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How Far Do Child Savings Accounts Stray From the Tax Code?: A Comparative Perspective

LORA CICCONI

I. INTRODUCTION

On February 28, 2007, California became the first state in the U.S. to propose "baby bond" legislation.[1] California Senate Bill 752 would give every child born in California a state-endowed savings account at birth.[2] The legislation was heavily criticized in the press immediately after it was unveiled; detractors attacked the bill as intervening in parenting and devaluing responsibility.[3] They questioned the fact that the $500 endowment was not means-tested and would benefit children of illegal immigrants.[4] One of the

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1. *See* S.B. 752, 2007-08 Leg., Reg. Sess. (Cal. 2007); Ryan Orr, *Nest Egg of $500 Proposed for Newborns*, DAILY PRESS (Victorville, CA), Mar. 2, 2007; Jim Sanders, *Proposal Would Give Cash to All Newborns*, SACRAMENTO BEE, Feb. 28, 2007.

2. *See* S.B. 752; Orr, *supra* note 1; Sanders, *supra* note 1.

3. Orr, *supra* note 1 (quoting Assemblyman Anthony Adams as stating, the "government is trying to take over every aspect of parenting" and Rick Piercy, founder and CEO of the Lewis Center for Educational Research as stating that people "learn the value of money by working for money"). *See also, e.g.*, Deborah J. Saunders, Editorial, *On Taxpayer-Funded Savings Accounts*, SAN. FRAN. CHRON., Mar. 11, 2007, at E5; George Skelton, *In the Political Murk Lurk a Few Really Foggy Ideas*, L.A. TIMES, Mar. 15, 2007, at B3.

4. Daniel Weintraub, *Immigration an Issue About More Than Just Facts*, SACRAMENTO BEE, Mar. 6, 2007, at B7 ("As soon as Steinberg and Dutton introduced the measure, a backlash erupted on the right. Not just to the idea of giving every child $500. But to the idea that a lot of the children would be the children of illegal immigrants."). State Senator Tom McClintock, a Republican from the San Fernando Valley, started an email campaign against the bill, stating that it would create incentives for "a new wave of illegal immigration." *Id.*

bill's original supporters withdrew his support of the bill just two days after it was introduced, reportedly responding to pressure from fellow Republicans.[5]

Despite the outraged responses of some critics, the proposed California legislation differs little in principle from laws Congress has considered at the federal level, and closely resembles existing policy in Britain and Canada.[6] In this paper, I examine the tax aspects of what are commonly termed "Child Savings Accounts" (CSAs).[7] In Part II, I look at CSAs as they currently exist in Britain, Canada, Singapore, Hungary and Korea, and as proposed in the United States. After examining the academic literature on the subject in Part III, I compare CSAs in other parts of the world and CSA proposals with existing provisions in the U.S. Tax Code (the "Code" or "Tax Code") in Part IV.

The goal of this exercise is not to advocate a particular form of CSA, but merely to illustrate the similarities and differences between our Tax Code and CSA legislation. This analysis suggests that some of these child savings proposals share much in common with current tax savings provisions in the Code when considering simple facets of the legislation such as tax-free growth, tax-free contribution, or withdrawal for specified uses. However, existing CSAs, and especially some of the academic proposals, drift further and further from the current tax code as additional facets are considered, such as lump-sum government subsidies, matching grants, and progressive schemes. To the extent that this paper helps discern the point at which CSAs and the current Code diverge, perhaps it will shed light on the political factors that have prevented CSA legislation from becoming law in America.

II. WHAT ARE CHILD SAVINGS ACCOUNTS AND WHAT DO THEY LOOK LIKE?

A. Overview

Child Savings Accounts may take a variety of forms, but broadly the term refers to a policy that encourages families to build assets for their children at

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5. *Dutton Rethinks Nest Egg Bill*, DAILY PRESS (Victorville, Cal.), Mar. 6, 2007; *Lawmaker Ditches Bill Giving Kids $500 Each*, VENTURA COUNTY STAR (Cal.), Mar. 4, 2007. A week after the California bill was proposed, the state of Oregon proposed a similar bill, with a smaller recommended state deposit of $200 per child for education expenses. H.B. 2790, 74th Leg., Reg. Sess. (Or. 2007). The Oregon bill was received far more favorably, and the issue of funding the children of illegal immigrants did not arise during the legislative hearing. *See* Bill Graves, *Tuition Jump-Start: $200 a Baby*, OREGONIAN (Portland, Or.), Mar. 8, 2007.

6. *See generally* Vernon Loke & Michael Sherraden, *Building Assets From Birth: A Comparison of the Policies and Proposals on Children Savings Accounts in Singapore, the United Kingdom, Canada, Korea, and the United States* (Wash. U. Ctr. for Soc. Dev., Working Paper No. 06-14, 2006), *available at* http://gwbweb.wustl.edu/csd/Publications/2006/WP06-14.pdf (describing various child savings schemes in existence across the world, as well as federal proposals in the U.S.).

7. Here I borrow from Loke and Sherraden's terminology. *Id.* at 1.

birth.[8] Most of the existing CSAs include a state-funded deposit at birth, coupled with savings incentives for family members to contribute to the child's account, such as tax breaks or matching programs.[9] Most countries impose severe restrictions on when account holders can make withdrawals, usually disallowing distributions until account holders reach age eighteen and restricting distributions to certain purposes, though some give the account holder more freedom.[10] Much of the legislation appears to be fueled by a desire to give children a chance at a healthy financial future upon reaching adulthood and improve the financial literacy and savings behavior of lower-income families. This is not always the case though, as some nations have developed these policies to expand access to higher education, and others have done so in an effort to increase birth rates.[11]

B. Existing and Proposed Child Savings Legislation Across the Globe

1. The United States

i. California Proposal

California legislators proposed the KIDS Account Act in an effort to increase asset ownership in the state—a high priority in California which has the fourth highest "asset poverty" rate in the nation.[12] The law would create a savings account for every child born in California on or after January 1, 2008 and make an initial $500 deposit into the account at birth.[13] The account would grow tax-free[14] until the child reached age eighteen, at which point the funds could be distributed, also tax-free, for three special purposes: higher education, home purchases, or retirement.[15] Withdrawals made before age eighteen, or for purposes other than those described above, would be subject to ordinary income tax, a 10% penalty, and the state's initial $500 deposit

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8. *Id.*
9. *See* Loke & Sherraden, *supra* note 6.
10. *Id.*
11. *Id.* at 3-13; *infra* notes 26-111.
12. The authors cited pilot programs across California and the U.S., which have shown that low-income people save when they have the correct incentives, and also argued that the law would help build financial literacy in California and improve California's economy because individuals who own assets lead more productive lives. S.B. 752, 2007-08 Leg., Reg. Sess. (Cal. 2007).
13. *Id.*
14. All references to tax in Part II.B.1.i refer only to state taxes. The bill does not discuss whether the KIDS Account is exempt from federal as well as state income taxes, though it does refer to certain sections of the Internal Revenue Code to govern distributions. *See id.*
15. *Id.*

would be withheld from distribution.[16] The child himself, along with his parents, legal guardians, grandparents, local organizations, or corporations could make voluntary contributions with after-tax funds to this account until the child reached eighteen.[17] The estimated cost of the California law is $270 million, approximately 0.3% of California's $100 billion yearly budget.[18]

ii. Oregon's Proposal[19]

A week after California legislators presented the California KIDS Account Act, legislators in the state of Oregon introduced a similar bill.[20] Oregon House Bill 2790 would award a grant of $100 to each parent in Oregon to establish an Oregon 529 education savings account.[21] The bill's sponsor stated that he planned to amend the bill so that once parents contributed $20, the state grant would increase to $200.[22] Parents would have to contribute at least $180 over the next two years or lose the state funds.[23] Because the funds would be deposited in a 529 education savings account, contributions would be after-tax, but the funds would grow free of both federal and state tax and could be withdrawn tax-free if used for education purposes.[24] The bill's author believed the legislation would help Oregonians save for college, and estimated that the law would cost Oregon taxpayers approximately $5 million per year.[25]

iii. Federal Proposals

Though the California KIDS Account Act was the first state legislation to propose a government-funded child savings account in the U.S., several

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16. *Id.*

17. S.B. 752, 2007-08 Leg., Reg. Sess. (Cal. 2007).

18. *Id.*

19. The California and Oregon bills bring up state and local taxation issues that are beyond the scope of this paper, which merely seeks to compare different types of legislation on very basic levels, such as tax treatment at contribution, growth, withdrawal, use restrictions at withdrawal, direct state funding, and progressivity.

20. H.B. 2790, 74th Leg., Reg. Sess. (Or. 2007).

21. *Id.* Like every state in the U.S., Oregon has a 529 Savings Plan which encourages families to save for higher education with a number of state and federal tax incentives. A 529 account is a state-sponsored education savings account that meets certain federal guidelines under section 529 of the Internal Revenue Code to qualify for tax-exempt growth and withdrawal for education purposes. *See* I.R.C. § 529 (2006). The specifics of 529 accounts are discussed in more detail in Part IV.B.

22. Graves, *supra* note 5.

23. *Id*.

24. I.R.C. § 529 (2006); Graves, *supra* note 5. The Pension Protection Act of 2006 eliminated the sunset provision in I.R.C. section 529 which would have disallowed tax-free withdrawals after 2010. James Pethokoukis, *A College Savings Plan with One Less Worry*, N.Y. TIMES, Sept. 17, 2006, at 5.

25. Graves, *supra* note 5.

similar federal bills have been introduced over the last twelve years, though none have become law.[26] The first major legislation was proposed in 1995 by Senators Bob Kerrey (D-Neb.) and Joe Lieberman (D-Conn.). The Senators proposed KidSave accounts, which would provide parents with refundable child tax credits to place into savings accounts for children under the age of seventeen.[27] Funds in the KidSave accounts would be available penalty-free for the children if used for educational expenses or retirement.[28] The KidSave legislation was not enacted, though a similar bill introduced in 1997 made it through a bipartisan Senate,[29] and a scaled-down version of it resurfaced in President Clinton's tax proposal that same year.[30]

In 1998 Kerrey and Lieberman, along with Senators John Breaux (D-La.) and Daniel Moynihan (D-N.Y.) proposed the KidSave accounts again, but this time it was framed within the social security system.[31] Senate Bill 2184 proposed opening a $1,000 individual retirement account for each child at birth, with an additional $500 contributed by the government for each of the first five years of the child's life.[32] Once the recipients began working, they could contribute 2% of their payroll withholdings into the retirement account.[33] The money could only be withdrawn free of penalty at retirement.[34] The

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26. The U.S. is the only economically developed nation in the world that does not provide direct monetary support to families with children. Background Information on Children's Savings Accounts, United States and KIDS Accounts, http://www.results.org/website/article.asp?id=838 (last visited Sept. 26, 2007).

27. *Id.*

28. David J. Peterson, Editorial, *Federal Lawmakers Must Forget Budget-Busting Tax Reductions: Getting Our Fiscal House in Order Is Far More Vital*, PORTLAND PRESS HERALD (Me.), Dec. 5, 1995, at 13A.

29. *See* S. 949, 105th Cong. § 101 (1997); Clay Chandler, *Clinton's Education Tax Cut Revisions Gain Little Support; Legislators of Both Parties See President's Package as Stumbling Block for Budget Bill*, WASH. POST, June 5, 1997, at A6; Clay Chandler, *Key Senate Democrats Backing Roth Tax Bill; Shifts Complicate White House Strategy*, WASH. POST, June 17, 1997, at A4; Matthew Miller, *A Stake in Every Pot*, N.Y. TIMES, Jan. 31, 1999, at 16 (noting that Kerrey's KidSave account made it through the Senate in 1997).

30. Donald Lambro, Commentary, *Ready to Deal on Tax Cuts?*, WASH TIMES, Jul. 3, 1997, at A14 ("[Clinton] endorsed 'Kidsave' tax-deferred savings accounts to help parents save for their kids' college costs."). In addition to the KidSave Accounts, other CSA legislation was also proposed in 1996 and 1997. Legislators in the House proposed The Children's Financial Security Act which would have established retirement accounts for children funded with $1,000 by the Treasury. The retirement accounts would have functioned essentially like IRAs. *See* H.R. 4253, 104th Cong., (1996); H.R. 194, 105th Cong., (1997). The legislation did not pass, and unlike the KidSave Accounts, was not reintroduced in later years.

31. *See* Social Security KidSave Accounts Act, S. 2184, 105th Cong. (1998). Kerrey had proposed a similar bill in 1997; Breaux, Moynihan and Lieberman added their support in 1998.

32. *Id.*; Press Release, U.S. Senator Bob Kerrey, How to Make Every Child in America Wealthy, Guaranteed (June 17, 1998) [hereinafter Kerrey Press Release June 1998].

33. Kerry Press Release June 1998, *supra* note 32.

34. *Id.* This concept was similar to an earlier savings initiative proposed by Kerrey a few years earlier which did not involve any direct government funding; in 1994 Kerrey had supported personal

sponsors argued that their proposal would help combat growing wealth inequality by helping the poor build assets, and would ensure that "every baby in America would enter life owning a piece of their country."[35] Despite the new social security framework, the bill failed to pass.[36]

In 1999 and 2000, legislators from both the Republican and Democratic parties proposed CSA bills in the 106th Congress, several of which were within Kerrey's social security framework.[37] The most noteworthy of these was Judd Gregg's (R-N.H.) and John Breaux's (D-La.) Bipartisan Social Security Reform Act, proposed in both 1999 and 2000.[38] The bill was mainly a social security reform plan, directing 2% of payroll taxes into individual retirement accounts, but it also included the establishment of Kerrey's KidSave accounts with $3,500 of designated government funds deposited over the first five years of a child's life.[39] Though the bipartisan social security proposal garnered support in the Senate[40] and generated positive press coverage,[41] the concept of KidSave accounts failed again in both 1999 and 2000.[42]

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investment plans to supplement social security, funded by cutting payroll taxes by 2%. *See* Press Release, U.S. Senator Bob Kerrey, Kerrey Applauds Breaux-Gregg Social Security Bill (July 15, 1998) (including timeline on social security reform and mentioning that Kerrey first proposed social security reform in 1994 with personal savings accounts) [hereinafter Kerrey Press Release July 1998].

35. William M. Welch, *Dem Plan Would Start Retirement Accounts for Babies*, USA TODAY, Jun. 18, 1998; Kerrey Press Release June 1998, *supra* note 32.

36. *See* The Library of Congress S. 2184 Bill Status, http://thomas.loc.gov/cgi-bin/bdquery/z?d105:SN02184:@@@X (last visited Oct. 2, 2007) (noting that the bill was read twice and referred to the committee on Finance on June 17, 1998, at which point no further action was taken).

37. *See* Bipartisan Social Security Reform Act of 1999, S. 1383, 106th Cong. (1999) (proposed by Judd Gregg (R-N.H.) and John Breaux (D-La.)); Bipartisan Social Security Reform Act of 2000, S. 2774, 106th Cong. (2000) (proposed by Gregg and Breaux); Social Security KidSave Account Act, S. 3200, 106th Cong. (1999) (proposed by Kerrey and Moynihan). *See also* Social Security Solvency Act of 1999, S. 21, 106th Cong. (1999) (proposed by Moynihan and Kerrey; KidSave accounts included within broader plan for social security reform). Also in 1999, Senator Bill Frist (R-Tenn), proposed the Child Savings Account Act, which would have allowed people to establish child savings accounts within Roth IRAs. S. 1013, 106th Cong. (1999). The bill gained no traction and did not receive as much press as the Bipartisan Social Security Reform Act.

38. S. 1383; S. 2774. Though Kerrey proposed his own bill, *see* S. 3200, he signed on to the Bipartisan Social Security Reform Act, which included his KidSave concept and received more legislative support as well as press attention. S. 1383; S. 2774.

39. S. 1383; S. 2774.

40. In addition to Senator Kerrey, Senators Chuck Grassley (R-Iowa), Fred Thompson (R-Tenn.), Chuck Robb (D-Va.), and Frank Thomas (R-Wyo.) supported the bill. S. 1383; S. 2774.

41. *E.g.*, David C. John, Editorial, *KidSave: An Innovative Step Toward Better Retirement Security*, HERITAGE FOUNDATION REPORTS, Oct. 27, 2000 (citing the positives of the KidSave plan including the fact that it is a loan, not a grant); Editorial, *Kid Save: An Investment in American Children's Financial Security*, HOUS. CHRON., Dec. 11, 2000, at A24; Matthew Miller, *KidSave: A Stakeholder at Price We Can Afford*, TIMES UNION (Albany, N.Y.), Mar. 8, 1999, at A7; Norman Ornstein, Editorial, *Like My Sons, Young Investors Deserve Stake in Future*, USA TODAY, Dec. 7, 1998, at 25A.

42. *See* Phillip Brownlee, *So When Will Congress Act on Social Security?*, RECORD (N.J.), Mar. 17,

The most recent version of a child savings account bill comes in the form of the Americans Savings for Personal Investment, Retirement, and Education Act, also known as the ASPIRE Act.[43] First introduced in the 108th Congress in 2004 by Senators Rick Santorum (R-Pa.), John Corzine (D-Tenn.), Patrick Kennedy (D-Mass.), and Thomas Petri (R-Wis.), the original ASPIRE Act looked more like Kerrey's early KidSave proposals.[44] No longer housed within the payroll tax system, the bill would give each child born in the U.S. a $500 savings account at birth, with low income families eligible for an additional $500.[45] The legislation would provide incentives for parents to contribute to the account, and funds could be used for post-secondary education at any time, or put towards retirement or a home purchase after the child reached age eighteen.[46]

The ASPIRE Act failed to pass,[47] but was reintroduced in the 109th Congress in 2005.[48] The 2005 version of the bill was essentially the same as the 2004 bill, with $500 initial deposits for all children and up to $1,000 for children of low income parents.[49] Parents could make after-tax contributions of up to $1,000 (Senate bill) or $2,000 (House bill) and receive dollar-for-dollar matching funds from the government of up to between $500 (Senate bill) and $1,000 (House bill) per year if they met certain means tests.[50] When the child reached age eighteen, the account would essentially be treated as a Roth IRA.[51] The government contributions would be repaid beginning when

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2000, at L11 (describing Kerrey's frustration that social security reform fell by the wayside once again); Library of Congress S. 3200 Bill Status, http://thomas.loc.gov/cgi-bin/bdquery/z?d106:SN03200:@@@X (last visited Oct. 4, 2007) (bill introduced and read twice in October of 2000; no further action taken).

43. *See* ASPIRE Act of 2004, S. 2751, 108th Cong. (2004). *See also* companion legislation H.R. 4939, 108th Cong. (2004).

44. *See* S. 2751; H.R. 4939. At this point Bob Kerrey, who had led earlier efforts for child savings accounts, was no longer in office.

45. S. 2751; H.R. 4939; *National Children's Savings Proposal Introduced Today; Local Organization Already Testing the Impact of Similar Accounts on Children and Families*, U.S. NEWSWIRE, Jul. 22, 2004 [hereinafter *National*].

46. *E.g.*, S. 2751; H.R. 4939; *National*, *supra* note 45.

47. *See* Library of Congress H.R. 4939 Bill Status, http://thomas.loc.gov/cgi-bin/bdquery/z?d108:HR04939:@@@X (last visited Oct. 5, 2007) (bill was introduced in July, 2004 and was not acted upon after that month); Library of Congress S. 2751 Bill Status, http://thomas.loc.gov/cgi-bin/bdquery/z?d108:SN02751:@@@X (last visited Oct. 5, 2007) (bill was introduced in July, 2004 and was not acted on after that month).

48. *See* ASPIRE Act of 2005, S. 868, 109th Cong. (2005) (introduced by Santorum, Corzine, Schumer, and Demint). *See also* companion bill H.R. 1767, 109th Cong. (2005) (introduced by Ford, Kenney, and English).

