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Building Blocks

New Programs Spur Working Poor To Begin Saving

Incentives, Counseling Inspire People to Clean Up Debts; Setting Aside $50 a Month Just Paying Bills Is a Struggle

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Americans are rotten at saving. To encourage thrift, the government hands out billions in tax breaks, mostly to the nation's wealthiest half. The other half, it's long been assumed, either cannot or will not save.

In recent years, a growing number of state governments, nonprofit groups, foundations and private companies have been running pilot programs to induce poor and working-class Americans to save. The results, they say, are surprising: When participants get the right incentives and financial counseling, many open savings accounts, arrange for payroll deductions, and begin accumulating assets.


Dorothy Beale

A Pennsylvania state program helped Michelle Simmons, 37 years old, to go from living on the streets to owning her own home, and inspired Dorothy Beale, 36, to clean up her debts and qualify for a mortgage. Another program outside St. Louis helped Charlin Hughes, a 36-year-old single mother of five, to begin saving for a home. Both programs offer to match participants' savings, but only if they consistently save and agree to attend financial-planning classes.

The programs are drawing support from both the left and the right. Advocates say they could become productive successors to liberal anti-poverty programs of the 1960s and conservative welfare reforms of the 1990s.

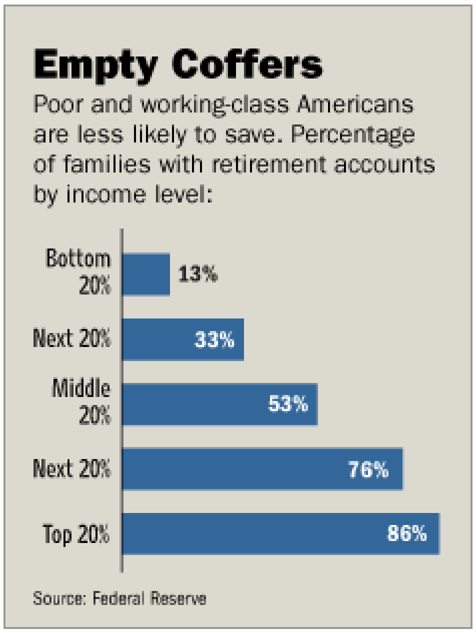
But proponents acknowledge it is difficult to persuade many poor people that they can afford to save, even with financial incentives. And rolling out such a program nationally would be expensive, costing about $40 billion over 10 years, according to one estimate.

Ms. Simmons says she was a "hope-to-die dope fiend" living in cardboard boxes on the streets of Los Angeles when she was arrested in 1998 for prostitution. Freed from prison after one year, she returned to her hometown, Philadelphia, and found low-paying work. With the help of a nonprofit agency that helps administer Pennsylvania's Family Savings Account Program, she got financial advice and opened an individual development account, or IDA.

The program offers to match participants' savings of up to $2,000 over three years with state and federal funds. Households with incomes of no more than twice the poverty level (about $40,000 for a family of four) are eligible. They must save at least $10 a week and attend a series of financial-planning classes. IDA savings must be used for college, job training, buying a home or starting a business.

By 2003, Ms. Simmons had saved $1,007. The program matched that amount, producing enough for the down payment on a $50,000 home from Habitat for Humanity.

There are more than 500 asset-building projects across the country, whose participants have opened more than 20,000 savings accounts. Thirty-three states support such programs on a small scale, using state funds and federal welfare-to-work subsidies for savings matches, and contracting with nonprofits to run the programs. Demonstration projects have also spread around the world from Canada to China. Great Britain last year became the first country with a national program of savings accounts for each child at birth.



The U.S. savings rate -- the percentage of after-tax income that Americans save -- has declined for nearly three decades. In 1984, it was 11%. In 2005, it dropped into negative territory, meaning that Americans were spending more than they earned.

One-third of U.S. households have no financial assets. An additional one-fifth have insignificant holdings. But households with about $2,000 or more in assets, including retirement savings, are ineligible for basic welfare programs, which provides a disincentive for the poor to save.

