About Think New Mexico

Think New Mexico is a results-oriented think tank serving the citizens of New Mexico. We fulfill this mission by educating the public, the media and policy makers about some of the most serious problems facing New Mexico and by developing effective, comprehensive, sustainable solutions to those problems.

Our approach is to perform and publish sound, nonpartisan, independent research. Unlike many think tanks, Think New Mexico does not subscribe to any particular ideology. Instead, because New Mexico is at or near the bottom of so many national rankings, our focus is on promoting workable solutions. We use advocacy and, as a last resort, legal action but only within the constraints of Federal tax law.

Consistent with our nonpartisan approach, Think New Mexico's board is composed of Democrats, Independents and Republicans. They are statesmen and stateswomen, who have no agenda other than to see New Mexico succeed. They are also the brain trust of this think tank.

As a results-oriented think tank, Think New Mexico measures its success based on changes in law or policy that it is able to help achieve and which improve New Mexico's quality of life. We are best known for our successful campaigns to make full-day kindergarten accessible to every child in New Mexico, to repeal the state's regressive tax on food, and to establish a Strategic Water Reserve to protect New Mexico's rivers.

Think New Mexico began its operations on January 1, 1999. It is a tax-exempt organization under section 501(c)(3) of the Internal Revenue Code. In order to maintain its independence, Think New Mexico does not accept government money. However, contributions from individuals, businesses and foundations are welcomed, encouraged and tax-deductible.

Think New Mexico's Board of Directors

Edward Archuleta, a 13th generation New Mexican, is the former Director of the Santa Fe office of 1000 Friends of New Mexico, a nonprofit organization that advocates responsible growth management and sustainable development. Edward previously served as the top assistant to former New Mexico Secretary of State Stephanie Gonzales.

Paul Bardacke served as Attorney General of New Mexico from 1983–1986. Paul was Chairman of Bill Richardson's successful 2002 gubernatorial campaign. He is a Fellow in the American College of Trial Lawyers. Paul currently handles complex commercial litigation and mediation with the firm of Sutin, Thayer, & Browne.

David Buchholtz has served on a long list of New Mexico boards and commissions and has advised several New Mexico governors on fiscal matters. David recently served as Chairman of the Association of Commerce and Industry. He is a shareholder with Brownstein, Hyatt, and Farber.

Garrey Carruthers served as Governor of New Mexico from 1987–1990. Garrey is Dean of New Mexico State University's College of Business, and was formerly President and CEO of Cimarron Health Plan. He is a member of the Board of Directors of the U.S. Chamber of Commerce and the New Mexico Business Roundtable for Educational Excellence.

Dr. F. Chris Garcia is a former President of the University of New Mexico and is currently a Professor of Political Science. He is the co-editor of, among other books, *Latinos and the Political System* and *New Mexico Government (3rd edition).* Dr. Garcia recently received the Governor's Distinguished Public Service Award.

Elizabeth Gutierrez is the Education Policy Advisor to Governor Richardson. She holds a PhD in educational leadership and public policy and serves on the Board of the Santa Fe Community College. Liz was a marketing executive with IBM for nearly two decades. *Liz is on leave from Think New Mexico's Board while she works for the state.*

LaDonna Harris is an enrolled member of the Comanche Nation. LaDonna is Chairman of the Board and Founder of Americans for Indian Opportunity. She is also a founder of the National Women's Political Caucus. LaDonna was a leader in the effort to return the Taos Blue Lake to Taos Pueblo.

Rebecca Koch is the owner of Rebecca Koch & Associates which provides management consulting services in the areas of development and strategic planning to local and national nonprofits. Rebecca was the organizational development consultant for the Santa Fe Business Incubator, Inc. She is a former President of the Board of New Mexico Literary Arts.

Edward Lujan is the former CEO of Manuel Lujan Agencies, the largest privately owned insurance agency in New Mexico. Ed is a former Chairman of the National Hispanic Cultural Center of New Mexico, the Republican Party of New Mexico and the New Mexico Economic Development Commission.

Fred Nathan founded Think New Mexico and is its Executive Director. Fred served as Special Counsel to New Mexico Attorney General, Tom Uduall. In that capacity, he was the architect of several successful legislative initiatives and was in charge of New Mexico's lawsuit against the tobacco industry.

Roberta Cooper Ramo is the first woman elected President of the American Bar Association. Roberta serves on the State Board of Finance and is a former President of the Board of Regents of the University of New Mexico. She is a shareholder with the Modrall law firm and serves on many national boards.

Stewart Udall served as Secretary of the Interior under Presidents Kennedy and Johnson. Prior to that, Stewart served three terms in Congress. He is the author of *The Quiet Crisis* that tells the story of humankind's stewardship over the planet's resources, and *To the Inland Empire: Coronado and Our Spanish Legacy* which celebrates Hispanic contributions to our history.

Dear New Mexican:

For more than two decades economic mobility has been largely stagnant in New Mexico. This is especially true for working low-income families.

The experts who study how to boost economic mobility urge placing more emphasis than we currently do on encouraging saving and increasing opportunities to build assets, like buying a home, obtaining a college education and starting a business.

Yet some government assistance programs continue to discourage asset-building by using asset limits to disqualify working, low-income families in New Mexico and elsewhere from receiving assistance. Likewise, those same programs focus on income transfers that, in many instances, are more band-aid than cure.

We believe, on the other hand, that owning assets gives working, low-income New Mexicans a bigger stake in New Mexico's future and a better shot at the American Dream.

One innovative way to encourage and broaden ownership in New Mexico (as well as to expand New Mexico's beleaguered middle class) is to make individual development accounts ("IDAs") widely available to working low-income families.

IDAs are interest-bearing savings accounts that are restricted to placing a down payment on a home, starting a micro-business or paying for college or vocational school. To create incentives to save, IDAs are matched by private or public money and sometimes both.

In order to receive the matching money, the IDA owner must successfully complete a financial literacy course designed to teach the basics of how to reduce debt, budget, manage a checking account, save and avoid financial pitfalls like credit card borrowing and predatory lending.

In this way, IDAs provide an incentive to work, save, and build assets as a route to enter the middle class. IDAs also provide the financial literacy tools to stay self-sufficient for the long-term.

Nationally, IDAs have demonstrated success by increasing rates of saving, home ownership, and educational attainment, and decreasing rates of credit card debt and welfare dependency. In addition, IDA owners are more likely to stay employed, work more hours, and increase their earnings.

It is a measure of the bipartisan appeal of IDAs that of the 15 states that offer state funds or tax credits to support IDAs, eight are so-called "blue" states and seven are so-called "red" states. In fact, it has been said that IDAs "combine the liberal objective of poverty reduction with the conservative dream of individual wealth building to achieve the shared goal of economic opportunity."

