet in the world of personal finance, one of the most powerful forces appears to be consumer inertia. People often procrastinate. They may feel so overwhelmed by information and choice that they become paralyzed when it comes to making important financial decisions, which only exacerbates financial insecurity. Inaction is a popular option, regardless of the outcomes, which magnifies the impact of initial conditions and default settings. On the other side, there are constant temptations to spend and difficulties in exerting self-control (Thaler 1994). Taking these human biases and tendencies into account, behavioral economics suggests ways to improve the outcomes of saving. In particular, problems of inertia and self-control can be overcome by effective policy and program design that anticipates behavior and uses automation and defaults as ways to promote sound financial choices (Madrian and Shea 2001; Choi et al. 2004).

Because the circumstances of individuals vary significantly across the population, policies must allow and encourage responsible engagement. A proactive assets agenda

should identify ways to make saving and asset accumulation easy and automatic (like opt-in defaults for structured saving plans), while preserving free choice by allowing participants to opt out and implement choices that are more responsive to their unique circumstances.

Incentives and Institutions

People do not make decisions in a vacuum; they respond to conditions that are often shaped by institutions. This perspective is useful when thinking about the process of saving, because it focuses attention on a set of influential factors other than individual characteristics like preferences and income that determine savings outcomes (Beverly et al. 2008). These factors include incentives and disincentives for saving (e.g., rates of return, tax breaks, and asset limits in public assistance programs), facilitation (automatic enrollment and automatic deposits into savings), restrictions, and subsidies. While there is more work to be done in defining these factors and learning how they potentially interact with one another, this approach elevates the influential role institutions play in determining how people save and build assets over time. It also reflects how households with higher incomes and greater wealth interact with a more supportive set of institutional factors than their counterparts farther down the economic ladder.

Public policy plays a significant role in creating the institutional arrangements that individuals confront. Government has rules about how financial products are marketed and sold, how employers treat employees, and how economic benefits are distributed. Most directly, the government offers incentives to people who behave in a prescribed way, such as making contributions to a particular type of savings account. These incentives are inscribed in the law even as they vary in their effectiveness. One challenge for policy is to be explicit about goals and objectives; another challenge is to achieve these goals in a cost-effective manner so benefits encourage behavior that would not occur otherwise. Current policy designed to promote saving could be strengthened by limiting the benefits that go to people who would save otherwise and by reaching the people who would affirmatively respond to a saving incentive. Incentives must not only be accessible, but they also have to work for the target population. One type of incentive, say, a direct match to deposits, may work better than another, for example, lowering tax liability.

Incentives are often accessed through a larger infrastructure that is used to support the saving process. This is particularly evident in the ways in which people are connected to accounts and savings plans associated with retirement security. Even though 401(k) plans are provided by the private sector, they are supported by public policies. Tax benefits are given to employers that offer the plans, and there are rules that govern withdrawals and contributions. While participation is voluntary, the use of automatic transfers allows individuals to precommit, which facilitates greater savings over the long term. Structured savings plans, such as 401(k) plans in the private sector, 403(b) plans in the nonprofit sector, the Thrift Savings Plan for federal employees, and 529 College Savings Plans, represent an effective infrastructure, and support a goal toward greater saving and asset accumulation (Clancy, Orszag, and Sherraden 2004).

Although technological developments offer ways to create new infrastructure, policymakers should continue to explore how to revise the current ones that have already been built around payroll deductions, filing taxes, and receiving public benefits. Each of these processes is associated with a distinct infrastructure that is shaped by public policy, organized by a set of institutional arrangements, and can be reformed to be more supportive of the saving process.

Table 12.1 Foundational elements of a proactive assets agenda

- Ensure every child has a lifelong savings account.
- Get students saving for postsecondary education.
- Enroll every worker in a retirement savings plan.
- Create an incentive to support flexible savings.
- Connect tax refunds to the saving process.
- Abolish predatory lenders and high-cost, low-quality financial services.
- Revamp public assistance to be both a safety net and a springboard back to independence.
- Promote responsible homeownership.
- Encourage new entrepreneurs.

A Proactive Assets Agenda

The ideas and policy proposals presented here are designed to promote saving and the gradual accumulation of assets by a greater number of Americans, with particular attention given to policies that target families with lower incomes and fewer resources. A range of advocates and policymakers whose work has been informed by the assets perspective shaped and incubated the policy guideposts described above. The proposals presented below are not exhaustive, but reflect ideas that have received attention in the last ten years, and in many cases, have been subjected to experimentation in the field. The subsequent pilot and demonstration efforts have generated evidence that has been used to further refine the policy proposals.

The costs of implementing these proposals vary. There are opportunities to generate substantial benefits from a new allocation of public resources, but there are also gains to be had from revising rules, facilitating partnerships, and connecting people with supportive infrastructures. Individually, a case can be made for implementing each proposal on its own terms, but taken together they represent a proactive agenda to further democratize asset building and the future of economic success for Americans of all income levels. To ensure this future, we need to create a new policy framework that creates opportunities for everyone to participate in the saving and asset building process, not just those who have already accumulated wealth (table 12.1).

Ensure Every Child Has a Lifelong Savings Account

One approach to encourage saving is to get the process started as early in life as possible. Connecting children to accounts can expose them to the experience of saving, facilitate the delivery of basic financial education during the school years, and jumpstart saving habits (Cramer and Newville 2009). Current research and successful demonstration projects suggest that children's savings accounts increase a sense of financial inclusion; promote financial literacy and fiscal prudence; protect against economic shocks; improve access to education; improve health and education outcomes; and help develop a future orientation (Scanlon and Adams 2005). To ensure that this is a transformative policy intervention, accounts should be offered to every child and connected to an enduring saving infrastructure.

There are many ways to ensure that every child gets an account. The United Kingdom issued vouchers to every child born between 2003 and 2010, which could

be redeemed for Child Trust Funds at participating financial institutions. The City of San Francisco is opening accounts for every kindergartener who enters their public schools. Savings accounts could also be opened automatically whenever a Social Security card is issued after a birth, as in the SEED for Oklahoma Kids experiment (Nam et al. 2012). These accounts could be held in a centralized account system or rolled out to other financial providers. To maximize their impact, children's savings accounts could be supported with additional incentives or benefits, such as a match on annual contributions or a larger initial contribution, targeted to families with lower incomes.

The design choices for a specific policy or product will depend on policy goals, but restricted access to account resources until the account holder is ready can help ensure the funds support productive investments in children's futures like postsecondary education. The ASPIRE Act (America Saving for Personal Investment, Retirement, and Education) proposal, introduced previously with bipartisan support in Congress, offered $500 to every child, with an incentive structure to encourage families to contribute more. After-tax contributions would be limited to $2,000 per year, and earnings would grow tax free. Funds would be held in default investment plans, but accountholders would have the option to transfer the funds to other account providers. Eventually, funds could be used to pay for postsecondary education, buy a home, or to promote retirement security.

The privately funded SEED National Initiative was a multiyear effort to develop, test, and explore how to implement a more inclusive children's savings account policy. Operating in twelve sites across the United States, the demonstration provided highly valuable insights into policy design (Sherraden and Stevens 2010). For instance, providers found outreach and account opening to be quite challenging when account opening was not automatic. Furthermore, evidence suggests that saving outcomes are often driven by the institutional features of the program, such as the presence of an initial deposit or a savings match, the delivery of financial education, or the ability to minimize the steps required to make deposits. A well-designed and inclusive children's savings account policy can help level the playing field, create learning opportunities for children and parents, and provide a foundation for lifelong asset accumulation.

Get Students Saving for Postsecondary Education

Graduating from college is one of the primary ways to raise earnings potential and climb the economic ladder. While college enrollment has steadily increased, nearly half of high-school students do not go on to obtain a degree, and many of those that do are often trapped under a mountain of student loan debt. Helping students save for college ahead of time can decrease reliance on loans and minimize debts upon graduation. In addition, students who have savings for college are probably more likely to see themselves as college bound, and are therefore more likely to be engaged in school. Research has shown that savings and account ownership are connected to college readiness, access, and degree completion (Elliott et al. 2011).

Currently, 529 College Savings Plans offer tax breaks for postsecondary educational expenses, but opening these accounts is voluntary and most beneficiaries are from middle- and upper-income families. A concerted policy effort to make 529 plans more progressive and inclusive would allow all students to take advantage of this existing infrastructure and begin saving for their future. Most importantly, we

can begin by making sure every student has an account, at least by the time they enter high school if not earlier. Beyond account opening, families with lower incomes should face incentives like matched deposits to make savings contributions more attractive. A number of states have begun to implement progressive incentives to encourage greater participation in the 529 plans among lower income families, and there would likely be sizeable benefits in scaling up these efforts (Huelsman and Black 2012).

The federal government considered exploring this potential through a large-scale demonstration program organized by the Department of Education in its GEAR UP college readiness program. Although it was not ultimately implemented, the proposal would have provided a set of high school students with savings accounts, along with an array of supportive services designed to prepare them for postsecondary education. Their experiences would be compared to a control group to assess the impact of the accounts on educational performance, college access, and degree completion. The intent was to solidify the research foundation for this approach and generate insights into effective program design and implementation.

Other policies can help students save for their future. One promising idea is to link college savings with Pell grants, one of the largest sources of funds to help students pay for their education. Instead of applying for a Pell grant at the time of enrollment, students might apply as early as middle school and have the resources deposited into their savings accounts. These funds, restricted for postsecondary education, would give students a head start in planning and saving for college and might also reinforce the idea that students are college bound. Thus, the impact may be greater than the impact of receiving a Pell grant at the time of college enrollment (Elliott 2012).

Enroll Every Worker in a Retirement Savings Plans

Nearly a quarter of retired workers rely on Social Security benefits to supply at least 90 percent of their monthly household income, while another quarter of people depend on Social Security benefits for at least half of their income (Calabrese 2011). Social Security is certainly an asset, and needs to be strengthened, but for many it will not be enough to achieve economic security during the retirement years. Everyone will need access to supplemental resources.

