



A Review of Children's Savings Accounts

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Children's savings accounts (CSAs) aim to improve the lives of low- and moderate-income people by increasing their financial security, developing their financial capability, and improving their educational outcomes. They are one of the policies advocated by the ranks of the asset-building movement: David Kirp includes them in *Kids First: Five Ideas for Transforming Children's Lives* (Kirp 2011). With their benefits increasingly recognized, CSAs have been adopted and proposed in numerous forms over the past two decades.

The CSA movement was catalyzed over 20 years ago with the publication of Michael Sherraden's ground-breaking book, *Assets and the Poor*. Among other ideas, Sherraden proposed providing savings accounts with subsidies to poor people, who typically lack incentives to save and access to mainstream financial institutions. These accounts, known as individual development accounts, or IDAs, offer matching contributions and provide financial education. They are intended to build assets for certain purposes, such as going to college or buying a house. IDAs have been funded through federal legislation and have been tested or implemented in more than 40 states (CFED 2011b). IDA-type programs are also active in many other countries (Han and Sherraden 2007; Sherraden, Schreiner, and Beverly 2003).

In Sherraden's initial vision, IDAs were universal and began at birth. In practice, most IDAs have been targeted at adults and implemented as short-term demonstrations. CSAs, while similar to IDAs, are designed to start at birth or very young ages.

This brief reviews CSAs and their benefits, provides international and domestic examples of CSA programs, and points to selected research on their effects—including their distributional impact.

What Are Children’s Savings Accounts?

Although they vary in design, most CSAs are savings accounts established in a child’s name with an initial “seed” deposit from a sponsor—a community organization, private institution, or government. Typically, families are not obligated to contribute to CSAs, but the seed encourages household savings simply by providing children with bank accounts and financial education. Seed money can be provided in one of two ways. First, the same seed amount can be provided to all participants. Second, it can be means-tested—for example, it might decline with income and eventually fall to zero for those with income above some threshold.

Some CSAs also include supplemental grants or matching incentives. The grants might be conditional on meeting certain milestones—for example, bonus grants for signing up for auto-deposit (Phillips and Stuhldreher 2011) or attending financial education classes (Mason et al. 2009). Alternatively, supplemental grants or matching incentives may be means-tested and deposited only in the initial year or periodically throughout the years. Like seed funding, supplemental grants aim to increase the amount saved; they may or may not require additional private (or household) saving.

One possible aim of CSAs is to help children build private assets. Studies suggest that matches provided against private contributions encourage additional private saving (Duflo et al. 2006). Accordingly, some CSAs include matching funds. Sponsors can match private contributions dollar for dollar, 50 cents per dollar, or at other rates. Another option is a multirate match structure, with the rate decreasing as household income rises. The match can occur in addition to or instead of a supplemental grant.

CSAs may be taxable or nontaxable. They may make use of existing saving vehicles, like 529 plans, or create a new vehicle for deposits. Such accounts also do not necessarily need to be made available at birth.

What Are the Benefits of CSAs?

Savings accounts aim to improve the lives of low- and moderate-income people economically, socially, and psychologically. They increase financial security by providing people with the means to help weather emergencies like a job loss. Savings accounts also develop financial capability; in demonstrating the value of saving and compound interest, they encourage people to save more (Butrica et al. 2008).

CSAs share the benefits of savings accounts. In addition, they have been associated with better educational outcomes (Elliott and Beverly 2011; Elliott, Jung, and Friedline 2010).

International Examples of CSAs

A number of countries have already implemented children’s savings accounts, including the United Kingdom, Canada, and Singapore.

United Kingdom

The United Kingdom began its Child Trust Fund in 2005 for all children born on and after September 1, 2002. A parent or guardian was responsible for opening an account in the child's name through the private sector and for managing the account (e.g., keeping all the paperwork, reporting certain changes of circumstances, and changing the account or provider).¹ The government then deposited seed money into the account. In its early years, the seed deposit was £250 (approximately \$400), with children in the poorest families receiving an additional £250. On children's seventh birthdays, the government made another deposit of £250; again, children in low-income families received an additional £250.