Given that New Mexico ranks so highly in child and adult poverty and given that IDAs have demonstrated strong results in other states, we believe now is the right time to construct a model statewide, state-supported IDA initiative in New Mexico.

In the following pages, we describe how that may be done taking advantage of the capacity that already exists in New Mexico and by refining the operation of New Mexico's Lottery to pay for it.

* * *

With this policy report, we welcome two new board members to Think New Mexico: Dr. F. Chris Garcia, former President of the University of New Mexico, and Edward Lujan, former CEO of the Manuel Lujan Insurance Agency. Chris and Ed are typical of the statesmen and stateswomen who serve on our board because they are always seeking ways to give back to New Mexico.

The same might be said of Think New Mexico's staff, pictured at right, who worked overtime to complete this report.

If you like what you read here, I want to encourage you to consider making a tax-deductible contribution in the enclosed reply envelope. We promise to put it to good use.

Fred Nathan

Founder and Executive Director

Lynne Loucks Buchen
Business Manager

Chris Chavez
Field Director

Kristina Fisher
Research Director

Lester Kevin Tsosie
Assistant Director

Fred Nathan
Executive Director

NEW MEXICO AND THE AMERICAN DREAM

The statistics are sadly familiar: New Mexico ranks highest among the 50 states for the percentage of its citizens living in poverty–18.1%, according to the Census Bureau's Current Population Survey. Tragically, the rate for children is even higher: 26.9%. That, too, is the highest percentage in the nation.

In addition, the percent of New Mexicans living at or below 100% of poverty has been stagnant at rates well above the national average stretching back at least two decades.

Over the same period, New Mexico's per capita income as a percent of the national average has fallen dramatically. In the early 1980's, the average New Mexican earned 82.5% of the average U.S. income. By the 2000 Census that percentage had fallen to 73.4%.

This leads to an important question: is hard work, sacrifice and determination enough to give a child born into poverty in New Mexico a real opportunity to scale the economic ladder to the middle class or beyond? In short, how vibrant is the American Dream in the Land of Enchantment?

New Mexico was once a place with greater upward economic mobility. This was especially true in the early post-World War II era. One important reason why so many working New Mexico families enjoyed a rising standard of living then was because of the GI Bill of Rights, enacted in 1944 to assist the eight million returning World War II veterans to readjust to civilian life. Some dubbed the landmark law "the magic carpet to the middle class."

Percentage of Children Living in Poverty in 2003

State	Percentage	State	Percentage
New Mexico	26.9	Wisconsin	15.4
Arkansas	26.8	Nevada	14.8
West Virginia	26.7	Missouri	14.7
Louisiana	25.5	Michigan	14.6
Texas	24.0	Kansas	14.5
Mississippi	23.1	South Dakota	14.0
North Carolina	23.1	Idaho	13.8
Alabama	22.3	Indiana	13.7
Montana	20.2	Virginia	13.5
Oregon	20.1	Iowa	13.4
New York	19.9	Wyoming	13.1
Florida	19.2	North Dakota	12.7
Arizona	19.1	Utah	12.4
Washington	19.1	Hawaii	12.0
Tennessee	18.7	Massachusetts	12.0
California	18.5	Colorado	11.9
Kentucky	18.1	Alaska	11.2
Georgia	17.7	New Jersey	11.2
Illinois	17.4	Delaware	11.0
South Carolina	17.4	Nebraska	11.0
Rhode Island	17.1	Vermont	10.9
Oklahoma	17.0	Maryland	10.6
Ohio	16.5	Connecticut	10.1
Maine	15.6	Minnesota	9.7
Pennsylvania	15.5	New Hampshire	7.2

Source: U.S. Census Bureau, Current Population Survey, "2004 Annual Social and Economic Supplement."

The G1 Bill succeeded because it focused on asset-building to foster opportunity and advancement. For instance, the G1 Bill helped veterans to pay for college education and worker training. It also provided loan guarantees for veterans who wanted to purchase a home, farm or business.

The impact of the G1 Bill on New Mexico was enormous. The University of New Mexico's enrollment, which had never been more than 1,800 before 1946, more than doubled to 3,649 in that year alone. The number of houses in New Mexico increased from 127,186 in 1940 to 251,209 in 1960, according to the U.S. Census Bureau, an increase of 97.5%. Meanwhile, from 1945 to 1950 the number of businesses in New Mexico increased by 71.4%, according to the Bureau of Business Research at the University of New Mexico.

The GI Bill is still in effect today–it is currently paying the college tuition of more than 2,700 New Mexicans–but it now requires a modest financial contribution from service members.

This policy report builds on New Mexico's successful experience with the G1 Bill. Specifically, it proposes a way for New Mexico to restore some upward economic mobility by increasing access to asset-building opportunities for a targeted group of working low-income families.

The G1 Bill led to a dramatic rise in economic mobility in New Mexico. *Photo courtesy of Nik Cecere, Santa Fe, NM.*

INDIVIDUAL DEVELOPMENT ACCOUNTS

Traditional welfare and anti-poverty programs have generally focused on income transfers, which address day-to-day emergency needs (for example, unemployment assistance). However, these programs are more band-aid than cure. They do not reduce poverty – the recipients remain poor even though their emergency needs have been met.

By contrast, Individual Development Accounts ("IDAs") center on providing working low-income individuals and families with opportunities to build assets, an essential but often overlooked step to climbing out of poverty. Specifically, IDAs are interest-bearing bank savings accounts, which are restricted, like the GI Bill, to placing a down payment on a home, starting or expanding a micro-business, or paying for college or vocational school.

To create incentives to save, IDAs are matched by private or public money. For example, a working low-income family establishes an IDA in which every deposit they make is matched in a separate trust or custodial account controlled by a third party, like a not-for-profit organization.

Individual Development Accounts are interest bearing savings accounts, held by credit unions and banks like this one in Silver City, circa 1880. *Photo courtesy Museum of New Mexico, #11419.*

State funded matches generally range from one dollar for every dollar saved to three dollars for every dollar saved. Deposits to savings accounts of up to $2,000 annually for an individual or $4,000 for a family household are typically eligible for matching dollars.