As the burden of saving for retirement has shifted from employers to employees, half the workforce does not participate in a retirement savings plan. These workers miss out on the positive features of a supportive plan structure, which include low-cost administration, professional stewardship of resources, economies of scale, and direct deposits from payroll. Since access to a savings plan is a fundamental pillar of an inclusive savings infrastructure, everyone should be automatically enrolled as a matter of course in a retirement savings plan, with the option to leave if they choose. These plans could be offered by the private sector, but the public sector is accumulating experience in operating savings plans as well, such as through the federal government's Thrift Savings Plan.

Calabrese (2011) has proposed a Universal 401(k) system, which has a number of essential components that build on the insights of behavioral economics and the role of institutions. First, automatic payroll deduction can be used to make deposits to professionally managed accounts. Second, the plan should be portable so it does not depend on continuous employment with a single employer or whether the employer

offers a plan. A "clearinghouse" (modeled after the federal Thrift Savings Plan) could be set up to create "default" and "low-fee" accounts for workers with very low incomes who might initially have small account balances, or who were otherwise unable to navigate the process of setting up and managing a private account. Third, enrollment is automatic so workers do not have to overcome inertia on their own but instead can "opt out" if they choose. This "opt-out" approach was found to increase participation from 36 to 86 percent in one influential study of an employer-sponsored retirement plan and the increase was higher for lower-income workers (Madrian and Shea 2001). The system could also build on the "next generation" of 401(k) enrollment through "Auto Investment," which gives employees the ability to contribute to balanced, low-cost investment options, and "Auto Escalation," which allows workers to automatically increase the amount of money they contribute to their 401(k) plan, often in association with pay raises.

The Obama Administration has proposed creating "Automatic IRAs," which would require all firms with five or more employees to automatically enroll their employees in a retirement plan and use payroll deductions to make deposits on a regular basis (Calabrese 2011). Firms that set up such accounts would qualify for a small, one-time tax credit to offset their administrative costs. Employees would be enrolled at a default rate of 3 percent of compensation but would have the option to change their contribution levels. Yet this approach needs to be extended in order to cover all workers, including part-time employees, contingency workers, and the self-employed, to be truly effective at improving retirement security across the board.

Create an Incentive to Support Flexible Savings

Research has demonstrated that accumulation outcomes improve when the saving process is made easier and supported by incentives. Current policy has several features that make the saving process more difficult. First, incentives embedded in the tax code are confusing and tied to an array of tax-preferred accounts with different qualified uses, exemptions, and penalties. Second, these incentives are primarily accessible by families with higher incomes and greater wealth. Each year the federal government allocates hundreds of billions of dollars in tax expenditures to support savings, but 90 percent of these savings accrue to households with incomes over $50,000 (Cramer, Black, and King 2012). Those with lower incomes and less wealth are not offered the same array of incentives and yet may need the most assistance getting started on the path toward greater savings and financial security. Third, the incentives offered prioritize retirement security, but families have a wide range of saving needs. Having access to a pool of flexible savings that can be tapped in an emergency or when an opportunity arises can make a family more economically resilient and secure.

If the goal is to generate more household savings, then we need to create an incentive that supports flexible savings for families getting started on building up their asset base. One way to do this is for Congress to create a Saver's Bonus that provides a dollar-for-dollar match that rewards low- and moderate-income families who save in a variety of savings vehicles. For example, every dollar deposited in a designated savings product could be matched with an additional dollar from the federal government, up to a $500 annual maximum. Eligibility for the bonus could be tied to eligibility for existing tax credits, such as the Earned Income Tax Credit (EITC). A wide range of savings products could be eligible for such a bonus including retirement savings plans, college savings accounts, savings bonds, and short-term CDs. Households have saving needs other than

retirement, and a larger array of incentivized saving options should increase the likelihood that they will choose to save. In this respect, the Saver's Bonus could jumpstart saving by families not reached by current policy.

Improving saving incentives could be accomplished in the context of tax reform, which should prioritize simplification of the tax code and consolidation of existing tax-preferred accounts. This might entail creating one class of accounts that are only for retirement and another that can be used for multiple purposes, such as education, homeownership, or other life exigencies. However, revamping the tax code should not be done to reward asset shifting; rather, we should strive to create an accessible and inclusive saving policy that ensures that all Americans can participate in the saving process. This approach has congressional champions, like Senator Robert Menendez (D-NJ) and Rep. Jose Serrano (D-NY), who support creating a Financial Security Credit based on the Saver's Bonus concept that would allow families to decide which saving option would best help them meet their goals.

Connect Tax Refunds to the Saving Process

There are several unique aspects of tax-filing time that make it conducive to promoting the saving process. One is its ubiquity, since the vast majority of working Americans must file their federal income tax forms every year. Another is the extensive infrastructure that already supports the tax-filing process, which includes commercial paid preparers and a network of community organizations that help lower-income households obtain the benefits available to them (Rothstein and Black, chapter 11, this volume). Perhaps most significantly, for many particularly low-income families, tax time triggers the largest check that they receive all year.

The average tax refund in recent years has hovered around $3,000, and over 24 million recipients of the EITC received refunds as large as $5,600 (Internal Revenue Service 2012). This creates one of the best opportunities during the year to set aside a meaningful amount of savings. The impact of the tax-time moment could be magnified with the creation of an accessible saving incentive, but the tax-filing process itself could also be reformed to make it more conducive to saving. One major obstacle is that many families do not own accounts where they can deposit their refunds electronically. In response, the tax-filing process should be reworked to ensure that people without savings vehicles are able to open accounts through their federal income tax return. This will make it easier for people to begin the saving process and will facilitate the entry of new savers into the marketplace.

Families should also be able to choose the savings goal and product that best meet their needs, whether that is developing a personal safety net, investing in a college education for their children, or securing their own retirement. If it did not restrict participation to those with a pre-existing account, the tax-time moment would expand the opportunity to save to those with little or no saving experience, while enabling access to a range of products that can accommodate each family's unique circumstances and priorities.

This concept is being tested in four major American cities through a project called Save USA, which allows families to open accounts when they file their taxes and benefit from matched contributions to their deposits. Initially piloted by New York City, preliminary data from the program suggest that low- and moderate-income Americans respond favorably to the opportunity to save at tax time (New York City Department of Consumer Affairs 2010).

Abolish Predatory Lenders and High-cost, Low-quality Financial Services

In today's world, everyone needs to be able to manage their money electronically. A basic bank account is a necessity and everyone should own one. Yet huge segments of society have been forced into the arms of the fringe financial sector, which includes payday lenders and check cashers, who make money by stripping assets from families struggling to make ends meet. These predatory purveyors of financial products should be banished from the marketplace. The Consumer Financial Protection Bureau (CFPB), created by the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010, was supposed to regulate the financial services marketplace with the primary goal of preventing people from being tricked into products they do not need or understand. If it is successfully empowered to meet its objectives, it can reshape the financial services marketplace.

The CFPB should exert authority over the provision of a range of financial products that impact consumers. This means that the bureau should embrace a mission of overseeing regulated financial institutions, such as banks, as well as nonregulated businesses, such as payday lenders, debt collection agencies, and mortgage brokers. Extending engagement with the nonbank sector should be particularly impactful. This is because the proliferation of abusive and unregulated financial practices played a notorious role in creating the financial crisis and bringing on the Great Recession (Fergus, chapter 4, this volume). The CFPB's congressional mandate is to make sure that all types of consumers have access to financial products and services that are fair, transparent, and competitive. Specifically, the agency has been tasked with ensuring that consumers are protected from abusive and deceptive financial practices and are able to get information that is understandable and timely. There should no longer be a safe haven for firms hiding large fees deep within disclosure forms written in unintelligible legalese.

The new CFPB will have to set clear and high standards for financial products and services. The future financial services industry will benefit from having a level playing field, which includes a set of consumer protections based on principles of fairness and transparency. This means making sure basic bank accounts are protected by FDIC insurance and not loaded with fees. There is no shame in getting back to basics, where banking and financial services are treated more like public utilities and less like winner-take-all casinos.

The CFPB must assume its full set of statutory authorities and make sure that fair rules are applied to banks and non-banks alike. If it does so successfully, it can remake the financial services landscape by elevating the interests of consumers and restoring accountability to the marketplace. By ensuring that consumers are better matched with appropriate savings and credit products in a fair and transparent manner, the CFPB can help rebuild the foundation for the financial system by restoring the previously essential characteristics of integrity and trust.

Revamp Public Assistance to Be Both a Safety Net and a Springboard Back to Independence

The Great Recession reinforced the value of having a social safety net, but shed new light on areas for improvement. In theory, public assistance programs are supposed to catch families when they are in need and provide support to get them back on their feet. In reality, the network of programs is poorly coordinated, often providing meager support, and is less effective than it should be in supporting people as they seek to move back

toward independence. Public assistance should both mitigate immediate hardship and promote greater economic security and mobility over time.

First, program rules must be streamlined to make the public benefits system easier for families to navigate and for caseworkers to manage. Currently, the confusing array of eligibility rules and requirements creates unnecessary barriers for delivering assistance, undercutting the objectives of the programs. Since many families seek support from and are likely eligible for more than one program at a time, it would be most productive to implement a single point of entry for applying for assistance.

Second, eligibility rules must reflect the important role savings and assets play in helping families get off public assistance. Many states still employ rules that ask families to spend down all of their resources before they are able to receive assistance. Some of these asset limits were set decades ago, before welfare added work requirements and time limits, and were never raised with inflation. Instead of maintaining policies that discourage saving and financial planning, these rules should be eliminated or substantially reformed. Previously, the Obama Administration proposed raising asset limits to $10,000 for households across a wide range of safety net programs. With this change, these programs can remove the disincentive to saving that can make it harder for families to leave assistance (Sprague and Black 2012).

