Policy Brief August 2011

Individual Development Accounts

What is an Individual Development Account?

Individual Development Accounts (IDAs) are matched savings accounts that enable low- to moderate-income individuals to save money and build financial assets for the specified purposes of purchasing a home, paying for postsecondary education expenses, or starting a small business. The match incentive is similar to that of an employer match for 40(k) contributions.

Asset building is an anti-poverty strategy that helps low-income people move toward greater self-sufficiency by accumulating savings and purchasing long-term assets. The theory behind this approach is that helping people purchase an asset, as opposed to simply increasing their income, provides stability that may allow them to escape the cycle of poverty permanently. Examples of long-term assets include a home, higher education and training, and a business. IDAs are considered asset building programs.

Who is Eligible for IDAs?

Many IDA programs are targeted towards individuals who are eligible for Temporary Assistance for Needy Families (TANF). Other programs set annual income thresholds between 150 and 200 percent of the Federal Poverty Guidelines (FPG) — between $33,525 and $44,700 for a family of four in 2011.

In order to qualify for Indiana's IDA program, participants must meet one or both of the following household income limitations:

- Participant is a qualifying individual that receives, or is a member of a household that receives, TANF under I.C. 12-14-2; or
- Is a member of a household with an annual household income that is less than 175 percent of the FPG.

In addition to the above mentioned income limitations, at the time of application, an IDA applicant must have earned income, be a resident of the State of Indiana, and must be able to save $35 per month.

Eligibility got IDAs in Indiana Based on Annual Household Income	
Family Size	**Annual Income Based on 175% of FPG in 2011**
1	$19,058
2	$25,743
3	$32,428
4	$39,113
5	$45,798
6	$52,483
7	$59,168
8	$65,853

Source: Indiana Housing and Community Development Authority, January 2011, www.in.gov/ihcda.

IDAs Match Rates and Uses

Currently Indiana's IDA program offers a minimum 3:1 match, which means for every dollar saved, IDA participants will receive at least a three dollar match on their deposit—up to $900 a year. However, state statute allows accounts to be matched up to 6:1, if additional funds are available. If an IDA participant successfully saves the required $400 a year, then the State will match it with $1,200, totaling a combined savings of $1,600. IDA guidelines require deposits come from earned income, and participants may deposit money from income tax refunds. Participants may **not** deposit money from TANF cash assistance. Finally, participants have an option of four savings plans: weekly; bi-weekly; monthly; or quarterly deposits in order to develop routine savings habits.

IDAs in Indiana can be used to purchase a home, pay for postsecondary education expenses, or start or expand a small business. Additionally, Indiana's IDA program is distinct from some in that it allows savings to be used for owner-occupied rehabilitation. This includes improvements to the participants home such as; energy efficient windows, siding roofing, water heater replacement, heating and cooling. It does **not** allow for non-essential improvements.

All IDA participants must save for a minimum of six months before they may make their first withdrawal for a qualified asset purchase. The length of time an IDA participant may be considered active, and therefore eligible for match, varies greatly depending on the savings rate of the individual IDA participant. While most participants' tenure lasts four years, with recent passage of new legislation, participants may now opt to be active for the lesser of four years or until they reach the state program match cap ($4,800).[1] Thus, if funds are available, some IDA participants may graduate in as little as two years.

How are IDAs Funded?

Matching sources include federal grants, state and local governments, financial institutions, and private foundations, and tax credits. States can use a variety of funding sources to match IDA contributions including general fund appropriations, federal and state TANF dollars, and

Community Development Block Grants (CDBG) funds.

Assets for Independence (AFI) are a federal program administered by the Department of Health and Human Services (HHS), Administration for Children and Families (ACF), Office of Community Services (OCS). AFI provides grants to enable community-based non-profits and state, local, and tribal government agencies to support innovative asset building projects that feature matched savings through IDAs, financial education, and related services that improve the economic status of working individuals and families. AFI is one of the major federal funding sources that support IDA programs and awards about 60 AFI grants each year.[2] In Federal Fiscal Year (FFY) 2010[1], AFI was allocated $24 million.[3] Awards are up to $1,000,000 for five-year awards. The average AFI project grant is approximately $350,000 for the five-year grant period.[4] Applicants must secure non-federal funds in an amount equal to or greater than their AFI project grant.

Many states also invest state and other non-federal funds into their IDA programs. Pennsylvania's IDA program started in 1997 and Pennsylvania was one of two states that were "grandfathered" into the Federal Assets for Independence Act (AFIA) Policy Demonstration for IDAs without having to make a formal application. This was due to the fact that the state had already invested at least $1,000,000 of non-federal funds in IDAs.

The other state "grandfathered" into AFIA was Indiana. Indiana started its program using TANF and state funds. Currently the Indiana Housing and Community Development Authority (IHCDA) receives $1,000,000 in state funds (either from the general fund or the Indiana Housing Development Fund) from the Indiana General Assembly. These funds are used to administer the program and match IDA accounts. Additionally, IHCDA sells $200,000 in tax credits to businesses to help support the IDA program for $0.50 on the $1.00. If all tax credits are sold, this means an additional $400,000 in revenue will be generated that can be used for IDA program administration and match funds.

