



Center for Public Policy Priorities

900 Lydia Street, Austin, Texas 78702

PH: 512.320.0222 FAX: 512.320.0227 www.cppp.org

BACKGROUND

Individual Development Accounts

What is an Individual Development Account?

An Individual Development Account (IDA) is an interest-bearing, tax-free savings account created to help low- and moderate-income families build assets and move into the middle class. Each dollar a participant saves in an IDA is matched by public or private sources (e.g., banks, foundations, etc.). IDA deposits are exclusively limited to earned income.

IDA programs generally restrict savings to purchase of the following assets:

- A first home;
- Post-secondary education or training; and
- Starting or expanding a small business.

Other purposes may include buying a car (for employment purposes), saving for retirement, or making home repairs.

Most IDA programs target families and individuals with earnings at or below 200 percent of the federal poverty level (\$37,700 annual income for a family of four in 2004); however, eligibility varies by program. The match rate can also vary—ranging from 1:1 to 7:1—depending upon program design and the source of matching funds. The timeframe for achieving the required savings can range from six months to five years.

More than 1,000 Texans have used an IDA to purchase a home, go to college, buy a car to get to work, or start a small business. These purchases are worth an estimated \$1.8 million.

At a minimum, IDAs normally require:

- A community organization capable of performing outreach, enrolling participants, coordinating financial literacy education, and case management;
- A financial institution to hold an escrow account;
- A source of matching funds (federal, state, private, or a combination of these).

IDA program participants attend mandatory financial literacy classes, which emphasize money management skills along with long-term financial planning. Account holders also receive training specific to their asset goals, such as a class for first-time homebuyers.

In 1998, Congress passed the Assets for Independence Act, which provides \$25 million annually in grants for IDAs to fund both administrative costs and matching funds. Nationwide, over 500 IDA initiatives are in operation, with at least 10,000 account holders. Since 1995, 34 states, including

Texas, have passed IDA legislation; 13 states have appropriated state funding for IDAs. There are over 20 IDA programs in Texas.

Why are IDAs Important?

IDA initiatives represent a major asset-building strategy that rewards work and saving, fosters self-sufficiency, and increases financial literacy. At least one-third of all American families—including a significant number of “unbanked” families—own virtually no assets. With no savings or assets, low-income families are unable to plan for the future and have no cushion against sudden unemployment, serious illness, or a family emergency. This leaves many low-income Texans trapped in a cycle of poverty that may lead to a regular reliance on government assistance.

IDAs offer an effective mechanism for moving working families towards self-sufficiency through purchase of a valuable asset. Studies have shown that IDAs:

Each dollar invested in an IDA yields a return of approximately five dollars to the economy in the form of new businesses, additional earnings, new or rehabilitated homes, reduced welfare expenditures, and human capital associated with greater educational attainment.¹

- Provide a strong incentive to save and build long-term assets;
- Are a gateway to the formal banking system;
- Promote community and economic development;
- Increase homeownership;
- Increase financial literacy for participants;
- Promote economic and community development; and
- Advance economic mobility;

IDAs are exempt from the asset limits in all of the major public assistance programs, including TANF cash assistance, CHIP, children’s Medicaid, and Food Stamps. This allows families to save for the future while meeting their short-term needs.

What funding is available for IDAs?

The main source of IDA funding is the Assets for Independence Act (AFIA), a federal grant program authorized in 1998 with \$25 million in annual funding. AFIA provides administrative and matching funds to eligible entities, including state and local governments and private nonprofit organizations. In addition to AFIA, state IDA programs have used general revenue, solicited private contributions, or leveraged other federal funding streams,¹ including:

- Temporary Assistance to Needy Families (TANF);
- Workforce Investment Act (WIA);
- Welfare-to-Work; and the
- Community Development Block Grant (CDBG).

What IDAs are available in Texas?

Since 2003, the Texas Workforce Commission (TWC) has administered a two-year IDA pilot program funded with \$560,000 from the TANF block grant. TWC awarded grants for administrative and matching funds to three organizations already operating IDA programs. These programs targeted current and former TANF recipients, serving approximately 135 individuals. This pilot expires in September 2005 unless continued by the 79th Legislature.

¹ The disadvantage to using federal funding such as TANF for IDAs is that these dollars may not be used to draw down AFIA funds. The only exception is CDBG, which may be used as a match for an AFIA grant.

Aside from the TWC pilot, more than 20 IDA programs are operating throughout the state. These IDA programs have produced hundreds of success stories throughout Texas, enabling over 1,000 Texans to purchase a home, go to college, buy a car to get to work, or start a small business. As of March 2004, these programs included nearly 1,500 active accounts with over \$1.6 million in savings.

Texas IDA Program Results and Current Activity			
Active Accounts	Total Individual Deposits (does not include match)	Number of Asset Purchases	Value of Assets Purchased (estimated)
1,448	\$1.7 million	1,086	\$18,700,000

Sources: Texas IDA Network, March 2004; CPPP Analysis, 2005.

What does the future hold for IDAs in Texas?

President Bush’s proposed FY 2006 budget included two recommendations to increase the number of IDAs nationwide:

- Full funding for AFIA at \$25 million annually;
- An IDA tax credit that would generate \$1.7 billion in matching funds for 900,000 accounts over 10 years.

During this legislative session, lawmakers will have an opportunity to enact legislation establishing a statewide IDA program that builds upon the achievements of current IDA programs in Texas.

For more information

- The **Texas IDA Network**, an informal organization of locally-based organizations committed to fostering the economic independence of low-income households through asset-based remedies to poverty. (Woody Widrow, Project Director, 512-477-4431, widrow@consumer.org; web site: <http://www.covenantcapital.org/html/publicpolicy/idanetwork.html>)
- CPPP’s **Family Asset Building Project**, an effort to help low-and moderate-income families build financial security through assets, savings, and financial literacy. Visit our web site at <http://www.cppp.org/products/policyanalysis/eitc.html> for all of the publications related to this project.