49. *See* S. 868; H.R. 1767.

50. *See id.*

51. *See id.* The law would allow tax-free withdrawal for approved purposes such as post-secondary education or home purchases. In addition to the 10% penalty for disqualified distributions under the Roth

the account holder reached age thirty.[52] Even though the bill garnered considerable positive press coverage[53] and was discussed at a Congressional hearing regarding building assets for low-income Americans,[54] the 109th Congress adjourned without taking any action on it.[55]

No member of the 110th Congress has reintroduced the ASPIRE Act. However, Congressman Jerry Weller (D-Ill.) reintroduced Kerrey's social security KidSave accounts again this past January.[56] In addition, Senator and Presidential Candidate Hillary Rodham Clinton recently called for the implementation of child savings accounts in a speech to the New America Foundation,[57] and earlier this year, a panel of mayors advocated a lifetime savings account for every child born in the U.S. beginning with a $500 deposit as a poverty-fighting strategy.[58]

IRA, however, any government contributions would be forfeited completely if the withdrawal were used for nondesignated purposes.

52. S. 868; H.R. 1767. Also during 2005, Congressman Jerry Weller (D-Ill.) attempted to revive Kerrey's social security KidSave accounts. *See* Social Security KidSave Accounts Act, H.R. 1041, 109th Cong. (2005). In addition, Senator Max Baucus (D-Mont.) proposed Young Saver's Accounts as part of his IRA reform, whereby parents would be able to direct IRA funds into accounts for their children. *See* Savings Competitiveness Act of 2006, S. 2431, 109th Cong. (2006). Similarly, Representative Clay Shaw (R-Fla.) proposed a law that would convert Coverdell savings accounts into 401Kids Savings Accounts, which would have expanded uses and could be rolled over into a Roth IRA. *See* 401Kids Family Savings Act, H.R. 5314, 109th Cong. (2006).

53. *See e.g.*, Ray Boshara, Editorial, *Share the Ownership*, WASH. POST, Feb. 8, 2005, at A23; David Brooks, Editorial, *Mr. President, Let's Share the Wealth*, N.Y. TIMES, Feb. 8, 2005, at A25; Julie Kosterlitz, *The Other Ownership Society*, NAT'L J. (Wash., D.C.), Mar. 5, 2005.

54. *See Building Assets for Low-Income Families: Hearing Before the Subcomm. on Soc. Sec. and Family Policy of the S. Fin. Comm.*, 109th Cong. (2005), *available at* http://www.senate.gov/~finance/hearings/statements/042805rs.pdf (statement of Rick Santorum).

55. *See* Library of Congress S. 868 Bill Status, http://thomas.loc.gov/cgi-bin/bdquery/z?d109:SN00868:@@@X (last visited Oct. 5, 2007) (bill was introduced in April, 2005 and was not acted upon after that month).

56. *See* Social Security KidSave Accounts Act, H.R. 242, 110th Cong. (2007) (like Kerrey's 1999 proposal, this legislation includes a $2,000 loan at birth into every child's social security account, would allow contributions of up to $500 per year. 401Kids Family Savings Act, H.R. 87, 110th Cong. (2007)).

57. Morton M. Kondracke, *"Income Insecurity" Emerges as Leading Issue in '08 Campaign*, ROLL CALL (Wash., D.C.), Feb. 8, 2007.

58. Rick Orlov, *Mayors Get Plan to Boost Middle Class; Strategy Would Get Feds Involved, Provide Savings for Kids' Education*, DAILY NEWS (L.A.), Mar. 22, 2007, at N4. Part III.A.1 of this paper discusses Michael Sherraden's proposal for Individual Development Accounts (IDAs), similar in substance to Child Savings Accounts, though broader in that they are not limited to children. *See infra* notes 118-134. A discussion of how IDAs have fared at the federal level in the U.S. is beyond the scope of this paper, but it is worth noting that while IDAs have not been enacted on a federal level, they were considered in various forms, including the Savings for Working Families Act which was introduced in the 106th, 107th, 108th, 109th, and 110th Congresses. IDAs were endorsed by Presidents Clinton and Bush, and were accorded some federal funding in the Assets for Independence Act, which grants money to nonprofit organizations to develop IDA programs. *See* Michael Sherraden, *Assets and Public Policy*, *in* INCLUSION IN THE

2. *Britain*

The concept of CSAs first received attention in Britain in 2000 when a study by the Institute for Public Policy recommended that the state give every child GDP£1,000 either at birth or at age eighteen, which would be available to them for higher education expenses, starting a business, or purchasing a first home.[59] Influenced by the think tank's plan, Prime Minister Tony Blair unveiled a universal CSA plan a year later[60] proposing that the government place GDP£500 in a child savings account for each child at birth, but limiting the wealthiest families to only half that amount.[61] Blair argued that the CSAs would reduce child poverty, help poorer families learn to save, provide every child with a financial stake in the country, and teach children the importance of saving.[62] Commentators noted that it built upon Margaret Thatcher's vision of a "property-owning democracy."[63]

Blair's plan was received mostly favorably[64] and CSAs became law in late 2003.[65] Currently, each child born in Britain on or after September 1,

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AMERICAN DREAM: ASSETS POVERTY, AND PUBLIC POLICY 3, 10-12 (Michael Sherraden, ed. 2005). *See also* Mark Schreiner et al., *Assets and the Poor: Evidence from Individual Development Accounts, in* INCLUSION IN THE AMERICAN DREAM: ASSETS POVERTY, AND PUBLIC POLICY 185, 187 (Michael Sherraden, ed. 2005). RAY BOSHARA, NEW AMERICA FOUNDATION, FEDERAL POLICY AND ASSET BUILDING 1-2 (2004), *available at* http://www.newamerica.net/files/archive/Pub_File_1291_1.pdf; *Building Assets for Low Income Families: Hearing Before the Subcomm. on Soc. Sec. and Family Policy of the S. Fin. Comm.*, 109th Cong. (2005), *available at* http://www.senate.gov/~finance/hearings/testimony/2005test/mstest042805.pdf (statement of Michael Sherraden).

59. Nicholas Timmins, *Call for State to Give Children Pounds 1,000 "Bond,"* FINANCIAL TIMES (London), Feb. 14, 2000, at 5. The researchers argued that the plan, which also called for matched parent contributions, would help bridge the widening gap between rich and poor in the nation, and reasoned that it could be funded by an inheritance tax. *Id.*

60. *E.g.*, David Hughes, *Labour Plans a GBP 250 Giveaway for Every Baby; Cash Bond Will Double for Children of Poorer Families*, DAILY MAIL (London), Apr. 26, 2001, at 2; Roland Watson & Melissa Kite, *Blair Promises Cash Gift to Invest in Every Baby's Future*, TIMES (London), Apr. 26, 2001.

61. *Id.* Parents could add funds which the government would match, and the accounts would grow tax-free. James Hardy & Oonagh Blackman, *Pounds 400 for Every Child in Britain*, MIRROR, Apr. 26, 2001; Hughes, *supra* note 60.

62. Hughes, *supra* note 60; Watson & Kite, *supra* note 60.

63. Hughes, *supra* note 60.

64. *E.g.*, Bruce Ackerman & Anne Alstott, *Tony Blair's Big Idea*, N.Y. TIMES, May 6, 2001, at 15 ("Tony Blair is the first major world leader to put stakeholding where it belongs—at the top of the list of political priorities."); Will Paxton, *Britain's Innovative "Baby Bond" Plan Advances Debate on Fighting Poverty*, AMERICAN BANKER, May 11, 2001, at 12 ("Reaction to the proposals in the media and among the public has generally been positive."). There was some criticism as well. *See, e.g.*, Edward Heathcoat Amory, *Welcome to Government by Gimmick; CDs for Yobs, Bank Accounts for Babies and a Calf that Decided Labour Policy*, DAILY MAIL (London), Apr. 27, 2001, at 12; J. Fletcher, *The Big Issue: Worthless Bit of Electioneering; Baby Bonds*, BIRMINGHAM EVENING MAIL, May, 3, 2001, at 11.

65. Michael White, *Blair Goes Looking for a Fight and a Third Term*, GUARDIAN (Manchester), Nov. 27, 2003, at 1.

2002 receives GDP£250 from the government which is placed in a Child Trust Fund; lower income families receive GDP£500 per child.[66] Parents can elect a provider to manage the fund, otherwise the government chooses one after a year.[67] When the child reaches age seven, the government makes another payment, again either GDP£250 or GDP£500, depending on the income level.[68] Parents, family members, and friends can contribute up to GDP£1,200 each year with after-tax funds, though these contributions are not matched.[69] The money grows tax-free until the child reaches age eighteen, at which point he or she receives the money without restriction and it becomes subject to normal tax rules.[70] Beginning in April 2007, foster children receive an additional GDP£100 for each year that they are in the state's care.[71]

Though the Child Trust Fund plan was launched only two years ago, the government has already deemed it a success, relying on research suggesting that the policy has increased savings behavior.[72] However, there is concern that low-income families are not participating in the program at the same levels as wealthier families.[73]

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66. *Tax Glossary*, FINANCIAL TIMES (London), Mar. 5, 2007, *available at* http://search.ft.com/ftArticle?queryText=tax+glossary&y=13&aje=true&x=6&id=070305006295&ct=0.

67. Child Trust Fund—Who Can Open an Account?, http://www.childtrustfund.gov.uk/templates/page____1240.aspx (last visited Oct. 6, 2007).

68. *Tax Glossary*, *supra* note 66.

69. *Id.* This is in contrast to the think tank's plan and Blair's original proposal. *See* Timmons, *supra* note 59; Hughes, *supra* note 60.

70. Child Trust Fund—Key Facts About the Child Trust Fund, http://www.childtrustfund.gov.uk/templates/Page____1177.aspx (last visited Oct. 6, 2007); Email from Child Trust to Lora Cicconi (Mar. 30, 2007) (on file with author) ("[w]hen the child reaches [eighteen] the fund will become subject to normal tax rules for savings and investments").

71. Child Trust Fund—Announcement on Extra Payments to Children in Care, http://www.childtrustfund.gov.uk/templates/page____1356.aspx (last visited Oct. 6, 2007). In addition to the Child Trust Fund program, Britain is experimenting with a pilot savings initiative which matches funds that poor families save up to a limit. *See* Sherraden, *supra* note 58, at 13.

72. *Ed Balls Launches Child Trust Fund Week*, GOVERNMENT NEWS NETWORK, Jan. 15, 2007 (Economic Secretary to the Treasury, Ed Balls, stated that "The Child Trust Fund's success has exceeded our expectations."). Less than a year after the program was implemented, nearly half of the parents surveyed stated that the Child Trust Funds would encourage them to save more than they otherwise would. *See* Elaine Kempson et al., *Saving for Children: A Baseline Survey at the Inception of the Child Trust Fund* 119 (2006), *available at* http://www.pfrc.bris.ac.uk/publications/pensions_savings/Reports/Saving_for_children_report.pdf.

73. *Farrow's View: Child Benefit*, MONEY MARKETING, Feb. 1, 2007 (While the Child Trust Funds have been successful in increasing savings, "when all is said and done, there seems little doubt that the CTF is missing its target audience—those on low incomes—by a country mile. Figures by the Treasury show that the take-up rate has been significantly lower in deprived areas, where children stand to benefit the most."). *Id.* Some parents have also raised concerns about certain aspects of the program, such as the fact that children born before the Trust Fund was initiated do not benefit from it. *See generally* Rajiv Prabhakar, *Attitudes Towards the Child Trust Fund: What Do Parents Think?* (Wash. Univ. Ctr. for Soc. Dev.,

3. Canada

In early 2004, Canadian Prime Minister Paul Martin proposed a "learning bond" to help low-income families save for education.[74] Concerned that poorer families were unable to take advantage of matching grants for families that contributed to tax-deferred Registered Education Savings Plans (RESPs), the Prime Minister proposed that the government make initial deposits into the accounts of children from low-income families.[75] The learning bond was announced in the March 2004 budget and currently provides families who receive the National Child Benefit—a means-tested welfare program—with initial state deposits of C$500 into the RESP accounts of their children born after 2003.[76] Families receive C$100 contributions each year until the child reaches age fifteen so long as they continue to receive welfare.[77] Parents can make after-tax contributions to the account, which are generously matched. The government matches up to 40% of a low-income family's RESP contributions up to C$500 per year, and matches 20% of contributions of up to C$2,500 for all families.[78] The RESP accounts, including the amount contributed from the Learning Bond, grow tax-free until distribution.[79]

The Learning Bond funds are intended to be used for higher education, and the tax and penalty schemes at withdrawal reflect this preference. If the recipient attends post-secondary education, he or she receives Educational Assistance Payments from his or her RESP. Though EAPs are taxed at normal levels, most recipients pay little or no tax when they receive the EAP income because they are in low tax brackets at the time of distribution.[80] Moreover,

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Working Paper No. 06-10, 2006), *available at* http://gwbweb.wustl.edu/csd/Publications/2006/WP06-10.pdf.

74. Heather Scoffield, *PM's Promises Weighing on Goodale; Throne Speech Initiatives Leave Finance Minister Little Flexibility*, GLOBE AND MAIL (Toronto), Feb. 4, 2004, at A7.

75. Philip Fine, *Learning Bonds to Kick-Start Saving for Tuition Fees*, TIMES HIGHER EDUC. SUPPLEMENT (London), Feb. 20, 2004, at 14.

76. Loke & Sherraden, *supra* note 6, at 8-9.

77. Ellen Roseman, *Learning Bond Sets Course for Low-Income Families*, TORONTO STAR, Mar. 24, 2004, at C1.

78. *Id.*; Ellen Roseman, *Tax Breaks Score Well on Impact, Relevance*, TORONTO STAR, Mar. 21, 2007, at F05. Previously, all families who contributed to their child's RESP—regardless of income level—received a grant equal to 20% of their own contribution up to C$2,000, a benefit that largely went to affluent families. *Id.* The C$2,000 limit was just increased to C$2,500 this year, though the lifetime limit on the matching funds is still C$7,200 which is equivalent to eighteen years of C$400 matching funds per year. *Id.*

79. Rob Carrick, *Hats Off to the New and Improved RESP*, GLOBE AND MAIL (Toronto), Mar. 24, 2007, at B9; Registered Education Savings Plan (RESP)—Frequently Asked Questions, http://www.hrsdc.gc.ca/en/hip/lld/cesg/publicsection/faq_resp.shtml (last visited Oct. 6, 2007).

80. *See* email from Canada Education Savings Program to Lora Cicconi (Apr. 20, 2007) (on file with author) ("EAPs are the property of the beneficiaries and are taxable income. However, as the beneficiaries

the EAP consists only of government funds and the earnings in the RESP account.[81] The amount that the family contributed to the child's RESP may be withdrawn tax-free.[82] If the account beneficiary never attends college, the full amount of the funds may be transferred to another child in the family.[83] However, if the parents withdraw the funds or roll them over into their retirement account, then the income is taxed at various rates, and all government deposits—but not earnings on those deposits—must be returned to Canada.[84]

The concept of learning bonds was generally well-received by the Canadian press,[85] and early evidence suggests that many families have taken

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are students and making little or no income at the time, they rarely pay any significant amount of taxes on this amount.").

81. *See* email from Canada Education Savings Program to Lora Cicconi (Apr. 30, 2007) (on file with author) ("Educational Assistance Payments (EAPs) are amounts paid from an RESP (Earnings + CESG + CLB + Alberta Grant) to an eligible beneficiary to assist with education-related expenses at the post-secondary school level. The accumulated interest is earned from the investments of both the grant and the contributions in the RESP.").

82. *See* email from Canada Education Savings Program to Lora Cicconi (Apr. 20, 2007) (on file with author) ("RESP contributions are the property of the subscriber and are tax sheltered. The contributions will not become income for tax purposes when withdrawn from the plan even if it is giving [sic] to the beneficiary."). But note that earnings on RESP contributions are taxable. *See infra* note 84.

83. *See* CANADA LEARNING BOND BROCHURE, at 6, *available at* http://www.hrsdc.gc.ca/en/hip/lld/cesg/publicsection/files/CLB-E-brochure.pdf; Registered Education Savings Plan (RESP)—Frequently Asked Questions, Human Resources and Social Development Canada, http://www.hrsdc.gc.ca/asp/gateway.asp?hr=en/hip/lld/cesg/publicsection/faqs_resp.shtml&hs=cgs (last visited Oct. 8, 2007).

84. *See* email from Canada Education Savings Program to Lora Cicconi (Apr. 20, 2007) (on file with author) ("Should a child decide never to pursue a post-secondary education, a subscriber has the option of transferring the earnings into a Registered Retirement Savings Plan (RRSP) or that of a spouse, or withdraw the money, subject to various tax rates. Under all these circumstances, the grant is returned to the Government of Canada, but the interest earned on the original contributions and on the grant remains the subscriber's. The contributions themselves are always the property of the subscriber(s) and not the beneficiary."). Similarly, if the RESP is not used or withdrawn within twenty-six years, the amount the parents saved is returned to them, and the money the government contributed via the learning bond or matching funds is returned to Canada. *See* CANADA LEARNING BOND BROCHURE, *supra* note 83, at 6.

85. *See, e.g.*, Carol Goar, Editorial, *Budget Contains One Bright Gem*, TORONTO STAR, Mar. 26, 2004, at A22; Simon Tuck, *Aid for Low-Income Eases a Single Mother's Fears*, GLOBE AND MAIL (Toronto), Mar. 24, 2004, at A1. On the other hand, some argued that the small amount of the bond would do little for poor students, *see* Nathan Greenfield, *University Bond Gives Poor Students a Start*, TIMES EDUCATIONAL SUPPLEMENT (London), Apr. 2, 2004, at 17, and that the money would be better spent at the post-secondary level, *see* Alan Caplan, *RESPs are OK but Funding Better Spent at Post-Secondary Level*, EDMONTON SUN, Apr. 3, 2004, at 66. There was also concern that the Learning Bond funds would affect lower-income families' welfare qualifications, *see* Ellen Roseman, *We Need This Education Review*, TORONTO STAR, May 19, 2004, at E06, but the government appears to have resolved this issue. *See* CANADA LEARNING BOND BROCHURE, *supra* note 83, at 6 (Canada Learning Bond will not affect other Canadian benefits).

advantage of it, though more families could be benefiting.[86] In addition, Canadian provinces have expressed an interest in contributing to child savings accounts. For example, in April 2005 Ontario Premier Bob Rae proposed an Ontario Learning Bond to supplement the Canada Learning Bond, with the Ontario government matching the federal government's contribution.[87]

4. Singapore

Singapore's CSA differs on a basic level from those proposed in the U.S. as well as those already implemented in Canada and Britain in that its purpose is to increase fertility rates rather than to increase savings or improve opportunities for the poor.[88] The Singapore Baby Bonus scheme, first introduced in April 2001[89] and enhanced in 2004[90] and 2005,[91] has two separate tiers. The first tier provides a cash gift of US$2,038.49 for the first and second child born to each family, and US$4,076.93 for the third and fourth children.[92] The money is directly placed into a savings account. The second tier provides for matched savings programs in interest-bearing Child Development Accounts (CDAs), though only second to fourth children are eligible for these.[93] The government matches funds contributed by parents on a dollar-for-dollar basis up to US$3,750 for the second child and US$7,500 for the third and fourth children when the child is between the ages of birth and six years.[94] Funds in the CDAs grow tax-free and can be used for fees charged

86. *See More than $1 Million Invested in Education Savings at One-Year Canada Learning Bond Anniversary*, CANADA NEWSWIRE, July 17, 2006.

87. *See* Ellen Roseman, Opinions, *Some of Rae's Proposals Would Improve Access to Education*, TORONTO STAR, Apr. 21, 2005, at A9.