Third, everyone getting support should be connected to a bank account where they can manage their finances and build up resources to facilitate their move back to independence. Without a basic transaction account, families receiving assistance end up paying more for financial services and have fewer resources to draw upon in meeting their immediate needs. This is not only an inefficient use of public funds but also a barrier to the development of the types of sound personal finance practices that are connected to achieving financial security over time.

Finally, public assistance programs should more effectively promote saving and asset-building activities. For instance, all families receiving rental housing assistance should have an asset account where a portion of their rent paid to the housing authority can be diverted. Currently, as housing assistance recipients' earnings rise, so does their rent. This rent structure has the unintended consequence of decreasing work effort. An alternative approach used in the Department of Housing and Urban Development's (HUD) Family Self-Sufficiency Program allows recipients of housing assistance to divert rising rent payments into an escrow account when their incomes rise. This enables them to build up savings as their earnings increase, while simultaneously working toward educational or occupational goals that promote economic independence (Cramer and Lubell 2011). This program and its alternative rent rules can serve as a model for delivering rental housing assistance in a manner that promotes independence over the long haul.

Promote Responsible Homeownership

For many families, homeownership is a key long-term wealth-building strategy. Owning a home forces saving by paying down a mortgage and opens up opportunities to appreciation, leverage, and access of neighborhood amenities. However, homeownership is not for everybody and it also carries risks. The rising number of foreclosures and defaults brought on by the bursting of the housing bubble reflects the limits and challenges of homeownership as an asset-building strategy (Reid, chapter 6, this volume). Some families may prefer to avoid the risks of homeownership by remaining renters, but for many others homeownership is a financially secure choice.

In the years preceding the Great Recession, the rise of subprime mortgage credit became corrosive when brokers made money not by matching buyers with appropriate products but by selling higher-cost mortgages. These mortgages often had higher rates, prepayment penalties, and additional fees for payoff information, modification, or late payment. According to federal lawsuits filed in the years since the Great Recession, black and Latino borrowers were systematically targeted for these higher-cost products and subsequently experienced higher rates of foreclosure in the crisis. Failures of the mortgage system have turned the dream of homeownership into a reality of debt and default. Since home equity represents the largest share of household net worth, and is especially significant for those striving to be a part of an expanded middle class, policymakers need to pay more attention to mitigating the risks of homeownership and make sure it can be pursued responsibly by families.

Policies can help to ensure that families are connected to appropriate mortgage products in a fair and transparent manner. Predatory subprime mortgages were a virus that infected the entire economy, and there is a strong case that they should be banished from the marketplace. This can be done with more effective oversight and market regulation. For many families, the 30-year fixed mortgage can facilitate the transition to homeownership, especially if it is paired with an extended process of saving for a reasonable downpayment. More effective underwriting of mortgages and a reformed housing finance system can maintain homeownership opportunities even for families with lower incomes.

A key variable for maintaining homeownership opportunities, even for families with lower incomes, is the network of support organizations operating in the nonprofit sector. These groups have a growing track record of offering an array of services that help families buy and retain homes. These services include providing housing counseling, helping families save for a downpayment, connecting families to appropriate mortgage products, and negotiating mortgage modifications if necessary. Expanding the capacity of these organizations can help make homeownership work for a broader range of American families.

Encourage New Entrepreneurship

Entrepreneurs are vital to the American economy but are challenged to access capital and overcome a playing field tilting to the advantage of larger firms. Small business ownership and the opportunity to build business equity is a significant asset-building opportunity. For many, this process begins with a microenterprise, which can be a productive welfare-to-work strategy for some individuals receiving public assistance (Klein, Alisultanov, and Blair 2003). Federal sources of start-up funding have declined, making it more difficult to launch microenterprises. If the American dream of stable employment and creative business ventures is to flourish, federal policy should support new enterprises with small-dollar business grants and loans and a tax code that does not discourage self-employment.

Current loan programs administered by the Small Business Administration and the Treasury Department's Community Development Financial Institutions Fund have a track record of expanding access to credit. While these programs can promote microenterprise, their funding has been curtailed in recent years. Creating new pathways for start-up ventures to thrive will require expanding the availability of capital resources accessible to striving entrepreneurs. These entrepreneurs must be protected from unfair competition created when large firms monopolize the marketplace.

Tax reform should create incentives to promote more flexible saving, which in turn can become a source of funding microenterprise ventures. Policy should not only support restricted and long-term accounts but should also encourage people to save in accounts that are more accessible and liquid. Another approach would be to modify the rules governing IRAs. Current regulations allow IRA withdrawals to be used for homeownership and educational attainment; withdrawals used for start-up business expenses incur a penalty. Given that building a business can lead to increased financial security and a more secure retirement, tax rules should encourage small business capitalization as well. Entrepreneurs should also have the option to borrow against other assets. The Small Business Administration could underwrite these loans to make this type of lending more attractive to financial institutions. The underwriting process could evaluate business plans to discourage ill-conceived ventures from possibly depleting individuals' hard-earned savings but would open up a new source of accessible capital.

The Future of Success

The rise of an assets perspective has generated a series of insights that have shaped the way policymakers think about social policy. Foremost among these is the recognition that the process of saving and asset building is especially consequential. Initial skepticism of this approach was based on concern that families with low incomes cannot and will not save. A series of pilot and demonstration programs have provided evidence to the contrary (Schreiner and Sherraden 2006). These efforts affirm that people can save if they are given access to the right kinds of incentives, supportive saving infrastructure, and consumer protections, even if they start out with few economic resources at their disposal. The extent to which these insights lead to better outcomes depends on the design and implementation of a series of effective policy reforms.

Now is an opportune time to critically examine changes in the policy world and explore ways to more effectively incorporate the "assets perspective" into future policy efforts. The Great Recession and the painfully slow recovery offer a poignant backdrop for this inquiry. The Federal Reserve reported that the average family lost nearly 40 percent of their wealth as a result of the recession, and the racial wealth gap has markedly grown (Wolff 2012). But even when the economy returns to full employment, incomes are likely to remain volatile. If families are unable to repair the damage to their household balance sheets, the impacts of the recession will linger for years to come and remain a major threat to long-term financial security for families up and down the economic ladder. Increasing asset accumulation is the key to financial security for everyone, particularly those starting the climb. Right now, the existing suite of federal policies does not offer adequate or equal support to families with few economic resources. These households can potentially benefit from a set of policy reforms that help them save, avoid ruinous debt, and build up their asset base.

This is potentially a watershed moment for conceptualizing and implementing broader social policy reform. Now is a time for thinking about the skills, education, assets, and policies necessary to promote household mobility, economic security, and resiliency in the twenty-first century. As the economy continues to change and income volatility rises, the future of success will increasingly have an assets component. Unless we adopt a proactive assets agenda, it remains an open question whether or not opportunities to achieve financial security will be open to everyone, especially those among us with fewer resources to draw upon.

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Chapter Thirteen

Asset Building Research and Policy: Pathways, Progress, and Potential of a Social Innovation

Michael Sherraden

When one writes a book in social research and policy, it seems quite unlikely that anyone will recall the book two decades later, much less convene a conference to assess its impact and future potential. In this regard, I feel enormously fortunate and grateful.

What occurred following publication of *Assets and the Poor* is probably not much different from the experiences of others who set out in some direction and eventually "get somewhere" in the sciences, arts, business, sports, or other fields of endeavor. From the outside, it may appear that there is one catalyst that made it all happen or that progress was inevitable. But it is seldom that simple. Inevitably, many factors play a role. In the case of asset-based policy, I have benefited from major contributions and active collaborations with a group of people in the United States and abroad who have worked to explore the potential of a particular insight about resources and social development.

These colleagues have worked steadily toward countless small and large achievements, and they have carried on through rough patches, with their combined efforts eventually adding up to something meaningful. These seekers have enjoyed every kind of support, from institutions, organizations, and funders. Luck has also fallen their way. Their work has carved out a foothold for this policy idea. As the chapters in this book reflect, these diverse efforts have generated knowledge, practical evidence, and insights, which have amplified the relevance of the initial idea. Today there is a stronger foundation for thinking about how to design, implement, and assess social policy informed by an "assets" perspective.

In this chapter, I begin with an overview of the pathways the asset-building field has taken and its progress to date. This history of the field's development serves as both an acknowledgment of the contributions of a wide range of people and institutions, and also as a case study in how a social innovation moves forward in the broader policy context. I then consider a number of specific areas for further learning and their implications for policymaking. These include the experience of implementing and studying effects of Individual Development Accounts (IDAs) and Child Development Accounts (CDAs) in particular. This chapter extracts some lessons from the past and identifies potential directions for the future. Even as the assets framework has influenced a broad set of research and policy discussions, much work remains to be done.

Pathways Traveled

This body of work would not have happened at all without the engagement and ongoing partnership of several key colleagues. Bob Friedman, Ray Boshara, Melvin Oliver, and Tom Shapiro all made significant early contributions to the field. To greatly oversimplify the trajectory of this work, Friedman and Boshara introduced the idea of asset building into Washington, DC policy discussions in the early 1990s. Oliver and Shapiro's award-winning book *Black Wealth/White Wealth*, published in 1995, changed how social scientists, and the broader public, understood race and wealth inequality.

Other individuals played key early roles. Janet Topolsky wrote the first Washington publications while at the Corporation for Enterprise Development (now simply CFED); Will Marshall at the Democratic Leadership Council saw the potential of asset building to influence policy; William Raspberry, a respected opinion writer for the *Washington Post*, described for his readers the upside of helping people lower on the ladder move up by owning assets; and Jack Kemp, then secretary of Housing and Urban Development, promoted asset building within President George H. W. Bush's Administration.

In 1992 and 1993, soon after publication of *Assets and the Poor*, I was in Singapore with support from a Fulbright Research Fellowship studying the Central Provident Fund, a multifaceted social policy based on large-scale asset holding. I am indebted especially to the National University of Singapore and Sudha Nair for research partnership. Going forward, I suspect the United States and other countries will have something to learn from Singapore's example.

