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INDIVIDUAL DEVELOPMENT ACCOUNTS FOR POOR AND NEAR POOR

House Bill 4038 (Substitute H-2)
Sponsor: Rep. Kirk Profit

House Bill 4195 (Substitute H-1)
Sponsor: Rep. Martha Scott

House Bill 4786 as introduced
Sponsor: Rep. Hubert Price, Jr.

First Analysis (12-10-97)
Committee: Human Services and Children

THE APPARENT PROBLEM:

The national welfare reform act authorizes states to create community-based individual development account (IDA) programs with the Targeted Assistance for Needy Families (TANF) block grant funds, and to disregard all money saved by the poor in IDAs when determining eligibility for all means-tested government assistance. The act also provides that only earned income can be saved in IDAs; designates nonprofit, community-based organizations as custodians of IDA accounts; and permits IDAs to be used for education, home ownership, and business capitalization.

According to the National Governor's Association, by January 31, 1997, 10 states had set up IDAs (Alabama, Arizona, California, Missouri, New Hampshire, North Carolina, Oregon, South Carolina, Tennessee, and Virginia) and even more have done so since.

Individual Development Accounts, or IDAs, are dedicated savings accounts, similar in structure to Individual Retirement Accounts (IRAs), which may only be drawn upon to purchase a home, finance an education or job training, or capitalize a small business. Accounts are managed by community organizations and held at local financial institutions. Public, private, or a combination of sources match the savings of low-income participants.

Supporters of IDAs note that accounts such as these shift the focus, both of policy makers and welfare recipients, from consumption to investment--from consumer spending to savings. The programs are designed to remove barriers to asset building, and to promote asset accumulation. Supporters also note that asset-based policy and incentives for the non-poor are a common occurrence in taxation policy, although less frequent in social welfare policy. For example, according to the IDA Evaluation Handbook, it is estimated the federal government spent over $160 billion in 1995, primarily through tax expenditures, to support home equity and retirement pension accounts for the non-poor, alone.

Legislation has been introduced to allow the state and local governments to participate in IDAs, and to ensure that individuals who invested in their future would not be penalized by having their eligibility for other assistance programs curtailed.

THE CONTENT OF THE BILL:

House Bill 4038 would add a provision to the Social Welfare Act (MCL 400.57i) to require that the Family Independence Agency (FIA) implement a program that would permit an individual receiving assistance to establish an Individual Development Account (IDA) for the payment of postsecondary education expenses; and, to disregard these funds when determining the individual's eligibility for assistance, and the amount of the grant the individual receives.

Under the bill, an individual (or another person on his or her behalf) could establish an account by contributing money derived from earned income. Money could be withdrawn from the account and expended only for payment of postsecondary educational expenses at eligible institutions. An "eligible institution" would mean a college, university, community college, state-licensed vocational or technical education program, or state-licensed proprietary school. "Educational expenses" would mean tuition and fees, books, supplies, and equipment required for courses of instruction.

House Bill 4195 would amend the Social Welfare Act (MCL 400.57j) to require the Family Independence Agency to operate a program that would allow an individual eligible for assistance to establish an individual development account (IDA) for business capitalization; and to disregard these funds when determining the individual's eligibility for assistance, and the amount of the individual's grant. The funds contributed to this account would have to be derived from earned income. Funds could be withdrawn and expended only for payment made directly to a business capitalization account that was established in a federally insured financial institution. An "individual development account" would be defined as a trust created in the United States that was funded through periodic contributions by the establishing individual, and that could be matched by or through a qualified entity. A "qualified entity" would mean either a nonprofit organization, or a state or local governmental agency acting in cooperation with a nonprofit organization. A "qualified plan" would mean a business plan that a) was approved by a financial institution, or by a nonprofit loan fund that had demonstrated fiduciary integrity; b) included a description of services or goods to be sold, a marketing plan, and projected financial statements; and c) could require the eligible individual to obtain the assistance of an experienced entrepreneurial advisor.

