



The benefits of saving at tax time: Evidence from the \$aveNYC evaluation



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ABSTRACT

Paper presents results of an evaluation of a tax-time savings program. \$aveNYC offers incentivized savings accounts to taxpayers filing their taxes at Volunteer Income Tax Assistance (VITA) sites in New York City. Participants who direct-deposited at least \$200 of their refund into the account and maintained the balance for a year received 50 cents per dollar saved. A comparison group was drawn from NYC VITA sites where the program was not offered. Propensity score weighting was used to balance the two groups. Study participants ($N = 353$) were surveyed via telephone halfway through the program, and again 8 months after the program ended. 70 percent of \$aveNYC participants surveyed received the match. The majority of those who received the match continued to save some portion of the money. At the second survey, there was no significant difference between groups in savings amount; this finding may be due to measurement limitations. \$aveNYC participants were less likely than comparison group members to have skipped paying bills or taken out a loan during the study period, and were more likely to have withdrawn money from savings. Findings suggest that tax-time savings programs can result in sustained emergency savings and prevent reliance on borrowing and unpaid bills.

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1. Introduction

\$aveNYC is a tax-time savings program based in New York City. The program was designed to encourage saving among tax filers at Volunteer Income Tax Assistance (VITA) sites, by offering them a matching incentive if they save a portion of their refunds for one year. The goal of the program is to promote short-term precautionary savings and increase financial security of low- and moderate-income (LMI) households.

Less than half of low-income households have \$500 in precautionary savings available in case of financial emergencies (Brobeck, 2008). At the same time, in recent years households are at increased risk of experiencing financial insecurity in the form of unemployment, medical emergencies, and other unexpected expenses (Hacker, 2007; Hacker et al., 2010). Tax-time savings programs are designed to leverage tax refunds into a stock of precautionary savings that may help low- and moderate-income households to smooth consumption and avoid financial ruin due to unexpected

expenses or income shortfalls. As one of the largest single checks many households receive all year, the tax refund represents a unique opportunity to set aside rainy day savings.

Tax-time savings programs such as Refund 2 Assets and the Extra Credit Savings Program have shown little long-term effect on savings volume (Beverly et al., 2001, 2006). However, evidence from \$aveNYC suggests that the program has the potential to increase both the likelihood of holding savings and the amount of savings (Key et al., 2012). This paper makes an important contribution to the limited literature on tax-time savings by attempting to replicate findings on the effect of \$aveNYC, using data from a more recent cohort of participants. In addition, we explore the effect of \$aveNYC on financial behaviors.

1.1. Review of literature

The personal saving rate in the U.S. has been declining since the 1980s, to a low of only 2 percent in the mid-2000s (Federal Reserve Bank of St. Louis, 2012). Although the Great Recession seems to have sparked increased saving in the early 2010s, savings levels remain low. In 2009, the median transaction account balance was \$4000, and less than 16 percent of households held certificates of deposit or bonds (Bricker et al., 2011). For low-income households (in the bottom quintile), median transaction account balance was

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only \$900, and the median value of all liquid assets was only \$1900 (Bricker et al., 2011). When asked to estimate their desired level of precautionary savings, respondents report a median value of \$5000 – more than the median account balance, and much more than the amount held by the lowest-income households (Bricker et al., 2012).

Savings can serve a variety of purposes, not the least of which is as a personal safety net in the event of unexpected expenditures or financial catastrophe. Unfortunately, LMI households, who are least likely to have precautionary savings, are also more likely to find themselves in a situation where such savings are necessary. One study, which used data from the Survey of Income and Program Participation, found that 11 percent of the sample had experienced some kind of material hardship (e.g., eviction, food insecurity, utility disconnection) during the year; for households below the poverty level, the incidence of material hardship was 36 percent (Beverly, 2001). For families that are barely getting by, events like unemployment or a shift to a female-headed household can spur a transition into poverty (McKernan and Ratcliffe, 2005). Even normative events like the addition of a new child to the household, can be associated with entry to poverty (McKernan and Ratcliffe, 2005).

For many of these events and hardships, a small stock of precautionary savings would suffice to help the household get through. However, without the availability of savings, households often turn to riskier methods of securing financial resources, such as incurring credit card debt or taking short-term loans. A study of the effects of transitory periods of unemployment on low-asset households found that these households increased their unsecured debt holdings during periods of reduced income (Sullivan, 2008). The majority (about two-thirds) of borrowers of payday loans take out the loans in response to unexpected expenses or an income shortfall (Lawrence and Elliehausen, 2008). Risky short-term solutions like these can lead to longer-term debt burdens. One national survey found that most payday loan borrowers took out more than 4 loans per year (Lawrence and Elliehausen, 2008). In other cases, households are able to ‘borrow’ money (interest-free) from family and friends (Edin and Lein, 1997). Although doing so does not increase formal debt loads or harm credit ratings, it can weaken communities because the borrower’s social network may no longer have money available to face their own hardships. If LMI households have some emergency savings set aside, they may be more likely to withdraw from savings, rather than borrow money, in order to get by.