88. *See* Loke & Sherraden, *supra* note 6, at 4; Susan Long, *More Babies Wanted: Bonus for Second and Third*, THE STRAITS TIMES (Singapore), Aug. 21, 2000, at 1. The governments of Germany and Australia also recently implemented plans to improve birth rates, but they are not discussed in depth here because they lack savings components. German parents of every child born on or after January 1, 2007 now receive up to 1,800 Euro a month for twelve months (depending on their pre-child salary) if one parent stays home to care for the child; if the other parent stays home for two months as well, the benefits extend to fourteen months. *See* Derek Scalley, *Germany Brings in Family Parents' Allowance*, IRISH TIMES, May 3, 2006, at 10. In Australia, mothers receive $4,000 upon the birth of each child. *See* Ross Guest, *Baby Bonus: A Dubious Policy Initiative*, 23 POL'Y 11 (2007).

89. *See* Pauline Leong, *First-Tier Baby Bonus Kicks Off from Next Month*, STRAITS TIMES (Singapore), Mar. 17, 2001, at 4.

90. *See Singapore Extends Cash Gifts to Stem Baby Blues*, JAPAN ECONOMIC NEWSWIRE PLUS, Aug. 25, 2004.

91. *See* Loke & Sherraden, *supra* note 6, at 4-5.

92. *Children Development Co-Savings (Baby Bonus) Scheme*, Singapore Government, http://www.babybonus.gov.sg (last visited Oct. 8, 2007).

93. *Id.*

94. *See* Loke & Sherraden, *supra* note 6, at 5. Overall, between the cash gift and the matching contributions, parents can receive up to US$1,875 from the government for their first child, US-$5,625 for

by approved institutions such as childcare, preschool, kindergarten, special education, early intervention programs, as well as medical expenses.[95] The funds cannot be withdrawn in cash for other purposes.[96] At six years of age, unused funds from CDAs are transferred to the child's Post Secondary Education accounts (PSEs) as CSAs can help parents finance post-secondary education costs.[97]

While Singapore may have the most substantial CSA policy worldwide,[98] the scheme does not benefit all children equally. This is primarily due to Singapore's pro-natal objective. First children benefit only from the cash gift under the Baby Bonus program, not the matching CDAs, and children fifth in birth order and beyond do not benefit from either tier.[99] Recent research also suggests that, as in Britain and Canada, low income families benefit less than higher income families in the matched savings component of the program.[100]

5. Hungary

Hungary's government expressed interest in creating CSA legislation in late 2005. The government aimed to model the plan after Britain's Child Trust

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the second child, and US$11,250 for the third and fourth children, assuming that they make maximum contributions to their children's CDAs. *Id.*

95. *Children Development Co-Savings (Baby Bonus) Scheme*, Singapore Government, http://www.babybonus.gov.sg (last visited Oct. 8, 2007); email from Liu Kong Weng, Family Services Officer, Baby Bonus and Adoption Branch, Ministry of Child Development, Youth and Sports to Lora Cicconi (Apr. 25, 2007) (on file with author). Note that the CDA savings can be used for all children, not just the beneficiary of the CDA. *Id.*

96. *See id.* ("Parents will not be able to withdraw the CDA funds in cash").

97. Loke & Sherraden, *supra* note 6, at 6. Family contributions to PSEs are also matched by the government, with a combined CDA and PSE cap of S$6,000 for the first child and S$12,000 for the second through fourth children. *Id.* at 6. Unused funds from PSEs are rolled over into the Central Provident fund, the country's primary retirement system. *Id.* at 3, 3 n.1, 6. Singapore also has a second initiative called the Edusave program, in which the government makes annual contributions into the accounts of all children between the ages of six and sixteen and additional merit contributions for academic achievement. However, this program differs from a CSA in that parents cannot contribute to the accounts, and the funds may only be used for enrichment programs, not standard education expenses. Moreover, the accounts may not be rolled over into retirement accounts like the CDAs and PSEs. *Id.* at 3-4.

98. *See* Press Release, Center for Social Development, *Singapore Announces "Baby Bonus" and Children's Development Accounts* (Mar. 2001), at 1, *available at* http://gwbweb.wustl.edu/csd/News/SingaporeCDA.pdf.

99. *See id.* at 2-3 (critiquing the program for failing to affirm the value of every child); Loke & Sherraden, *supra* note 6, at 14-15. Based on birth data, about 1.6% of children were excluded from the Baby Bonus program because they were fifth birth order or higher, and 46% missed out on the matched saving programs in the CDAs and PSEs because they are firstborn. *Id.* at 15. Though note again that CDA funds can be used for all children, not just the CDA beneficiary. *Children Development Co-Savings (Baby Bonus) Scheme*, Singapore Government, http://www.babybonus.gov.sg (last visited Oct. 8, 2007).

100. Loke & Sherraden, *supra* note 6, at 15 (indicating less than 45% of low-income families made contributions to their children's CDAs, whereas 80% of wealthier families contributed).

Funds,[101] but the purpose for the legislation was more closely related to Singapore's scheme since the government hoped that incentives would increase the national birth rate.[102]

Hungary's baby bond legislation was implemented in January of 2006.[103] Children born after December 31, 2005 receive an initial deposit of US$180 at birth, and low income children receive two extra payments of US$140 at seven and eleven years of age.[104] Orphans and foster children receive US$56 annually.[105] Parents can contribute up to US$568 per year into the tax-free accounts, and the government will match up to US$28 per year for all participants, and up to US$57 per year for those on welfare.[106] At age eighteen, children can withdraw the money without any restrictions, as in Britain, and presumably they must pay income tax on the withdrawal.[107] While it is likely too early to tell whether the CSA legislation will have as much success in Hungary as it has in Britain, one early report suggested that few parents have taken full advantage of the program.[108]

6. South Korea

South Korea began its CSA initiative less than a year ago. In August 2006, the Korean Ministry of Health and Welfare announced that it would establish CSAs beginning in January 2007. Though these accounts would receive no initial state deposit, Korea would match any savings dollar-for-dollar up to US$30 a month. The plan was officially implemented in January 2007,[109] and while currently the program is only available to 37,000 Korean foster children, the government plans to expand it gradually. First it will incorporate children born in Korea utilizing public assistance, then it will include children of the working poor so that by 2010 all low- and middle-income children—approximately 50% of all Korean newborns—will be

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101. *See Gov't to Initiate Baby Bond*, HUNGARIAN NEWS AGENCY, Nov. 7, 2005.

102. *See Gov't Submits Baby Bond Bill*, HUNGARIAN NEWS AGENCY, Nov. 27, 2005.

103. *See Banks Ready to Kick Off Baby Bond Scheme in January*, HUNGARIAN NEWS AGENCY, Dec. 28, 2005.

104. *See id.*

105. *See id.*

106. *See id.*

107. *See* International CSA Programs, Corporation for Enterprise Development, *available at* http://www.cfed.org/focus.m?parentid=2&siteid=288&id=311#10 (last visted Oct. 8, 2007).

108. *See Gov't Baby Bond Savings Scheme Unpopular*, HUNGARIAN NEWS AGENCY, Aug. 23, 2006.

109. *See* MICHAEL SHERRADEN ET AL., CENTER FOR SOC. DEV., ASSET-BASED POLICY IN SOUTH KOREA: PROPOSALS FOR DEMONSTRATION AND POLICY 2 (2006), *available at* http://gwbweb.wustl.edu/csd/Publications/2006/Korea_Update_12_21_06.pdf; *S. Korea Takes Steps for Social Investment*, United Press Int'l, Mar. 26, 2007, *available at* http://www.upi.com/International_Intelligence/Briefing/2007/03/26/s_korea_takes_steps_for_social_investment/5408/.

eligible.[110] Because this is a novel idea, it is difficult to discern how these accounts will be treated from a tax perspective.[111]

C. Scholarly Attention

While CSAs only began to attract major political support in the last decade or so[112] and have only recently become law in several countries,[113] prominent scholars in the economics, social work, and tax fields have been arguing in favor of some sort of program for wealth transfer to youth for over four decades.[114] The academic literature in this area has influenced the policy debate on Child Savings Accounts,[115] even contributing to the enactment of legislation.[116]

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110. *See* Loke & Sherraden, *supra* note 6, at 10; Press Release, Global Assets Project, *Child Development Accounts Proposed in South Korea* (Aug. 29, 2006), *available at* http://gwbweb.wustl.edu/csd/Publications/2006/Korea_CDA_8-29-06.pdf.

111. Due to the limited research available on the Korea plan, when I compare the various CSAs in Part IV, I often leave Korea out of the analysis. In addition to the U.S., Britain, Canada, Singapore, Hungary, and Korea, there is evidence that other countries are considering CSAs as well. In April 2005, the independent think tank New Zealand Institute proposed the introduction of a "Kiwi Savings Account" to improve asset accumulation among New Zealanders, which closely resembled the plan that the Institute for Public Policy Research developed in Britain in 2000. *See Report Proposes Savings Regime Be Introduced at Cradle*, NEW ZEALAND PRESS ASSOCIATION, Apr. 6, 2005. The New Zealand government immediately responded by calling the proposal too costly, *see $4bn Savings Plan Too Costly, Says Government*, NEW ZEALAND HERALD, Apr. 6, 2005, but it received considerable attention in New Zealand. *See, e.g.*, Simon Collins, *Saving Basis of a Healthy Society*, NEW ZEALAND HERALD, Apr. 6, 2005; Kristina Greene, *Mixed Reviews on Kiwi Savings*, CHRISTCHURCH PRESS, Apr. 19, 2005, at 5. Nevertheless, the New Zealand government has taken no action to establish any form of child savings accounts.

112. U.S. proposals began to appear in Congress in the mid-1990s. *See supra* notes 26-30 and accompanying text.

113. Britain, Canada, and Singapore adopted their CSAs in the early 2000s. *See supra* notes 60-101 and accompanying text.

114. *See infra* notes 119-193 and accompanying text.

115. For example, Michael Sherraden has testified before Congress and presented papers to government commissions on this issue. *See Building Assets for Low Income Families: Hearing Before the Subcomm. on Soc. Sec. and Family Policy of the S. Fin. Comm.*, 109th Cong. (2005), *available at* http://www.senate.gov/~finance/hearings/testimony/2005test/mstest042805.pdf (statement of Michael Sherraden); Michael Sherraden, Assets and the Poor: Implications for Individual Accounts and Social Security, Invited testimony at the President's Commission on Social Security (Oct. 18, 2001) [hereinafter Sherraden Social Security], transcript *available at* http://www.csss.gov/meetings/Sherraden_Testimony.pdf.; *CSD Core Staff*, Center for Social Development, http://gwbweb.wustl.edu/csd/about/staffcopy.htm.

116. Michael Sherraden worked with government of Britain to develop Child Trust Funds. *See, e.g.*, Michael Sherraden, Letter to the Editor, *Better Baby Bonds*, N.Y. TIMES, May 13, 2001, at 12 ("Over the last two years, I have worked with government officials and researchers in England on the asset-based strategies that led up to Mr. Blair's [Child Trust Fund policy]."). Other news articles suggest Tony Blair drew from the work of Bruce Ackerman and Anne Alstott in developing Child Trust Funds. *See, e.g.*, Matthew Miller, *No Cake! A Piece of Pie for All*, TIMES UNION (Albany), Sept. 12, 2004, at B5 ("Inspired partly by Anne Alstott and Bruce Ackerman's book 'The Stakeholder Society' (which called for every

This section seeks to briefly describe the scholarly input in this area. However, in order to engage in a full analysis of the academic work on Child Savings Accounts, it is necessary to delve into some literature that has advocated programs that are considerably bolder and broader than the CSA legislation that has actually been enacted or seriously proposed in the United States. Specifically, some scholars have set forth endowments for youth without any savings component whatsoever. In order to differentiate between the various proposals, I discuss them in three different sections beginning with the proposals that most resemble the existing CSAs and gradually expanding to proposals advocating universal wealth transfers with few limitations.[117]

1. Endowment Plus Savings: State Directed Funds with Savings Incentives and Restrictions at Distribution

The proposals described in this Part most closely resemble existing CSAs. The state provides an initial endowment for the recipient deposited into a savings account. Contributions to the account by the account holders and others are encouraged with various incentives. Distributions are only allowed for specified purposes.

i. Sherraden: Individual Development Accounts

Michael Sherraden is a professor of social work at Washington University, the founding Director of the Center for Social Development,[118] and one of the most vocal proponents of asset-building strategies for the poor.[119]

American to receive an $80,000 stake from the government when they reach adulthood), Tony Blair has introduced modest 'baby bonds.'"). Note, though, that while Ackerman and Alstott praised Blair's Child Trust Fund Proposal, *see* Ackerman & Alstott, *supra* note 64, Sherraden wrote a letter to the editor of the New York Times cautioning that Ackerman and Alstott's proposal in *The Stakeholder Society* differed considerably from Britain's legislation. Sherraden, *supra* ("'Tony Blair's Big Idea,' by Bruce Ackerman and Anne Alstott may give the impression that the new United Kingdom policy is similar to the writers' 'baby bond' proposal, which would give a large lump-sum payment to everyone who graduates from high school, regardless of need . . . The United Kingdom policy gives greater benefits to the poor than to the well-off. . . . The Blair policy envisions lifelong asset-building and is progressive. This is quite different from giving every teenager a large check.").

117. Due to this framework, the proposals are not discussed in chronological order.

118. The Center for Social Development is a think tank dedicated to asset-building and civil involvement. *See* Center for Social Development website, http://gwbweb.wustl.edu/csd/about/index.htm (last visited Oct. 8, 2007).

119. Sherraden is credited with pioneering the concept of Individual Development Accounts (IDAs), described *infra* notes 122-134, which Presidents Clinton and Bush supported, and which received some federal funding in the Assets for Independence Act. *See Building Assets for Low Income Families: Hearing Before the Subcomm. on Soc. Sec. and Family Policy of the S. Fin. Comm.*, 109th Cong. (2005) (statement of Michael Sherraden); Ross Kerber, *United Way to Give Grants to Those Who Save*, BOSTON GLOBE, Dec. 17, 2005, at A1. However, at this point, no national IDA plan has been implemented (though some were

Sherraden published *Assets and the Poor*[120] in 1991, in which he criticized the U.S. welfare system's focus on income redistribution[121] and argued in favor of an asset-based welfare policy.[122] To put this policy into practice, Sherraden proposed Individual Development Accounts (IDAs).[123] IDAs would be similar to IRAs in that they "would be optional, earnings-bearing, tax-benefited accounts" restricted to certain purposes.[124] IDAs would have several additional components, however. Like CSAs, IDAs would be available to all Americans, whereas IRAs are limited to wage earners and their spouses.[125] More importantly, IDAs, though available universally,[126] would target the poor in a progressive scheme. Accordingly, the savings incentive would be in the form of matching funds, rather than tax subsidies, at least for low-income recipients.[127] While Sherraden believed that youth would benefit the most

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considered, *see supra* note 59) and IDAs only exist on a relatively small scale at the local level, funded primarily by nonprofits. *See* Kerber, *supra* ("IDAs [were] first developed by the Clinton administration in 1999. Under President Bush, the Department of Health and Human Services increased annual funding for IDAs from $10 million to $25 million for each of the last five years, still a drop in the bucket of overall social spending.").

120. *See generally* MICHAEL SHERRADEN, ASSETS AND THE POOR: A NEW AMERICAN WELFARE POLICY (1991). Sherraden published his first article on asset-based welfare in 1988, *see* Michael Sherraden, *Rethinking Social Welfare: Towards Assets*, 18 SOC. POL'Y 37 (1988), and published several other articles on the topic before *Assets and the Poor. See* SHERRADEN, *supra*, at xvii. Since publishing *Assets and the Poor*, Sherraden has remained very active in advocating asset-based strategies. *See, e.g.*, Sherraden, *supra* note 58; Sherraden Social Security, *supra* note 115; Center for Social Development website, http://gwbweb.wustl.edu/csd/ (last visited Oct. 8, 2007).

121. *See generally* SHERRADEN, *supra* note 120, at 35-94.

122. *See id.* at 95-293. Sherraden argued that assets were critical to a redistribution system because while income transfers affect only consumption, assets have a variety of important social, economic, and psychological effects beyond consumption, such as improving household stability, developing human capital, and increasing personal efficacy, and political participation. *Id*. at 147-66.

123. *Id.* at 220.

124. *Id*. at 220. Sherraden's IDAs were the subject of a research program called the American Dream Demonstration (ADD). The ADD ran from 1997 to 2003 and analyzed the savings behavior of 2,353 participants. While the research could not determine whether participants saved more than they would have in the absence of the IDA program (the data was not set up to answer this question and participants were self-selected), the ADD suggested that the poor could and did save an average of $700 per year including matching funds. *See* SCHREINER et al., *supra* note 58, at 185-213.

125. SHERRADEN, *supra* note 120, at 223.

126. *Id.*

127. In *Assets and the Poor*, Sherraden did not specifically describe the tax treatment of contributions to and withdrawals from IDAs. Instead, he merely stated that his IDAs would sometimes tax-deferred and sometimes tax-exempt. *Id.* at 223 ("[d]eposited funds and earnings on funds would be in whole or in part tax-benefited (sometimes tax-exempt, sometimes tax-deferred) when used for designated purposes."). This might suggest that contributions would be made with pre-tax funds, and sometimes taxed at withdrawal, whereas other times escaping tax at both ends. In later testimony for the President's Commission on Social Security, Sherraden clarified his stance on this issue a bit, suggesting that IDAs would function like traditional IRAs for wealthy individuals, with the pre-tax at contribution, tax at withdrawal scheme, while

from IDAs and surmised that the accounts could be created as early as birth,[128] he would make them available to all citizens—not just children born after a certain date.[129] Sherraden suggested that a national IDA policy could be funded by fully taxing social security benefits and removing or limiting a number of tax benefits that primarily accrue to the wealthy.[130]

Sherraden's proposal is very restrictive at the time of grant and even more restrictive than the existing CSA legislation. Under Sherraden's proposal, the government would only make an asset transfer into the IDA if the accountholder made a deposit himself, effectively conditioning the asset transfer upon the savings behavior of the accountholder.[131] IDAs would also be restricted in terms of contributions and withdrawals. Accountholders would only be permitted to contribute to their IDAs at certain milestones, such as graduation from grade school and high school,[132] and withdrawals would only be allowed for certain designated uses, such as education and training.[133] Unqualified withdrawals would result in substantial penalties, with all subsidized deposits and earnings reverting to a national fund.[134]

ii. New America Foundation: American Stakeholder Accounts

Ray Boshara, Director of the Asset Building Program at the New America Foundation, published a position paper on asset-building in 2003[135] in which

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the poor would receive matching grants in place of the tax deduction because they have little or no tax liability. *See* Sherraden Social Security, *supra* note 115, at 3. For the purposes of this paper, I assume that this is the tax scheme that IDAs follow.

128. SHERRADEN, *supra* note 120, at 220-21.

129. *Id*. at 221. In this respect IDAs differ significantly from CSAs. All Americans would be eligible to contribute to and receive matching grants in IDAs, whereas existing CSAs and proposals for CSAs would only benefit those born after a certain date, and most have features that begin to diminish after age eighteen. For example, there is no further government funding for the Britain, Canada, Hungary, or Singapore CSAs after the beneficiary reaches adulthood.

130. Such tax benefits include deferments for pension contributions, exclusions for employer-contributed medical premiums, home mortgage interest deductions, and capital gains exclusions, among others. SHERRADEN, *supra* note 120, at 229-30.

131. *Id.* at 222. This is more restrictive than existing CSAs in Britain, Canada, Singapore, and Hungary, in which the government deposits some funds into the account regardless of the recipient's actions. Though note that Sherraden notes that the poor's matching funds could come from other government funds, such as the Earned Income Tax Credit or welfare transfers. *Id*.

132. *Id*. at 221.