After returning to Washington University in St. Louis, I was appointed as founding director of the Center for Social Development (CSD) in 1994. Forming this Center was the idea of my dean, Shanti Kinduka. I had been reluctant to start, knowing that it would mean decades of work ahead, but the assets work was already becoming too large for me to address as an individual scholar. In the subsequent years, CSD has become a leading academic center in studying innovations in social policy, with asset building remaining the largest area of work.

The interaction between knowledge generation and policy discourse has been energetically dynamic, each informing the other. Even before we knew very much about how people would respond if given access to structures and incentives to accumulate assets, my proposal to create IDAs—inclusive and progressive matched savings accounts—was enacted by Congress in the Assets for Independence (AFI) Act of 1998. The original version of this legislation was introduced in 1991 when Ray Boshara was a staffer for Chairman Tony Hall in the House Select Committee on Hunger. As an extended demonstration project, AFI has provided approximately $25 million a year to support local organizations providing IDA accounts. Along with other field demonstrations and pilot efforts begun during the 1990s, IDA initiatives have generated data and experience that in turn has informed subsequent policy proposals.

Other major proposals emerged in addition to IDAs. During the late 1990s, working with Bob Friedman of CFED, I was a cofounder and cochair of the Growing Wealth Working Group (GWWG), a collection of academics and policy analysts examining a range of asset-based social policy options. The efforts of the GWWG directly informed a series of policy proposals put forth by President Clinton. Specifically, he proposed in his 1999 State of the Union address a system of matched savings accounts for the poor, called Universal Savings Accounts (USAs). I had proposed this name as part of GWWG discussions and I still think it is the best name for a universal savings policy. Additional consultation with the White House and Treasury Department led to a different proposal the following year for a multipurpose, progressively funded system of

Retirement Savings Accounts (RSAs), where contributions would be matched dollar-for-dollar by federal funds. In his 2000 State of the Union address, President Clinton characterized RSAs as a way to take the Individual Development Account concept to a new level. These proposals did not get enacted, but they reflected a high level of engagement among policymakers and a growing interest for exploring ways to leverage the asset building concept into large-scale policy.

In September 2000, CSD organized and hosted an academic meeting on "Inclusion in Asset Building: Research and Policy Symposium" at Washington University in St. Louis. In 2000 and 2001, matched savings were included in bipartisan Congressional proposals to develop individual accounts within the Social Security system. In October 2001, I testified before President George W. Bush's Commission to Strengthen Social Security, advocating inclusion and progressivity in individual accounts above and beyond social insurance (in other words an "add on" progressive account). CSD data on IDAs were quoted in both the 2012 *Economic Report of the President* and in the *Final Report* of the Commission, with progressivity included in some of the policy options. In 2005, Trina Williams Shanks and I took similar positions in testimony at a hearing on "Inclusion in Asset Building" before the Subcommittee on Social Security and Family Policy of the US Senate's Finance Committee. This policy event occurred in large part because of the work of Ray Boshara, then at the New America Foundation. During the 2008 presidential election campaigns, various forms of progressive savings policy were offered by leading candidates. All of these developments from the field of asset building reflect how the interactions between research, policy discussions, and political discourse have continued to evolve since the initial enactment of IDAs.

Across the Atlantic, US data from IDA research influenced Prime Minister Tony Blair in the United Kingdom to propose a vision for "assets for all" in the form of a Child Trust Fund, a universal and progressive account at birth. Gordon Brown, then chancellor of the Exchequer, made the decision to fund the Child Trust Fund beginning in 2005. Unfortunately, the 2008 financial crisis and subsequent global economic challenges coupled with changes in UK government in 2010 led to the demise of the Child Trust Fund and the Savings Gateway (a program similar to IDAs). These asset building policies fell victim to "austerity" and were put on hold.

In less developed countries around the world, other efforts have sought to incorporate the objectives of savings and asset building into microfinance activities. For example, YouthSave is a project designed to explore the potential of children's savings accounts in four developing countries—Colombia, Ghana, Kenya, and Nepal. Funded by the MasterCard Foundation, YouthSave is being implemented by a consortium of organizations, including CSD, Save the Children, the New America Foundation, and Consultative Group to Assist the Poorest (CGAP) of the World Bank, and is generating new insights into how youth throughout the developing world respond to new savings opportunities.

Bob Friedman, founder of CFED, deserves central recognition for "thinking up" large US policy demonstrations in asset building. Friedman conceived of the American Dream Demonstration (ADD) to test IDAs, as well as the Savings for Education, Entrepreneurship, and Downpayment (SEED) initiative to test Child Development Accounts (CDAs). While research results from ADD and SEED have greatly informed policy design in the United States and elsewhere, data are not the only—and perhaps not the most important—influence. These demonstrations have made asset-based policy "real" for the public, journalists, and policy makers, creating living examples of people building assets for their future. The influences of ADD and SEED continue. As this chapter goes to press, we are studying SEED experimental results at age four, especially

among the most disadvantaged families, and these results may have the potential to inform future policy.

Ray Boshara and Reid Cramer and their teams at the New America Foundation have been valuable partners in a number of projects, including SEED and YouthSave. They have been remarkably effective in taking insights from the field and incorporating them into policy proposals, providing leadership for an ongoing process of policy design and development that continues to garner the attention of policymakers in Washington, DC.

A number of colleagues at the Center for Social Development at Washington University in St. Louis have been instrumental in moving research projects and ideas forward. These contributors include Karen Edwards, Lissa Johnson, Margaret Clancy, Gena Gunn McClendon, and Li Zou. I am very gratified to say that each has achieved her own recognition, nationally and internationally, for distinctive contributions. I mention only brief highlights. Edwards is a national expert on Native American asset building initiatives as well as state-level asset-based policies. Johnson led development of Management Information System for Individual Development Accounts (MIS IDA), which made possible high-quality data on savings in IDAs in ADD and many other programs. MIS IDA holds the record as Washington University's most licensed technology product. Clancy is the leading national expert on progressive features of 529 college savings plans; she has informed progressive policy changes in many states and she also worked with the State of Oklahoma to implement the SEED OK experiment. McClendon has played an important role in state and regional asset-building efforts, with a lead role in the Southern coalition and CSD's work among Historical Black Colleges and Universities. Zou has extended CSD's international reach, particularly in East and Southeast Asia, including a Korean policy to create child accounts for all children in institutional settings. At the end of the day, these dedicated people, along with their counterparts in many other organizations, are the pathway and the potential of asset building innovation.

I want to acknowledge Mark Schreiner who has worked with CSD on so many projects. Schreiner has impeccable standards for clear thinking, quality data, and objective analysis and reporting. We have all learned from Schreiner, and he has improved our work.

Most of all I am indebted to Margaret Sherraden who does so much excellent work at CSD. Her major works include the major qualitative research on IDAs, *Striving to Save* (2010, with Amanda Moore McBride), and *Financial Capability and Asset Building* (2013, with Julie Birkenmaier and Jami Curley). When Margaret Sherraden, who happens to be my wife, publishes, she may be listed in the bibliography as "M. Sherraden" and some readers assume this is me, so I often get undeserved credit. Sometimes I confess in public that, without this confusion, my career would not have been nearly as successful. Audiences laugh uneasily at this for they know I am telling the truth. Everyone at CSD, and among our research colleagues, knows how well-informed, smart, constructive, and productive Margaret Sherraden always is.

American philanthropic institutions have played an instrumental role in making this work possible. I can say, without any qualification, that if the idea of inclusive asset building is ever to achieve a lasting contribution this will be because of American foundations. Only in the United States is there such strong support for testing social innovations. Foremost, I thank the Ford Foundation, where early vision from Susan Berresford and Melvin Oliver coupled with exceptional work by Frank DeGiovanni, Lisa Mensah, Kilolo Kijakazi, and others has supported and nurtured the asset-building field. The Charles Stewart Mott Foundation, where Jack Litzenberg awarded CSD its first grant funding, has been equally as supportive. Benita Melton of the Mott Foundation has also supported asset building thoughtfully and consistently, the F.B. Heron Foundation, especially when Sharon King served as the president, has given

us funds that have supported many productive asset-building innovations. While too numerous to mention by name, many other good colleagues at the Annie E. Casey Foundation, MasterCard Foundation, Lumina Foundation for Education, Levi Strauss Foundation, Citi Foundation, Wells Fargo Advisors, Atlantic Philanthropies, and other foundations have been invaluable and deeply appreciated partners.

I would also like to shine a light on doctoral graduates trained at CSD who are doing excellent work in this field. They have been an integral part of this process. They include Deborah Adams, Li-chen Cheng, Sandy Beverly, Ed Scanlon, Cindy Sanders, Min Zhan, Fred Ssewamala, Amanda Moore McBride, Trina Williams Shanks, Jami Curley, Michal Grinstein-Weiss, Chang-keun Han, William Elliott, Gina Chowa, Vernon Loke, Youngmi Kim, Kristen Wagner, and Jin Huang. Many of these scholars are now familiar names in this body of applied scholarship in the United States and abroad. Ford Foundation funding has supported their training and, consistent with Ford Foundation's goals, many of the CSD-trained PhD graduates—and graduates to come—are scholars of color. Although I did not anticipate it at the outset, the training of doctoral students turns out to be my most productive contribution to this body of applied scholarship, and also the most satisfying work in my career.

In asset building publications, I have greatly benefitted from writing and editing partnerships with Mark Schreiner and Signe-Mary McKernan in publishing *Can the Poor Save?* (2007) and *Assets and Low-income Families* (2008), the latter funded through a grant from the US Department of Health and Human Services.

Reid Cramer and his colleagues at the New America Foundation organized the Assets@21 conference, which generated this book, edited by Cramer and Trina Williams Shanks. Of course, I am also indebted to many scholars and social philosophers who have come before, and many applied scholars today, who have contributed immeasurably to this body of work.