The Child Trust Fund encouraged families and friends to make tax-deferred contributions up to £1,200 (approximately \$1,950) each year. Accounts accrued tax-free interest until children's 18th birthdays. At age 16, children took over legal ownership of the accounts, and at age 18 the accounts automatically converted to adult savings accounts. Withdrawals before age 18 were prohibited, but there were no restrictions on how the funds could be spent once the accounts matured.

In 2010, the government announced that the Child Trust Fund was being phased out to cut government spending. For children born after August 3, 2010, the government dramatically reduced benefits to only £50 and eliminated the supplemental birthday payments. On January 2, 2011, the government stopped contributing to all Child Trust Fund accounts.

In their place, the government established Junior Individual Savings Accounts (ISAs), which are tax-free savings accounts for children under age 18. There are two types of Junior ISAs: cash, and stocks and shares (in the latter, cash deposits are invested). The money in the account belongs to the child but cannot be withdrawn until he or she turns 18 (with some exceptions). Anyone can deposit money in the account, but total deposits each tax year cannot exceed £4,000. As with a Child Trust Fund account, the Junior ISA is in the child's name, but the person who opens the account is responsible for managing it. The child takes over the Junior ISA at age 16 and can withdraw the money at age 18. If he or she does nothing, the Junior ISA automatically becomes an adult ISA. Monies in the Junior ISAs come from private contributions only: there is no government seed deposit, supplemental grant, or match.

Canada

Canada has established three related programs to support saving for children's education. It began offering children's savings accounts in 1998 through Registered Education Savings Plans (RESPs)—special accounts that are registered with the Government of Canada and earmarked for post-secondary education. RESPs are opened through financial institutions and feature lifetime tax-deferred private contribution limits of \$50,000 Canadian dollars. Through the Canada Education Savings Grant (CESG), the government annually matches 20 percent of the first \$2,500 of private contributions into the RESPs of children under age 18. Children in low-income families receive an extra 10 or 20 percent, depending on their income level, of the first \$500 of private contributions. The lifetime limit for CESGs is \$7,200. In addition, the government deposits Canada Learning Bonds (CLBs) worth \$500 into the RESPs of

children in low-income families, along with an extra \$100 annually until age 15. The lifetime limit for CLBs is \$2,000.

Singapore

Singapore has been praised for its “cradle-to-grave” and “highly innovative” asset-based policies (Loke and Sherraden 2009). The Baby Bonus program covers children from birth until age 6; the Edusave Scheme covers children ages 7 to 16; and the Post-Secondary Education Scheme covers children ages 7 to 20.

Singapore introduced the Baby Bonus program in 2001. Under the current scheme, parents receive a cash gift from the government of up to \$6,000 Singapore dollars each for their first and second children and \$8,000 each for their third and fourth children. Parents who open a child development account (CDA) receive a dollar-for-dollar government match for their contributions: up to \$6,000 each for their first and second children, \$12,000 each for their third and fourth children, and \$18,000 each for their fifth and subsequent children. Different from CSAs in the United Kingdom and Canada, Singapore’s CDAs are designed specifically for the child care, education, and health care of children age 12 and younger (Ministry of Social and Family Development in Singapore 2013). After that age, the government closes the CDAs and transfers unused balances to children’s post-secondary education accounts (PSEAs).

The Edusave Scheme was introduced in 1993 to help parents pay for enrichment programs and school-related fees. At age 7, each student automatically gets an Edusave account into which the government makes annual contributions. Since 2009, these contributions have been \$200 for primary school students and \$240 for secondary school students. The government also provides students with a top-up grant periodically. The last top-up was \$130 per student in 2011. In addition, the government makes annual merit-based contributions (Ministry of Education in Singapore 2011). At age 16, the government closes the Edusave accounts and transfers unused balances to children’s PSEAs.

The Post-Secondary Education Scheme was introduced in 2005 to help finance post-secondary education expenses. The government opens PSEAs automatically and transfers unused balances from CDAs and Edusave accounts into them. If parents have not saved up to the CDA contribution cap, they can continue to contribute to PSEAs and receive the government’s matching grant until the contribution cap is reached or until the child turns 18, whichever is earlier. In addition, the government periodically contributes to each child’s PSEA. In 2010, the government top-up was \$100 or \$200 for children between ages 7 and 12 and \$250 or \$500 for children between ages 13 and 20, depending on the value of their families’ home. At age 30, the government closes the PSEAs and transfers unused balances to adults’ Central Provident Fund accounts.