133. *Id.*

134. SHERRADEN, *supra* note 120, at 223. There would be penalties on the funds contributed as well as the reversion of the government contributions. *Id*.

135. *See* RAY BOSHARA, NEW AMERICA FOUNDATION, AMERICAN STAKEHOLDER ACCOUNTS (2003), *available at* http://www.newamerica.net/publications/policy/american_stakeholder_accounts. This position paper was a shortened version of a paper written by Boshara's New America colleague, Reid Cramer. The revised version of the longer paper is REID CRAMER, NET WORTH AT BIRTH: CREATING A NATIONAL SYSTEM

he proposed that an American Stakeholder Account (ASA) be created for every child in America under the age of eighteen in order to reduce poverty and economic inequality.[136] Boshara's scheme proposed that every child in America born after September 2002 would receive a stakeholder account.[137] Approximately twelve months following birth, a deposit of $2,000 would be placed into the account.[138] Merit deposits of $1,000 would be made following kindergarten and grade school graduation, and a $2,000 deposit would accrue at high school graduation.[139] In addition, up to three $500 deposits would be made if the accountholder completed community or national service.[140]

Anyone could contribute after-tax funds of up to $1,000 per year into an individual's American Stakeholder Account, and earnings and withdrawals for specified purposes would be tax free.[141] Lower income accountholders would be eligible for an additional $500 per year in the form of an earned income tax credit refund if they placed the money directly into the account.[142] Unlike Sherraden's IDAs which were not structured as loans, the government funds placed into ASAs would be repaid by accountholders over a ten-year period.[143] Boshara estimates that the proposal would cost approximately $14 billion per year,[144] though he did not suggest a particular funding source.[145]

Boshara's proposal is closest to the existing CSA legislation in that it advocates an endowed account at birth—regardless of the recipient's savings behavior—yet also contains savings incentives and additional benefits for low-income families. Boshara's plan also adds an interesting twist to the basic

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FOR SAVINGS AND ASSET BUILDING WITH CHILDREN'S SAVINGS ACCOUNTS (2006), *available at* http://www.newamerica.net/files/Net%20Worth%20at%20Birth%20Revised%20(PDF,%2044%20pp.).pdf.

136. BOSHARA, *supra* note 135, at 1. Boshara highlighted the growing wealth inequality in the country, noting that the bottom 60% of this country currently own only 5% of the nation's overall wealth. He argued that this leads not only to economic insecurity, but to reduced opportunity for the next generation. Like Sherraden, Boshara also noted the various benefits that individuals derive from holding assets assets, such as household stability, educational attainment, civic involvement, and health. *Id.* at 1-2.

137. *Id.* at 1.

138. *Id.* at 2.

139. *Id*.

140. BOSHARA, *supra* note 135, at 2.

141. *Id.* at 2-3. No withdrawals would be permitted before age eighteen, and withdrawals after that age would only be permitted for post-secondary education, home purchases, and small business capitalization. *Id.* at 2.

142. *Id.*

143. *Id.*

144. BOSHARA, *supra* note 58, at 3 (citing FRED T. GOLDBERG, JR. & JODI BIRK COHEN, CENTER FOR SOCIAL DEVELOPMENT, THE UNIVERSAL PIGGY BANK: DESIGNING AND IMPLEMENTING A SYSTEM OF SAVINGS ACCOUNTS FOR CHILDREN (Symposium on Inclusion in Asset Building) (Sept. 2001), *available at* http://gwbweb.wustl.edu/csd/Publications/2000/PolicyReport-Goldberg.pdf).

145. *Id.* at 3. He does suggest, however, that ASAs, though expensive, might eventually pay for themselves by reducing public expenditures and improving economic growth. *Id.*

CSA concept by including merit deposits for meeting educational milestones and completing community service,[146] thus providing motivations not only for saving but also for other positive behavior as well.

2. Capital Accounts: No Savings Component, But Restrictions at Distribution

Like those described in Part A, the proposals in this Part provide a state endowment for youth and retain the concept of restrictions upon withdrawal. However, in the capital account proposals the funds are not distributed until adulthood, and are not placed into a savings vehicle.

i. Tobin: National Youth Endowment

Though some recent proposals to make a one-time wealth transfer to youth have received considerable media attention in the U.S.,[147] the concept is not novel. In 1968, Nobel Prize winning economist James Tobin argued in a short essay on inequality[148] that the federal government should grant every high school graduate[149] an endowment of $5,000 (the equivalent of approximately $29,000 today) as part of its anti-poverty strategy.[150] Tobin surmised that these "National Youth Endowments" could be drawn on for authorized purposes, such as tuition and living expenses while in a qualified education or training program, but only until the recipient reached age twnty-eight. Tobin did not discuss how these endowments would affect recipients'

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146. *Id*. at 2.

147. In particular, Bruce Ackerman and Anne Alstott's book, *The Stakeholder Society*, received considerable media attention, as described *infra* note 176. Some news reports have even suggested that Ackerman and Alstott began the debate on stakeholding, *see The Germ of a Good Idea*, ECONOMIST, Apr. 12, 2003 ("Like many original ideas in political economy, [the concept of Child Trust Funds] was born in America. The debate was started in 1999 by two American academics, Bruce Ackerman and Anne Alstott, in their book The Stakeholder Society."), but the concept was developed much earlier as Part III.B shows.

148. *See* James Tobin, *Raising the Incomes of the Poor*, *in* AGENDA FOR THE NATION 77 (Kermit Gordon, ed. 1968). As noted by Ackerman and Alstott, Tobin was not the first public figure to develop a stakeholding concept, *see* Ackerman & Alstott, *supra* note 64 (stakeholding has a rich polical history dating back to Thomas Paine). However, Tobin appears to be the first economist to put forth the idea as a viable anti-poverty tool in the U.S. For more information on historical initiatives that have used the stakeholding concept, *see* BRUCE ACKERMAN & ANNE ALSTOTT, THE STAKEHOLDER SOCIETY 6 (GI Bill), 11 (Homestead Act), 12-13 (British prime pinister Margaret Thatcher selling public housing to residents at bargain rates during privatization; Czech prime minister selling businesses to the public in move to free-market system; citizens of Alaska sharing revenues from oil company) (1999). Sherraden also discusses historical asset transfer strategies in some detail. *See* SHERRADEN, *supra* note 120, at 191-95.

149. Tobin, *supra* note 148, at 92 (if graduation was not attained, at age nineteen). *Id.*

150. Tobin called this part of his anti-poverty strategy investment in human capital. The other primary part of Tobin's anti-poverty strategy included income maintenance, possibly via a credit or negative income tax. *Id*. at 93-114.

income tax upon receipt, but did state that they would function as a loan, with every dollar of the grant consumed increasing the recipient's income tax liability until the loan was repaid in full with interest.[151] Tobin compared his program to the GI bill of rights and the Educational Opportunity Bank proposed by President Johnson in 1967.[152] He believed that its advantage lied in the fact that individuals would be assisted "directly and equally, rather than indirectly and haphazardly."[153] He argued that repayments would ultimately cover most of the outlay, and that until then, the government could fund the program by borrowing in the capital markets rather than relying on tax expenditures because the program would represent a social investment.[154]

ii. Klein: Universal Personal Capital Accounts

A few years later, UCLA law professor William A. Klein made a similar, though more developed, proposal as part of his work at the Institute for Research on Poverty.[155] With the goal of reducing poverty and equalizing resources, Klein argued that every child who graduated from high school or reached age eighteen should receive a Universal Personal Capital Account funded with approximately $10,000 ($48,089 in today's dollars) from the government.[156] Klein believed that the funds should only be drawn on for specific uses in order to make the program politically feasible,[157] but also

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151. *Id.* at 92. The repayment would not begin until age 28. *Id.*

152. Tobin, *supra* note 148, at 92. The Educational Opportunity Bank was a proposed system whereby the government would set up a bank to borrow money at government rates and lend to students, regardless of resources, for post-secondary education. The students would pay back by promising a percentage of their lifetime salaries. *See* Karl Shell, et al., *The Educational Opportunity Bank: An Economic Analysis of a Contingent Repayment Loan Program for Higher Education*, 21 NAT'L TAX J. 2-3 (1968). The proposal was the brainchild of Milton Friedman and had the support of President Johnson and other academics, but it was kept off the policy agenda by certain higher education groups and key members of Congress who foresaw conflict with some of the administration's supporters. *See* Norman C. Thomas, *Policy Formulation for Education: The Johnson Administration*, 2 EDUCATIONAL RESEARCHER 4, 8 (1973).

153. Tobin, *supra* note 148, at 92.

154. *Id.* at 92-93. Tobin does note that monetary authorities would have to neutralize inflation impact, "temporarily displacing other investments, public and private, of lower social priority." *Id.* at 93.

155. *See* William A. Klein, A Proposal for a Universal Personal Capital Account (Institute for Research on Poverty Working Paper No. 422-77, 1972); William A. Klein, A Proposal for a Universal Personal Capital Account (UCLA Working Paper, revised version, 1975) [hereinafter Klein Revised Proposal] (on file with author).

156. Klein Revised Proposal, *supra* note 155, at 1-2. While Klein anticipated that some might argue the accounts should be limited to the poor, he believed the issue was not as important as it might initially appear; he theorized that there would be no net benefit for the children of the wealthy and their parents because increased income taxes from financing the accounts would be offset by any benefits received. *Id.* at 14.

157. *Id.* at 2 ("[The Universal Personal Capital Account] must provide taxpayer-nonrecipients, to some significant extent, with the satisfaction of knowing that their tax dollars are being spent for purposes

recognized that a strict use limitation could lead to an overuse of benefits.[158] As a result, his plan would allow recipients to use the funds for educational or medical expenses, with any remainder at age sixty-five available to purchase as an annuity.[159]

The Universal Personal Capital Accounts—which would not be repaid[160]—would be managed by the recipients,[161] grow at an interest rate of about 3% plus a cost-of-living escalator, and escape taxation until withdrawal.[162] Amounts distributed from the accounts would be treated as taxable income; a result that Klein argued was sensible given that the poor would likely face no tax liability and the wealthy should bear the cost of a program designed to promote equality and reduce poverty.[163] Klein did not attempt to compile a direct estimate of the cost of his program, but strongly preferred that funding come from the income tax.[164] He concluded that while the Universal Capital Accounts would not be a panacea for poverty, they would provide recipients with a sense of security and freedom to make choices, while also restricting uses "in cognizance of the public's inclination to attach strings to gratuitous transfers."[165]

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that they consider, for paternalistic or selfish or whatever reasons, desirable or meritorious from their own perspective.").

158. *Id*. at 2-3.

159. *Id*. at 1-3. Klein rejected the possibility that the uses should be expanded to include purchasing a home or business or legal services. He argued that expanding the list of permissible uses would mean greater current outlays and would open the door to quibbles about which uses are meritorious or not. Klein Revised Proposal, *supra* note 155, at 7-8.

160. *Id*. at 1-16 (no mention of repayment).

161. *Id*. at 5-6.

162. *Id*. at 4. Because the accounts would not be transferable, they would increase each year corresponding to life insurance premiums in order to reflect the risk of loss in the event of death before age sixty-five. *Id*. at 5. Klein believed it was important that the rate of return not be too high given that the accounts would grow tax-free, but also noted that the rate not be too low lest wealthy people draw on their Universal Personal Capital Accounts to finance education "while preserving or augmenting private funds that would have been used for such purposes except for the fact that such funds produce a higher rate of return." Klein Revised Proposal, *supra* note 155, at 4-5.

163. *Id*. at 15. Conversely, Klein suggested that there might be a deduction for non-living expenses of education when taxing withdrawals. *Id.*

164. *Id*. at 3-4, 14.

165. *Id*. at 16. Klein also noted that his accounts sought to "reduce economic inequality while at the same time pursuing goals that are not entirely compatible with one another: limitation of use, discouragement of misuse, freedom of choice, and fair distribution of welfare benefits." Klein Revised Proposal, *supra* note 155, at 16.

iii. Haveman: Universal Personal Capital Accounts for Youths

In the late 1980s, University of Wisconsin economist Robert Haveman published *Starting Even*,[166] a book addressing the poverty and growing economic inequality in the United States.[167] Like Sherraden, Haveman argued that simply expanding the current income redistribution system would not reduce poverty or inequality at reasonable costs.[168] He instead proposed a plan that would expand opportunities and provide incentives to increase the efficiency and independence of the poor.[169] Haveman envisioned scaling back social security benefits for the highest earners and creating personal capital accounts which would replace income subsidies like food stamps and public housing with a reformed personal income tax.

Haveman's Universal Personal Capital Accounts for Youths paralleled Klein's Universal Personal Capital Accounts. Haveman's accounts would be funded by a direct grant of $20,000 (the equivalent of approximately $34,000 today) which each child would receive at age eighteen.[170] The funds would be placed into an account which would bear interest, and could be drawn upon for "human capital investments of [the recipient's] choice," including purchases of education, training, and healthcare services.[171] As in Klein's proposal, any residual funds at retirement would be available at that time,[172] and recipients would not be required to repay the funds they received.[173] Haveman estimated that the capital account portion of his plan would cost approximately $10-15 billion (approximately $16-25 billion today),[174] but did not discuss funding options in detail.[175]

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166. ROBERT HAVEMAN, STARTING EVEN: AN EQUAL OPPORTUNITY PROGRAM TO COMBAT THE NATION'S NEW POVERTY (1988).

167. *See generally id.*

168. *Id.* at 149.

169. *Id.*

170. *Id*. at 169.

171. HAVEMAN, *supra* note 166, at 169.

172. *Id*.

173. *See id*. at 168-69 (referring to the Universal Personal Capital Accounts for Youth as a "capital grant").

174. *Id*. at 177.

175. *Id*. at 172-77 (appendix to chapter seven entitled "How Much Would All This Cost" discusses costs but not funding). In addition to Tobin, Klein, and Haveman, a few other scholars have set forth somewhat similar proposals. For example, in 1992, Isabelle Sawhill, then of the Urban Institute, argued in favor of a wealth transfer of $5,000 ($7,100 today) to inner city teenagers who remain childless and graduate from high school with a decent academic record. The funds could be used for education or job training. Sawhill argued that this type of generous reward might be necessary to create an incentive for low-income teenagers to remain childless, especially given that the welfare system and norms in the inner city tilt the other way, and that early childbearing harms the prospects of two generations. *See* Isabelle V. Sawhill, *The Underclass: An Overview*, 136 PROC. OF THE AM. PHIL. SOC'Y 380, 389 (1992). *See also* ROBERTO

3. Stakeholder Society: Endowment, No Savings Incentives, and No Distribution Restrictions

The proposals described in this section include a state-funded endowment for youth with no savings component and no restrictions on how the money is spent once it is distributed.

i. Ackerman and Alstott: Stakeholder Society

Bruce Ackerman and Anne Alstott's 1999 book, *The Stakeholder Society* arguably represents the boldest contribution to the scholarship in this area.[176] Concerned with growing economic inequality in this country and the disparate opportunities of youth from the upper and lower classes,[177] Ackerman and Alstott proposed that every American receive an $80,000 stake (approximately $96,000 in today's dollars) in America at age eighteen.[178] The recipient could use the money however he or she saw fit,[179] but the distribution of the funds would depend on citizenship, residency status,[180] and educational attainment.[181] Only U.S. citizens (by birth or naturalization) who lived in the U.S. for at least eleven years would be eligible to receive the funds.[182] Further, only high school graduates who planned to attend college would get the full $80,000 at age eighteen.[183] Those who failed to graduate high school would enjoy only the interest on their stake, and those with non-educational plans for the money would receive their stake in yearly $20,000 installments (plus interest)

MANGABEIRA UNGER, WHAT SHOULD LEGAL ANALYSIS BECOME? 14-15 (1996) (proposing capital account for youths directed towards education).

176. *See* BRUCE ACKERMAN & ANNE ALSTOTT, THE STAKEHOLDER SOCIETY (1999). *The Stakeholder Society* received considerable press and was reviewed in a number of publications, *see e.g.*, Merrill Goozner, *Forty Acres and a Sheepskin*, AMERICAN PROSPECT, Mar.-Apr. 1999, at 90; Matthew Miller, *A Stake in Every Pot*, N.Y. TIMES, Jan. 31, 1999, at 16, and is consistently mentioned in law review articles, *see, e.g.*, Patricia E. Dilley, *Taking Public Rights Private: The Rhetoric and Reality of Social Security Privatization*, 41 B.C. L. REV. 975, 1040-44 (2000); James R. Repetti, *Democracy, Taxes and Wealth*, 76 N.Y.U. L. REV. 825, 839-40 (2001); Vicki Shultz, *Life's Work*, 100 COLUM. L. REV. 1881, 1929 (2000); Donald B. Tobin, *Investing in Our Children: A Not So Radical Proposal*, 73 U. CINN. L. REV. 457, 492-94 (2004); Lawrence Zelenak, *Taxing Endowment*, 55 DUKE L.J. 1145, 1176-77 (2006).

177. ACKERMAN & ALSTOTT, *supra* note 148, at 2, 26-31.

178. *Id*. at 4. The amount is based on college tuition numbers; when the book was published, $80,000 would pay for four years of tuition at a private college. *Id*. at 51-55. Private tuition had increased to nearly $23,000 by the 2002-2003 school year. *See* Average Undergraduate College Costs, by State, 2002-2003, U.S. Dep't of Education, http://www.ed.gov/students/prep/college/thinkcollege/early/students/edlite-college-costs.html (last visited Oct. 3, 2007).

179. ACKERMAN & ALSTOTT, *supra* note 148, at 5.

180. *Id.* at 48.

181. *Id*. at 5, 7-8, 46-49, 51-56.

182. *Id.* at 48.

183. *Id*. at 52.

between the ages of twenty-one and twenty-four.[184] The stakeholding plan, which the authors estimated would cost over $250 billion in 1999,[185] would be financed by a 2% tax on Americans with wealth over $80,000 (in 1999 dollars),[186] as well as the return of the $80,000 (again in 1999 dollars), plus the interest from each recipient at death.[187]

Ackerman and Alstott's plan clearly looks more like a human capital account proposal than those plans proposed by Sherraden and Boshara and the existing CSAs where government funding is not associated with any sort of savings program. However, the stakeholding proposal differs from the capital accounts in that it includes no use restrictions. In this respect, the authors were careful to distinguish their proposal from the capital account concept, rejecting in principle the notion of "freedom within boundaries."[188] While the authors acknowledged that spending restrictions may not be meaningful for college-bound recipients, they saw those restrictions as very limiting for those not planning to pursue higher education,[189] and argued that recipients without

184. ACKERMAN & ALSTOTT, *supra* note 148, at 57-58. Moreover, participation in crime would reduce, and maybe even eliminate the stake. *Id*. at 49-51.

185. *Id*. at 28. While acknowledging that stakeholding is an expensive solution to the problem of growing wealth inequality, Ackerman and Alstott argued that alternative ideas—such as educational programs—have accomplished little in the last 150 years. *Id*. at 28-29. The authors noted that so long as the wealthy can insulate themselves from the poor and funnel money into their own local school systems, the effectiveness of educational programs will be compromised. *Id*.

186. ACKERMAN & ALSTOTT, *supra* note 148, at 95. Ackerman and Alstott did not argue that the wealth tax was justified solely based on the stunningly disproportionate distribution of wealth (though they did note that the wealthiest 1% of this country owned between 21.2% and 38.5% of its wealth in 1995). *See id*. at 95-96. Instead, they argued that such a distribution would be acceptable if each American began with a roughly equal stake, but this is not the case, therefore the wealth tax is justified because Americans face vastly different opportunities; those who have benefited the most under this system should share the most. *See id*. at 97-100.