Assets and the Poor may have spurred this discussion, but this body of work is now broad and multifaceted. Reviewing developments over these last two decades clearly demonstrates that the process of moving an idea and social innovation forward involves a wide array of people and organizations playing distinct and constructive roles. As a result of this work and collaboration, asset building and asset-based policy is now thought of as its own "field" of research and policy. Time and continued research will determine if the ideas in *Assets and the Poor* ultimately have merit as the basis for social policy. If this should occur, then many people may someday live with greater security and greater capacity to reach their potential. For an applied scholar, this would be the highest reward possible.

The Context and Future of Asset Building

In the following section, I attempt to lay the groundwork for the future of the field of asset building by drawing on research conducted at CSD and elsewhere. While it is impossible to know the exact course of the field, sketching out a vision of how the field might progress will help readers identify areas of possible collaboration. These thoughts and observations will be presented succinctly, a necessary hazard of summarizing over 20 years of work into a few pages.

Income Support Policies and the Industrial Era

Most social policies oriented toward the poor have focused on income support. These policies arose during the twentieth century to support households in an emerging

system of industrial production. Many of these policies have been successful in important respects. Indeed, the twentieth century creation of the "welfare state" is one of the great achievements of modern civilization, with its focus on easing uncertainty and hardship across lifetimes and across generations.

But nothing stays the same. Today we find ourselves in a transition to information-age technology, a postindustrial society, and a more global economy. Long-term economic trends toward greater labor competition, downward pressure on earnings, and growing financial returns to capital compared to labor have all led to rising income and wealth inequality in most countries. These conditions seem unlikely to reverse themselves in the foreseeable future.

Social policies that were designed for the industrial era are no longer a perfect fit with current conditions. We live in a period of strain and searching in both private markets and public policies. Opinions about what should happen next are sharply divided. Although usually interpreted in the political terms of Left and Right, the underlying conditions are being played out on the historical and technological stage, which does not always align with past political assumptions about how the world works. In the midst of such transformation, it is challenging to see where we are headed and to devise an effective policy response.

Asset Inequality

In the United States, there is extreme and growing asset inequality by income and by race (Oliver and Shapiro 1995; Taylor, Fry, and Kochhar 2011). As Oliver and Shapiro (1995) have documented, these patterns have arisen neither randomly nor solely because of individuals' "choices" in the market. Historically, asset inequality has been brought about by officially or quasi-officially sanctioned institutions and policies. Oliver and Shapiro have effectively outlined how policies such as widespread land confiscation, slavery, Jim Crow laws, residential and mortgage discrimination, exclusion of black farmers from US Department of Agriculture programs, unequal educational opportunity, and legalized predatory lending. These and other institutional arrangements have generated wealth inequalities over a very long period of time (Oliver and Shapiro 1995). More recently, following the Great Recession, losses of home equity have disproportionately affected people of color, who were more likely to hold high-cost and toxic financial products. The racial wealth gap has significantly expanded so that the average family of color now owns a nickel for every dollar of net worth held by the average white family (Taylor, Fry, and Kochhar 2011).

Assets and Well-being

Although poverty is typically measured according to specific income thresholds, well-being is not determined solely by income. Accumulated savings and other assets also matter (Oliver and Shapiro 1995; Shapiro 2001; Sherraden 1991). While income supports consumption, assets can provide stability during income shortfalls and can be used for long-term investments in education, homes, business enterprise, or other purposes that support social development over time. There is also increasing evidence that asset holding, in addition to material benefits, may change outlooks, attitudes, and behaviors in positive ways. Research by William Elliott and Sandy Beverly (2011b) has found that having a savings account in a child's name, controlling for demographic factors

including even the amount of money in the savings account, is strongly associated with postsecondary educational success.

Dual Policy: Asset Building for the Nonpoor, but Not for the Poor

Policies oriented toward assets and savings emerged in the latter half of the twentieth century, but overwhelmingly served the top half of the income distribution. Federal structures to promote asset building took shape in the form of tax-advantaged saving plans and other tax benefits, including 401(k) retirement plans, 529 college savings plans, Health Savings Plans, and tax benefits for home owners. These policies amount to over $500 billion per year; they have grown rapidly and are enormously regressive (Sherraden 1991; Howard 1999; Cramer 2012).

Through these social policies, the federal government is in the business of generating asset inequality—a sad outcome of misguided governance. If the United States wishes to support retirement savings or homeownership for all Americans regardless of income, a progressive policy would allocate a greater share of this budget to the poor. A proportional policy would be to give everyone the same dollar amount. For example, an annual subsidy of $1,000 to every household to offset shelter costs might be more effective than the current mortgage interest deduction. The current system represents terrible housing policy, where most people receive nothing and a wealthy few receive subsidies on their second homes. Not only is such policy unfair, but it also promotes misallocation of capital to large and frequently underutilized houses. At least 90 percent of tax benefits for asset building—which are in every way public expenditures—goes to the top half of the income distribution, and more than 30 percent goes to the top 10 percent of earners. In other words, current asset-building policies overwhelming favor those who are already the wealthiest among us.

At the same time, most means-tested support policies for the poor, such as welfare cash transfers, apply an asset test to determine program eligibility. These rules create a disincentive for asset accumulation above very minimal levels. Thus, we have an inconsistent set of policies with a double standard: generous asset building incentives for those at the top and penalties for asset building among those at the bottom. Over the past two decades, thanks in part to the asset-building discussions represented in this book, penalties against accumulating assets while on public benefits have moderated somewhat. This is a major and little-discussed policy change with important implications, but there is still a very long way to go.

The Role of Research, or the Lack of It, in Policy Formation

Remarkably, Congress has passed highly regressive tax benefits that favor the wealthy into law without calling for rigorous research to determine whether these are effective public expenditures. However, when even targeted asset-building policies for the poor are proposed, the committee rooms of Congress and the hallways of think tanks ring with steadfast calls for rigorously researched evidence of the proposed policy's effectiveness. Discourse about the merits of asset-building initiatives for the poor adopts a questioning stance regarding the perceived cultural flaws, questionable morality, and profligate individual behaviors of lower-income Americans. In the arena of policy for the poor, asset-building strategies are often interpreted as a way to improve the poor, shape up "the savings habit," strengthen morals and outlooks, and increase "financial literacy."

Notably, most proponents of these improve-the-poor "theories" (more often, these are only unspecified assumptions) hold a 401(k) plan or its equivalent and do little or nothing to "behave" in creating their savings, which are automatic and heavily subsidized.

Assets and Behavioral Outcomes

It has never been my goal to "shape up" behaviors of the poor. The argument in *Assets and the Poor* is that asset holdings—not saving behavior—matters. This may seem a fine distinction to some readers, but it is fundamental, and I come back to this a little later.

Notwithstanding this point, it is nevertheless possible—indeed likely—that asset holding has positive psychological, social, and behavioral outcomes, as originally hypothesized in *Assets and the Poor*. As noted above, for example, there is growing evidence of positive associations between both financial and nonfinancial wealth and children's educational attainment and other developmental outcomes (Conley 2001; Elliott and Beverly 2011b; Lerman and McKernan 2008; Nam, Huang, and Sherraden 2008; Shanks et al. 2010), and that these effects operate at least in part through changes in expectations (Zhan and Sherraden 2003; Sherraden and McBride 2010; Kim et al. 2013; Loke et al. 2013).

What Policy Direction?

Social policy for the poor should be about more than maintenance and survival; it should also be about development. Accordingly, the main policy idea in *Assets and the Poor* is to offer an Individual Development Account to everyone beginning as early as birth. Money could accumulate in these accounts, through individual deposits supported with a progressive matching system, for which lower-income families would receive the greatest public support. The original proposal for Individual Development Accounts was for universal, progressive, and lifelong asset building, and I continue to see this as the right policy direction. The past 21 years have witnessed some progress in the United States, though we remain a very long way from these core policy principles: universal (everyone participates), progressive (greater public support for the poor), and lifelong (from birth through old age).

Testing an Innovation: IDAs

Policy Tool for Testing an Idea

At the outset, we needed a policy tool that could carry the asset building idea. In this regard, a major challenge with any innovation is to discern large, complex circumstances, and then make a simple, tangible proposal. IDAs emerged for this purpose, and have carried this weight. Fundamentally, IDAs are not the main point. IDAs represent one expression of an idea that is made real to be tested in the world. I emphasize this because IDAs have made a great deal of progress but should not be considered as an end in-and-of themselves. IDAs were designed to communicate the policy concept that the poor also deserve to have support with saving, and since they were not receiving subsidies through the tax system, they should be funded directly. In this form, the idea is testable, and IDAs have been in a demonstration mode for two decades, with many variations in the United States and other countries.

What have we learned in this process? In brief, (1) the poor can save when they have structures and incentives to do so; (2) saving is explained mostly by institutional

arrangements, as in a 401(k) plan; (3) individual behavior is not enough: there has to be a structured platform and plumbing; (4) it is much easier to build on an existing policy platform rather than try to create a new one (in retrospect, we were quite naïve not to see this at the outset); and (5) as theorized in *Assets and the Poor*, it is asset accumulation that matters most for outcomes in well-being. In sum, asset-based policy is not all about improving choices, behaviors, and other individual constructs. There is so much that could be discussed on each of these topics; allow me to make just a few observations.

Not Just Savings but also Well-being Outcomes

CSD proposed and designed the ADD experiment because we value research knowledge and were not aware of any other saving experiment that has tested not only for changes in net worth but also impacts on long-term well-being—in this case home owning and repair, educational attainment, and business ownership, all of which are goals of IDAs articulated in the ADD. ADD takes a rigorous look at whether people are better off because of IDAs.

In 401(k) research, for example, there has been no comparable experiment, randomly assigning participants to 401(k)s versus not, and no clear understanding of whether 401(k)s increase total savings, net worth, or much less well-being in retirement. Despite the lack of experimental evidence of impacts of 401(k)s, there is almost no academic or political discussion about eliminating them. We might reasonably ask if the evidence bar should be higher for 401(k)s. Why should policies that include the poor have to prove long-term well-being, yet policies for the nonpoor seem to have no such requirement?

