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ASSET BUILDING PROGRAM

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CALIFORNIA ASSET BUILDING POLICY OPTIONS:
Providing All Californians a Stake in the Economy and a Means to Get Ahead

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BACKGROUND

What are asset-building policies?
Asset building is about giving all Californians access to the government-sponsored financial tools and incentives that have created and sustained economic prosperity for higher-income families. Today, for example, the federal government spends over $300 billion per year to help individuals and families acquire assets through home mortgage deductions, tax incentives, business investments and retirement savings programs. There's only one problem with these effective policies--more than 90 percent of that money goes to households already making over $50,000 per year. The goal of asset building policies is to grow the middle class from the bottom up by extending similar opportunities for investments, housing purchases and higher education to lower-income individuals and families.

What is the "asset gap" in California?
The need to spur widespread asset ownership in California is immense. Some 7.8 million California households, or 29 percent, would only last three months at the *poverty* level if forced to deplete all of their assets. That's the fourth worst "asset poverty" rate in the nation, more than twice California's "official" poverty rate of 12 percent — and possibly more consequential. When families don't have enough assets, they may be one medical emergency or one layoff away from government dependence. They face great challenges to buy a home, send their kids to college, start a business, reduce or manage their debts, or make long-term investments. And pass on opportunities to future generations? Forget it. Just imagine any family trying to survive — let alone thrive — in today's economy without assets.

The potential of asset building:
While the need to broaden asset ownership is great, the promise is even greater. Those with assets not only have brighter economic prospects, they're better, happier and more productive citizens. This Jeffersonian insight is buttressed by recent research, which finds that when families — including very poor families — own assets (as distinct from income), they are more likely to stay married, work harder, enjoy better physical and mental health, make educational plans for their children, feel more confident about and in control of their futures, take better care of their property, and be involved in community and political affairs. Who doubts that California and the rest of the nation will be better off with more savers, investors and owners? We certainly can learn from history: Nearly one-quarter of U.S. adults today have a legacy of asset ownership directly traceable to the Homestead Act; in addition, the GI Bill — once dubbed "the magic carpet to the middle class" — has returned to the nation seven dollars for every one invested.

How can asset-building policies help all Californians?
Asset building policies provide a rare political opportunity for bipartisan cooperation to address stubborn poverty issues with initiatives that emphasize personal responsibility. Asset building includes a range of simple proposals that can have broad, deep and immediate impact with little cost; and others that, with a modest investment, would radically transform the long-term economic outlook for California's children from one of uncertainty and fear to sustained prosperity and growth. Some of these policies have been tested in California. More than 5,000 people of modest income are already saving in matched savings accounts. In Silicon Valley, 1,300 savers — with average median incomes of $24,000 — have saved over $1.5 million. More than 500 people have used their savings to buy homes, go back to school and start college funds for their children.

A MENU OF ASSET POLICY OPTIONS

The following are a sampling of additional asset-building policies, most of which are already occurring in other states or are being considered.

SUMMARY TABLE OF SAVINGS AND ASSET-BUILDING POLICY OPTIONS

PROPOSAL	Annual Estimated Cost	LEGISLATION NEEDED?
I. Build long-term assets for the 540,000 Californians born each year		
1) Create "California Kids" accounts	$160 million per year	Yes
2) Launch the "Cradle to College" Initiative	$178 million/yr to cover full-time fees at Community College	Yes
3) Match college savings of low-income families	$7.7 to $15 million	Yes
II. Build the savings and assets of California adults		
1) Create California Ownership Accounts	$439 million/yr	Yes
2) Incentivize first time home ownership	TBD	Yes
3) Launch California CARES (Creating Access to Retirement Security)	$13.5 million over first five years. Eventually self-sustaining	Yes
III. Leverage the federal Earned Income Tax Credit to help Californians save		
1) Initiate EITC awareness campaign	Approximately $1 million. Leverage private dollars and free PSAs	No
2) Create California EITC	$600 million	Yes
3) Link EITC Recipients to 529 savings plans	Administrative costs	No
4) Allow state income tax filers to split their refunds	Administrative costs	No
IV. Bring un-banked Californians into the financial mainstream		
1) Bring benefits recipient into the financial mainstream	Administrative costs	No
2) Bring immigrants into the financial mainstream	Administrative costs	Yes
V. Build the financial literacy of all Californians		
1) Allow financial literacy as work requirement for TANF recipients	Administrative costs	Yes
2) Launch financial literacy publicity campaign	Minimal cost incurred by private sector	No
3) Initiate "Bank at School" program	None; services donated and other costs incurred by private sector	No
VI. Adjust assets limits on public benefits programs		
1) Adjust TANF asset limits	Minimal in other states	Yes