House Bill 4786 would add a new section to the Social Welfare Act (MCL 400.57k) to establish a program, operated by the Family Independence Agency (FIA), that would allow an individual eligible for family independence assistance to establish an individual development account for first-time home buyers. Under the bill, the FIA would be required to disregard funds, including accrued interest, in a development account when determining the individual's eligibility for family independence assistance, in accordance with the following provisions:

The bill would define an individual development account to mean a trust created or organized in the U.S. that was funded through periodic contributions by the establishing individual, in accordance with the provisions of the bill, and that could be matched by or through a qualified entity for a "qualified purpose," as described under the bill. Under the bill, an individual who was eligible to receive family independence assistance, or another person on behalf of that individual, could establish a development account in order to accumulate funds for a "qualified purpose," which would be defined, under the bill, to mean only for the payment of qualified acquisition costs with respect to a qualified principal residence for a qualified first-time home buyer, if paid from an individual development account directly to the persons to whom the qualified acquisition costs were due. However, an individual could only contribute money to a development account that was derived from earned income, as that term is defined under Section 911(d)(2) of the Internal Revenue Code. Money from a development account could only be withdrawn and expended for a "qualified purpose," as that term is defined under the bill.

In addition, the bill would define "qualified acquisition costs" to mean the costs of acquiring, constructing, or reconstructing a qualified principal residence. The term would include any usual or reasonable settlement, financing, or other closing costs. "Qualified entity" would be defined to mean either a nonprofit organization, which is exempt from taxation as described under Section 501(a) of the Internal Revenue Code; or a state or local governmental agency acting in cooperation with a nonprofit organization. "Qualified first-time home buyer" would mean a taxpayer and, if married, the taxpayer's spouse, who had no present ownership interest in a principal residence during the three-year period ending on the date of acquisition of the qualified principal residence to which the provisions of the bill applied. "Qualified principal residence" would mean a principal residence within the meaning of Section 1034 of the Internal Revenue Code, the qualified acquisition costs of which did not exceed 100 percent of the average area purchase price applicable to that residence, as determined in accordance with Section 143(e) of the Internal Revenue Code. "Date of acquisition" would mean the date on which a qualified first-time home buyer entered into a binding contract to acquire, construct, or reconstruct the qualified first-time home buyer's principal residence.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, House Bill 4038 would result in an indeterminate increase in costs to the state, as it would require the FIA to incur administrative costs associated with the establishment and maintenance of irrevocable education accounts. House Bill 4195 would also result in an indeterminate cost increase as more clients would be eligible for cash assistance resulting from asset and income disregard. The HFA reports that House Bill 4786 has no fiscal impact. (12-9-97)

The Family Independence Agency's 1997-98 budget includes an appropriation of $100,000 for the establishment of individual development accounts.

BACKGROUND INFORMATION:

Three related bills are under consideration by the House Urban Policy and Economic Development Committee. Those bills, House Bills 5306-5308, would create the Individual or Family Development Account Program Act.

ARGUMENTS:

For:

As the National Governor's Association Issue Brief entitled "Building Assets and Economic Independence Through Individual Development Accounts" notes, owning assets gives people a stake in the future--a reason to save, to dream, and to invest time, effort, and resources in creating a future for themselves and their children. People move forward economically through savings and investment, not through spending and consumption. As a noted proponent of IDAs has said: Income may feed people's stomachs, but assets change their heads. Helping former and potential welfare recipients to re-think their circumstances, to plan for a future, and to imagine themselves moving from dependency to self-sufficiency, is a laudable goal. These bills would enable state and local governments to pursue that goal.

For:

According to the National Governor's Association, the distribution of assets in the United States is much more unequal than is the distribution of income. Although the top 10 percent of Americans commands 40 percent of national income, the top one percent controls as many assets as the bottom 80 percent. Unfortunately, asset deficiency usually places home ownership, entrepreneurship, and higher education out of the reach of many Americans and, in doing so, prevents them from advancing economically. Individual development accounts would help the poor acquire assets.

Against:

Two of the three bills would allow the creation of individual development accounts for acceptable purposes: education beyond high school; and, first-time home ownership. These are examples of investment and savings that the State of Michigan should endorse, and where possible, promote with incentives. However, the third bill--House Bill 4195--would allow the poor to establish a savings account that would be used only to start a small business. This bill would put existing small businesses at a great disadvantage, since it would require them to compete with new businesses which might offer similar services.

Response:
Many impoverished regions, whether urban or rural, have too little investment and too few small businesses, rather than too many. As a result, there is little to no price competition for necessary goods and services. The lack of price competition often means that consumers in regions with little investment pay too dearly. House Bill 4195 would allow for small business investment where now there is little or none.

POSITIONS:

The Michigan Federation of Private Child and Family Agencies supports the legislation. (12-9-97)

The Michigan Association for the Education of Young Children supports House Bill 4038. (12-9-97)

The Family Independence Agency supports the concept of individual development accounts. (12-9-97)

The National Federation of Independent Business-Michigan opposes House Bill 4195. (12-9-97)

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■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.