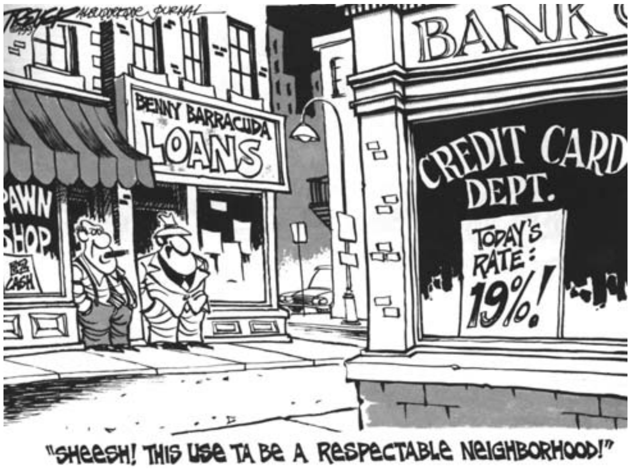
Ultimately, the IDA funds from both the savings and the trust accounts are paid directly to the asset provider – for example, a mortgage provider or an accredited school. (IDA owners can access their own savings accounts for emergency uses, such as a medical emergency, but cannot access the trust account for emergencies.)

In order to receive the proceeds of the trust account, the IDA owner must successfully complete a financial literacy course. These courses are designed to teach the basics of how to reduce debt, budget, manage a checking account, save, invest and avoid financial pitfalls like credit card borrowing and predatory lending. IDA owners also receive training specific to their asset goals, such as a class for first-time homebuyers.

In this way, IDAs provide an incentive to work, save, and build assets as a route to enter the middle class. They also provide the financial literacy tools to stay self-sufficient for the long-term. Traditional welfare programs, on the other hand, sometimes discourage asset-building by using asset limits to disqualify working low-income families from receiving assistance.[1]

An IDA may be likened to an Individual Retirement Account (IRA), a 401(k) matching plan or a 529 college savings plan, but designed for low-income indi-

1] *In New Mexico, money in IDAs is exempt from consideration as an asset for the purposes of public assistance eligibility.*



Financial literacy courses teach IDA owners to avoid financial pitfalls like credit card borrowing and predatory lending. Reprinted by permission of John Trever and the Albuquerque Journal. *Permission does not imply endorsement. Copyright 1991.*

viduals and families who work paycheck to paycheck. IRAs, 401(k)s and 529 plans do not attract low-income people, who generally have little or no income tax liability, because the primary incentive for saving in these programs is to defer taxes.

In addition to encouraging savings, an IDA can lead to owning a home or business. President George W. Bush is right when he says that ownership brings "security, dignity and independence." These values are three of the primary attributes of IDAs, which dovetail perfectly with the President's vision of an "Ownership Society." (President Bush, in fact, is currently supporting bipartisan congressional legislation to increase the availability of IDAs.)

IDA initiatives have grown rapidly nationwide in the past decade. There are now more than 500 local and statewide IDA initiatives reaching approximately 25,000 Americans, according to the New America Foundation. Remarkably, about 81% of IDA owners are women.

Many of the benefits of asset-building for working low-income families are both tangible and obvious: greater rates of home ownership, increased educational attainment and lower dependence on welfare. This, of course, is worthy of attention in a state ranked highest in child poverty.

Indeed, children directly feel the greatest benefits from asset-building. For example, children in families that own their homes demonstrate a 9% lower high school dropout rate and up to a 4% lower teen pregnancy rate than children of renters with identical socioeconomic characteristics, according to a 1997 national study conducted by economists at the University of Michigan.

(These are two areas where New Mexico could use some help. Only Mississippi and Texas have higher teen pregnancy rates than New Mexico, which is nearly 50% higher than the national average, according to the National Vital Statistics reports of the U.S. Department of Health and Human Services. In terms of high school graduation rates, New Mexico ranks 46th, according to the National Center for Education Statistics of the U.S. Department of Education.)

The evidence suggests that working low-income individuals and families behave like the rest of society when presented with economic incentives to save: 59% of IDA owners are more likely to stay employed, and 41% are more likely to work more hours. This was one of the major findings of The Ford Foundation's Down Payments on the American Dream Policy Demonstration ("Ford Foundation study"), the largest study of privately funded IDAs in the United States.

Other studies have found that the benefits of the financial literacy training are even more valuable than the matching funds. "Account holders typically comment that they join IDA programs for the matching funds, but they stay because of the [financial literacy] training," according to Robert Friedman and Ray Boshara of the Corporation for Enterprise Development, which has extensively studied IDAs.

This is demonstrated by the change in behavior of IDA owners toward savings and credit card debt. A 2004 Brookings Institute study reported that researchers who interviewed graduates of the Illinois IDA initiative found that six to 12 months after successfully completing the financial literacy training, 76% were reducing credit card debt and 74% were saving more.

Beyond these positive behavioral changes, IDAs open doors to the financial mainstream. In Illinois, more than 65% of IDA graduates reported opening bank accounts (34.4% checking, 31.2% savings) and, perhaps most significantly, 26% of IDA graduates reported opening a checking or savings account for the first time.

Only 25.5% of New Mexico's low-income families own any assets that pay interest, such as bank savings accounts, according to a 2002 study by the Asset Development Institute. That means that, at a minimum, nearly three quarters of working low-income New Mexico families do not have bank accounts and, therefore, no access to the financial mainstream.

So where do New Mexicans without bank accounts go for financial services? One good clue is that there are now four payday lenders for every McDonald's in New Mexico, according to a 2002 study by the New Mexico Public Interest Research Group. Payday lenders commonly charge triple-digit interest rates, and while they offer rapid access to cash, they entrap low-income consumers into a perpetual cycle of debt.

IDA owners, on the other hand, move from "unbanked" to "banked" and become much less likely to return to predatory lenders because they now qualify for other bank services including mortgages, business loans and check cashing at much more reasonable rates. In Illinois, 40% of the IDA owners reported using payday lenders less after completing their financial literacy training.

The bottom line on the potential of IDAs is illustrated by a 2005 study of IDAs in Texas by the Center for Public Policy Priorities, which found that for every $1 invested in an IDA, there is a return to the state economy of nearly $5 in the form of new businesses, increased earnings, new or rehabilitated homes, reduced welfare expenditures, and human capital associated with greater educational attainment.

This may explain why the IDA concept has met with bipartisan congressional support. In 1998 Congress passed the Assets for Independence Act (AFIA), which has provided more than $131 million to fund state and local IDA initiatives.

Many states now have IDA initiatives, and an increasing number of states have begun to appropriate state dollars for IDAs or offer tax credits to private sector IDA match contributors. The chart on page 11 summarizes these initiatives, which now include 15 states from every region in the nation. The bipartisan appeal of IDAs is illustrated by the fact that these state-financed IDA initiatives include eight so-called "blue states" and seven so-called "red states."