SAVINGS AND ASSET-BUILDING POLICY OPTIONS EXPLAINED

I. Build Long-Term Assets for the 540,000 Californians Born Each Year

1) Create "California Kids" accounts

California could launch the CA Kids account program, providing a one-time, $300 deposit in an investment account at birth for the 540,000 children born in California each year. At just over $160 million a year, this relatively small investment—it's less than three-tenths of one percent of the state's $100 billion budget—would be transformative. These accounts embody expectations; they are hope in concrete form. And, as any financial educator will tell you, financial education is taken more seriously when people — including kids — have an account of their own to manage, with real money with which to make investment decisions. If we are witnessing the gradual rise of the "investor class" or ownership society, which most Americans view as a good thing, the sooner kids and adults become comfortable with private savings accounts, the better.

Assuming low-income families managed to save or leverage just $50 per month, this small investment would grow to nearly $19,000 when the child turns 18—enough to comfortably cover the first three years of tuition and fees at a public university in California. If the child does not use the account for college, it grows to $34,000 by age 30 and $185,000 by age 65. Besides post-secondary education and training, CA Kids funds could only be used for a down payment on a first home or rolled over into a retirement savings account. If the account is used any other way, the at-birth deposit must be returned to the state, along with penalties and taxes. The accounts also provide a perfect catalyst and centerpiece to build the financial literacy of all young Californians.

Alternatively, if this program is currently cost prohibitive, a stripped down version of CA Kids is possible. The state could help families open an investment account for every child without the initial $300 deposit. This would at least offer children and their families a platform for long-term savings. Further, the state could encourage tax filers to deposit tax windfalls from various tax credits—i.e., the Earned Income Tax Credit, the Child Tax Credit, etc.—into these accounts. The easier the state makes it for people to make deposits into their CA Kids accounts, the more likely it is that people will do so.

2) Establish the "Cradle to College" initiative

California could pursue an initiative similar to one under development in Kentucky by providing a college savings account for every child as part of the state's Scholarshare College Savings 529 program. The state government could fund each account with enough money for a child to attend a community or technical college in California, and parents could contribute additional funds. To withdraw the money, Kentucky will require one year of full-time military or community service. Incentives could also be included for those who stay in the state to pursue their careers, particularly those who pursue lower-paying, but "socially-beneficial" professions, such as teaching, law enforcement, social work and the military.[1] California could consider these types of programmatic features. If the government contribution would be available to students at all income levels planning to attend an in-state community college and available as a credit towards in-state university tuition for other students, a proposal such as this could cost California an estimated $178 million annually.

3) Match the college savings of low-income families.

Several states, including Colorado, Louisiana, Maine, Michigan, Minnesota and Rhode Island, provide matching funds as an incentive to encourage low- and moderate-income families to save for post-secondary education in 529 plans. All 50 states administer these plans which allow parents to set up low cost tax deferred accounts to begin saving for their children's college educations. Some states allocate user fees from out of state accountholders in 529s to fund a savings match for low- to moderate-income state-resident families, while others provide a savings match through state appropriations.[2] Similarly, California could opt to provide a 1-to-1 savings

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[1] In June 2004, Kentucky's State Treasurer and Secretary of State introduced the Cradle to College Commission to examine a similar proposal. Currently, the Commission, which is made up of government, business, academia, and social activism leaders, is refining the idea and identifying long-term financing options including integrating the initiative into the state's existing 529 program < http://www.cradletocollege.ky.gov/>.