187. *Id.* at 13, 78. Like Haveman and Sherraden, Ackerman and Alstott argued that their proposal could reduce the growing inequality in this country, expand access to higher education, and improve the lives of young Americans who are not college-bound. Ackerman and Alstott argued that stakeholding would limit economic disparity by guaranteeing access to a four year college education for all students, and equalize the playing field by allowing lower-class students to focus on academic work rather than part-time jobs and scholarship applications. *See id*. at 52-58. But Ackerman and Alstott posited that the greatest benefits of stakeholding would go to those who do not pursue a college education. ACKERMAN & ALSTOTT, *supra* note 148, at 56. The authors argued that this group of stakeholders will derive the most utility from their stake as they are given so few advantages in today's society. *Id.* They would receive the same $80,000 as those who attend college (albeit over a four year period in their twenties), *id*. at 56-59, and the money could be used for additional training, to weather unemployment, to purchase a home, to send children to daycare or private school, *id*. at 65-74 (profiling various hypothetical individuals in various situations and surmising how the $80,000 stake could change their lives). Taken together, the authors suggested that these possibilities would engender a new culture that encourages children and teenagers to examine their long term plans and act responsibly. *Id*. at 75-76.

188. ACKERMAN & ALSTOTT, *supra* note 148, at 215.

189. *Id* at 215-216.

college plans should be as free and unlimited as those bound for college to spend their stake as they please.[190] The lack of use restriction in combination with the non-existent savings components, makes the stakeholder proposal the least analogous to the existing CSAs of all the academic proposals.[191]

III. Existing Savings Incentives in the U.S. and Child Savings Accounts: A Comparative Analysis

A. Savings Incentives Comprise Most Tax Expenditures in the U.S.

Michael Sherraden makes the simple, but perhaps concealed, point that government spending in the U.S. comes not only from direct expenditures, but also from tax expenditures.[192] While direct expenditures consist of funds that the government doles out, tax expenditures consist of money that the government does not collect in the first place because it chooses to subsidize a certain activity. Tax expenditures, which make up approximately 25% of all government spending on social policy, are sometimes viewed as "hidden" because they fail to show up on budget tables, and because recipients of such expenditures commonly do not view the tax breaks they receive as government assistance.[193]

While direct expenditures often focus on policies that supplement income, tax expenditures mostly subsidize asset-building.[194] Over the last several

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190. *Id*. at 215-16. On the other hand, the fact that only college bound eighteen year-olds would receive the full lump sum $80,000 under the stakeholder plan, and that those who do not graduate from high school would only receive the interest on their stakes, suggests that Ackerman and Alstott's scheme is not as free of limits as it first appears. One could view the variations in how the funds are distributed as simply an alternate means of restricting use; while Haveman, Klein and Tobin would provide funds universally but place restrictions on grant, Ackerman and Alstott place related restrictions on how the money is distributed in the first place. *See infra* note 314 and accompanying text.

191. In addition to Ackerman and Alstott, Richard Freeman, a labor economist at Harvard University, briefly put forth a stakeholding-like proposal as well in his 1999 book on inequality in America. *See* RICHARD B. FREEMAN, SOLVING THE NEW INEQUALITY 16-18 (Joshua Cohen and Joel Rogers, eds. 1999). Freeman proposed that each American receive a trust fund worth his or her social security pension at birth. He argued that the program would represent a step towards an asset-based egalitarian strategy by giving all citizens a share of the nation's capital and allowing the poor to subsist without depending on income transfers. The program would be funded through progressive taxes on inheritance, wealth, and income and there would be no restrictions on how to spend the money—similar to the stakeholder scheme. However, Freeman stated that in order to prevent cross-generational inequality, the plan might only allow recipients to spend the income from their capital, in which case it would not provide for an endowment in the same sense that Ackerman and Alstott's plan would. *Id.*

192. *See* Sherraden Social Security, *supra* note 115, at 11.

193. *Id.*

194. *Id.* On the other hand, those in favor of a consumption tax system might argue that expenditures in the form of tax subsidies for savings are not expenditures at all, but merely a necessary component of an accurate consumption tax system. *See, e.g.*, Karen C. Burke & Grayson M.P. McCouch, *Social Security*

years, U.S. tax policy has taken a decided stance in favor of saving, which leads some to argue that our current system looks more like a consumption tax than an income tax.[195] The largest of these tax expenditures are also the most familiar as the Code allows individuals to make tax-free contributions to retirement accounts and education savings accounts,[196] deduct home mortgage interest on up to $1 million of mortgage indebtedness as well as interest on a $100,000 home equity loan,[197] and benefit from reduced rates on capital gains and dividend distributions.[198] The Joint Committee on Taxation estimates that these subsidies cost the government approximately $268 billion in 2006[199] and the Office of Management and Budget believes that they will be $253 billion

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Reform: Lessons From Private Pensions, 92 CORNELL L. REV. 101, 103 (2007) (contrasting "Liberal" and "Libertarian" views of Social Security tax treatment).

195. *See, e.g.*, Lester B. Snyder & Marianne Gallegos, *Redefining the Role of the Federal Income Tax: Taking the Law "Private" Through the Flat Tax and Other Consumption Taxes*, 13 AM. J. TAX POL'Y 1, 4-5 (1996) ("many of the concepts referred to in the consumption tax bills borrow heavily from current income tax law").

196. *See* I.R.C. §§ 401(a); 401(k); 403(b); 408; 529; 530 (2007).

197. *See* I.R.C. § 163(h). The tax incentives for home purchases, including the home mortgage interest deduction, home equity interest deduction and capital gains exemptions have been sharply criticized as inefficient, *see, e.g.*, Martin A. Sullivan, *Economic Analysis: The Economics of the American Dream*, 106 TAX NOTES 407, 407 (2005) ("[the mortgage interest deduction] is a huge subsidy that causes massive efficiency-draining distortions in the economy"), regressive, *see e.g.*, Deborah A. Geier, *The Taxation of Income Available for Discretionary Use*, 25 VA. TAX. REV. 765, 783 (2006) ("The home mortgage deduction is also suspect on fairness grounds. The upside-down nature of these subsidies is well-known."); Sullivan, *supra*, at 407, not furthering the goal of home ownership, *see, e.g.*, Edward L. Glaeser & Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction*, 17 TAX POL'Y & THE ECONOMY 37, 40 (2003) ("the home mortgage interest deduction is a particularly poor instrument for encouraging homeownership since it is targeted at the wealthy, who are almost always homeowners."); Geier, *supra*, at 783, and unduly expensive, *see, e.g.*, Sullivan, *supra*, at 407 ("repealing the mortgage interest deduction would allow rates to be cut across the board by 10 percent"). President Bush's Tax Advisory Panel recommended repealing the deduction and replacing it with a 15% credit. *See* PRESIDENT'S ADVISORY PANEL ON FEDERAL TAX REFORM, SIMPLE, FAIR AND PRO-GROWTH: PROPOSALS TO FIX AMERICA'S TAX SYSTEM 72-74 (Nov. 2005). Notwithstanding the almost universal agreement that this deduction is highly problematic and the advisory panel's recommendation, most scholars agree that it will not be repealed for political reasons. *See e.g.*, Sullivan, *supra*, at 407-08; Daniel Gross, *Location, Location—Deduction*, SLATE MAGAZINE, Apr. 14, 2005 (We're talking about the home-mortgage-interest deduction, which has become too successful to be killed).

198. *See* I.R.C. §§ 1(h); 1222; 1223.

199. *See* JOINT COMMITTEE ON TAXATION, JCX 11-07, SELECTED DATA RELATED TO THE FEDERAL TAX SYSTEM 8 (2007), *available at* http://www.house.gov/jct/x-11-07.pdf. Other major expenditure areas included: exclusion of employer contributions to health care ($90.6 billion); exclusion of capital gains at death ($50.9 billion); tax credit for children under seventeen ($46 billion); earned income credit ($42.1 billion); deduction for charitable contributions ($29.1 billion); exclusion of cafeteria plan benefits ($27.9 billion); deduction of nonbusiness state and local, sales and personal property taxes ($40.4 billion). *Id.* The Joint Committee on Taxation did not reveal the total tax expenditure estimates for 2006, so one cannot determine precisely what percentage of the expenditures consist of those that encourage savings.

in 2008.[200] That $253 billion figure does not even include the deductibility of property taxes ($13 billion), capital gains exclusion on home sales ($39 billion), exclusion of net imputed rental income ($36 billion), stepped-up basis at death ($36 billion), or exclusion of interest on life insurance savings ($22 billion). If those numbers are included in expenditures for incentives to save, then the estimated 2008 total expenditures directed towards savings reaches almost $400 billion.[201]

Michael Sherraden relies on the fact that many of these savings incentives accrue to high income individuals[202] in order to argue that public policy has

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200. *See* REID CRAMER, ROURKE O'BRIEN, & RAY BOSHARA, NEW AMERICA FOUNDATION, THE ASSETS REPORT 2007: A REVIEW, ASSESSMENT, AND FORECAST OF FEDERAL ASSETS POLICY 13 (2007) (citing OFFICE OF MANAGEMENT AND BUDGET, EXECUTIVE OFFICE OF THE PRESIDENT, BUDGET OF THE U.S.GOVERNMENT, FISCAL YEAR 2008, ANALYTICAL PERSPECTIVES, tbl. 19-1) *available at* http://www.newamerica.net/publications/policy/the_assets_report_2007. Note that there are some discrepancies between the Office of Management and Budget table and the Joint Committee on Taxation table. *Id*. at 13. The Office of Management and Budget table assumes that deferred retirement plans will cost $112 billion in 2008, while the Joint Committee predicts $141.5 billion. JOINT COMMITTEE ON TAXATION, *supra* note 199, at 8. There are clearly some line items included in one table and not the other, which may help explain why there appears to be a predicted decrease in expenditures from 2006 to 2008.

201. CRAMER, ET AL., *supra* note 200, at 13.

202. Tax incentives for savings primarily benefit the wealthy. Home mortgage deductions are regressive because the deduction grows in value as tax brackets increase. Taxpayers earning over $200,000 (approximately 3% of taxpayers), accounted for 28% percent of the expenditures in 2006, and those earning over $100,000 (approximately 14% of taxpayers), accounted for nearly 70% of the entire expenditure, or $42.5 billion. *See* JOINT COMMITTEE ON TAXATION, *supra* note 199, at 11 tbl. 8. Reduced rates for capital gains produce even more disparate results: The Joint Committee on Taxation indicated that in 2005, 88% of the benefit of lower capital gains rates would benefit individuals with incomes over $200,000, and 95% of the benefit going to those with incomes over $100,000. *See* JANE G. GRAVELLE, CONGRESSIONAL RESEARCH SERVICE, CAPITAL GAINS TAXES: AN OVERVIEW 6 (Jan. 24, 2007), *available at* http://www.nationalaglawcenter.org/assets/crs/96-769.pdf. Though figures for retirement savings are not as easy to come by because a number of different provisions in the tax code are implicated, they also mostly benefit the wealthy because the size of the tax benefit is based on the taxpayer's bracket. A model by the Urban Institute suggests that about 70% of tax benefits for direct contribution retirement plans (such as 401(k) plans) accrue to the top 20% of earners, with more than half of the benefits going to the top decile. The figures for IRAs were not as skewed due to lower contribution limits, but 60% of benefits still went to the top 20% of earners. *See* LEONARD E. BURMAN ET AL., URBAN INSTITUTE, DISCUSSION PAPER NO. 16, DISTRIBUTIONAL EFFECTS OF DEFINED CONTRIBUTION PLANS AND INDIVIDUAL RETIREMENT ACCOUNTS 13-14, (2004), *available at* http://www.urban.org/UploadedPDF/311029_TPC_DP16.pdf. The Urban Institute also found that education savings accounts generally benefit the wealthy. *See generally* SUSAN DYNARSKI, URBAN-BROOKINGS TAX POL'Y CTR., HIGH-INCOME FAMILIES BENEFIT MOST FROM NEW EDUCATION SAVINGS INITIATIVES (2005), *available at* http://www.urban.org/UploadedPDF/411147_new_edu_savings.pdf.

On a more general level, note that some scholars have cautioned that relying on distributional tables in analyzing tax policy issues is problematic because they are often oversimplified and fail to take into account income transfers such as the Earned Income Tax Credit. *See* Michael J. Graetz, *Distributional Tables, Tax Legislation, and the Illusion of Precision*, in DISTRIBUTIONAL ANALYSIS OF TAX POLICY 15-78 (David F. Bradford, ed. 1995); JOINT ECONOMIC COMMITTEE STUDY, A GUIDE TO TAX POLICY ANALYSIS:

shaped asset inequality in this country.[203] His point is well taken, and provides a strong thesis in favor of CSAs and other policies that subsidize asset-building strategies for the poor. But the sheer dollar amount spent on these savings incentives also begs the question of just how far some forms of CSAs stray from provisions in the Tax Code that already exist.

B. How Do Components of Child Savings Proposals Compare with Existing Code Provisions?

Given that the U.S. spends hundreds of billions of dollars annually subsidizing savings behavior in the U.S., it is worth asking how tax provisions that create incentives for saving differ from the CSA legislation. In this section, I examine the various child savings proposals within the framework of the existing U.S. Tax Code—specifically, I consider traditional and Roth IRAs and 401(k)s, as well as education savings accounts.[204] Starting with the most basic concept of a tax-based savings incentive—pre-tax contributions or tax-free withdrawals—I gradually add in more complex provisions such as direct subsidies and matching grants in an attempt to determine at what point existing CSAs and proposed CSA legislation differ from current U.S. tax law.[205]

1. Tax Treatment at Contribution

i. Existing Code

Tax provisions intended to encourage saving are often based on the simple premise that individuals may contribute pre-tax money into a savings account. In the Code, traditional 401(k)s and IRAs reflect this philosophy. The Treasury explicitly sanctions tax-free contributions to retirement accounts

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THE CENTRAL TENDENCY OF FEDERAL INCOME TAX LIABILITIES IN DISTRIBUTIONAL ANALYSIS (2000), *available at* http://www.house.gov/jec/tax/table2.htm.

203. SHERRADEN, *supra* note 120, at 12. Sherraden is certainly not the only scholar to make this observation. *See, e.g.*, BOSHARA, *supra* note 135, at 3; BURMAN ET AL., *supra* note 202, at 13-14.

204. While I recognize that there are a number of other savings vehicles, including nonprofit-sponsored 403(b) plans, state government-sponsored 457 plans, and SIMPLE IRAs under Section 408(p), I consider only the above plans in order to keep the analysis more manageable. I also do not discuss other Code provisions related to children or education to the extent that they are not savings vehicles, such as the Child Tax Credit, Earned Income Tax Credit, Lifetime Learning Credit, Hope Credit, or the student loan interest deduction.

205. The capital account and stakeholder proposals are not addressed in the contribution, growth, and withdrawal sections of this Part (Parts IV.B.1-4), because they are not savings vehicles in the first place. These proposals become relevant in Parts IV.B.5-7 when I discuss withdrawal restrictions, direct state funding, and regressivity.

in Section 401(k),[206] which allows employees to earmark a certain portion of their pre-tax compensation for an employer-sponsored retirement account plan. The designated funds are not taxed upon receipt, and the account grows tax-free until withdrawal.[207] Individual Retirement Accounts (IRAs)[208] also allow a deduction for contributions and tax-free growth, without the necessity of an employer-sponsored plan.[209]

In contrast to the traditional savings vehicles, Roth IRAs and the new Roth 401(k)s[210] do not allow pre-tax contributions.[211] Instead, after-tax funds are placed in savings accounts, and the tax benefits accrue upon withdrawal, as discussed below.[212] State-sponsored qualified tuition plans governed by Section 529 (also known as 529 accounts) and 530 Coverdell education savings accounts work in the same manner.[213]

ii. Existing CSAs and CSA Proposals

None of the existing CSAs allow pre-tax contributions into child savings accounts. For example, Britain's Child Trust Accounts, Hungary's Baby Bonds, and Canada's Learning Bonds require parents to make after-tax contributions into their children's accounts,[214] and Singapore does not offer pre-tax contributions either. [215]

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206. 401(k) accounts were enacted in 1978, while deferred compensation arrangements were available pre-1978 but they were not formalized. *See* EMPLOYEE BENEFIT RESEARCH INSTITUTE, HISTORY OF 401(k) PLANS: AN UPDATE (2005), *available at* http://www.ebri.org/pdf/publications/facts/0205fact.a.pdf.

207. *See* I.R.C. §§ 401(a) (discussing qualified pension profit-sharing and stock bonus plans), 401(k) (employer-sponsored cash or deferred arrangements are qualified plans if they meet certain criteria), 219(a) (deduction allowed for qualified retirement contributions), 219(e)(2) (qualified retirement contribution means contribution to 401(k) or similar plan).

208. IRAs were enacted in 1975. *See* Larry Ozanne, *Individual Retirement Accounts*, in THE ENCYCLOPEDIA OF TAXATION AND TAX POLICY 215 (1999), *available at* http://www.urban.org/Uploaded PDF/1000535.pdf.

209. *See* I.R.C. §§ 408(a) (defining individual retirement account), 219(a), 219(e)(1) (allowing deduction for qualified retirement contributions to IRAs and other retirement vehicles), 408(e) (explaining that IRA is exempt from taxation until distribution) (2007). While not as directly comparable to CSAs as 401(k)s and IRAs, it is worth noting that the home mortgage deduction works in a relatively similar manner as the savings vehicles that allow pre-tax contributions by allowing a deduction for the interest paid on a home mortgage. *See* I.R.C. §§ 163(a), 163(h)(1)-(3).

210. Roth IRAs were enacted in 1998. Roth 401(k)s were enacted in 2001 but the legislation only became effective in 2006. *See* IRS., DESIGNATED ROTH CONTRIBUTIONS TO CASH OR DEFERRED ARRANGEMENTS UNDER SECTION 401(K) (2006), *available at* http://www.irs.gov/pub/irs-regs/td_9237.pdf.

211. *See* I.R.C. §§ 408A(b) (defining Roth IRA), 408A(c) (explaining that no deductions are allowed for contributions to Roth IRAs).

212. *See infra* notes 247-50.

213. *See* I.R.C. §§ 529-30 (showing no provision for pre-tax contributions); *infra* notes 220-222.

214. *See supra* notes 69-70, 77-78, 101-106 and accompanying text.

215. *See* email from Lora Cicconi to Liu Kong Weng, (Apr. 26, 2007) (on file with author) (asking

Proposals for CSAs put forth by academics and legislators in the U.S. mostly include after-tax contributions as well; the federal ASPIRE Act, Social Security KidSave Accounts, the California KIDS Account Act, the proposed Oregon law, and Boshara's ASAs would all function this way.[216] Sherraden's IDAs are the only exception; under at least one version of his plan, lower income individuals would contribute after-tax funds and receive matching grants in place of tax subsidies, but higher income individuals would be able to deduct their contributions in lieu of matching grants.[217]

2. *Contribution Limits*

i. *Existing Code*

All of the savings provisions in the Code limit the amount of contributions that can be placed into the savings vehicles. For example, combined contributions to 401(k)s and Roth 401(k)s may not exceed $15,000 a year, with catch-up contributions of an additional $5,000 allowed for those over fifty years of age.[218] Contribution limits for IRAs are considerably lower; taxpayers can contribute only $4,000 to traditional and Roth IRAs combined[219] with catch up contributions of an additional $1,000.[220] Contributions to

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whether parents could make pre-tax contributions to the accounts); email from Liu Kong Weng, Family Services Officer, Baby Bonus and Adoption Branch, Ministry of Child Development, Youth and Sports, to Lora Cicconi, (Apr. 27, 2007) (on file with author) (answering that my understanding was correct; parents may not make pre-tax contributions). The information about the taxation of the CSAs in Korea is not as readily available at this point as the program was just implemented this year. *See supra* notes 109-110.