Broader Goal

The savings programs have their roots in the work of Washington University professor and social worker Michael Sherraden. His 1991 book, "Assets and the Poor," argued that governments and charitable groups should move beyond traditional welfare's aim to provide the poor with income to meet immediate needs. The broader goal, he wrote, should be to help the poor save money, which can provide them a stepping stone to escaping poverty.

He proposed that the federal government provide IDAs for every child at birth, regardless of family income, tapping public and private funds for initial deposits. The poor would get bigger initial deposits, and also matches for their personal savings, up to a limit. He argued that the accounts, coupled with financial education, would promote long-term savings for college, job training, buying a home or starting a business.

To Mr. Sherraden's surprise, his book was widely discussed by economists and others, and he became well-known in the anti-poverty world. Some critics, mainly from the political left, expressed skepticism that the poor would be able to save, given their struggles just to make ends meet. But Mr. Sherraden's proposals drew interest from community groups, governors, members of Congress, and from the first Bush and Clinton administrations. Private foundations stepped in with funds for testing the approach. Led by the Ford, Charles Stewart Mott and Annie E. Casey Foundations, philanthropic groups continue to provide much of the money for such programs. Mr. Sherraden says he is frustrated that the programs have yet to expand beyond experimental projects.

Advocates of asset-building programs concede it is difficult to get low-income people to save. "The biggest hurdle is just getting them to believe they can save," says Chris Krehmeyer, executive director of a St. Louis nonprofit social agency, Beyond Housing/Neighborhood Housing Services. Given "the struggles of keeping the utilities on, paying your bills, keeping the car running and just dealing with life," he says, even $10 a week is a huge amount.

In Washington, support for a bigger federal role in asset-building programs for low-income Americans ranges from conservative Republicans such as Sen. Rick Santorum of Pennsylvania, former housing secretary Jack Kemp and former House Speaker Newt Gingrich, to left-of-center Democrats and potential 2008 presidential candidates Hillary Clinton and John Edwards.

Thus far, budget deficits and partisan politics have stymied advocates of a nationwide policy. During his 2000 presidential campaign, George W. Bush advocated fighting poverty "by building the wealth of the poor." He proposed a $1 billion tax credit for banks that match some savings deposits of low-income workers. As president, he didn't make the proposal a priority, and it died in the House, in part for reasons unrelated to the proposed credit.

In 2001, Congress created the Saver's Credit, the only federal savings incentive designed for low- and middle-income households. It reduces taxes on savings of up to $2,000 a year for people making less than $50,000 a year. But Americans who don't owe income taxes aren't eligible. About 40% of Americans don't earn enough to have an income-tax liability, according to the Retirement Security Project, an academic venture sponsored by the Pew Charitable Trusts.

The government spends about $150 billion a year on tax breaks to encourage retirement savings, which mainly benefit the affluent. About 70% go to the top one-fifth of earners, the Pew project concluded. Many simply shift existing savings into tax-favored accounts. The 40% of Americans who don't have tax liabilities do not qualify for these breaks. And most low-income workers do not have jobs that offer 401(k) retirement plans.

"We are kidding ourselves if we think we are expanding savings" with "a grotesque array of savings incentives that do nothing for low-income Americans," says Fred Goldberg, the top Treasury Department tax official and Internal Revenue Service commissioner in the administration of President George H. W. Bush.

Numerous ideas have been floated for encouraging low-income workers to save more. Making enrollment in 401(k) plans automatic for new hires is one. Giving taxpayers the option of saving all or part of their annual tax refunds -- sometimes by offering them a financial incentive -- is another. Tests of that concept in Tulsa, Okla., by a community and academic team, and in St. Louis, by H&R Block and the Retirement Security Project, showed that some people were willing to save a portion of their refunds.

More ambitious, and costly, are the proposals to roll out IDA-like accounts on a national scale. A bipartisan bill introduced in Congress to establish so-called Kids Accounts for every newborn, with greater federal funding for the poor, would cost an estimated $40 billion over 10 years.