[2] For instance, Rhode Island matches contributions up to $500 per year based on family size and income. A 2:1 match ($1,000 maximum per account) is offered to state-resident families with an adjusted gross income (AGI) at or below 200% of the poverty level. Families with an AGI between 201% and 300% of the poverty line are eligible for a 1:1 match ($500

match up to $500 annually for families earning 200% or less of the federal poverty. Such an initiative could cost the state between $7.7 million to $15 million.[3]

II. Build the Savings and Assets of California Adults

1) Create California ownership accounts.

Any Californian working hard but still earning below $30,000 per year should be offered dollar-for-dollar matching funds for savings that lead to a first home, post-secondary education or training, or retirement. We could call these "California Ownership Accounts." To make this simple, the state could deliver the matching funds through state tax returns for amounts saved in IRAs, Roth IRAs, or California's "529" college savings plan. With rising tuition and housing costs, and only 39 percent of California workers having an employer-sponsored retirement plan, California Ownership Accounts will reward hard work, thrift and saving, and give struggling but industrious California families a real shot at the American Dream. The estimated price tag of these accounts is $430 million a year.

2) Create a tax credit for first time California homebuyers.

California is presently a land of high home prices, rising rents, and the lowest homeownership rate in the country. If left unchecked and untreated, these trends will certainly jeopardize the state's fiscal, economic and social health for years to come. Only 19 percent of California families can afford the cost of a median-priced home, down 5 percent from a year ago. A median-priced home in California costs $465,540, requiring a minimum household income of $107,880 annually, according to September 2004 data.

A "California Homebuyers Tax Credit" would be available to qualifying households for the three years after purchasing their first home. This kind of temporary tax relief targets Californians who could raise the state's homeownership rate, that is, families that are capable of buying a home but deterred by the increased financial commitment in succeeding years. Or, alternatively, California could implement a state-wide "sweetener" to federally-sanctioned Individual Retirement Accounts (IRAs), which can be used for first-time homeownership. These accounts use federal tax incentives to encourage savings but are of little value to lower-income families that don't have a tax liability. The state could create a refundable tax credit, modeled on an extension of the federal Savers' Credit, which would go to qualified taxpayers who contribute to these accounts. Although this would cost money in the short run, benefits will eventually be realized through an expanded tax base.

3) Security for Seniors: California CARES (Creating Access to Retirement Security)

Only 39 percent of California workers participate in an employment-sponsored retirement plan. Social Security payments alone — which average $901 per month in California — will not sustain individuals in their retirement. Many companies do not offer retirement plans because they are too complex and costly.

To help companies overcome these barriers, the California CARES initiative would simply allow small businesses to participate in pooled accounts managed by the state's current retirement system. This would create portable 401(k)-style retirement accounts that California workers could take with them from job to job, without a creating a complex state bureaucracy or excessive cost for employers. Further, it would create an individual-based pension program to augment the current employer-based and the Social Security systems. Any worker who wanted to participate could elect to have tax-deferred contributions deducted directly from each paycheck. Employers could also choose to contribute to employee accounts independently, or match employee contributions.

California CARES is modeled on legislation currently being forwarded by lawmakers in the state of Washington. The measure has attracted both Republican and Democratic sponsorship when it has been introduced over the last several sessions. Washington State estimates that its start-up costs would be $13.5 million over five years, but that

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maximum per account). To be eligible for a match, the 529 savings plan must be opened when the child is 10 years of age or younger. Matches occur annually for up to five years.

[3] Information regarding the number of low-income participants in Scholarshare was not available. Therefore, this estimate assumes that one-fifth of the 154,176 Scholarshare accountholders have an income equal to 200% or less of the poverty level and contribute between $250-500 a year. If all participants saved $500 each annually, the state would incur a $15 million expense. If it is assumed that participants saved half that amount and receive $250 in matches, then the cost to the state drops to $7.7 million.

the program would eventually be self-sustaining. Pennsylvania is also in the process of developing a similar proposal.