216. The 1998 version of Kerrey's KidSave legislation would have allowed some form of pre-tax contributions in that it would have diverted payroll taxes from social security into the KidSave account. *See* Social Security KidSave Accounts Act, S. 2184, 105th Cong. (1998) *available at* http://www.govtrack.us/congress/bill.xpd?bill=s104-2184. It is hard to view the pre-tax contribution in that legislation as a savings incentive, however, because unlike voluntary pre-tax contributions allowed under 401(k) plans or IRAs, Kerrey's KidSave legislation required mandatory payroll tax contributions to KidSave accounts. Moreover, the latest version of the KidSave legislation does not divert payroll taxes and instead only allows after-tax contributions of $500 per year. *See* Social Security KidSave Accounts Act, H. 242, 110th Cong. (2007), *available at* http://govtrack.us/congress/bill11.xpd?bill=h110-242.

217. *See supra* note 127.

218. *See* IRS, Retirement Plans FAQs Regarding Designated Roth Accounts (2006), *available at* http://www.irs.gov/retirement/article/0,,id=152956,00.html#5 (last visited Oct. 3 2007).

219. *See* I.R.C. §§ 219(b)(1) (contribution lesser of table amount or AGI), 219(b)(5)(A) (table showing $4,000 limit), 408A(c)(2) (contribution limit to Roth IRAs determined by Section 219 less any amount contributed to traditional IRAs).

220. *See id.* §§ 219(b)(5)(B)(ii). Moreover, allowable contributions for Roth IRAs begin to phase out at higher income levels. *See* IRS, PUBLICATION 590, INDIVIDUAL RETIREMENT ACCOUNTS 58 (2006) (Roth IRA contributions begin to phase out at $95,000 for singles; $150,000 for married couples), *available at* http://www.irs.gov/pub/irs-pdf/p590.pdf. Allowable deduction amounts also phase out for traditional IRA contributions if the taxpayer or his or her spouse is covered by an employer retirement plan. *Id.* at 15-16 (if covered by a retirement plan at work, deduction begins to phase out at $50,000).

Coverdell accounts cannot exceed $2,000 annually.[221] Contributions to 529 savings accounts are not federally restricted. In order to qualify for Section 529 tax treatment, qualified tuition plans must "provide[] adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary."[222]

ii. Existing CSAs and CSA Proposals

Most existing and proposed CSAs have contribution limits just like the savings vehicles already present in the Code. In Britain, parents can contribute no more than GDP£1,200 per year into their children's Child Trust Funds.[223] In Canada, parents can contribute up to C$4,000 per year with a C$42,000 limit,[224] though Canada only matches contributions up to C$2,500 per year.[225] Hungary has a US$568 contribution limit, but only matches up to US$28 for middle and upper income families.[226] While it does not appear that Singapore or Korea have contribution limits to their accounts, they each have limits as to what the government will match.[227]

Most CSA proposals would also place restrictions on the amount of funds parents and others can contribute to their children's accounts. The ASPIRE Act would limit contributions to $1,000 (Senate bill),[228] as would Boshara's ASAs.[229] The current KidSave legislation would only allow contributions of up to $500 per year.[230] Because the Oregon CSA would be set up as a 529 savings account, the contribution limits established by the state would apply.[231] But the California proposal does not appear to place a limit on parental

221. *See* I.R.C. § 530(b)(1)(A)(iii) (2007). Contribution limits begin to decrease as income increases above $95,000 for single taxpayers and $190,000 for married taxpayers for Coverdell accounts. *See id.* § 530(c).

222. *See id.* § 529(b)(6). It is unclear whether this creates a meaningful restriction for contributions. *See* DYNARSKI, *supra* note 202, at 2 (noting that there is no limit on contributions to 529 savings accounts and that unlike IRAs or Coverdell accounts, the ability to contribute to these plans does not phase out at certain income levels).

223. *See supra* notes 70.

224. *See* Canada Revenue Agency, Registered Education Savings Plans (RESPs), http://www.cra-arc.gc.ca/E/pub/tg/rc4092/rc4092-e.html#P36_4823 (last visited Oct. 14, 2007).

225. *See supra* note 78.

226. *See supra* note 106.

227. *See supra* notes 94, 109-111.

228. ASPIRE Act of 2005, S. 868, 109th Cong. § 3 (2005). The House bill would allow up to $2,000 per year. *See* companion bill H.R. 1767, 109th Cong. § 4 (2005).

229. *See* BOSHARA, *supra* note 135, at 2.

230. Social Security KidSave Accounts Act, H. 242, 110th Cong. § 2 (2007).

231. *See* H.B. 2790, 74th Leg., Reg. Sess. (Or. 2007).

contributions.[232] While Sherraden would not limit contributions to his IDAs on a yearly basis, he would only allow individual and state deposits at certain milestones.[233]

3. Tax-Free Growth

i. Existing Code

The realization principle embedded in the U.S. tax code already guarantees that taxpayers need not incur tax liability every time an asset increases in value; instead, taxpayers are only taxed when a realization event occurs, such as the sale of property.[234] The reduced tax rate on capital gains further softens the blow from capital appreciation by allowing taxpayers to avoid ordinary income tax liability on certain types of assets if holding requirements are met.[235] The government has chosen to further subsidize savings by providing tax-free growth even when a realization event does occur or if the gain would be categorized as ordinary income so long as the assets are invested in a tax-preferred savings vehicle. Sections 401(k) and 408 provide for tax-free growth of investments,[236] and funds in Roth IRAs and Roth 401(k)s as well as education savings accounts may also earn income that is not includable in the accountholder's taxable adjusted gross income.[237]

ii. Existing CSAs and CSA Proposals

In this respect, existing and proposed CSA accounts resemble very closely the certain Code provisions. Britain's Child Trust Funds, Hungary's baby bonds, Canada's Learning Bonds and Singapore's matching grants are all deposited into accounts that grow tax-free, along with parental

232. *See* S.B. 752, 2007-08 Leg., Reg. Sess. (Cal. 2007).

233. *See* SHERRADEN, *supra* note 120, at 222.

234. *See* I.R.C. § 1001(b) (2007); Eisner v. Macomber, 252 U.S. 189, 212 (1920). Note that even taking out a mortgage on a property is not considered a realization event, even though the taxpayer now has the liquid funds available to pay tax. *See* Woodsam Assoc., Inc. v. Comm'r, 198 F.2d 357 (2d Cir. 1952).

235. *See* I.R.C. §§ 1(h), 1221, 1222.

236. *See, e.g.*, *id.* §§ 501(a) (organization described in 401(a) is exempt from taxation under this section), 401(k) (employer-sponsored deferral plans meet 401(a) requirements), 408(e)(1) (IRAs exempt from taxation).

237. *See, e.g.*, *id.* I.R.C. §§ 408A(a) (except as otherwise provided, Roth IRAs are treated in same manner as IRAs), 402A(a), 402A(e)(1)(applicable retirement plan that includes Roth 401(k)s is not disqualified as an applicable retirement plan under 401(a) which is exempt from tax under § 501(a)), 529(a) (qualified tuition program under § 529 shall be exempt from taxation), 529(c)(1) (neither beneficiary nor contributor to § 529 account must include distribution or earnings from § 529 account in gross income), 530(a) (§ 530 accounts shall be exempt from taxation).

contributions, until withdrawn.[238] Sherraden's IDAs[239] and Boshara's ASAs[240] would also benefit from tax-free growth, as would the accounts in the ASPIRE Act,[241] the current KidSave bill,[242] and the proposed California and Oregon bills.[243]

4. *Treatment at Withdrawal*

i. *Existing Code*

The divergence of traditional and Roth-type tax-preferred savings methods at contribution continues at withdrawal. Because traditional 401(k)s and IRAs are funded with pre-tax contributions, the entire amount withdrawn from the savings account is subject to ordinary income tax at withdrawal.[244] This is the case even if the gains would otherwise be capital gains and even if no penalty is assessed upon withdrawal.[245]

In contrast, Roth IRAs are funded with after-tax contributions, but receive advantageous tax treatment at withdrawal. There is no tax on distributions made after the taxpayer reaches the age of fifty-nine and a half or for other certain qualified distributions[246] so long as they are made five years after the

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238. *See supra* notes 70, 79, 95, 106, and accompanying text. It is not yet clear whether Korea's CSAs are tax-exempt accounts.

239. *See* SHERRADEN, *supra* note 120, at 223.

240. *See* BOSHARA, *supra* note 135, at 3.

241. *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 3 (2005). *See also* companion bill H.R. 1767, 109th Cong. § 4 (2005).

242. *See* Social Security KidSave Accounts Act, H. 242, 110th Cong. § 2 (2007).

243. *See* S. 752, 2007-08 Leg., Reg. Sess. §§ 1, 2 (Cal. 2007); H. 2790, 74th Leg., Reg. Sess. §§ 1, 3 (Or. 2007). While in most cases the treatment of capital accounts or stakeholder accounts is not relevant in Parts III.B.1-4 because they are not savings provisions, in this case it is worth noting that Klein specifically discusses the tax treatment of his Universal Personal Human Capital Accounts and states that recipients will not be taxed on the growth in the accounts. *See* Klein Revised Proposal, *supra* note 155, at 4.

244. *See* I.R.C. §§ 402(a) ("any amount actually distributed to the distributee [by trusts described in 401(a)] shall be taxable to the distributee . . . under section 72 (relating to annuities)), 401(c) (employer-sponsored retirement plans meet the requirements of 401(a)), 408(d) ("any amount paid or distributed out of an individual retirement plan shall be included in gross income by the payee or distributed, as the case may be, in the manner provided under section 72"), 72(a) (2007) ("except as otherwise provided in this chapter, gross income includes any amount received as an annuity . . . under an annuity, endowment or life insurance contract).

245. *See supra* note 244 in which the relevant code sections make no distinction between capital gains and ordinary income.

246. *See* I.R.C. § 408A(d)(1) ("[a]ny qualified distribution from a Roth IRA shall not be includible in gross income"). Qualified distributions from a Roth IRA include distributions after the taxpayer is fifty nine and a half, distributions made to a beneficiary after the death of the individual, distributions attributable to a disability, or distributions for a first home purchase. *See* I.R.C. § 408A(d)(2)(A)(i)-(iii). Distributions

Roth IRA is opened.[247] Moreover, nonqualified distributions are tax-free to the extent that they represent the amount the individual contributed to the Roth IRA. Only when distributions begin to exceed contributions must the account-holder report income,[248] reflecting the fact that tax has already been paid on contributed funds.

Roth 401(k)s work in a similar manner in that distributions after retirement or for other qualified purposes are tax-free.[249] However, unlike Roth IRA distributions, nonqualified Roth 401(k) distributions are not completely excludable from income until the distribution exceeds the contribution. Instead, Roth 401(k) distributions are taxed based on the proportion of the distribution attributable to earnings,[250] thus, nonqualified distributions are partially taxed even if they are less than the contributed amount.

Section 529 qualified tuition plans and Coverdell education savings accounts, which are also funded with after-tax contributions, may be withdrawn tax-free for educational purposes.[251] Moreover, as with the Roth-type retirement methods, distributions in excess of qualified expenses (in this case education expenses only) result in ordinary income treatment only to the extent that they exceed contributions or to the extent that a certain portion of the

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for a first home purchase are also considered qualified. *See* I.R.C. §§ 408A(d)(2)(A)(iv), 408A(d)(5),72(t)(2)(F). Note that these qualified distributions overlap with the exceptions to the 10% penalty on early distributions for both traditional and Roth IRAs described *infra* notes 265-274.

247. Distributions made during the five-year period starting with the individual's first contribution to the Roth IRA are not qualified distributions, even if they otherwise meet the criteria described above. *See* I.R.C. § 408A(d)(2)(B).

248. *See id.* §§ 408A(d)(2)(C), 408(d)(4) (2007); Treas. Reg. § 1.408A-6 Q&A (4) ("[a] distribution that is not a qualified distribution . . . is includable in the owner's gross income to the extent that the amount of the distribution . . . exceeds the owner's contributions to all of his or her Roth IRAs").

249. *See* I.R.C. §§ 402A(d)(1) (qualified distributions not reportable in gross income), 402A(d)(2) (qualified distribution has same meaning as in I.R.C. § 408A(d) (Roth IRA distribution provision) except that purchase of first home is not a qualified distribution for Roth 401(k) purposes).

250. *See* IRS, PROPOSED REGULATIONS, DESIGNATED ROTH ACCOUNTS UNDER SECTION 402A, 26, CFR 10 (2007), *available at* http://www.irs.gov/pub/irs-regs/14645905.pdf (ordering rules of section 408A do not apply; instead income from Roth 401(k) distributions are determined under 72(e)(8), which bases income on the proportion of the distribution not attributable to a contribution. Therefore, if a nonqualified distribution of $5,000 is made and the account consists of $9,400 of contributions and $600 of earnings, the individual should report $300 of income, as $4,700 of the distribution can be attributable to previous contributions).

251. *See* I.R.C. § 529(c)(3)(B)(i)-(ii) (2007) (neither in-kind or cash distributions for education expenses includable in gross income). This provision was set to sunset in 2010 but the Pension Protection Act of 2006 made the tax-free withdrawal permanent. *See* James Pethokoukis, *A College Savings Plan with One Less Worry*, N.Y. TIMES, Sept. 12, 2006, at 5. *See also* I.R.C. § 530(d)(2)(A) ("[n]o amount shall be includible in gross income under paragraph (1) if the qualified education expenses of the designated beneficiary during the taxable year are not less than the aggregate distributions during the taxable year").

distribution may be attributable to earnings not used for qualified educational purposes.[252]

ii. Existing CSAs and CSA Proposals

There is no uniform tax treatment of CSA withdrawals among the existing CSAs or CSA proposals. Some existing CSAs and proposals which require after-tax contributions allow tax-free withdrawals for qualified purposes, similar to Roth IRAs. For example, parents may use the funds in Singapore's Children's Development Accounts for qualified purposes without paying any taxes.[253] The federal ASPIRE Act would also allow for tax-free withdrawals for approved uses,[254] as would both the California and Oregon legislation.[255] With similar restrictions on use, Boshara's ASAs could be withdrawn tax-free as well.[256]

Canada takes a somewhat hybrid approach. The government allows tax-free withdrawal of funds that account holders or their families contributed to the RESP accounts so long as the money is used for post-secondary education expenses. However, Canada does require that government contributed funds, as well as earnings on the entire account, be reported in ordinary income once withdrawn.[257] The contributions, which are made with after-tax dollars, escape a second layer of taxation at withdrawal, but all earnings on those contributions as well as government contributed funds are taxed.

In contrast, all of the money in Britain's Child Trust Funds, and presumably in Hungary's baby bond accounts, are subject to ordinary income

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252. *See* I.R.C. §§ 529(c)(3)(A) ("distribution under a qualified tuition program shall be includable in the gross income of the distribute in the manner as provided under section 72"), 530(d)(1) ("any distribution shall be includible in the gross income of the distribute in the manner provided in section 72"). The formula for calculating reportable income for Coverdell accounts somewhat resembles the treatment of distributions from Roth 401(k)s. The taxpayer must first determine the portion of the distribution that represents tax-free earnings (multiply the distribution by a fraction with basis as numerator and total amount in account as denominator), then must take the tax-free earnings portion and multiply it by the percentage of the distribution attributable to education expenses. *See* I.R.C. § 530(d)(2)(B); IRS, PUB. NO. 970, TAX BENEFITS FOR EDUCATION, at ch. 7 (2006), *available at* http://www.irs.gov/publications/p970/ch07.html.

253. *See* email from Liu Kong Weng, Family Services Officer, Baby Bonus and Adoption Branch, Ministry of Child Development, Youth and Sports, to Lora Cicconi, ("the funds in the Children Development Account (CDA) are not taxable") (Apr. 25, 2007) (on file with author).

254. *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 7 (2005). *See also* companion bill H.R. 1767, 109th Cong. § 7 (2005). It is not as clear how the KidSave legislation would treat withdrawals. The funds would be invested in the Thrift Savings plan and would only be available at retirement, but the law does not specify whether the funds could be withdrawn tax-free at that point. *See* Social Security KidSave Accounts Act, H. 242, 110th Cong. (2007).

255. S. 752, 2007-08 Leg., Reg. Sess. § 2 (Cal. 2007); H. 2790, 74th Leg., Reg. Sess. § (Or. 2007).

256. *See* BOSHARA, *supra* note 135, at 3.

257. *See supra* notes 81-82 and accompanying text.

tax when withdrawn at age eighteen—even the funds contributed by the account holders and their families with after-tax dollars.[258] In these countries, the scheme resembles neither the traditional or Roth plans in the U.S. in that after-tax funds must be used to contribute to the accounts, yet the funds are taxed once again at withdrawal. While this set-up certainly varies from most savings incentives, the tax liability at both contribution and withdrawl is mitigated because government funds are contributed to these accounts, albeit not in proportion to savings behavior. Moreover, the beneficiary may be exposed to very low tax rates at withdrawal. When the beneficiaries receive their Child Trust Funds, they are most likely to be either attending school or earning wages on the lower end of the income scale due to their young age and recent entry to the labor market.[259]

The recognition that beneficiaries face very low tax rates at withdrawal may help explain why most CSA proposals favor a Roth-like tax scheme.[260] Under the current Code, prudent taxpayers can customize their savings plans based on their current and expected incomes. They may invest in Roth IRAs if they believe they are in a lower tax bracket now than they will be at retirement, and a traditional IRA if the opposite is true. Ultimately the taxpayer is making nothing more than an educated guess about his or her future tax liability at retirement age. In contrast, a CSA system that gave participants the choice between a traditional tax-at-withdrawal scheme and a Roth tax-at-contribution scheme would give taxpayers considerably more flexibility since the taxpayer who contributes to the account is separate from the taxpayer who withdraws from the account.[261] Parents could be fairly certain that their child will face a lower tax marginal rate while attending post-secondary school or working in low income jobs than the parents themselves face at contribution time, and thus would always opt for the pre-tax contribution plan.[262] The government might never recoup its lost revenues

258. *See supra* notes 70, 107 and accompanying text.

259. The Canadian government noted this in its discussion of the tax treatment of withdrawals. *See supra* note 82 and accompanying text. William Klein made a similar observation in his paper, though in reference to the poor, rather than the young. *See* Klein Revised Proposal, *supra* note 155, at 15 (though withdrawals from Universal Personal Capital Accounts are taxable, the poor will likely not pay taxes on distributions from their Universal Personal Capital Accounts because they face low tax rates to begin with).

260. It might also help explain why education savings accounts in the U.S. are structured in the Roth manner.

261. This is somewhat reminiscent of income splitting between spouses, only it occurs over time and between parent and child rather than concurrently between spouses.

262. While theoretically there exists the same risk in the current U.S. 401(k) and IRA system, it seems that taxpayers can never be certain that they will face very low tax rates at retirement (or whenever they withdraw the funds), whereas parents investing in a CSA could be fairly sure that their children would be in a very low tax bracket when receiving distributions from the CSA, either because they are in post-secondary school, or because they are just entering the job market.

because recipients would generally be in a very low tax bracket at distribution.[263] Even CSA legislation like Britain's, which technically requires after-tax funds at contribution and tax at withdrawal, may effectively only tax at one point to the extent that the majority of beneficiaries preside in very low tax brackets at distribution.

5. Restrictions on Withdrawal Uses

i. Existing Code

All of the savings provisions in the Code considered here have penalties for early withdrawal. For example, funds in an IRA may only be withdrawn free of penalty before the taxpayer reaches age fifty-nine and a half,[264] if the taxpayer is separated from service after age fifty-five,[265] dies or becomes disabled,[266] uses the funds for medical expenses,[267] higher education expenses,[268] a first home purchase,[269] health insurance premiums if unemployed,[270] or if they are part of a series of substantially equal payments for the remainder of the taxpayer's life.[271]

Roth IRAs are subject to a similar scheme. The same 10% penalty that applies to early distributions under traditional IRAs applies to any

263. One might argue that the fact that many of these CSAs provide matching grants in addition to tax-free withdrawal alters this picture because the contribution is still subsidized, even though made with after-tax dollars. But the matching scheme poses less of a risk of game-playing than the pre-tax contribution, as matching grants go directly into the savings account for the child, whereas pre-tax contributions allow parents to reduce their overall tax liability and spend the saved funds on whatever they please.