In New Mexico, IDAs were mentioned in the state welfare reform plan in 1996, but were not included in the state's 1998 welfare reform law, which was

State-Supported IDA Programs

State	General Funds	Tax Credits	Match Rate
Arkansas		✔	3:1
Colorado		✔	Varies
Connecticut	✔	✔	2:1
Hawaii		✔	2:1
Indiana	✔	✔	3:1
Maine		✔	2:1
Maryland	✔		Varies
Minnesota	✔		3:1
Missouri		✔	1:1
North Carolina	✔		2:1
Oregon		✔	1:1 to 5:1
Pennsylvania	✔		0.5:1
South Carolina	✔	✔	3:1
Tennessee	✔		2:1
Vermont	✔		1:1

Source: "Summary Tables: IDA Policy in the States," Center for Social Development, Washington University, March 2004

intended to end dependency and promote self-sufficiency. However, in 2003, New Mexico became the 35th state to pass an IDA law, the "Individual Development Act" which was enacted with big bipartisan margins.

Although the law establishes a framework for IDAs, it fails to provide state dollars or offer tax credits to the private sector to encourage matching dollars. Nevertheless, the law is a promising start and provides a useful foundation to build upon.

Still, there are fewer than 200 IDAs in New Mexico today and only approximately 500 more IDAs are planned within the next five years–supported entirely by private charitable dollars and some federal funds. That represents less than one half of one percent of the eligible population.

Given that New Mexico ranks first in the nation for child and adult poverty, and given that IDAs have demonstrated impressive results in addressing poverty, we believe that now is the right time to develop a comprehensive model IDA initiative for New Mexico.

Clearly, it is going to require a contribution of state General Fund dollars to build an IDA initiative that will reach more New Mexicans and leverage a greater commitment from the private sector and the federal government.[2] It will not be easy: in the 2005 legislative session, Representative Janice Arnold-Jones (R- Albuquerque) and Senator Richard Martinez (D-Espanola) separately introduced legislation to provide state funding for IDAs, but neither bill was successful.

The rest of this report describes our proposal for how to construct and fund such a comprehensive model initiative for New Mexico.

2] *State funding to support IDAs would not violate Article 9, Section 14 of New Mexico's Constitution, the so-called Anti-Donation Clause, which prohibits the state from making donations of government funds, because that clause also specifically makes an exception for "indigent persons," such as those who are at or below 100% of poverty. Moreover, according to New Mexico Attorney General Opinion 97-02, the purpose of the anti-donation clause is "to prevent the investment of public funds in private enterprise. It was not intended to affect government services to the public or the accomplishment of government functions." IDAs serve many government functions, such as lessening welfare dependency and generating greater tax revenues.*

MAKING NEW MEXICO THE MODEL STATE FOR IDAs

In terms of crafting a more comprehensive model IDA initiative in New Mexico, the good news is that there is more than a decade's worth of experience with other state IDA initiatives from which New Mexico can learn. The bad news is that "every calculation based on experience elsewhere fails in New Mexico," as Territorial Governor Lew Wallace famously said.

It should also be acknowledged that traditional anti-poverty programs have historically over-promised and under-delivered. President Lyndon Johnson, for example, promised "total victory" in his "War on Poverty" in 1964. IDAs have succeeded, in part, because their approach is more targeted and less ambitious than previous efforts.

Eligibility: Working Low-Income New Mexicans who will Commit to Saving

IDAs focus on a subset of the population in poverty: those who are willing to sacrifice by saving part of their paycheck and who are also willing to commit to completing a financial literacy course. Sacrifice and commitment were also a prerequisite to the GI Bill's benefits. Traditional anti-poverty programs, by contrast, rarely ask for any type of commitment or sacrifice.

The savings and financial literacy requirements, which some critics assail, have the effect of automatically separating those individuals and families that IDAs can help from those that they cannot, which leads to a higher success rate. (For example, only 16% of the IDA owners in the Ford Foundation study dropped out.) Some people in New Mexico and elsewhere are simply not ready or willing to accept the discipline required to own an IDA.

IDAs boost educational attainment and college enrollment. *Photo courtesy the University of New Mexico and photographer Tom Brahl.*

Current state law limits eligibility for IDAs to 200% of poverty, which means that about 450,000 New Mexicans, or about 50% of all households, are eligible, with incomes ranging up to $64,780, under certain circumstances. In terms of designing a model IDA initiative supported with state General Fund dollars, we would recommend prioritizing and narrowing that universe by restricting eligibility to 100% of poverty or approximately 185,000 New Mexicans with household incomes ranging up to $32,390.

Reaching the national average for the percentage of New Mexicans living at or below 100% of poverty would require reducing that group of 185,000 by about 61,000. That should be the initial goal for any model IDA initiative in New Mexico.

One advantage of targeting working low-income individuals and families at or below 100% of poverty is that they are all eligible to receive federal and state tax rebates, which can be used to meet their IDA match. For example, they are all eligible for the Earned Income Tax Credit (EITC), created by Congress in 1975 to offset the burden of Social Security and Medicare payroll taxes for working low-income families. They are also all eligible to receive the Low Income Comprehensive Tax Rebate (LICTR), which New Mexico's Legislature established in 1972 to offset the regressive nature of the gross receipts tax on low-income people.

IDAs support the development of micro-enterprises. Bueno Foods, the Southwest's premier producer of New Mexican and Mexican foods, began as a micro-enterprise when Joe Baca, above, his three brothers and his father scraped together $1,000 each to start the Ace Food Store in 1946. Today, Bueno Foods is still owned and operated by the Baca family in Albuquerque and employs 250 New Mexicans (400 during peak season). *Photo courtesy of the Baca family.*

Taken together, the rebates provide enough money to at least partially meet the IDA owner's annual savings goal, and in some instances reach that goal with money left over. In 2003, 188,180 New Mexico households received the EITC, which ranged from $2 to $4,300 with an average refund of more than $1,800. LICTR ranges from $20 to $450 with an average rebate of about $95. In addition, in some cases low-income working families may be eligible for a partially refundable federal Child Tax Credit (CTC).

A good way to increase the likelihood of success of a model IDA initiative in New Mexico would be to strongly encourage IDA owners to receive their EITC, CTC and LICTR rebates by direct deposit into their IDA accounts. It is sometimes easier to save a portion of a rebate, which seems like found money or a windfall, than it is to part with a portion of one's paycheck.

Greater use of direct deposit would also reduce the number of "refund anticipation loans," in which tax preparers charge very high interest for loans to working low-income individuals and families in return for advance payment of their EITC.

In addition, direct deposit reduces postage, handling and printing costs for the IRS and the New Mexico Taxation and Revenue Department. ("TRD") For that reason, TRD might want to encourage low-income filers to use part of their rebate to start an IDA by including instructions and contact information for IDA enrollment with state tax forms.