Experimental Impacts of IDAs

IDAs were proposed as lifelong accounts, but they have been implemented as short-term savings targeted toward low-income adults. Research to date on IDAs assesses this short-term version. In the ADD experiment, there is a positive impact after four years of an IDA program on homeownership among initial renters when the experiment ended (Mills et al. 2008). Fortunately, we were able to follow up with members of both the treatment and control groups six years later. This is important, but long-term efficacy of impacts is a lot to expect. It is not uncommon to find that impacts of social and economic interventions deteriorate over time, after the treatment group no longer has the treatment.

In the follow-up period, both treatment and control groups continued to increase homeownership, even into the subprime crisis. At wave four (data collected in 2008–2009, ten years after the experiment began and six years after it ended), the IDA treatment group overall had increased homeownership by 148 percent, and the control group by 100 percent. The "difference-in-difference" between treatments and controls from wave one to wave four was 5.5 percentage points. However, statistically controlling for other factors, the control group had caught up with the treatment group in homeownership so that the difference, while positive, was no longer significant (Grinstein-Weiss et al. 2012). The same pattern occurred with the renters subsample (Grinstein-Weiss et al. 2013a). These findings may be understandable given that the IDA treatment had not existed for the past six years. There is also evidence that controls had positive housing assistance (in fact, 22 controls reported having an IDA, and others reported downpayment assistance); both groups had good quality mortgages at low interest rates. In other words, both groups show signs of IDA or other housing support, and both groups have done quite well, with no sign at wave four of losing their homes, despite the financial and economic crisis.

Moreover, in additional subgroup analysis, those with median sample income and higher (still a very low-income population) did experience a significantly positive impact of IDAs on homeownership rates and duration at year ten, even after six years with no IDA program in place. Perhaps this is a random result—we do not know—but increased homeownership was a hypothesis of the experiment, and positive results on homeownership impact among those who are poor but with high higher incomes raises a key question about who may benefit most from IDAs (Grinstein-Weiss et al. 2012). Nor can we speculate about impacts on homeownership had the IDA program continued across the full ten years or longer. This remains an important research and policy question (recall that IDAs were proposed as life-long accounts).

Turning to another ADD outcome at the wave four follow up, we find a positive impact on education, another major goal of IDAs. Although only 7.6 percent of the IDA treatment group indicated education as an IDA use, the overall pattern for enrolling in education is positive for the whole treatment group. Specifically, several subgroups revealed noteworthy patterns. Males were found to have positive impacts on enrollment, acquiring a degree or certificate, and increased educational level; all of these with meaningful effect sizes and significant differences (Grinstein-Weiss et al. 2013b). How might these results be interpreted? There is a disturbing current trend in the United States of low-income males declining in educational attainment compared to females. IDAs appear to have a meaningful educational impact with this subgroup even after the program has ended, and this is an important finding. Results overall suggest that educational use of IDAs may be a desirable policy strategy. Combined with the generally distressing news regarding student loans, this may suggest a potentially positive role of savings for educational financing.

ADD also finds positive impacts on home repair in the wave four follow up, with a greater reported home appreciation rate and less forgone repairs. Two of five measured impacts related to home repair yield significantly positive results that appear to be economically meaningful. It may be that the modest savings sums in IDAs had greater impact on home repair than on home purchase. In contrast, data from the wave four follow up found no significant results of IDAs for business ownership or retirement savings.

In sum, the rigorous follow-up results for IDAs, six years after the program ended, find positive impacts for two of the five uses of IDAs—home repair (appreciation and repairs) and education (among males)—along with suggestive results in regarding homeownership rate and duration (for those above median income). For a long-term follow-up, six years after the program ended, and data collected in the midst of the Great Recession, these results are noteworthy, if not impressive.

In another IDA experiment, *learn*$ave [sic] in Canada, IDAs were targeted toward education and enterprise. The final report (Leckie et al. 2010) finds positive impacts on budgeting and setting financial goals, self-reported savings behaviors, enhanced educational attitudes, higher educational enrollment, and microenterprise start-up (*learn*$ave was focused on educational enrollment and small business start-up). To our knowledge, ADD and *learn*$ave are the only two long-term experimental studies of saving policy on well-being. It is once again instructive that large saving policies such as 401(k)s and IRAs have never been through an experimental test of impacts on long-term well-being.

Limitations in the ADD Experiment

Overall, there seems to be a tendency to speak of experiments as an idealized "gold standard" rather than an actual research project in the world. Like every other research

project, the ADD experiment has some advantages and some limitations. Field research is always a bit messy and there is a tendency to sweep research method and data complexities under the rug. Interpreting the results of the ADD experiment presents a few challenges, which are good to acknowledge so that they might be avoided going forward. These challenges include the following.

Small Sample Size in ADD

The initial small sample size reduces power and makes it very challenging to find statistically significant differences, even when effects sizes are meaningful.

Sample Imbalance in ADD

Random assignment is not always perfect and controls in ADD appear to have been better off at baseline. While analyses can control for observed differences, there could still be unmeasured differences in level of economic functioning that we are unable to control for.

Multiple Uses of IDAs in ADD

The five possible uses of IDAs make it hard to find significant effects. For example, only 7.6 percent of treatments said they had an educational use for IDAs, but the experimental test is on the full population. There are potential statistical approaches for handing this, though none are very satisfying. For research purposes, it would be far better to test one thing at a time.

Measurement Error and Noise, Especially in Assets and Liabilities

This is common in survey research and has been well documented in ADD. We have undertaken tests to ascertain the effects of measurement error and report this (Schreiner and Sherraden, forthcoming). We also acknowledge that that there is no evidence that measurement error is not randomly distributed across treatments and controls. However, measurement error, even when random, has the effect of creating noise and damping effects that might exist.

Policy and Community Environment of Tulsa

We have evidence that controls had mortgages of the same quality (fixed rate, similar reasonable interest rate) as treatments, along with evidence of other homeownership programs in Tulsa. Thus, it seems that controls, even if they did not participate in homeownership programs at the focal agency, may have participated in other homeownership programs in Tulsa. If Tulsa is a special environment with rich homeownership services, then the larger policy question remains unanswered. If IDAs were to be offered where there was a more typical level of housing assistance, perhaps the follow-up impact of IDAs would be different. As it is, we do not know how Tulsa compares with other local contexts and this limits what we can say about housing impacts.

Multiple Research Studies and Methods

CSD proposed and designed the ADD experiment because we value experimental evidence as a rigorous scientific test. Additional research studies on ADD are also valuable. Each study has strengths and weaknesses. To take an example, there are validity challenges in survey research (respondents might not interpret questions the way they are intended), and these are greatly reduced in-depth interviewing.

In ADD, we also monitored all savings transactions for all participants. This very thorough data set shows that low-income people can save and has been perhaps the most influential of all evidence relating to IDAs. When we started IDAs, it was common to hear that poor people could not save, or even that saving would be harmful to them. The ADD saving research has done a great service in getting past these objections; we seldom hear them anymore. Another lesson is that simple data can be important. Sometimes the policy process does not require experiments. Detailed descriptive and relational data can be very helpful in documenting IDA savings amounts, as well as participant and program variables associated with savings and asset accumulation. More than financial incentives are at work in IDAs. Other program features include restrictions (mentioned above), information, facilitation (assistance or automatic features), expectations or targets (represented in ADD by the “match cap” or amount of money that can be matched each month), and so on. One important finding in ADD is that, controlling for many other individual and program variables, the match cap (expectation or target) has a much stronger influence on saving performance than the match rate (financial incentive). Overall, program variables together are more strongly associated with saving performance than are individual characteristics. This overall result holds promise for the potential role of well-designed policy to increase savings and asset accumulation (Schreiner and Sherraden 2007).

In-depth interviews have been another great source of knowledge in ADD. Qualitative research has illuminated how IDA participants think about saving and how this may affect their lives. To give an example: The research team found that people really do create different mental “buckets” to save for different purposes. This means that financial assets in the household are not perfectly fungible. People like the restrictions of IDAs to make longer-term saving possible. This has both theoretical and policy relevance (Sherraden et al. 2006). These interviews also shed light on the meaning and experience of being an IDA participant. Two-thirds of participants described the IDA program positively.

As an example, one participant said: “It gets you back on the track. You know, get you back going up the ladder. But saving is not easy and not everyone succeeds.” Another participant commented: “Because when you have only what you’re earning and there’s none left over (which I saw a lot in my life) to not even take ten dollars out, you’re looking at a very grim world. Because it spells no hope. And when you have no hope, you cannot move to the next phase of things, even if you want it” (Sherraden and McBride 2010).

Turning to other IDA research and homeownership, the publication *Evidence Matters*, published by the US Department of Housing and Urban Development (2012) features an article on “Individual Development Accounts: A Vehicle for Low-Income Asset Building and Home Ownership.” This article summarizes IDA and homeownership research and concludes: “Studies show that participants in Individual Development Accounts experience positive outcomes, such as accelerating the move to homeownership, obtaining safe mortgages, succeeding as home owners, and avoiding foreclosure.” In addition to the ADD demonstration research cited above, this chapter cites IDA research published by several other sources, including the Urban Institute (Rademacher et al. 2010) and an IDA program in Australia, called Saver Plus (Russell 2008).

Russell et al. (2012) provide updated results on Saver Plus, finding that 83 percent of participants reached their savings goal; the average amount saved among the whole group (including noncompleters) over ten months was $598 in Australian dollars; 87 percent of participants were still saving the same amount or more 12 months postcompletion; 70 percent had increased their savings and asset holding; and 85 percent felt they had

more control over their finances. In addition, 87 percent said they were better able to plan for the future; 79 percent better equipped to deal with unexpected expenses; and 84 percent better able to deal with financial problems. Turning to educational outcomes, 89 percent reported that the education product they were saving for had a positive effect on their own or their child's educational experience.