264. *See* I.R.C. §§ 72(t)(1) (general provision stating that 10% penalty applies on early distributions for retirement plans), § 72(t)(2)(A)(i)-(iii) (10% penalty does not apply to distributions made after the taxpayer reaches age fifty-nine and a half) (2007).

265. *See id.* § 72(t)(2)(A)(v) (10% penalty does not apply to separation from service after age fifty-five).

266. *See id.* § 72(t)(2)(A)(i)-(iii) (10% penalty does not apply to distributions made to a beneficiary on or after the death of the employee, or attributable to a disability).

267. *See id.* § 72(t)(2). The medical expenses must exceed 7.5% of the taxpayer's adjusted gross income. *Id*.

268. *See* I.R.C. § 72(t)(2)(E) (2007). The distributions may not exceed the qualified education expenses of the taxpayer for the taxable year. *Id.*

269. *See id.* § 72(t)(2)(F). The home purchase exception is limited to $10,000 and only applies to those who have not owned a home for the last two years. *See id.* § 72(t)(8).

270. *See id.* § 72(t)(2)(D).

271. *See* I.R.C. § 72(t)(2)(A)(iv) (2007). *See also id.* § 72(t)(2)(A)(vi)-(vii) (exception for dividends and levy against retirement plan). In addition to penalties for unqualified withdrawals, IRA and 401(k) accountholders may also be subject to a 50% excise tax to the extent that they do not take minimum distributions required after age 70 and a half. *See id.* §§ 408(a)(6), 408(b)(3), 401(a)(9). These rules only apply to Roth IRAs if the accountholder dies. *See* Treas. Reg. § 1.408A-6, Q&A (14) (1999).

nonqualified Roth IRA distribution that is includable in gross income,[272] as well as to nonqualified distributions not includable in gross income that year to the extent the distribution is allocable to a conversion from a traditional IRA and was made within five years of the contribution.[273] However, because income tax is levied only on the amounts in excess of contributions to the Roth IRA,[274] the 10% penalty will only apply to distributions in excess of contributions.[275]

The 401(k) plan rules are stricter. For traditional 401(k)s, distributions made prior to age fifty-nine and a half are subject to a 10% penalty even if necessary for a financial hardship such as education or a home foreclosure.[276] The penalty is only excepted if the taxpayer dies or is permanently disabled,[277] experiences a separation from service,[278] has significant medical expenses,[279] takes early retirement at fifty-five years of age,[280] receives distributions as part of substantially equal payments over the taxpayer's lifetime,[281] or receives distributions required by divorce or separation agreement.[282] Roth 401(k)s are subject to the same rules as traditional 401(k)s,[283] though because income is only recognized in proportion to the contributions/earnings ratio in the

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272. *See id.* § 1.408A-6, Q&A (5)(a) (stating that 72(t) 10% penalty rules apply to nonqualified Roth IRA distributions); *supra* note 247 for list of qualified Roth IRA distributions, which all overlap with the exceptions from the 10% penalty in 72(t).

273. *See id.* § 1.408A-6, Q&A (5)(b).

274. *See* I.R.C. § 408A(d)(2)(C) (2007); Treas. Reg. § 1.408A-6 Q&A (4) (1999) ("A distribution that is not a qualified distribution . . . is includable in the owner's gross income to the extent that the amount of the distribution . . . exceeds the owner's contributions to all of his or her Roth IRAs").

275. *See* I.R.C. § 72(t)(1) (10% penalty applies only to portion of distribution includible in gross income); Treas. Reg. § 1.408A-6 Q&A (4) (only distributions in excess of contributions are income).

276. *See* I.R.C. § 72(t)(1) (2007). *See also id.* § 72(t)(D)-(F) (the first home purchase, higher education, and health insurance exceptions only apply to IRAs, not other qualified deferred compensation plans like 401(k)'s). In order to qualify as a 401(k) plan, an employer may only allow hardship distributions in certain circumstances as defined in Treas. Reg. § 1.401(k)-(1)(d). But even if an employee can prove that such a hardship exists, the withdrawal is not exempt for the 10% penalty or ordinary income tax, as described above. *See id.* §§ 72(t)(1), 72(t)(2)(D)-(F). It is also important to note that although hardship distributions are permitted by law, employers do not have to allow them.

277. *See id.* § 72(t)(2)(A)(i)-(iii).

278. *See id.* § 72(t)(2)(A)(v).

279. *See* I.R.C. § 72(t)(2)(B) (2007). Again, these must exceed 7.5% of the taxpayer's adjusted gross income. *Id.*

280. *See id.* § 72(t)(2)(A)(i)-(iv). This exception does not apply to IRAs. *See id.* § 72(t)(3)(A).

281. *See id.* § 72(t)(2)(A)(iv).

282. *See* I.R.C. § 72(t)(2)(C) (2007). This exception does not apply to IRAs. *See id.* § 72(t)(3)(A).

283. Section 72—which mandates the 10% tax on early distributions under 72(t)—still governs Roth 401(k)s. *See id.* §§ 402(a) (distributions of 401(a) plans taxed under section 72); 402A(e)(1)(A) (Roth 401(k) plans qualify as 401(a) plans); IRS, PROPOSED REGULATIONS, DESIGNATED ROTH ACCOUNTS UNDER SECTION 402A, 26, CFR 5 (2007), *available at* http://www.irs.gov/pub/irs-regs/14645905.pdf ([u]nder section 402(a), a distribution under 401(a) is taxable under section 72).

account,[284] the 10% penalty applies to only to a portion of the distribution, rather than the entire distribution as it would under a traditional 401(k).

Withdrawals from the education savings provisions are also subject to a 10% penalty if includable in gross income. Funds used for higher educational expenses (section 529 qualified tuition program) or elementary, secondary, or higher education expenses (section 530 Coverdell accounts) are not includable in income, but distributions in excess of educational expenses are includable in income to the extent they are attributable to tax-free earnings on contributions.[285] For Coverdell accounts, the only exceptions to this rule exist if the payment is made to a beneficiary on or after his or her death, attributable to a beneficiary's disability, made on account of a scholarship, or made for a beneficiary attending a military academy.[286] Further, because any remaining balance in a Coverdell savings account after the beneficiary reaches age thirty must be distributed within thirty days, any amount of forced distribution reportable in earnings is subject to the 10% penalty as well.[287]

ii. Existing CSAs and CSA Proposals

CSAs vary considerably in the flexibility allowed at withdrawal. For example, Singapore has a policy far more restrictive than the rules governing IRAs, 401(k)s and education savings accounts in the United States. The funds in Singapore's Children's Development Accounts are completely restricted to education and medical spending.[288] Unused funds may be rolled over into

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284. *See* IRS, PROPOSED REGULATIONS, DESIGNATED ROTH ACCOUNTS UNDER SECTION 402A, 26, CFR 10 (2007), *available at* http://www.irs.gov/pub/irs-regs/14645905.pdf.

285. *See* I.R.C. §§ 530(d)(4) (tax is increased by 10% for taxpayer who receives distribution for other than educational expenses), 529(c)(6) ("[t]he tax imposed by section 530(d)(4) shall apply to any payment or distribution from a qualified tuition program in the same manner as such tax applies to a payment or distribution from a Coverdell education savings account"), 529(c)(3)(A) ("distribution under a qualified tuition program shall be includable in the gross income of the distribute in the manner as provided under section 72 to the extent not excluded from gross income under any other provision of this chapter"), 530(d)(1) ("[a]ny distribution shall be includible in the gross income of the distribute in the manner provided in section 72"). While funds in 529 savings accounts may only be used for higher education expenses, *see id.* §§ 529(e)(3), (e)(5). Funds in Coverdell education accounts may be used for elementary and secondary education expenses as well. *See id.* § 530(b)(2).

286. *See id.* § 530(d)(4)(B)(i)-(iv). The 529 provision does not specify exceptions to the 10% penalty. *See id.* § 529 .

287. *See* I.R.C. § 530(b)(1)(E) (2007). The parent of a child with a Coverdell account who does not use the funds for education cannot liquidate the Coverdell account himself or herself, even if willing to pay taxes and penalties—the funds go directly to the child after age thirty. No similar provision requiring distribution to the child beneficiary exists in 529 accounts, which can be transferred to another child. As a result, the 529 savings accounts have more flexibility at withdrawal than the Coverdell accounts. *See* DYNARSKI, *supra* note 202, at 5.

288. *See* Official Baby Bonus website, http://www.babybonus.gov.sg/bbss/html/index.html (last visited Oct. 14, 2007); email from Liu Kong Weng, Family Services Officer, Baby Bonus and Adoption

other education and retirement savings vehicles,[289] but parents may not withdraw any money in cash, because the funds are available only for government-approved uses until retirement.[290]

On the other hand, Canada's CSAs have fewer penalties for nonqualified distributions than U.S. savings vehicles. Because Canada's CSAs exist as part of RESP education savings accounts, funds may only be withdrawn without penalty for postsecondary education purposes. However, if neither the account beneficiary nor his or her siblings attend college,[291] the parents can withdraw the funds or roll them over into their retirement account and retain all of their contributions, as well as earnings on the government contributions. They must only return the government contributed funds.[292] Though the plan differentiates between funds distributed for education and those simply withdrawn—with no penalty at all for education spending—it is more generous than the IRAs, 401(k)s, or education savings accounts in the Code. Money contributed to the account by the parents, earnings on those contributions, and earnings on the government funds are all returned free of penalty regardless of how the funds are used.

Britain's Child Trust Funds are even more liberal at distribution. When children reach 18 years of age, they receive the money in their CSAs, which includes both the government contributions and the contributions by the accountholders' families and friends, as well as earnings on those contributions. While the distribution is subject to ordinary income tax, there is no penalty if the money is used for something other than what the government might deem a worthwhile cause.[293] The British government chose not to impose use restrictions after a series of public consultations led officials to conclude that restrictions would impose additional compliance costs and run counter to the policy objective of helping young individuals become aware of both financial opportunity and responsibility.[294]

In contrast to the varied treatment that current CSAs impose at withdrawal, proposals for CSAs in the U.S. are generally restricted at withdrawal with penalties similar to existing Code provisions. The ASPIRE

Branch, Ministry of Child Development, Youth and Sports, to Lora Cicconi, ("[p]arents will not be able to withdraw the CDA funds in cash") (Apr. 25, 2007) (on file with author).

289. *See* Loke & Sherraden, *supra* note 6, at 5-6.

290. *See supra* note 289. One might argue that the Coverdell accounts are restricted in a similar way for parents, as the parents themselves cannot liquidate the account if the child does not attend college. In that event, the funds must go to the child beneficiary, but the account can still be liquidated, albeit by the beneficiary rather than the parents. *See* DYNARSKI, *supra* note 202, at 4-5.

291. *See supra* notes 83-84 and accompanying text.

292. *See id.*

293. *See supra* note 70 and accompanying text.

294. *See* CRAMER, *supra* note 135, at 27 & n.75. Korea's government has not specified any use limits on its CSAs yet.

Act, for example, would function with the same distribution rules as Roth IRAs. Designated withdrawals would be allowed, but other withdrawals would be subject to the 10% penalty to the extent that they are attributable to earnings rather than contributed funds.[295] In order to account for the fact that the contributions begin as early as birth, the ASPIRE Act would disallow any withdrawals before the recipient reaches eighteen years of age.[296] To ensure that direct government endowments are not misused, nonqualified withdrawals from the government contribution portion of the account are subject to a 100% penalty. Much like the Canadian approach, the account holder under the ASPIRE Act will lose all government contributions if he or she takes a distribution for nonqualified purposes.[297] The California Kids Account Act would treat distributions almost exactly like the ASPIRE Act,[298] and the Oregon bill would presumably have the same distribution rules as a 529 account under the current Code, allowing tax-free withdrawals for education.[299] The latest version of the social security KidSave legislation is the least liberal of the United States CSA proposals, because it would only allow distributions when social security benefits begin to accrue or on the death of the recipient.[300]

Academic proposals for CSAs have generally called for restrictions at withdrawal as well. Boshara's ASAs, like the ASPIRE Act accounts, would disallow withdrawals before age 18 and then only allow penalty-free

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295. *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 6 (2005). *See also* companion bill H.R. 1767, 109th Cong. § 6 (2005).

296. The issue of distributions before age eighteen does not usually arise in Roth IRAs because individuals must have earned income to contribute to a Roth IRA.

297. This might not be as burdensome as it might first appear because distributions are assumed to derive first from contributions, then earnings, and then government contributions, therefore an accountholder could avoid the forfeiture of government contributions so long as he or she retained at least the government contribution amount in the account. Further, only government contributions are subject to the 100% tax, not earnings on those contributions. *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 6 (2005). *See also* companion bill H.R. 1767, 109th Cong. § 6 (2005). It is also worth noting that the accounts under the ASPIRE Act may rolled over into § 529 savings accounts or Roth IRAs, but because neither rollover would minimize the penalties for early distributions (the ASPIRE Act accounts are already subject to Roth IRA distribution rules, and are more liberal than § 529 distribution rules, and the government contribution forfeiture would continue in the rollover), I do not discuss it as a possibility that would provide different results at distribution.

298. *See* S.B. 752, 2007-08 Leg., Reg. Sess. §§ 1,2 (Cal. 2007). The law would allow the accountholder to withdraw funds after his or her eighteenth birthday for educational expenses, a first home purchase, or retirement savings penalty-free. Nonqualified distributions would be subject to the 10% penalty to the extent that they represented earnings rather than contributions, and the government funds would be withheld by the Treasury in those cases. *Id.*

299. *See* H.B. 2790, 74th Leg., Reg. Sess. §§ 1, 3 (Or. 2007).

300. *See* Social Security KidSave Accounts Act, H.R. 242, 110th Cong. § 2 (2007). This scheme is reminiscent of the Singapore CSA plan which does not allow for any cash distributions.

withdrawals for education, home purchase, or business capitalization until retirement.[301] In Sherraden's IDAs, non-designated withdrawals would result in substantial penalties, and all government contributions and earnings would revert to an IDA Reserve fund.[302]

In this part, we can begin to consider the universal capital account and stakeholder plans as well because the withdrawal restriction is an issue that applies regardless of whether the proposal includes a savings component. Tobin, Klein, and Haveman's capital accounts would all place severe restrictions on account withdrawals.[303] Tobin's National Youth Endowments could only be drawn upon for approved training and education programs,[304] and Klein's and Haveman's Universal Personal Capital Accounts could only be drawn upon for education or medical expenses.[305] With all of these proposals the restriction on withdrawal is presumably equivalent to a bar on nonqualified distributions—there does not appear to be an option to withdraw funds for non-designated purposes and pay a penalty as with the current Code savings provisions.[306] Klein argued that use restrictions were necessary because any poverty relief program must accept the constraint that taxpayer non-recipients want "the satisfaction of knowing that their tax dollars are being spent for purposes that they consider . . . desirable or meritorious from their own perspective."[307] However Klein recognized that this use limitation might lead to overuse of a certain type of benefit, and in order to mitigate this possible consequence, Klein (and Haveman, though not Tobin) believed that the accounts should be available for retirement if not used for education or medical purposes.[308]

In contrast to the capital account proposals, the stakeholder proposals would place no restrictions on the use of funds. Ackerman and Alstott forcefully rejected the concept that recipients should only be able to use funds for certain purposes. They argued that any use limitations would unduly restrict the choices of those not going to college given that investing in human

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301. *See* BOSHARA, *supra* note 135, at 2. Boshara notes that the Roth IRA distribution rules could apply, though he does not specify whether there would be a 100% tax on government contributions. *Id.*

302. SHERRADEN, *supra* note 120, at 223. Sherraden does not specify what those substantial penalties would be, but it appears that they would be in addition to the reversion of the government contributions. *Id.*

303. *See supra* notes 148-176. This is similar to the Singapore plan and the proposed KidSave accounts. *See supra* note 302.

304. *Id.*

305. *Id.*

306. *Id.*

307. Klein Revised Proposal, *supra* note 155, at 2. Klein notes that this could either be viewed as "achieving positive externalities or enlisting political support." *Id.*

308. *Id.*

capital may not be the best life plan for many Americans.[309] Some individuals might prefer to use their stake to move out of an unsafe neighborhood, or spend the money on an "unforgettable wedding" or foreign travel.[310] Despite their almost visceral objection to use restrictions,[311] Ackerman and Alstott's stakeholding plan would limit the government's manner of doling out funds, only providing the full $80,000 to high school graduates going on to college. High school graduates without college plans would receive their $80,000 over four years in their twenties, and non-high school graduates would only receive the interest on their stake.[312]

6. Direct State Funding and Matching Programs

While it may seem somewhat disingenuous to distinguish between direct state funding and tax incentives,[313] the distinction may be of importance to the American public and to legislators, as the most notable difference between existing tax law and the proposed child savings legislation in the U.S. (as well as existing CSAs) is the direct government grant and/or matching funds apparent in many of the latter. Neither 401(k) plans, IRAs, nor education savings accounts have any entitlement or matching component. Taxpayers may lower their tax liability by contributing to savings vehicles, but they do not receive any initial government funds nor do they receive matching grants for each dollar saved.[314] In contrast, the existing CSAs—as well as CSA proposals and much of the academic literature—are built upon the concept that the government should make an initial deposit into CSAs and often match family contributions to give families a head start towards savings.

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309. *See* ACKERMAN & ALSTOTT, *supra* note 64, at 215-16.

310. *Id.*

311. *Id.* at 216. ("[w]e are repelled by programs that require kids from the wrong side of the tracks to justify their lives to a government bureaucrat").

312. *Id*. at 7-8, 38, 53-57. This observation might lead one to argue that, in practice, Ackerman and Alstott's plan is not exceptionally more liberal than the human capital accounts or the CSA-like proposals. Moreover, the authors concede that if use restrictions were the political price for enacting stakeholding, they would be willing to pay. *Id*. at 215.

313. *See supra* notes 192-94 (discussing how social policy programs are funded either directly or via tax expenditures).

314. Of course, the Code does have direct funding programs related to family size, but they appear outside of the savings provisions. For example, the Earned Income Tax Credit refunds money to families in a complicated formula that depends on both income levels and the number of children that they have. *See* I.R.C. § 32(a) (2007). The Tax Code also provides partially refundable tax credits for each child a family has so long as their income is below a certain amount. *See id.* § 24(a)-(b). The Code also provides a credit for two-earner families with children, but it is not refundable. *See id.* § 21(a).

i. Matching Funds

On a theoretical level, the incentive of a matching grant does not vary significantly from the incentive of a pre-tax contribution. In either scenario, the government is giving the taxpayer a subsidy that grows in proportion (though not necessarily in direct proportion) to the amount the taxpayer contributes to a savings account. However, two characteristics of the matching grants in the CSAs distinguish them significantly from a pre-tax contribution.[315] To begin with, while the distributional effects of a pre-tax contribution tool are a direct function of the structure of the tax system, a matching plan gives the government the flexibility to distribute the savings tool in a variety of different ways. For example, savings incentives based on pre-tax contributions primarily benefit the wealthy, because the advantage of the incentive increases as tax rates progress.[316] In contrast, governments that have implemented CSAs have structured their matching programs to benefit all participants equally or to target the poor. For example, in Korea and Singapore the government matches funds contributed into CSAs on a dollar-for-dollar basis up to certain variable limits.[317]

For example, in Korea and Singapore, the government recognized that even with a 20% matching grant across the board for the nation's education savings accounts, poor families still showed very low participation rates. Thus, it created an enhanced matching program that matches up to 40% of the first C$500 that low income families contribute annually to their children's education savings accounts.[318] Hungary's plan also makes additional matches for lower income families,[319] and the ASPIRE Act seeks to achieve a similar goal by matching funds that only low income families deposit into the CSAs.[320] While Sherraden does not specify the precise matching ratio for his

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315. In addition to the two distinctions I discuss in the text, there is also the more obvious point that a matching program puts funds directly into the savings account, whereas pre-tax contribution allows the individual to reduce his or her tax liability and use the saved funds for purposes other than the savings account. I do not focus on it in the text as a major difference between CSAs and the Code because I view it as primarily administrative, though this difference does influence the way the rest of the analysis plays out. *See infra* note 327.