Examples of CSAs in the United States

Though the United States has no national children's savings account program, it has similar account structures that could be used to launch one—structures including IRAs, 529 plans, basic savings accounts, savings bonds, certificates of deposit (CDs), Coverdell education savings accounts, and custodial accounts under the Uniform Gifts to Minors Act or the Uniform Transfers to Minors Act.

IRAs and 529 college savings plans, for example, provide tax advantages and share some of the same features and goals as CSAs. IRAs are designed to help save for retirement, but they do permit penalty-free early withdrawals for first-time home purchases and post-secondary educational expenses. 529 plans are designed to help defray children's college expenses. Anyone can contribute money to a 529 plan on behalf of a beneficiary. As of 2014, 49 states and the District of Columbia offer state-based 529 plans (College Savings Plans Network 2014).

National Efforts

CSA proposals have been floated, and a number of demonstrations have taken place. First introduced in 2004, the New America Foundation's proposal for the America Saving for Personal Investment, Retirement, and Education (ASPIRE) Act would create children's savings accounts. At birth, children would receive a \$500 government deposit in a lifetime savings account. Depending on family income, some children would receive a supplemental contribution of up to \$500. After-tax private contributions would be permitted up to \$2,000 a year and would be matched by the government up to \$500 a year, depending on income level. Withdrawals would not be permitted until age 18. Between ages 18 and 25, account balances could be used only for higher education. After age 25, balances could be used for homeownership or retirement in accordance with Roth IRA regulations. Although parents would initially serve as custodians, it is unclear when children would take over the accounts (Friedline 2012). Although the ASPIRE Act has been regularly introduced in Congress, it still has not passed into law.

The Young Savers Account (Savings Competitiveness Act of 2006, S. 2431) and 401Kids Accounts (The 401Kids Family Savings Act of 2006, H.R. 5314) were proposals for children's savings accounts (Boshara 2006; Rist and Humphrey 2006). The former was essentially a Roth IRA, and the latter was a Coverdell education savings account that could be used to buy a first home or to roll over into a Roth IRA to save for retirement.

In March 2014, Representative Joseph Crowley (D-NY) announced a proposal for CSAs under which every child born in the United States would receive a USAccount with a seed deposit of \$500. Families could deposit up to \$2,000 into the account annually and the government would match deposits dollar for dollar up to \$500 per year. The proposal also calls for expanding the child tax credit up to a maximum of \$500 annually. USAccounts would be established through the Social Security Administration, although families could move them to an approved financial services institution. Children could access the funds at age 18 and use them to pay for college, to buy a home, or to start a small business. The funds could also be rolled over into a 401(k), IRA, or traditional private savings account.

Institutional Efforts

From 2003 through 2008, the Center for Social Development led an experiment on children's savings accounts known as the Saving for Education, Entrepreneurship, and Downpayment (SEED) demonstration. The program was piloted in 12 states and communities across the United States and Puerto Rico and included 1,171 participants. All SEED accounts received an initial deposit of up to \$1,000. Match dollars were available to encourage private contributions. Many programs also used benchmark incentive dollars for staying in the program or attending financial education classes, for example, to increase account balances. At the end of 2007, the average participant had accumulated \$1,518; balances ranged from \$885 to \$2,626 (Mason et al. 2009).

In 2008, the Center for Social Development and RTI International, together with the State of Oklahoma, launched a research experiment known as SEED for Oklahoma Kids (SEED OK). Though similar to the larger SEED demonstration, SEED OK focuses on promoting asset building beginning at birth and testing whether children's savings accounts increase savings beyond what individuals would have saved without them. The experiment selected newborns from birth records, and 2,704 of their caretakers agreed to participate in the study. Participants were randomly assigned to treatment and control groups. The treatment group received an Oklahoma College Savings Plan 529 account with a seed deposit of \$1,000. In addition, treatment group members were encouraged to open their own private Oklahoma 529 accounts and were given \$100 seed deposits if they did so. Finally, those with low and moderate incomes had their contributions matched up to \$250 each year. Members of the control group did not receive a 529 account, though they could open one on their own.