Considered as a whole, IDA research represents substantial knowledge building over a relatively short period of time. While it is always prudent to consider limitations, as I do, we can also say that this body of work has generated a number of useful insights, which already have informed policy discussions in the United States and abroad, and will very likely continue to do so. Especially noteworthy are insights on program structures including the potentially positive role of target savings amounts, restrictions on use of savings, and other factors beyond merely financial incentives. Based on these results, there is reason to believe that policy can be designed to promote saving and asset building across a wide range of households, including those with lower incomes and initially fewer resources.

Return to Original Concept: Child Development Accounts

In *Assets and the Poor*, IDAs were proposed as universal, progressive accounts beginning at birth. This may have been the first written proposal for an inclusive (universal and progressive) children's savings account. In 1991, at the request of HUD Secretary Jack Kemp and the Bush White House, I developed a proposal for all children in America to begin life with an account. Between 2000 and 2004, I worked with the UK government on the Child Trust Fund, a universal, progressive child development account. In 2003, I wrote an op-ed with Ray Boshara for the *New York Times* on universal CDAs. From 2000 onward, with CFED and other partners, CSD planned for a demonstration of CDAs, and designed research for a large CDA initiative known as SEED, funded by the Ford Foundation as well as the CS Mott Foundation, Lumina Foundation for Education, and others. Over the past several years, multiple bills for CDAs have been introduced in Congress, often with bipartisan support. From 2004 through the present, CSD has worked with other partners in implementing the SEED demonstration and research, including a major CDA experiment in Oklahoma—"SEED OK"—launched with Governor Brad Henry in June 2008.

Child Development Accounts are saving and asset building accounts, initiated by public policy. Ideally, CDAs are lifelong (from birth), universal (available to all), and progressive (providing greater subsidies to the poorest children). Some countries have initiated CDA policies. Singapore has the most extensive CDA policies, with initial deposits and matching deposits available to all children that now total more than USD 30,000. The UK Child Trust Fund, which operated from 2005 to 2010, was universal and progressive, with accounts at birth for all children and larger deposits for children in the poorest families. Other policy examples are in Korea and Canada (for a review of CDA policies, see Loke and Sherraden 2009). Interest in CDAs has also grown in the United States, as shown by legislative discussion of several bills at the federal level.

Although CDAs generate savings and asset accumulation, CDAs are not primarily about money. Asset accumulation in CDAs is viewed as a means to other ends, primarily child development and education, and other aspects of lifelong well-being.

Saving behavior matters for CDAs, but it is not the primary focus. Initial public deposits and saving subsidies are quite common in CDAs. By design, CDA policies can be very paternalistic, with automatic enrollment, restrictions on access to funds until a certain age, and restrictions on use of funds. This is the nature of most CDA policy, and by design, SEED OK, described in the following section, has similar paternalistic features.

Saving for Education, Entrepreneurship, and Downpayment

Following ADD, we were able to return to the original IDA concept of accounts at birth. SEED had many parts and many audiences. Much of the SEED experience is documented in *Lessons from SEED* (Sherraden and Stephens 2010). This publication offers a review of the effort to date and summarizes some of its key findings and policy implications. SEED is a policy, practice, research, and communication initiative designed to test the efficacy of and inform policy for a national system of savings and asset-building accounts for children and youth. The first phase of the demonstration was done through twelve community-based sites. These sites included over 1,170 children across a range of ages, from preschool through young adulthood. They offered a range of benchmarks and incentives, including initial deposits and a match for personal savings. As of 2007, participants had accumulated $1.8 million from all sources and on average each child had a total accumulation of a little more than $1,500 (Mason et al. 2009).

One community-based site in Michigan (known as "MI SEED") was set up as a quasi-experimental design with half of the selected Head Start centers serving as control sites and the others comprising the treatment group. Like all the community-based sites, recruiting was a challenge at the beginning, but eventually 495 accounts were opened. These accounts had a total accumulation ranging from $227 to $16,724, with an average of $1,483. Average quarterly net savings was $19, with 31 percent of accounts receiving additional deposits from participants (Loke, Clancy, and Zager 2009). It was not easy for these families of low-income preschoolers to save, and some did not completely understand 529 accounts as an investment platform, but many did see accounts as an opportunity for their children (Williams Shanks, Johnson, and Nicoll 2008).

SEED OK is also undertaking a true experiment, with random assignment in a statewide population. The purpose of SEED OK is to provide experimental evidence on the effects of a universal financial intervention in a newborn population. In this regard, the first description of SEED OK was titled *The Universal Model in SEED* (Sherraden and Clancy 2005). SEED OK aims at testing whether institutions for saving and asset accumulation can be extended successfully to the full population, in a progressive rather than regressive manner, potentially over a lifetime, and whether this eventually increases savings, asset accumulation, attitudes and behaviors of parents, and attitudes, behaviors, and achievements of children.

SEED OK selected a probability sample of infants born in Oklahoma in 2007. Three minority groups—African Americans, American Indians, and Hispanics—were oversampled (Marks, Rhodes, and Scheffler 2008). The primary caregivers (mostly mothers) of selected infants were invited by letter to participate in the SEED OK study. The invitation letter informed caregivers that their infants had a 50–50 chance of receiving an Oklahoma 529 account with a $1,000 initial deposit if they participated in the study. After the baseline telephone interview, SEED OK randomly assigned caregivers to the treatment group or control group both groups had over 1,300 participants. Outcomes are measured at later points in time, using Oklahoma 529 account data and data from follow-up survey interviews.

Design of SEED OK

I hope the reader will bear with me, because I need to go a bit "into the weeds" here. This discussion may seem "academic" or "wonkish," but the purpose is fundamentally important for the potential of an inclusive asset-based policy.

In SEED OK, the primary focus is on effectiveness of the SEED OK policy structure, including its entitlement and automatic (paternalistic) aspects. As noted above,

this is not primarily about improving individual behaviors. If shown to be effective, a policy structure of universal accounts at birth could become a public good, an institutional framework for asset accumulation, in the same way that highways are a public good for transportation, and a clean water supply is a public good for population health (Goldberg 2005).

The key policy questions for SEED OK are about creating and testing a universal and progressive system for asset building beginning at birth in a full population (in this case, the population of the State of Oklahoma). To be sure, measurement of the policy test is carried out at the individual level, but this does not mean that SEED OK is a narrow test of individual saving behavior. The whole policy structure, including automatic account opening, initial deposits, and matching deposits, is being tested.

The 529 accounts in the SEED OK experiment have different treatment conditions embedded, including automatic account opening, initial deposit, matching deposits for low-to-moderate income families, information, and certain restrictions on access and use. These policy features bundled together represent the overall policy test. In this regard, it is fundamental to note that any control child can have an Oklahoma 529 (or any other 529 account, or any other savings account), opened and deposits received in his or her name at any time, completely without restriction, but without the policy features of the SEED OK treatment condition—that is the essence of the experiment.

Individual savings performance is meaningful in SEED OK, but SEED OK aims to test the total impact of the policy. Researchers sometimes test impacts of savings plans and programs with broader measures than individual savings. Tests can include multiple measures of savings and assets, sometimes including saving subsidies (e.g., see Duflo et al. 2006). In a similar way, SEED OK is designed to test multiple outcomes, including account holding, participant 529 savings, total 529 assets accumulated, and later attitudinal and behavioral outcomes.

From the outset, the guiding vision and purpose of SEED OK has been to test the impacts of a universal and progressive CDA policy structure. Individual saving behavior alone can never result in universal and progressive asset accumulation—no one would believe this is remotely possible. Therefore, SEED OK, as a policy demonstration, does not focus on individual saving behavior alone, or even primarily. SEED OK tests universal (everyone participates) and progressive (greater subsidies for the poorest) asset-building policy. Therefore, the essential outcomes are the percentage of accounts held that serve as a measure of "universality" and the total assets accumulated in these accounts that are an indication of "progressivity."

Allow me to summarize the policy design, that is, the treatment condition being tested. SEED OK uses the Oklahoma College Savings Plan, or "OK 529," an existing state-sponsored 529 education savings program. A state-owned OK 529 account was automatically opened for every treatment child, unless caregivers declined this account. A $1,000 initial deposit was automatically deposited into each state-owned OK 529 account.

Caregivers in the treatment group were sent information about the OK 529 plan and encouraged to open their own (private, not state-owned) OK 529 account with the child as beneficiary. Caregivers who opened their own "participant-owned" account by April 15, 2009 received a $100 account-opening incentive, the minimum initial amount required to open an OK 529 account. For income-eligible caregivers in the treatment group, deposits into participant-owned OK 529 accounts earn matching deposits. Members of the control group did not receive any information from SEED OK about the OK 529 plan, were not eligible for the state-owned OK 529 account, and were not offered any SEED OK financial incentives. However, they could and can open their own OK 529 accounts, just as any nonstudy participant can.

In addition to these state-owned and participant-owned OK 529 accounts, SEED OK research also examines a third type of OK 529 account, those opened for SEED OK children by adults other than the study participant, such as grandparents, aunts and uncles, or friends. These other private accounts can be opened for both treatment and control group children. SEED OK does not provide any incentives or information specifically for owners of these other OK 529 accounts.

Outcomes of Interest

The key outcomes of interest for the impact assessment are as follows: (1) participation in the form of holding one or more 529 accounts for the intended beneficiary; (2) individual savings in 529 accounts for the intended beneficiary; (3) total assets in 529 accounts for the intended beneficiary; (4) factors associated with savings and asset accumulation; (5) other measures of household assets, liabilities, and net worth; (6) social, psychological, and behavioral changes of parents; and (7) eventual social, psychological, and behavioral changes of children.

As described in the first description of SEED OK titled *The Universal Model in SEED* (Sherraden and Clancy 2005), SEED OK aims at testing whether institutions for saving and asset accumulation can be extended to the full population, in a progressive rather than regressive manner, potentially over a lifetime, and whether this eventually increases savings; asset accumulation; attitudes and behaviors of parents; and attitudes, behaviors, and achievements of children.

Regarding the first outcome of interest—participation measured as account holding is a desirable policy goal and should be a measured impact. This is the test for universality. In well-being terms, there is evidence that account holding in a child's name, controlling even for amount of savings in that account and other observed variables, is associated with later college success (Elliott and Beverly 2011a, b).