Administrative Partners: Not-for-Profits

To make a substantial impact on New Mexico's low-income population, it will be necessary to gradually increase the number of IDAs available in the state. For instance, to reach the goal of decreasing the number of New Mexicans living at or below 100% of poverty to the national average within a decade would require annually graduating approximately 3,000 working low-income families or 6,000 working low-income individuals from the IDA initiative. (Pennsylvania, although a larger state than New Mexico, currently has 9,000 active IDA owners.)

State government does not have the capacity to individually work with that many people and creating a whole new anti-poverty bureaucracy within state government to administer IDAs would doubtless be a mistake. Fortunately, the not-for-profit sector in New Mexico has the capacity and the willingness to work along side IDA owners to administer a larger scale IDA initiative.

There are already three excellent New Mexico not-for-profits which are working with IDA owners on a small scale. They recruit and enroll participants, provide counseling, training, case management as well as track deposits and withdrawals. They are:

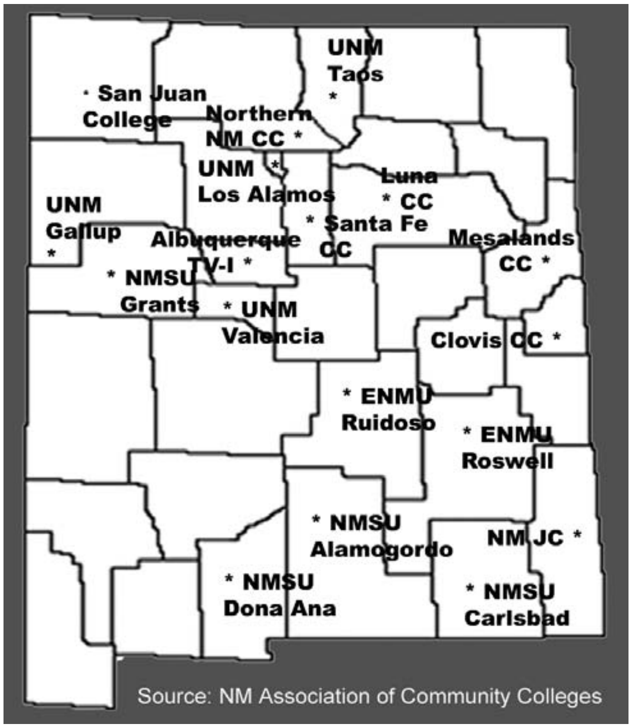
- Women's Economic Self-Sufficiency Team ("WESST Corp."), a statewide economic development group with offices in five cities that provides training, technology assistance and loans to women and minority entrepreneurs. Since 1989 WESST clients have started more than 1,800 businesses and created more than 2,800 jobs;
- Northwest New Mexico Community Development Corporation ("NWNMCDC") focuses on expanding funding available for business, housing and other community development needs in McKinley, Cibola and San Juan counties; and
- Navajo Partnership for Housing, Inc. ("NPH") provides innovative and flexible homeownership financing opportunities for Navajo families.

NWNMCDC administers 125 IDAs, WESST Corp administers 48 IDAs, mostly in Albuquerque, and NPH administers 5 IDAs for Navajo families in Shiprock.

In addition, the New Mexico Association of Community Action Agencies, the lead agency for an outstanding consortium of nine organizations in communities throughout New Mexico, recently secured a $1 million grant from the federal government that they will use to make 522 IDAs available by 2009.

There are other not-for-profits that would likely become involved if the state made an investment of state General Fund dollars to help pay for the matching contributions. Other states, for instance, use a request for proposal process and have attracted United Way agencies and tribes, among others.

IDAs are often used to make the down payment on a home, like these under construction in Albuquerque, 1942. *Photo courtesy Museum of New Mexico #183307.*



The Small Business Development Centers located on the campuses of New Mexico's 18 community colleges could provide financial literacy training to IDA owners.

Financial Literacy Education Partners: Small Business Development Centers

Another way to increase the likelihood of success of a larger scale IDA initiative in New Mexico and to keep costs low would be to take advantage of the state's extensive system of Small Business Development Centers (SBDC). They provide an ideal infrastructure for providing the financial literacy course to IDA owners, as there is an SBDC located on the campus of each of New Mexico's 18 community colleges. Financial literacy courses are already a major part of SBDCs' curriculum, and it would not be difficult to tailor those courses to IDA owners.

Ideally, the financial literacy course should be for one hour every month for the first year after an owner sets up an IDA. That's because financial literacy courses reach the point of diminishing returns in terms of effectiveness after about 12 hours. A study of IDAs by the Center for Social Development at Washington University found that IDA owners increased their net savings by $1.20 per month for each of the first six hours of financial literacy training, and $0.56 per month for the seventh through twelfth hours of financial literacy training, but there was little evidence of increased savings resulting from further training.

Account Partners: Banks and Credit Unions

In order to be effective, a model IDA initiative would also require the active participation of banks and credit unions throughout the state. Nationally, 81% of IDAs are held in banks and the other 19% are held in credit unions, according to a February 2005 study by the U.S. Comptroller of the Currency.

Participating financial institutions express strong support and long-term commitment to IDAs, the Kenan Institute of Private Enterprise at the University of North Carolina Business School (UNC study) concluded after conducting a survey in 2003 of 230 financial institutions that sponsor IDA initiatives.

The UNC study found that there are several factors that motivate financial institutions to hold IDAs. These include strengthening their links to the local community, complying with the federal Community Reinvestment Act, and enhancing their long-term profitability.

Individuals and families who begin their banking experience with IDAs tend to remain loyal to their first bank. The UNC study states that while IDA customers "are not immediately profitable, they will

Plastering a house in Chamisal, 1940. *Photo by Russell Lee, courtesy the Library of Congress, LC-USF 34-37082.*

likely become so as their incomes grow and their demand for higher margin banking products and credit increases." A 2004 study by the U.S. Comptroller of the Currency found that in one initiative, each IDA customer opened an average of four other accounts with their bank.

The Community Reinvestment Act ("CRA") requires federal banking regulators to rate how well financial institutions are meeting the credit needs of low-and moderate-income residents in their geographic area.

Financial institutions may receive CRA credit for providing IDAs, providing matching funds, making grants or loans for operating expenses to IDA initiatives, providing staff to participate in development and oversight of IDA initiatives, and making loans to IDA owners.

There is a broad network of banks and credit unions with branches located in nearly every community in New Mexico that could potentially handle many more IDAs than they handle right now. Currently, Wells Fargo and First Financial Credit Union are the financial partners for most of the existing IDAs in New Mexico.

Bottom Line: Cost

How much would a larger scale model IDA initiative cost in terms of General Fund dollars?