III. Leverage the Federal Earned Income Tax Credit (EITC) to Help All Californians Build Assets

The federal EITC is available to full- or part-time workers in California whose household income is $35,458 or less, depending on family size. The maximum payment is $4,300 for a family with two or more children and income of less than $14,000. In 2004, 2.4 million California families and individuals claimed $4.2 billion in federal EITC benefits.

1) Launch an EITC awareness campaign
The IRS estimates that $1.3 billion—or $1,700 for every eligible California family—of potential EITC refunds went unclaimed by 750,000 Californians in 2004. This money, left in Washington, D.C., instead could be used by Californians to buy homes, go back to school, or spend as consumers. The number of Californians dependent on public services would also be reduced. Other states have launched effective EITC awareness campaigns to bring more of these dollars into their states that could serve as a model for California. For example, California could create an EITC awareness campaign similar to a successful initiative in Washington state. In 1999, after the IRS estimated that 40 percent of eligible Washingtonians were not applying, the state spent $316,000 to develop materials to raise awareness of the credit, conduct a media campaign and set up a hot line. Significant media time was donated, the toll-free number received 67,000 calls and the state spent less money on this awareness campaign each year. Five years later, an estimated 80 percent of eligible Washingtonians - thousands more families - are receiving the credit.

A similar campaign would, of course, cost more in California. But if every dollar the state invested brought almost $20 into the hands of California's working poor families - as it did in Washington - it would be worth it. The state can make a small, cost-effective investment that will yield significant returns for working poor Californians. Foundation funding could be sought to develop and pay for the campaign, which could heavily rely on free Public Service Announcements.

2) Create a California EITC
Fourteen states and the District of Columbia currently have a state EITC that works in concert with the federal EITC to bring more benefits to working families. California could create a state EITC and link its eligibility rules to the federal EITC for administrative ease. This tax credit should be refundable, since the state has a high personal income tax threshold. A California family of three with one full-time worker earning minimum wage would be raised out of poverty if they could receive both a state and federal EITC. For example, according to the California Budget Project, a state EITC equal to 15 percent of the federal credit could provide up to $583 more a year for a family with more than one child and up to $353 more a year for a family with one child. The California Budget Project estimates that a state EITC at 15 percent of the federal EITC would cost a little over $600 million a year.

3) Link EITC recipients to college savings options (529s)
A few states, including Maine and Rhode Island, recently launched efforts to increase the participation of low-income EITC recipients in their state's 529 matched savings plan. The initiative is virtually cost-free, as it relies on foundation-funded community tax coalitions to provide outreach to low-income individuals who receive the federal EITC. Further, for a minimal cost, information about enrolling in 529s could also be included in EITC promotional materials.

4) Allow California state income tax filers to split their refunds into "money to save" and "money to spend."
The tax system can be a gateway to the financial system and to building savings and assets. These cash infusions are often the best chance people have to save some money in any given year, particularly low-income working families receiving the EITC. People may spend rather than save their refunds because they do not have an easy way to convert a portion of their refunds into savings. To facilitate and incentivize the saving of tax refunds, California should allow refunds to be split among multiple accounts. Under this proposal, people could deposit their refund into IRAs, 529 college savings plans or a variety of other savings accounts. If it is easier for people to

save right on their tax forms, to split their refunds into "money to save" and "money to spend," people will save more, perhaps much more. Recent research finds that many Americans—including lower income ones—can and will save their refunds if offered appropriate incentives and a clear way to do so. The federal government has signaled their intention to implement this change to the tax filing process by the 2007 tax year; and California could enact a similar strategy to help its citizens save their state income tax refunds as well.

IV. Bring all Californians into the Financial Mainstream

At least 10 million U.S. families — most of them earning less than $25,000 per year — are “unbanked,” meaning they lack checking or savings accounts. An estimated 25 percent of California adults don’t have a checking account at a financial institution. These unbanked Californians pay more to check cashing outlets and others for basic financial services do not have a safe place to keep their money, and have few opportunities to build their credit or savings.