The SaveNYC program aims to support LMI families in establishing small-dollar, short-term precautionary savings. Asset building research thus far has focused to a large extent on Individual Development Accounts (IDAs), demonstrating that even very low-income households can save when provided with institutional supports (Schreiner et al., 2001). Nevertheless, savings for low-income households are undeniably limited by income constraints, and amounts saved in IDAs are generally less than the cost of the investments for which participants are saving (such as a down payment for a home). For example, participants in the American Dream Demonstration averaged net monthly savings of about \$17, or \$558 in total across the entire program (Schreiner and Sherraden, 2005). SaveNYC and similar programs address some limitations of IDAs by focusing on short-term, unrestricted savings accounts, and funding them with tax refunds.

Because tax refunds are relatively large sums of money that are outside the usual flow of income, they have the potential to be put toward a variety of purposes that would not ordinarily be considered for regular income, including savings (Shefrin and Thaler, 1988; Romich and Weisner, 2000; Mammen and Lawrence, 2006). It is important to keep in mind, however, that most households have a plan for their tax refunds prior to filing their taxes

(Romich and Weisner, 2000; Mammen and Lawrence, 2006). These plans may include saving, paying down debt, or making major purchases that were not possible earlier in the year (Mammen and Lawrence, 2006). Households with children often report devoting their refunds to their children’s well-being, by putting the money toward school supplies, clothing, allowance, or family vacations (Romich and Weisner, 2000; Mammen and Lawrence, 2006).

Existing evidence on tax-time savings programs is mixed. The Refund 2 Assets program (R2A), which also offered savings accounts to tax filers at VITA sites, but without an incentive, found that there was no significant effect of the program on the average amount of refund saved 3–5 months later (Beverly et al., 2006). The Extra Credit Savings Program (ECSP), which served VITA filers as well, required participants to deposit their entire refund (Beverly et al., 2001). Although ECSP offered a 10 percent match to participants who had some funds remaining in the account at the end of the calendar year, they too found that after 3 months, the median account balance was less than 5 percent of the original refund amount.

On the other hand, research on an earlier cohort of SaveNYC participants found that the program was associated with a nearly \$300 increase in savings 6 months after participants were eligible for the match (Key et al., 2012). However, the study also found a moderating effect of children in the household, such that there was a large effect on savings for households without children, and no statistically significant effect for households with children. The authors of the study theorized that this finding is consistent with research showing that caregivers tend to spend refund money on their children (Romich and Weisner, 2000; Mammen and Lawrence, 2006); parents may save money in the SaveNYC account until they get the match, and then spend the money on their children, just as they would have done in the absence of the program.²

The evaluation of tax-time savings programs is complicated by the difficulty of defining precautionary savings, due to their temporary-but-not-too-temporary nature. For example, although the evaluation of R2A found no effect on average amount of refund saved 3–5 months later, the program had a 15 percent take-up rate and a median contribution of 39 percent of refund amount (Beverly et al., 2006). Almost 9 months later, 34 percent of participants still had some of their refund saved (Beverly et al., 2006). It is possible that account holders withdrew their money out of necessity, in order to address one of the financial emergencies mentioned above. In fact, in-depth interviews with participants in ECSP found that respondents withdrew their savings for purposes such as financing maternity leave, or getting through a spell of unemployment (Beverly et al., 2001). In these cases, the savings served their precautionary purpose.

Furthermore, existing evidence indicates that tax-time savings programs may generate precautionary savings that would not otherwise exist. For example, over 75 percent of R2A participants said that the program had helped them save more of their refund, spend the refund more slowly, and resist spending temptations (Beverly et al., 2006). Likewise, follow-up surveys with ECSP participants suggested that the program had helped them to spend their refunds

² For the analyses presented in this paper, we tested the moderating effect of having children in the household by using a children by treatment interaction term. We ran each regression model with and without an interaction term. For every outcome, the interaction term was not significant ($p > 0.11$ for all). In this cohort of SaveNYC participants, there was no evidence of a moderating effect of children in the household. We also compared the two groups on program use. There were no significant differences between the two groups with regard to the likelihood of withdrawing the money early, receiving the match, or saving or spending the match once it was received. There was also no difference in the amount of match money received. Among those who received and spent a portion of their match money, individuals with children were more likely to report that they had spent some money on household expenses (73% compared to 46%, $p < 0.05$).

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