One expense, of course, would be the matching funds, the cost of which depends on the level of the match. The Ford Foundation study analyzed 13 IDA initiatives across the nation involving nearly 2,500 IDA owners and found that 29% of IDA owners had a match rate of 1:1; 52% had a 2:1 match rate; 16%

had a 3:1 match rate and 6% had match rates from 4:1 to 7:1.

The researchers discovered that higher match rates tended to decrease saving because with a higher match rate, a lower level of saving is needed to reach a particular asset accumulation goal. A 7:1 return for every dollar is more like a handout than a method for teaching disciplined savings.

On the other hand, the lower the match rate, the lower the participation level and the longer it takes IDA owners to reach their asset accumulation goals. Increasing the match from 1:1 to 2:1 reduces the savings rate by $3.53 per month for the typical IDA owner, but increases the participation rate by 5.4%. (The researchers noted that IDA owners had average monthly net savings deposits of $25.42 on an average savings target of about $42.)

Taking these factors into account, we recommend using a 1:1 match rate for state General Fund dollars with a bonus 2:1 match rate for those who consistently save some amount every month. (Not-for-profits that administer IDAs would still have the option and the flexibility to use private and Federal dollars to increase the match, where appropriate, and also to provide IDAs to working individuals and families up to 200% of poverty, as Federal law allows.)

The remaining cost for a larger scale IDA initiative would be providing the financial literacy courses, plus the labor costs of the not-for-profits for providing counseling, training and case management. The federal government allows up to 15% of federal IDA grant money to be used for administration. Given the labor-intensiveness of the work, we believe that 20% would be more realistic for a state-supported IDA initiative.

The bottom line is that the total annual cost for 1,000 IDAs at the 2:1 bonus match rate, annually capped at $1,000 for individual IDAs and $2,000 for family IDAs–and assuming a 16% dropout rate–would be about $500,000. (Interestingly, the Ford Foundation study found that IDA owners generally viewed the match caps as goals rather than limits.) In addition, there would be a cost of about $100,000 for the financial literacy and not-for-profit counseling and case management component.

Thus, the total annual cost would be approximately $600,000 in General Fund dollars for every 1,000 IDAs. This cost should be weighed against the increased earnings and tax receipts that would result from the IDA owners working more hours and staying employed and, over the longer term, the reduced welfare expenses as well as intangible benefits like increased financial literacy and the increase in human capital associated with higher educational attainment.

Part of the cost might be shared with private foundations and the Federal government. (The Credit Union Association of New Mexico recently made a three-year grant of $50,000 per year for IDA matching funds, and the Federal government recently awarded a $1 million Assets for Independence Act grant to New Mexico.) Of course, if the state invested General Fund dollars, that would likely leverage more dollars from the private foundations and the Federal government.

The next section suggests a source of General Fund dollars to pay for IDAs on a more comprehensive scale.

INDIVIDUAL DEVELOPMENT ACCOUNTS AND THE NEW MEXICO LOTTERY

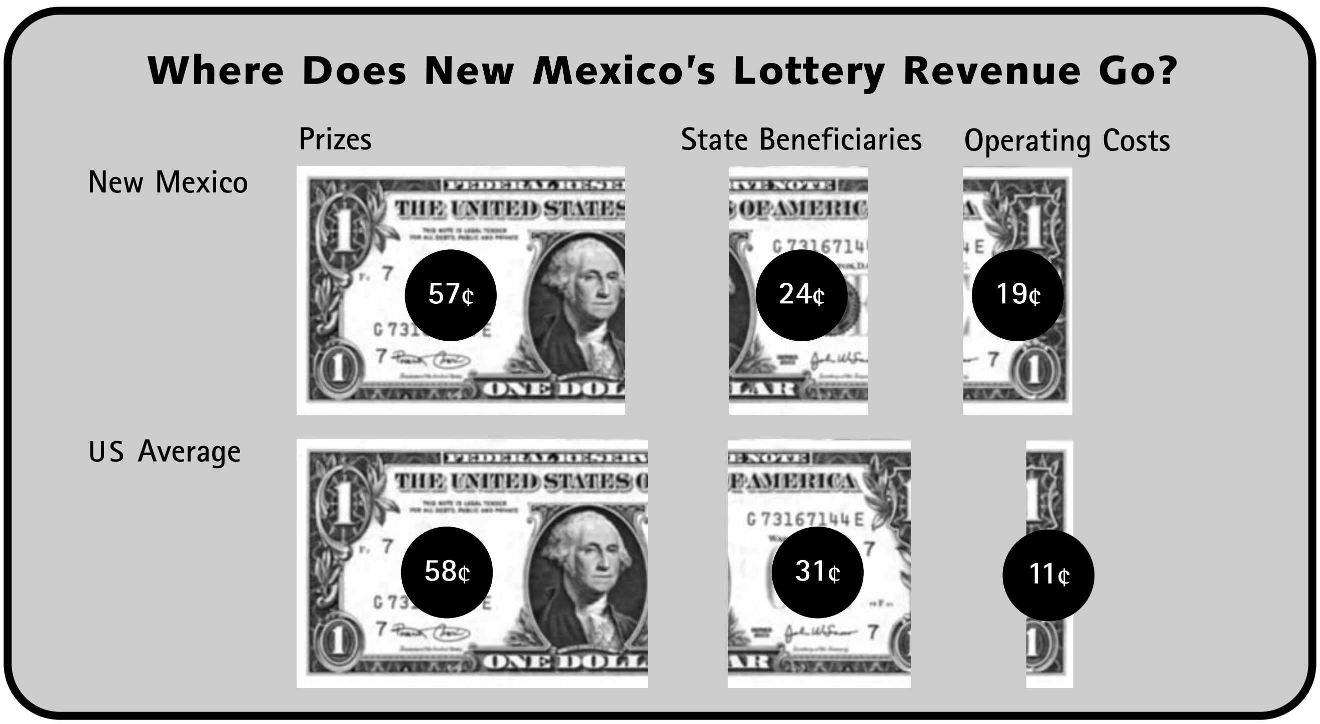
An appropriate way to make IDAs more accessible to working low-income New Mexicans would be to pay for them through the New Mexico Lottery, and reduce the regressive impact that the lottery has on this same population.

New Mexico is currently one of only a half dozen states to use lottery proceeds to provide in-state college tuition. That is a commendable purpose, and our proposal, described below, would actually increase revenue for scholarships and, at the same time, would provide a stable source of recurring revenue for a more comprehensive IDA initiative.