In early results, nearly 100 percent of the treatment group had 529 accounts compared with less than 3 percent of the control group, and the difference in average 529 assets was around \$1,040. Looking at just the privately owned 529 accounts, however, the results are slightly less encouraging. Around 16 percent of the treatment group had their own private 529 plan, compared with less than 1 percent of the control group. Although treatment group members saved significantly more in their accounts than control group members, the amounts and difference were small—an average of \$47 compared with only \$13 (Nam et al. 2013). Further, it is unclear whether the increased savings in the 529 plans were from new savings or savings transferred from other assets.

City and State Efforts

San Francisco's Kindergarten to College (K2C) program gives every public-school kindergartener a child savings account with an opening deposit of \$50. The city deposits an additional \$50 in the accounts of children eligible for free and reduced-price lunches. Families are also eligible for a one-to-one match on their contributions up to \$100; those who make monthly automatic deposits receive an additional \$100. The program was piloted in the 2010–11 academic year with 1,200 students in 18 schools and rolled out to all entering kindergarteners over two years (Phillips and Stuhldreher 2011).

Mississippi has a pilot program that has provided 529 plans to 500 children across the state and deposited \$50 into their accounts. The children with 529 plans are also receiving financial education in

the classroom, and their parents are receiving training that encourages them to save for their children's future. In Michigan, the Oakland Livingston Human Services Agency recruited Head Start families to participate in CSAs. Participating families were provided a Michigan 529 plan, an initial contribution of \$800, and a \$200 match. Additional contributions were matched one to one.

Maine, Nevada, and, most recently, Rhode Island automatically deposit funds into the 529 plans of all young children. In Maine, children born since 2013 receive a \$500 Alford Grant for future education expenses.² The grant is deposited into their Maine 529 account if they have one or is invested by the Alford Scholarship Foundation until children are ready to use it. Since 2013, Nevada's College Kick Start Program has provided public school kindergarten children with a 529 plan with an initial deposit of \$50. Starting in 2015, Rhode Island will give every child born or adopted after July 1, 2010, a \$100 CollegeBound *baby* grant of \$100 to deposit in a CollegeBound *fund* 529 plan.

Through a partnership in Texas, the state Office of the Attorney General's Child Support Division piloted a program that encouraged using 529 CSAs specifically for children in the child support system.³ The program—Child Support for College (CS4C)—originally targeted custodial parents who received lump sum child support payments to deposit at least a portion of that payment into a Texas 529 college savings plan of their choice (Osborne, Dillon, and Bellows 2013).⁴ After four sessions with a financial coach, participants were eligible for a 20 percent match on their initial deposit and a 10 percent match on subsequent deposits, up to \$500. The program also encouraged noncustodial parents to make separate contributions to the 529 plan. The CS4C program evolved after its 2012 beginning and most recently targeted low-income parents who received regular child support payments. Financial education sessions were no longer required, and all new CSAs were seeded with \$100 for the first \$25 deposited and received one-to-one matching contributions on all deposits, up to \$500. The program ended in August 2013. A follow-up study shows that one-third of those inquiring about the program participated in a financial education session, and that two-thirds of those participants opened a CSA. Account balances averaged close to \$775 at the end of the program, of which \$440 came from participants and the rest from CS4C program incentives (Osborne, Dillon, and Bellows 2013). Unfortunately, deposits were not tracked after participants reached the maximum match, so account balances may be higher.

The Kansas child support program, in partnership with the state treasurer, has a program to help low-income noncustodial parents save for their children's college education by reducing their child support debt when deposits are made into the Kansas 529 college savings accounts. Noncustodial parents who participate and make qualifying deposits into a Kansas 529 college savings account will receive forgiveness of their state-owed child support debt on a 2:1 ratio for every dollar deposited.

Finally, a 2011 CFED resource guide noted that states have the flexibility to design many features of their 529 plans and that many states use incentives to encourage saving in these plans. The CFED analysis found that 10 states had matching grant programs, 3 states offered tax credits based on a percentage of 529 contributions, and 1 state had both types of incentives (CFED 2011a).