How Many People Participate in IDA Programs?

Since AFI began in 1999, nearly 81,000 individuals have opened IDAs and more than 24,000 participants have used their IDA savings and match funds for asset purchases.[5]

In Indiana, IDA participants used their funds as follows:

- 40 percent of participants advance training through education;
- 35 percent of participants realize the American dream of homeownership;
- 25 percent of participants use program for entrepreneurial efforts; and
- These asset purchases generate close to $500,000 in property and income taxes.

In State Fiscal Year (SFY) 2010[1], Indiana had 1,053 IDA accounts that were matched with state funds and a total of $456,174 was saved by IDA participants. It should also be noted that despite the downturn in the national and state economies, 94 percent of Indiana IDA participants fully

[1] Federal Fiscal Year runs from October 1st to September 30th. Indiana's State Fiscal Year runs from July 1st through June 30th.

met their savings requirement.

Additionally, since the program's inception, Hoosiers have saved over $2.7 million and 4,181 accounts have been opened.

Participant Savings in Indiana, SFYs 1997-2010

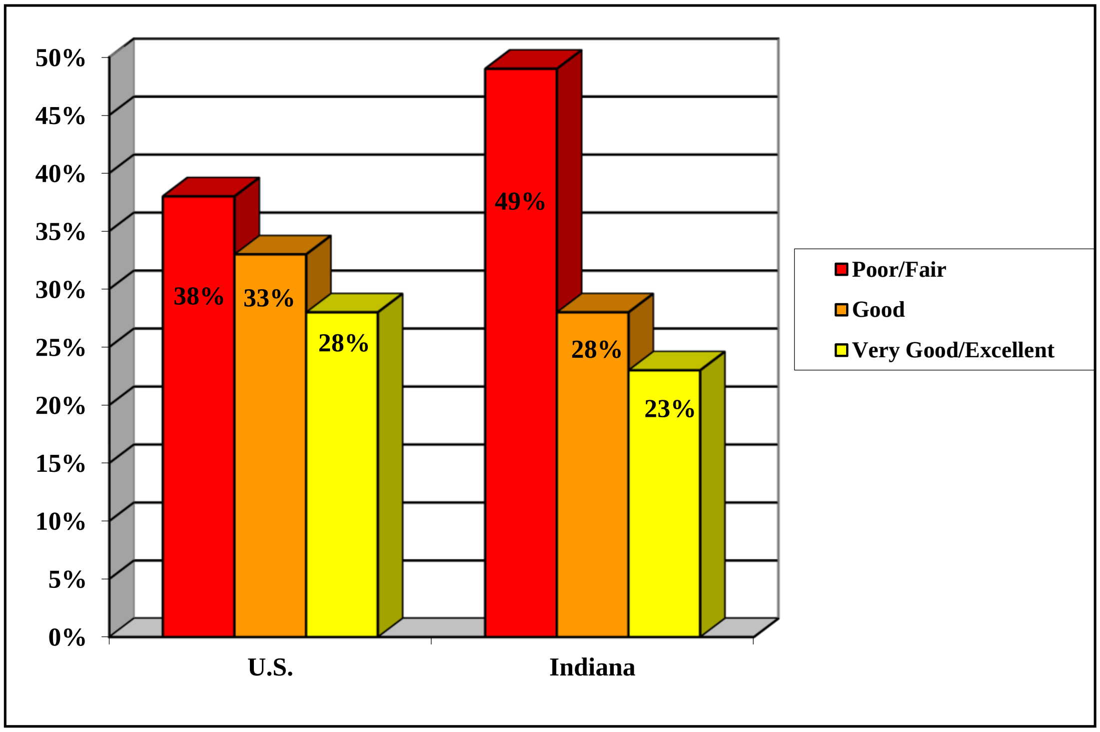
Year	Participant Savings	Accounts Matched	Avg. Savings	% Fully Saved
97-98	$65,926	351	$187.82	58.13%
98-99	$125,406	509	$246.38	47.90%
99-00	$234,983	978	$240.27	51.18%
00-01	$262,886	997	$263.68	43.32%
01-02	$166,495	606	$274.74	34.39%
02-03	$242,958	902	$269.35	48.23%
03-04	$261,386	1049	$249.18	59.42%
04-05	$270,543	1006	$268.93	65.98%
05-06	$274,080	973	$281.69	80.86%
06-07	$349,176	1198	$288.81	93.13%
07-08	$456,791	1128	$404.96	96.39%
08-09	$463,689	1101	$421.15	94.46%
09-10	$456,174	1053	$433.21	94.21%

Source: Indiana Housing and Community Development Authority, January 2011. www.in.gov/ihcda.

How do IDAs Benefit Indiana?