First, however, some background. State lotteries offer players who win instant riches and, unlike the GI bill and IDAs, require no real sacrifice. Unfortunately, however, the chances of winning the jackpot are remote. In fact, according to our calculations, a person's chances of being struck by lightening are more than 500 times greater than winning the New Mexico Lottery's Powerball jackpot. (The chances of being struck by lightening are about one in 280,000, according to the National Weather Service, versus one in 146,107,962 of winning the Powerball jackpot, according to the New Mexico Lottery website.)

States have gone into the lottery business for one simple reason: it is a popular way to raise revenue. Lotteries, however, are remarkably inefficient at that task: only about 31 cents of every dollar players spend on state lotteries actually make their way into a state treasury, according to the State & Local Government Finances division of the U.S. Census Bureau.

In New Mexico, the ratio is even smaller: only about



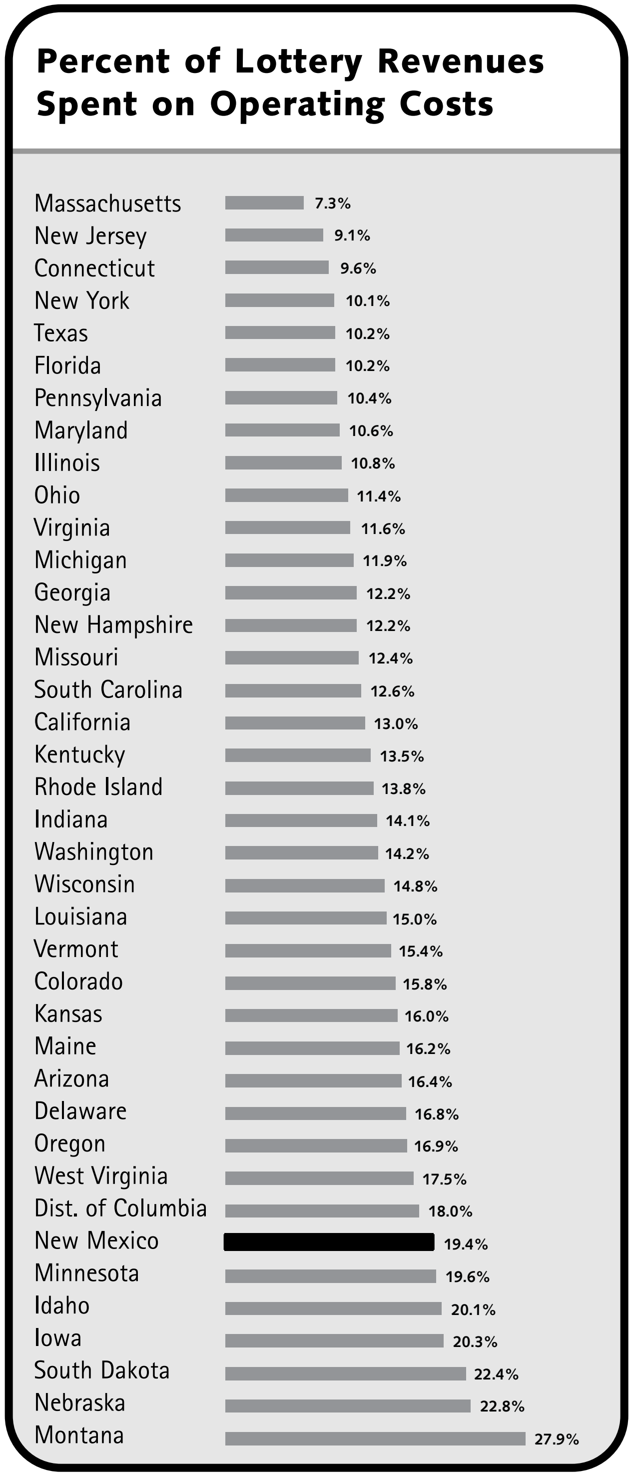
Sources: New Mexico Data from 2004 New Mexico Lottery Authority Annual Report, U.S. Data from International Gaming and Wagering Business (June 2004), as compiled by the Tax Foundation

24 percent of lottery revenues last year actually went back to the state to pay for college scholarships, according to the New Mexico Lottery Authority's 2004 Annual Report, or about $35.9 million out of $148.7 million in ticket sales.

Meanwhile, the New Mexico Lottery spent approximately 57 cents of every dollar of revenue on prizes for players and spent the remaining 19 cents for various forms of operational expenses like promotions, advertising, vendor fees, retailer commissions and salaries. In effect, the New Mexico Lottery spends 19 cents for every 24 cents it collects for lottery scholarships.

In fact, New Mexico ranks seventh highest of 39 state lotteries for the percentage of lottery revenue spent on operating expenses, according to the Tax Foundation, a nonpartisan research organization. Specifically, New Mexico spent 19.4% on operating expenses versus the 11.3% average for the other 39 state lotteries that were ranked. (New Mexico also ranks fourth highest on spending for operating expenses in a separate ranking of 37 state lotteries by the Taxpayers' Network, using figures from the Census Bureau's State & Local Government Finances division.)

New Mexico's relatively small population base does not explain why the New Mexico Lottery spends such a relatively high percentage on operating expenses. There are ten lottery states that have fewer citizens than New Mexico, and six of those states spend a smaller percentage on operating expenses than New Mexico. They are: Delaware, Maine, New Hampshire, Rhode Island, Vermont and West Virginia. If the lottery's operating expense were only a function of population, one would expect all of these smaller states to spend a greater percentage, not a smaller one, than New Mexico on operating expenses.



Source: Data from International Gaming and Wagering Business 25 (June 2004); Tax Foundation.

New Mexico's rural character also does not explain why the New Mexico Lottery spends such a relatively high percentage on operating expenses. Kentucky, New Hampshire, and South Carolina are each more rural than New Mexico, according to the U.S. Department of Transportation, yet all three spend less than 13.5% of their lottery revenues on operating costs.

Although the New Mexico Lottery is one of only two lotteries that has increased sales every year of their existence, it still struggles with persistently low returns for scholarships and relatively high operational costs on a percentage basis. When asked about that issue in 1997 by the *Albuquerque Journal* in an article entitled "N.M. Lottery Costs Rank High," former New Mexico Lottery Chief Executive Officer Ralph Decker said:

"We'd like to not worry about the percent [available for scholarships]. To me, the bottom line to the kids of New Mexico should be how much money is coming in. If the amount returned is more this next year, you should be happy."

Decker's statement was made in 1997 when 26.6% of New Mexico Lottery revenue was going to college scholarship beneficiaries. That percentage represents the high water mark, as the percentage received by college scholarship beneficiaries has declined since then.