Guidelines for Establishing CSAs

Establishing a CSA program requires careful consideration of its design and administration. Having said that, there are now many models of successful CSA programs that states and organizations can consult.

The following design decisions are key:

- whom the program is targeted to;
- what savings vehicle to use;
- whether accounts will be seeded and by whom;
- how much the seed amount will be;
- whether the program will provide supplemental grants;
- under what conditions participants receive supplemental grants;
- how much the supplemental grants will be;
- who can make private contributions;
- whether there are contribution limits;
- whether the program will match private contributions;
- under what conditions it will match private contributions;
- how much the match will be;
- when participants can withdraw funds and for what purpose;
- what are the permissible investments for accounts;
- who will administer the account (e.g., financial institution, public sector, or another third party); and
- what fees and costs will be assessed against accounts for investments and administrative services.

Administering a CSA program requires

- establishing accounts;
- developing systems to properly credit private contributions from different sources (e.g., parents, grandparents, friends, and employers) and matches or subsidies (if they exist) to each child's account;
- providing periodic financial statements to households that show the balance in each child's account to date and break out the share from private contributions, matches and subsidies, and investment earnings; and
- determining whether account withdrawals are allowable based on child's age and purpose.

Published guides provide more detailed information about starting a CSA (Brooks et al. 2006; Osborne, Dillon, and Bellows 2013). This brief is not intended to discuss these design and administration options in detail. It does, however, provide a few examples of issues that must be addressed:

Taxability

Researchers have questioned the consequences associated with not taxing income in CSAs (Butrica et al. 2008). Nontaxability is worth more to those with higher incomes. Some child account proposals have tried to make the proposal more progressive by providing higher levels of contributions or matches at low and moderate income levels. But the same principle applies even if the rich are excluded: for instance, the account might still be worth more to the middle-income qualifying family than the low-income one.

Choice of CSA Vehicles

CSA programs might create new saving vehicles or use existing account structures. Rist and Humphrey (2006) discuss some of the advantages and disadvantages of using IRAs and 529 plans as CSAs. Compared with 529 plans, IRAs are more flexible in their uses and receive more advantageous treatment in calculating need-based financial aid because the formula excludes them from assets. However, IRA assets are countable for determining eligibility for public benefits. In contrast, assets in 529 plans may or may not affect public benefits. With the passage of the 2008 Farm Bill, 529 plans no longer count against asset limits for the Supplemental Nutrition Assistance Program. However, they count against asset limits for Temporary Assistance for Needy Families in some states, and against assets limits for Supplemental Security Income benefits (Greer and Levin 2014).

Another complication with using many existing tax vehicles for CSAs is that they are often considered poorly designed from a tax, education, or budget policy perspective. For example, 529 plans predominantly benefit high-income individuals; they have not been proven to aid in expanding educational opportunity; and they create an unnecessary level of intermediation since states hire other financial institutions to run the accounts. Roth IRAs, in turn, have been used to play budget games, since, unlike 529 plans and traditional IRAs, lost tax revenue is deferred into the future—well beyond and not accounted for in 10-year budget windows. Roth accounts also heavily favor those whose investments turn out well over those with low or negative returns on their assets.

The extension to child accounts does not add significantly to those inefficiencies. Yet it is unclear whether long-term policy objectives for low- and moderate-income individuals should be attached to vehicles that, from many other perspectives, tend to operate against their interests and that might need reforming.

Age at which Accounts Are Provided

If child accounts are to be used to make people more financially literate from young ages, then providing accounts at birth is less important than helping children become aware of the accounts and their potential. A community, for instance, might make a substantial effort to get its school children to start bank accounts earning interest that can compound.

Notes

1. The government opened accounts for children whose parents who failed to, as well as for children in foster care arrangements.
2. Between 2008 and 2013, parents had to open a Maine 529 plan before their child's first birthday to be eligible for the Alford Grant. Starting in 2014, children automatically receive the grant at birth (Clancy and Sherraden 2014).
3. For more information, see <http://raisetexas.org/childsupportforcollegeinitiative/>.
4. The average lump sum child support payment was \$2,444 in August 2011.

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