Lack of financial literacy may also play a factor in asset poverty. Asset poverty measures a family's financial vulnerability to economic shocks—if one's income was suddenly cut off due to unemployment, a medical emergency, or even divorce. According to a national survey conducted by the Networks for Financial Institute at Indiana University, approximately two thirds (61%) of adults in the United States understood financial literacy concepts including managing, spending, and saving money wisely. In Indiana, only half of survey respondents felt they understood financial literacy concepts. Additionally, the survey found that the financial areas U.S. adults feel they need the most help in are investing, retirement planning, and taxes.

Knowledge of Financial Literacy, U.S. and Indiana, 2007



Source: Networks Financial Institute. (2007). *What is the Foreclosure Rate so High in Indiana?* Retrieved Networks Financial Institute at Indiana State University web site: www.networksfinancialinstitute.org.

It is common practice for organizations providing IDAs to require financial literacy education, or case management, budget counseling, and homebuyer workshops. Due to the lack of financial literacy and its suggested relationship to economic behavior — especially among low-income families — as reported by the Federal Reserve in 2003, educational initiatives area critical component of the program.[6]

Indiana's IDA financial educational program is substantial and involves 12 hours of core financial literacy training, followed by asset-goal specific training for entrepreneurs, homeownership, and education. Basic financial training includes: setting and reaching financial goals; understanding credit scores; differentiating between needs and wants; knowing consumer rights; and and developing and maintaining a household budget. Homeownership counseling includes information on: knowing how much one can and can't afford; purchase and closing process; and maintenance basics. Small business training helps recipients to: develop target markets; write a business plan; develop a marketing plan; and learn about small business loans and other resources for entrepreneurs. Finally, education and career counseling training provides: counselors for career goals; help with searching and applying; information about grants and scholarships; and job training programs.[7]

How can the IDA Program be Strengthened?

There are several ways for Indiana to strengthen the IDA program that would expand allowable uses for IDA funds and allow more Hoosiers the opportunity to save and build assets.

1. **Indiana's Pilot IDA Program for Newly-Arrived Refugees**
   Indiana is sponsoring a pilot program in which newly-arrived refugees (less than three years) will be eligible to participate in the IDA program, allowing them to enter the state economy in order to: purchase a home; start a small business; pursue post/secondary education; or purchase a car for work and/or educational purposes. It is funded by the Office of Refugee Resettlement (ORR) and administered in Indiana by IHCDA. These are two agencies work together to recruit clients and assist them throughout the process. These clients will also participate in financial literacy and asset building courses and receive a dollar for dollar match from ORR ($2,000 limit for individuals, $4,000 limit for families) making this a very popular and highly competitive program.[8] The following are national statistics from 1999-2008, according to the Office of Refugee Resettlement:[9]

   - 21,512 IDA accounts have been opened since the start of the program;
   - 79 percent of accounts have been successful with at least one asset purchase;
   - The average home purchased cost $111,855 — 22,203 homes were purchased;
   - The average vehicle purchased cost $7,710 — 10,041 vehicles were purchased;
   - Participants saved $30.7 million; and
   - The average participant saved $1,567.

2. **Increase Public Awareness and Participation through Tax Preparation[10]**
   In 2007, in compliance with the Pension Protection Act of 2006, the Internal Revenue Service began giving taxpayers the option of electronically splitting their tax refund among two or three financial institution accounts. Consumers now can choose to divide their refunds between their IDA and a checking account, for example, which would give them immediate access to some of the funds while allowing them to save the remainder for longer-term goals.

   In addition, a small-scale demonstration of refund splitting was conducted in the 2004 tax season by the Doorways to Dreams (D2D) Fund in Boston, Massachusetts.

   - 516 tax filers given the opportunity to open an account to split their refunds, 27 percent accepted the offer, and 15 percent were able to participate after meeting account-opening criteria;
   - 47 percent of their refunds, or an average of $606. This represented at least a 90 percent increase over their existing savings; and
   - Four months later, two-thirds of participants continued to save a portion of their refunds.

3. **Expand IDA Uses, as defined in Indiana Code, to Include Additional Needs Such as Automobile Repairs, Child Care, and Mortgage Payments[11,12,13]**
   Over the years, Pennsylvania has expanded the uses of IDA program funds and has one on the most flexible IDA programs in the country. IDA funds in Pennsylvania can be used for to purchase a home, start or expand a small business, or to pay for postsecondary education, the

same as Indiana, but can also be used for automobile purchases, insurance costs, child care, college savings plans, and/or retirement.

While some IDA programs do not allow vehicle purchases due to the fact that an automobile is a depreciating asset, transportation constraints, such as costs of automobile repair or lack of public transportation should be considered.

Indiana has recently expanded the state IDA program to cover asset preservation activities such as owner-occupied rehabilitation, but does not allow IDA funds to be used to purchase an automobile. Indiana should consider including purchasing of and/or repair of a vehicle in order to increase the work participation, as does Kansas, Illinois, and Pennsylvania.

Some states have begun to allow IDA funds to be used to make mortgage payments to avoid mortgage default and foreclosure. However, IDA program participants have one of the lowest rates of mortgage default and foreclosure. This may be a way Indiana can expand use of IDA program funds to preserve a family's asset in emergency cases, such as unemployment.

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