Regarding outcome three, total assets accumulated is a desirable policy goal and should be measured as an impact. This is the main test of progressivity, and total assets matter. There is growing evidence that financial assets in a household, controlling for other observed variables, are strongly associated with educational performance (e.g., Conley 2001; Elliott and Beverly 2011b; Shanks et al. 2010).

Regarding outcome five, impacts on assets, liabilities, and net worth are weak hypotheses because the dollar value of the SEED OK intervention is small compared to the dollar values of many of these variables on average, and variance in assets and liabilities is large. Thus, differences between treatments and controls would be challenging to detect statistically. In addition, assets and liabilities measures are problematic in SEED OK, with range (instead of interval) variables used at baseline, a low response rate and high percentage of missing information in the supplementary mail survey on assets and liabilities at baseline, and inconsistent data collection methods between the baseline and wave two surveys. Unfortunately, for these reasons, it seems unlikely that analyzing the impact of SEED OK on household assets, liabilities, and net worth can be informative. We sincerely regret these conditions. However, at the same time, we caution against "hanging our hat" on outcomes derived from inadequate measurement.

Regarding outcomes six and seven—in our view the most important outcomes in SEED OK—will ultimately be the attitudes and behaviors of parents and children related to development and education, which we will learn more about as SEED OK continues. A mediating hypothesis is that total 529 assets accumulated will be positively related to these attitudes and behaviors.

Logic of Impact Assessment in SEED OK

SEED OK creates the essential experimental conditions for an impact assessment and policy test. Any control participant in SEED OK has the option to open and deposit into an OK 529 account. Thus, controls have the same access to 529s as treatments. What they do not have, by design, are the same subsidies and institutional assistance offered to treatment participants—because this is the policy test.

It is fundamental to note that the treatment following the baseline survey—automatic 529 account opening with deposit, unless rejected, plus matched savings—is not the same as holding a 529 account and having money in it at a later point in time. The latter are outcomes to be measured. As noted, some public policies are quite paternalistic and allow little individual choice—such as Social Security—yet we can and do measure later outcomes when these represent the policy goal.

This point can be illustrated concretely in SEED OK. Among the over 1,300 treatment participants, only one rejected the 529 account with the $1,000 deposit (our SEED OK partners in the Oklahoma Treasurer's office reported that this was due to religious beliefs forbidding earnings on capital). In the intent-to-treat (ITT) approach, this person remains in the treatment group for analysis. This case reflects that the offering of the automatically opened account is not equivalent to holding an account and having 529 assets later. Between the intended policy and its outcomes are implementation and several years of program operation.

Potential Fallacies in Logic for SEED OK Impact Analysis

In America, we, of course, tend to have a strong individualistic bias. This bias prevents some people from seeing effective policy structures that are all around them, some of which depend very little on individual behaviors. For example, some researchers may take the position that automatically opened accounts with initial deposit that remain in place over time cannot be part of the impact that is measured later. We do not agree with this position because (1) it confuses the intended treatment with conditions later; and/or (2) takes a mistaken position that participants must do something, that is, behave in some way, for later conditions to be counted as impacts. These assumptions are fallacies.

The fallacies can be illustrated by other examples. Think of two simultaneous experiments, both with the same goal of increasing the number of 529 accounts opened and the amount of assets accumulated. The intervention for Experiment A is information and education about 529 College Savings Plans, financial advising, and guidance in opening accounts. Let us call this the "financial education strategy." The intervention for Experiment B is simply to open a 529 account (which can be rejected) and make a deposit. Let us call this the "account strategy." For both Experiment A and Experiment B, the outcomes of interest are the same—number of 529 accounts held and assets accumulated in 529 accounts.

Treatment phases for both experiments are completed. Both experiments cost the same, $1,000 per participant, and the money for both interventions is "spent" at this phase. One year later, impact assessments are conducted to test for the intended impacts in each experiment separately. It is likely that the two strategies do not have identical impacts (indeed, it is likely that the account strategy in this example will be more effective). In this example, what could be the possible logic of counting the intended impacts of Experiment A, but not counting the intended impacts of Experiment B?

Rejecting the impacts of Experiment B would confuse the treatment with later conditions of participants. In an experiment, it does not matter if the content of an intervention is largely the same as the content of what is later measured as an impact. To take

other examples, an intervention could be to deliver knowledge, and the impact could be knowledge held later; or the intervention could be to deliver immunization for disease protection, and the impact could be disease protection later. There is nothing whatsoever incorrect about such experiments. If 529 accounts held and 529 assets accumulated at a later point in time are the policy goals in the SEED OK, then these are appropriately measured as impacts.

We can illustrate in another way that the impact data in SEED OK provide an empirical test of an intended policy. Compare to MI SEED (a different impact assessment in SEED), which was also intended as a universal 529 in a specific population, but without automatic account opening. MI SEED required "opting in" and the later account-holding rate in that program was 62 percent in the treatment group (Marks et al. 2009). In SEED OK, the automatic enrollment led to almost 100 percent later account holding. Thus, we can use the empirical impact data from both experiments to draw a conclusion that one approach does not lead to a fully inclusive policy, and the other one does. This has something in common with 401(k) experiments that find automatic account opening affects participation (Choi, Laibson, and Madrian 2004; Madrian and Shea 2001). Of course, this is a major policy point based on impact data—that is, the policy test is based on participants' actual outcomes.

Turning to the second potential fallacy in logic, that participants must do something ("behave") for later conditions to be counted as impacts, we can use the example of public health experiments that test for the impacts of fluoride in the water supply or universal immunizations at birth. Participants may do nothing at all, and may not even be aware, yet impacts would be assessed regarding their later health outcomes. Similarly, impacts should be assessed regarding the later wealth outcomes among participants in SEED OK. In this regard, it is "financial health" (in this case 529 accounts held and assets accumulated) that we are seeking to affect, and so should measure. To be sure, we should also measure the impact of SEED OK on participants' own 529 savings, but this is not the primary goal of the SEED OK study.

Longer term, because asset accumulation in CDAs is not viewed as an end itself, but as the means to lifelong well-being, it will also be important to measure a range of family and child development outcomes over time.

With all of the above in mind, what do we know about the impacts of SEED OK so far? Regarding account holding, SEED OK has created 100 percent participation, compared to less than 2 percent for the control group. Regarding savings by participants, SEED OK data show participant savings increasing by 16 percent for the treatment group and less than 2 percent of the control group, a highly significant difference. Regarding amounts of participant savings, the mean effect is $46 across the whole treatment group (significant) and several hundred dollars conditional on being a saver. Regarding total asset accumulation, the mean effect is over $1000 (highly significant and meaningful) (Nam et al. 2013).

We will also have data on changes in attitudes and behaviors. At wave two, when the children in SEED OK are four years old, we will test for evidence of impacts among the most disadvantaged parents on factors such as parental expectations for child's educational success, reported child's development, and other factors.

We are asking whether account holding and asset holding matters for well-being, not simply individual savings. In systematic qualitative analysis of in-depth interviews with SEED OK mothers, treatment respondents report being "excited" regarding the meaning of the account, and that the account helps to create educational opportunities for their child. Mothers say that they are grateful that people other than family members

"care about what happens to their kids" (Gray et al. 2012). At this writing, we also have presented preliminary results on positive impacts on child social-emotional development at age four (Huang et al. 2013), although more work lies ahead.

If positive effects of SEED OK continue to be documented, then the policy implications would be clear: The poorest children among us also should be included in public subsidies for asset building. This would be fairer than current asset-based policy and would represent a public investment in the development of children. As I wrote long ago in *Assets and the Poor*, the best applications of asset building will probably be with children—because the payoffs can be higher over a lifetime.

Conclusion

This work has come a long way. Much more could be said about the pathways and progress of the field, but this book covers many of the main themes and stories. I do not take the progress of asset-building research and policy for granted—people have worked very hard, none of it has happened by accident—nor do I assume that the next 21 years will be equally as productive as the first 21. Evidence seems promising, but this too could change. It is possible that this idea will run its course and return to a footnote—though this does not seem likely at the moment.

The title of the symposium where the chapters in this book were initially presented was Assets@21, suggesting that this body of work is now "grown up." In some respects, that is so. The idea of asset building as a policy strategy was an infant in 1991—nascent, wide-eyed, and awkward. However, now the idea has gone through its adolescence and is sitting at the table as a healthy young adult. Both policy experience and research results have nurtured this growth and asset building is "speaking up," no longer easy to ignore.

This substantial progress is due to the efforts of so many people, researchers and practitioners alike, who have added to the rich experience and knowledge regarding asset-based policies. While inclusive asset building—meaning universal and progressive policy—is today far from achieved, the basic idea is almost main stream in policy discussion. In research, theory and evidence are growing rapidly. It will be interesting to see how this body of work develops in the years ahead.

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Josh Wright is the executive director of ideas42. In addition to leading the organization, Josh focuses on projects in financial services, economic mobility, and education. Josh has extensive experience in the for-profit, nonprofit, and public sectors; industry experience in financial services, media and entertainment, housing, and youth development; and functional expertise in business strategy, new business development, and new venture creation. Immediately prior to joining ideas42, Josh headed up the Office of Financial Education and Financial Access at the US Department of the Treasury. At Treasury, he was a leading proponent of using behavioral insights in program constructions. This included using tax time for simplified choice options for savings (i.e., US Savings Bonds on the Tax Forms) and financial access account opening (i.e., MyAccountCard Pilot) as well as the use of prize competitions to spur behaviorally informed technology product development and local government innovation in financial access and education. Previously, Josh held positions at the Center for Community Change, Booz Allen Hamilton's Commercial Management Consulting business, and was a senior executive at Bertelsmann's Random House, Inc. In addition, Josh served for two terms as an elected city councilmember for the City of Takoma Park in Maryland. He holds a BA from Wesleyan University and an MBA from the Yale School of Management, with concentrations in business strategy and finance.

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