1) Bring benefit recipients into the financial mainstream
The state can leverage its delivery of benefits—CalWorks, unemployment, and child support—to help bring unbanked Californians into the financial mainstream. In California, 28 percent of adults don’t have a checking or savings account, according to the US Census. Nationally, the estimate is that 10 percent of all households don’t have accounts. In San Francisco, the Brookings Institution estimates that one in five San Francisco adults---and half of its Blacks and Latinos—don’t have accounts.

Legislators should consider introducing a measure to direct the state to begin sending benefits via direct deposit to benefit recipients’ bank accounts. Caseworkers could be trained to educate recipients about the benefits of bank account ownership and help them open a low or no cost account at a local financial institution. If people did not open an account on their own, the state could open a limited use bank account for them, which would be attached to their existing benefit cards. CalWorks is currently delivered using a benefit card. Unemployment and childcare are still delivered by paper check, but should be also delivered by benefit card.

2) Bring California immigrants into the financial mainstream
An estimated 50 percent of California immigrant Latinos may be “un-banked.” Two states, Illinois and Nevada, have recently taken legislative action to officially recognize the cards issued by foreign consulates and used by hundreds of thousands of immigrants for purposes of identification, to establish credit and to open bank accounts. The uses of these cards, such as the Mexican Matricula Consular Card, are allowable under the Patriot Act and other federal laws. State laws provide additional assurance to banks that these activities are legal, as there is significant confusion amongst banks about what they can and cannot do in this area. These laws will also make it easier for the states to buy securities based on mortgages purchased by recent immigrants who lack a Social Security Number but have an Individual Taxpayer ID Number.

V. Build the Financial Literacy of Californians

1) Allow financial education to fulfill TANF work requirement
Similar to other states, including Delaware and Illinois, California could allow financial literacy training to be included as an allowable work activity for CalWorks recipients. This could particularly benefit older teens receiving welfare that are transitioning into adulthood.

2) Launch financial literacy publicity campaign
Many states and localities have implemented financial literacy and savings campaigns targeted at youth and parents through the America Saves program. Local initiatives typically provide access to no-fee savings accounts, free workshops, one-on-one counseling, seminars with financial experts and wealth building clubs for residents. The America Saves campaign is managed by the Washington-based Consumer Federation of America Foundation (CFAF). Costs should remain low, given that volunteers would donate their time to provide most of the services. The state of Delaware, which is considering launching its own campaign, estimated that the cost would be about $250,000, which could be donated by the private sector.

3) Initiate a "Bank at School" program

Delaware has also developed a school curriculum, "Bank At School," that seeks to provide children with a fundamental understanding of money matters and personal financial responsibility by actually bringing a bank to school, setting up savings accounts, and giving them the opportunity to engage in basic banking activities. This model has been duplicated in other states, including Illinois and West Virginia. With most services donated, costs would be minimal and could be even lower if the program were conducted as an online class.

VI. Adjust Asset Limits in Public Benefits Programs

1) Adjust TANF asset limits.

Government assistance programs such as CalWorks employ an income and asset test to screen applicants for eligibility. California has set its CalWorks asset limit at $2,000, which means that applicants must have no more than $2,000 in countable assets to be eligible. While some assets—such as the family's home, their cars, and an Individual Development Account—are excluded from this $2,000 limit, any retirement savings in an IRA or 401(k), college savings in a 529, or EITC refunds that are not spent within two months can be counted.

At a minimum, California should reform its CalWorks asset limits to exclude all retirement and educational savings accounts, especially if new incentives for saving such as those described throughout this memo are adopted. In any case, asset limit reform will help California to avoid sending a mixed message of encouraging working families to save while penalizing them if they need temporary assistance. California can look to Ohio and Virginia—two states that have removed their TANF asset limits—for direction. This simplification may not only help these families achieve long-term self-sufficiency, but also reap administrative cost savings through a more streamlined eligibility process.

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