Pennsylvania started its Family Savings Account Program eight years ago, making it one of the first statewide IDA programs. The program gets about $1 million annually from the state, and another $1 million from federal welfare funds.

Starting a Halfway House

After Ms. Simmons was released from a California prison, she found work in Pennsylvania as a telemarketer. She wanted to start a halfway house for women newly released from prison, so she took a self-employment course run by the Women's Opportunities Resource Center, a local social-service agency. She learned there about the savings-match program, and signed up. To save money, she shopped at thrift stores and went without cable television, a cellphone or manicures.

Today, she owns a three-story townhouse in Norristown, just north of Philadelphia, which she bought in 2003. She has regained custody of two daughters, who have their own bedrooms. Not far away stands the halfway house she opened. In three years, she has housed 33 women fresh from jail and "graduated" 17 to jobs and housing, she says. She urges residents to open IDAs. "I sell it," she says. "I tell them, 'This is an investment, y'all.' "

Ms. Beale and her three children were living in her mother's house when she heard about Pennsylvania's IDA program in 2003. Despite her $40,000-a-year hospital clerical job, debt had piled up after a divorce. She'd had her car repossessed and had exceeded limits on three credit cards. She opened an account and signed up for evening money-management classes. "I hadn't even realized I was spending more than I was making," she says.

To save, she cut out manicures and cable television, and shopped only for "needs, not wants." By saving $80 a month, she accumulated about $1,000 in a year. She added another $1,000 from her tax refund, entitling her to the $2,000 maximum match. With help from agency counselors, she cleaned up her credit rating by paying off small debts and negotiating payment plans with her credit-card companies and utilities. By September 2004, she had a $77,000 mortgage for a townhouse in northeast Philadelphia.

In her kitchen "bill corner," Ms. Beale keeps her budget in a journal. She still saves about $50 a month, and also contributes to a 401(k) retirement account and a college-savings plan for her children. She has opened savings accounts for all three.

With funding from Ford and other foundations, a consortium of social-service organizations is testing Mr. Sherraden's idea to encourage savings early in life at 13 sites across the country. At Delmar-Harvard Elementary School in mostly working-class University City, Mo., outside St. Louis, 50 students are in the third year of a four-year pilot program managed by Beyond

Housing. Each student received an initial $500, and a promise that his or her own savings would be matched dollar-for-dollar. They receive $2 for attending each weekly meeting of the "I Can Save" club.

On a recent afternoon, more than a dozen second- and third-graders met after school, then trudged a couple blocks to Commerce Bank to make deposits. Nine-year-old Jessica Washington deposited $50. "I earned it, and my mom gave me some," she said. Seven-year-old Alexia Luckett deposited her $4 check for attending meetings. Sometimes she brings her earnings from cleaning her room, but this time, she said, "my mom didn't have the money."

The children do not know their balances. But all agree on what the money is for: college. That is drummed into them by their teachers and parents, who also attend workshops. The most recent data show that through November, the 7- to 9-year-olds had saved a total of $64,093. The average account contained $866.

Beyond Housing also oversees IDA accounts for about 80 adults. One year ago, Ms. Hughes, the single mother of five, was homeless. Now she has $50 a month deducted for her IDA from the $31,000 a year she earns working at an insurance office.

According to Beyond Housing accounts manager Linda Thomson, if Ms. Hughes saves $1,500 over 30 months, sometime in 2007 she will get a two-to-one match of $3,000 -- half from United Way of Greater St. Louis Inc. and half from federal funds. With that $4,500, plus closing costs from the nonprofit, she could get an affordable mortgage of about $85,000, Ms. Thomson says.

Last fall, a fire destroyed the townhouse Ms. Hughes had been renting since May, along with her family's possessions. A member of her church provided temporary housing. By December, her savings plan was still on track. "It was hard to save, but for the money coming out of my check automatically," she says.

Ms. Hughes says she tells her kids "no" a lot. There were no Christmas presents this year. "I have to lead by example," she says. "I can't tell my kids what to do if I don't do it myself."