316. *See supra* note 204.

317. Singapore's policy is very generous, matching dollar for dollar contributions up to US$3,750 for the second child and US$7,500 for third and fourth children. *See supra* note 95 and surrounding text. Currently Korea matches savings of up to US$30 per month. *See supra* note 110 and surrounding text.

318. *See supra* notes 74-77 and accompanying text. Now all families receive 20% matching grants for contributions up to C$2,500, but low income families receive an additional 20% match for the first C$500 that they contribute. *Id.*

319. *See supra* note 107 and surrounding text.

320. The ASPIRE Act would match dollar for dollar funds contributed by low income families, up to $500 (Senate bill) and $1,000 (House bill). *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 6 (2005); companion bill H.R. 1767, 109th Cong. § 6 (2005).

proposed IDAs, he envisions progressive match rates.[321] Boshara's ASAs would not have a strict matching program, but there would be an additional tax credit for low income families who placed funds directly into the account.[322]

A more relevant distinction exists between the matching funds that many CSA policies include and the pre-tax contributions allowed in traditional 401(k)s and IRAs. This distinction includes the tax treatment of the various policies at withdrawal. The tax and/or subsidy treatment of any sort of savings vehicle at contribution does not exist in a vacuum; it can only be fully understood when also considering the correlating treatment when the funds are withdrawn. While 401(k)s and IRAs allow pre-tax contributions, all of the funds in the account are taxed upon withdrawal to compensate for the fact that they were not taxed up front. In contrast, because many of the CSAs follow a Roth-type tax scheme, allowing tax-free withdrawals in return for after-tax contributions results in subsidies at both ends of the transaction. Taxpayers receive a matching non-tax subsidy at contribution as well as a tax subsidy at withdrawal. This type of treatment is not recognizable in the Code, and suggests that even those CSAs that follow a tax scheme similar to Roth IRAs and 401(k)s are actually quite far removed from any Code incentives once we consider the matching subsidies.[323]

ii. Direct State Deposits

While the Code lacks any type of direct subsidies in its savings vehicles, government endowments are nearly a constant across all existing CSAs, CSA proposals, and even the boldest academic proposals. In Britain, families receive between GDP£250 and GDP£500 at birth depending on income, with an additional installment of an equal amount when the child reaches the age of seven.[324] The Canadian government places up to C$2,000 in the education savings accounts of low income families over the first fifteen years of the

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321. *See generally* SHERRADEN, *supra* note 120, at 221-23.

322. *See* BOSHARA, *supra* note 135, at 2. On the other hand, certain CSAs do not match funds that are contributed into the accounts. For example, Britain does not match contributed funds, *see supra* notes 67-68 and surrounding text, nor would the KidSave legislation, the California KIDS Account Act or the Oregon legislation. *See* Social Security KidSave Accounts Act, H.R. 242, 110th Cong. § 2 (2007); S.B. 752, 2007-08 Leg., Reg. Sess. §§ 1-2 (Cal. 2007); H.B. 2790, 74th Legis., Reg. Sess. §§ 1, 3 (Or. 2007). The British government does deposit additional funds into the child's account when he or she reaches age 7, but these deposits are not conditioned upon savings behavior. *See supra* notes 67-68 and surrounding text.

323. However, the fact that the matching funds may only go into the child's savings account, as compared to a pre-tax contribution which reduces tax liability thereby freeing up funds for any use, suggests that the matching program at grant plus tax-free withdrawal is not as problematic as a pre-tax contribution and tax-free withdrawal. *See supra* notes 264, 317.

324. *See supra* note 67 and accompanying text.

child's life.[325] Singapore distributes US$2,038.49 for the first and second children and US$4,076.93 for the third and fourth children,[326] and Hungary deposits approximately US $140 in every child's account.[327] None of the existing CSAs require repayment of the government deposit or matching funds.

CSA proposals in the U.S. have also called for government endowments, though some are structured as loans. The ASPIRE Act would place between $500 and $1,000 into an account at birth[328] and the current version of the KidSave legislation provides $2,000 in government funds,[329] but both would need to be repaid by the recipients.[330] The California and Oregon bills would also require state contributions of between $200 (Oregon) and $500 (California), but those sums need not be repaid.[331]

Academic proposals have called for some form of direct state assistance as well. Boshara's ASAs would include a $2,000 seed deposit plus an additional $3,000 at educational milestones, all of which would be repaid over a ten year period.[332] The capital accounts include substantial state funding, ranging in inflation-adjusted terms from approximately $29,000 (Tobin)[333] to approximately $48,000 (Klein).[334] Tobin's plan would require repayment via additional tax liability beginning at age 28, but neither Klein nor Haveman's accounts were structured as loans.[335] Ackerman and Alstott's stakeholder scheme calls for the largest government endowment of $96,000 in today's dollars, and requires repayment of the initial funds including interest at death to the extent possible.[336] Only Sherraden's IDAs lack an initial deposit because, similar to Korean savings accounts, they are funded entirely by a matching scheme.[337]

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325. *See supra* note 77 and accompanying text.

326. *See supra* notes 88-97 and accompanying text.

327. *See supra* notes 107 and accompanying text. Korea's new plan does not place any government funds into the CSA at birth and only provides matching grants. *See supra* notes 109-10 and accompanying text.

328. *See* ASPIRE Act of 2005, S. 868, 109th Cong. (2005). *See also* companion bill H.R. 1767, 109th Cong. (2005).

329. *See* Social Security KidSave Accounts Act, H. 242, 110th Cong. (2007).

330. *See id.*; ASPIRE Act of 2005, S. 868, 109th Cong. (2005). *See also* companion bill H.R. 1767, 109th Cong. (2005).

331. *See* H.B. 2790, 74th Legis., Reg. Sess. §§ 1, 3 (Or. 2007). The original version of the California bills required repayment, but not the version amended as of April 18, 2007, *see* S.B. 752, 2007-08 Leg., Reg. Sess. §§ 1-2 (Cal. 2007).

332. *See* BOSHARA, *supra* note 135, at 2.

333. *See* TOBIN, *supra* note 148.

334. *See* KLEIN, *supra* 155.

335. *See supra* notes 148-75.

336. *See supra* notes 176-90.

337. *See* SHERRADEN, *supra* note 120, at 220-23.

7. *Progressivity*

Another feature that distinguishes the existing Code from the CSAs and CSA proposals is the progressive nature of many CSAs. As described above, most savings initiatives in the Code are regressive because the encouragement to save stems only from the reduction in tax liability.[338] In contrast, most existing CSAs have progressive schemes. Britain gives an extra GDP£250 to low income families at birth and when the child reaches age seven.[339] Canada's C$2,000 Learning Bond is only available to poor families, and the government provides additional matching grants for poor families as well.[340] Hungary provides a higher match limit for lower income families,[341] and Korea's program demonstrates concern for the poor in that it currently only applies to foster children, and even at full implementation will only apply to children of low- and middle-income working families.[342] Of the existing CSAs, only Singapore's program is not means-tested.

In terms of the legislative proposals, the ASPIRE Act provides additional funds at lower income levels,[343] but the Social Security KidSave Act, as well as the California and Oregon bills, apply universally.[344] The academic CSA proposals also vary considerably. While Sherraden's proposal would apply to all Americans,[345] it would target the poor in its matching program. Boshara's IDAs would provide an additional tax credit to low-income families who put the funds directly into their child's ASA. However, none of the capital account proposals are means-tested, nor is the stakeholder plan.

C. *Putting It All Together*

Examining each of the factors above individually does not tell us much about how CSAs compare to the Code; a big picture analysis is required. Taking the tax treatment at contribution, growth, and withdrawal together with the state funding and progressivity factors allows us to more easily determine at which point CSAs and CSA proposals diverge from existing savings laws in the Code. It quickly becomes apparent that while certain CSAs and

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338. *See supra* note 202.

339. *See supra* notes 65-66 and accompanying text.

340. *See supra* note 77 and accompanying text.

341. *See supra* note 107 and accompanying text.

342. *See supra* note 110 and accompanying text.

343. It does so both in the initial deposit and in the matching program. *See* ASPIRE Act of 2005, S. 868, 109th Cong. § 6 (2005). *See also* companion bill H.R. 1767, 109th Cong. § 6 (2005).

344. *See* Social Security KidSave Accounts Act, H.R. 242, 110th Cong. § 2 (2007); S.B. 752, 2007-08 Leg., Reg. Sess. §§ 1-2 (Cal. 2007).H. 2790, 74th Leg., Reg. Sess. §§ 1, 3 (Or. 2007).

345. Sherraden worried that a program targeting the poor "would tend to stigmatize participants and make the program politically vulnerable," though it would be less expensive. *See* SHERRADEN, *supra* note 120, at 223.

proposals differ from the Code on a number of levels, others share many qualities with the Code provisions at first glance. This section first examines the CSAs and CSA proposals that share little in common with the Code, and then moves on to those that first appear to resemble Code provisions, but ultimately concludes that even those policies are irreconcilable with our current savings vehicles.

1. CSAs and CSA Proposals with Few Code Characteristics

Certain CSAs look quite different from the Code even when considering the tax treatment at contribution, growth, and withdrawal in combination with use restrictions. For example, Britain's Child Trust Funds and Hungary's baby bonds do not resemble a traditional or a Roth savings program because, not only are the contributions to the accounts required to be made with after-tax funds, but the proceeds of the the account are taxed upon withdrawals as well.[346] Singapore's policy has the same tax treatment at growth and withdrawal as a Roth IRA, but looks different from the Code because it places no annual limits on what parents can contribute to their child's account. But the fundamental departure from the Code for all three of these CSAs lies in how each restricts the use of funds at withdrawal. For example, the funds in Britain and Hungary's CSAs are not subject to any use restrictions, setting them apart from savings provisions in the Code which have been primarily geared towards education, home purchases, and retirement. Singapore's program differs for the opposite reason—the money that parents save in the Children's Development Account is completely locked up unless used for qualified purposes. While the account can eventually be rolled-over into a retirement plan, the money cannot be withdrawn in cash until that point, thereby eliminating the flexibility to withdraw funds (albeit while incurring a penalty) if necessary that the Code provides.

Britain, Hungary, and Singapore's schemes diverge further from the Code when one considers that in all three countries children are immediately given state funds to open an account. Lower income children receive additional funds in Britain (initial and additional deposits) and Hungary (additional matching grants), and second to fourth birth order children in Singapore receive additional state endowments at birth and higher match limits. Such components are unfamiliar territory to the Code which bases its savings incentives only on reductions in tax liability and exhibits a regressive pattern.

Not surprisingly, as we move from the CSAs and CSA proposals to the capital account and stakeholder proposals we see fewer similarities with our

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346. Hungary's program arguably looks somewhat like a traditional IRA plan due to its matching component (to the extent that a matching program is similar to a pre-tax contribution), but this analysis does not hold for Britain's CSAs which includes no matching grants.

existing system. The capital account and stakeholder proposals differ substantially from the Code as they have no savings component. This is an element upon which all of the Code provisions we have considered thus far are centered. As a result, we cannot even compare their tax treatment at contribution, growth, and withdrawal to the Code because they are not savings accounts that allow accountholders to make contributions in the first place. Capital accounts and the stakeholder proposals also recommend endowments far larger in size than CSA proposals, whose small subsidies appear more palatable.[347]

The stakeholder concept is clearly the most incongruous of principles underlying our current savings vehicles because it not only lacks a savings component and provides for the largest endowment, but it places no restrictions on how the money can be spent. This is in direct contrast with the Code, which only provides tax benefits for savings, does not allow for direct state funding, and restricts the use of savings account funds primarily to education and retirement.

2. CSAs and CSA Proposals with Several Code Characteristics

If we look only at the contribution, growth, withdrawal, and use restriction factors, some existing CSAs do not differ much from savings vehicles in the Code. For example, if we ignore the state funding and progressivity factors, Canada's CSAs and Oregon's bill are very similar in form to 529 or 530 savings accounts. Parents may contribute after-tax funds into an account for their child up to an annual limit. The funds grow tax-free and can be withdrawn free of penalty and free of tax if used for postsecondary educational expenses. Similarly, looking only at these factors, the ASPIRE Act, the California bill, and Boshara's ASAs all work in a very similar manner as Roth IRAs. After-tax funds are contributed to an account which grows tax free, and funds can be withdrawn tax- and penalty-free if used for designated purposes. Otherwise a standard 10% penalty applies.

However, the CSAs and CSA proposals that initially resemble Code provisions begin to look dissimilar when we consider the progressive nature of the matching grants and direct subsidies. For example, Canada's policy

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347. For example, the Office of Management and Budget estimates that tax expenditures for retirement saving will total $112 billion in 2008. *See* CRAMER, ET AL., *supra* note 200, at 13. Boshara estimated that his stakeholder account would cost approximately $14 billion per year, or approximately 10% of the current cost of retirement expenditures. BOSHARA, *supra* note 135, at 3. Capital account proposals and especially stakeholder proposals would likely make up a much larger proportion of our current spending given that government endowments would range from $30,000 to $96,000. Ackerman and Alstott estimated their stakeholding plan at $255 billion, more than twice the amount of all our tax expenditures for retirement combined and nearly equal to all of our estimated tax expenditures for saving in 2008. *See supra* note 200 and accompanying text.

looks quite diferent from 529 or 530 savings accounts when the 40% match rate for low income families is added. The matching grant completely changes the design of the program because it means that contributions, while still after-tax, are nonetheless subsidized. As a result, while the program ostensibly follows a 529/530 tax scheme, in reality the program provides subsidies at contribution, growth, and withdrawal which none of the U.S. programs allow.[348] The state-funded deposit of up to C$2,000 represents a further leap away from the tax code because it provides a benefit in the absence of any savings behavior on the part of the participant. This is in contrast to the current Code provisions, which only provide tax breaks for amounts saved. Moreover, both the matching grant and deposit primarily benefit lower-income individuals in Canada, an approach foreign to Code savings incentives which are mostly enjoyed by the wealthy.

A similar analysis holds for several other CSAs and CSA proposals. The ASPIRE Act and Boshara's ASAs, which otherwise resemble Roth IRAs, would provide initial deposits for all children, as well as matching grants for low income families.[349] Unlike the Roth IRA, both would allow non-tax subsidies when the account is initially opened (regardless of savings behavior), progressive subsidies at contribution, and tax benefits at withdrawal. The same is true for the KidSave Accounts, as well as the California and Oregon bills,[350] except that these plans are not subsidized at contribution in the same manner as Canada's CSAs, the ASPIRE Act, and Boshara's ASAs.[351]

A close examination of Sherraden's IDAs suggests that, unlike most CSAs and CSA proposals, the IDAs are actually quite similar to exisiting savings provisions in the Code. Due to the fact that Sherraden's IDAs would be taxed at withdrawal, the matching grants do not pose the same problem as the matching grants in the Roth IRA-type proposals which result in subsidizing contributions on top of tax-free withdrawal. In addition, IDAs would *only* provide matching funds and not an initial deposit; all government grants would be conditioned upon savings. Furthermore, the funds in Sherraden's IDAs

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348. *But see supra* note 325 (fact that subsidy at contribution is in form of matching grant rather than tax break is less problematic than if scheme were pre-tax contribution, tax-free withdrawal, because at least the matching funds apply directly to the child's saving account, and do not simply reduce the tax liability of the parent, freeing up funds for completely non-savings related uses).

349. Boshara's ASAs would not provide a matching grant per se, but would allow an additional tax credit for low income families who put it directly into the ASA. *See supra* note 324.

350. Note that the KidSave accounts do not resemble Roth IRAs as closely as the ASPIRE Act or Boshara's ASAs in the first place because the government funds would be placed into social security accounts and could only be used for retirement, and the Oregon bill more closely resembles 529 education savings accounts than Roth IRAs.

351. In addition, these accounts are not means tested, which makes them more similar to the Code than the Canada law, ASPIRE Act, or Boshara's ASAS which grant low-income families additional benefits.

could only be withdrawn penalty-free for education and retirement, similar to our current savings vehicles. As a result, Sherraden's plan looks fairly similar to traditional IRAs or 401(k)s, except that the pre-tax contribution portion of the traditional savings vehicle is replaced by an after-tax contribution matching funds for low income individuals.[352] Of course, this replacement is significant because Sherraden's matching program is progressive, whereas our current system of subsidizing contributions with pre-tax dollars is regressive.

IV. CONCLUSION

Prominent scholars have been advocating innovative CSA proposals for over forty years. At least five countries have adopted CSAs with varying designs and benefits for accountholders and their families. Yet, despite legislative efforts over the past ten years, and a tax policy that has favored savings vehicles, the U.S. has failed to enact CSAs. The purpose of this paper was to examine just how far CSAs stray from our current Code provisions by comparing existing and proposed CSAs to the Code.

Certain CSAs and CSA proposals differ substantially from the Code on almost every level. Looking at the tax treatment of the accounts at contribution, growth, and withdrawal, Britain, Hungary, and Singapore's CSAs look quite different than the Code. Moreover, the capital account and stakeholder proposals lack any sort of savings component at all. This distinguishes these policy instruments so sharply from the Code so as to make it almost impossible to make an accurate comparison. The fact that all of these policies also contain direct government endowments takes us even further from the Code's regressive structure for savings vehicles.

But what is perhaps most interesting is that several CSA proposals in the U.S. are similar to the savings vehicles in the Code in their tax (and penalty) treatment at contribution, growth and withdrawal (e.g., the ASPIRE Act, Boshara's ASAs, the California legislation, and Canada's CSAs). Yet, the government funding inherent in these CSAs is enough to set them apart substantially in principle from the Code. A matching grant changes the very design of the CSAs from vehicles that resemble our current Roth scheme of after-tax contribution/tax free withdrawal, to ones that subsidize at the time of contribution as well as at withdrawal. Direct government deposits are

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352. This similarity with traditional IRAs and 401(k)s is consistent with Sherraden's plan that pre-tax contributions would stay in place for high income earners, and be replaced with matching grants for low income earners. *See id.* Note also that the pre-tax contribution, tax at withdrawal scheme does not result in the same tax evasion opportunity described *infra* note 264 and surrounding text because Sherraden's IDAs do not have a separate contributor and beneficiary. IDAs would not be limited to children under a certain age; instead, each individual would receive an IDA to which he or she, along with others, can contribute. As a result, the same person making contributions would make the withdrawal.

similarly distinguishable from the Code because they create a subsidy regardless of the recipient's savings behavior, whereas savings incentives in the Code depend on the accountholder contributing to the account. Only Sherraden's IDAs, with their tax at withdrawal and lack of direct subsidy, somewhat resemble our current system. But as with nearly all of the CSAs and CSA proposals, the fact that IDAs are progressive distinguishes them from our current savings provisions whose incentives derive solely from reduced tax liability and naturally benefit the wealthy.

Enacting CSA legislation would mean redefining our concept of a "savings vehicle" from a tax break to a direct government subsidy. While there may be much to say on the advantages of the latter given that incentives based on reductions in tax liability primarily benefit the wealthy, the point of this paper is not to compare these approaches but merely to discern what are the real differences between the Code and CSA legislation. To that effect, it may help to shed light on exactly what factors have prevented CSA legislation from serious consideration in the U.S. despite a half-century of academic argument in favor of such proposals and a movement in favor of such policies across the world.