In fact, the New Mexico Lottery Authority projects that the percentage of lottery revenues that will be left for college scholarships, after paying prizes to players and operating costs, will continue to decline over the next five years. Specifically, their budget projections, recently presented to the New Mexico Legislature predict that the percentage will decline from 23.2% in Fiscal Year ("FY") 2006 to 23% in FY2007 to 22.3% in FY2008 to 21.4% in FY2009 before edging up to 22.1% in FY2010.

We believe that New Mexico can do better for the beneficiaries of our state lottery revenues. If the percentage of lottery revenue earmarked for scholarships were raised from the current approximately 24% to the national average of about 31%, it would represent an increase of nearly $10.5 million dollars. That difference is more than enough to pay for a more comprehensive IDA initiative and, at the same time, expand the availability of college scholarships for deserving New Mexico high school students.

One way to achieve this increase is to follow the example of those states that have adopted the philosophy that their lotteries exist to serve some specific public good. These states put the beneficiaries first by setting statutory minimum percentages of lottery revenues that must go to the beneficiary programs, like scholarships, *before* paying for prizes and operating costs.

They include Delaware, Kansas, New Jersey and Pennsylvania, which set their statutory minimums for beneficiaries at 30%, as well as Georgia, Louisiana, Oklahoma (which enacted a lottery in 2004), North Carolina (which enacted a lottery on August 31, 2005) and Tennessee, which set their statutory minimums for beneficiaries at 35%.

New Mexico, by contrast, does not have a statutory minimum percentage of lottery revenues for its beneficiaries. Instead, lottery scholarships receive whatever is left over *after* prizes and operating costs are paid out. As the nearby chart demonstrates, on an annual percentage basis, that percentage has historically ranged from 22% to 26.6%.

New Mexico law does, however, establish a statutory minimum for the percentage of lottery revenues that must be given away to players as prizes: 50%. Because New Mexico sets a statutory minimum per-

States with Specified Minimum % of Lottery Revenues for Beneficiaries

Georgia	35.0%
Kentucky	35.0%
Louisiana	35.0%
North Carolina	35.0%
Oklahoma	35.0%
Tennessee	35.0%
California	34.0%
Delaware	30.0%
Kansas	30.0%
New Jersey	30.0%
Pennsylvania	30.0%

Source: State statutes; Compiled by Think New Mexico.

Percentage of of New Mexico's Lottery Revenues Used for Beneficiaries

FY '96	22.11%
FY '97	26.64%
FY '98	23.67%
FY '99	21.97%
FY '00	22.15%
FY '01	22.40%
FY '02	22.11%
FY '03	24.16%
FY '04	24.14%
FY '05 (projected)	23.97%
FY '06 (projected)	23.19%
FY '07 (projected)	23.00%
FY '08 (projected)	22.27%
FY '09 (projected)	21.38%
FY '10 (projected)	22.07%

Sources: 2004 New Mexico Lottery Authority Annual Report, "Historical Review: A History of New Mexico Lottery Performance," compiled by Think New Mexico; New Mexico Lottery Authority Budget Projection with Actual Unaudited FY 05, July 2005.

centage that must be paid out to players, it seems only reasonable to also set a statutory minimum percentage of lottery revenues that is reserved for beneficiaries.

(Likewise, there is no reason that New Mexico could not establish a statutory percentage cap on operating costs, including retail commissions and vendor fees. In Massachusetts, North Carolina, South Carolina, and Virginia, such operating costs cannot exceed 15% by law. In Texas, they cannot exceed 12%.)

There are many good reasons to expand the slice of the lottery revenue pie reserved for beneficiaries by establishing a statutory minimum percentage of lottery revenues for scholarships and IDAs. First, such an approach makes more resources available to the beneficiaries without raising taxes.

Second, this approach helps ensure the lottery scholarship program's sustainability into the future. Revenue projections for 2005 from the New Mexico Lottery

Authority and the Higher Education Department indicate that the lottery scholarship program faces a potential shortfall of about $2 million in the 2011 budget year when the costs of scholarships will exceed annual revenues and current cash reserves will be depleted. This is because lottery revenue is not projected to keep pace with student demand for the scholarships and rising tuition costs.

Senate Majority Leader Michael Sanchez, the primary sponsor behind the Lottery Scholarship, is right when he says, "We made a promise to the people of the state of New Mexico that the Lottery Scholarship was going to be available for their kids and we need to keep that promise."

Third, and perhaps most importantly, investing a portion of the New Mexico Lottery income in IDAs represents a good opportunity to mitigate the lottery's regressive nature. The National Gambling Impact Study Commission has documented the regressiveness of lotteries generally – that is, that low-income people spend a higher proportion of their income and often a higher dollar amount on lottery tickets than high-income people.

Just how regressive is the New Mexico Lottery? It is difficult to sort out the answer because statistics on how much is spent on lottery tickets on a per capita income basis do not exist, but the New Mexico Lottery does maintain sales statistics by county. Through the Inspection of Public Records Act, we obtained those sales statistics and compared them to Census data by households for New Mexico's counties.

That comparison revealed that residents of poorer counties in New Mexico generally spend more money on lottery tickets than those in wealthier counties. Take, for example, the median household in Guadalupe County (22.4% poverty rate), with an income of $23,359, which spent a whopping $464 on lottery tickets in 2004, while the median household in Los Alamos (2.7% poverty rate), with an income of $92,052, spent only $114 on lottery tickets in 2004.[3]

That lottery revenues disproportionately come from low-income New Mexicans is compounded by the fact that the revenues go disproportionately to higher-income students. For example, a report in the *Chronicle of Higher Education* found that 64% of lottery scholarship funds in New Mexico go to students whose families make at least $50,000 a year, well over the state's median income of approximately $34,000.

This "reverse Robin Hood effect" needs to be weighed against the enormous good that the lottery scholarships provide. For instance, the New Mexico Lottery has boosted in-state college enrollment by approximately 6%, according to University of New Mexico economists Melissa Binder and Philip Ganderton. Some of those students are economically disadvantaged students who are the first members of their family to attend college and who would not have been able to attend but for the lottery scholarship program.

3] *The New Mexico Lottery website contains a section entitled "Lottery Myths." "Myth #1" is that "Lotteries take advantage of the poorer economic strata of our society." The New Mexico Lottery's portraying this fact as "myth" is contradicted by every credible study on the subject, including the research cited by the lottery's own website. For example, the website mentions an isolated fact from a "May 1997 New Republic" article about state lotteries but neglects to mention the title and conclusion of that article: "Gaming the Poor: How State Governments Make Big Bucks by Conning the Most Vulnerable."*

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Moreover, Binder and Ganderton found that the lottery scholarships re-direct high school students from out-of-state institutions to New Mexico universities. Since 1997, the lottery scholarships have kept more than 32,000 of our best students in New Mexico. The lottery scholarship program is especially impressive when compared to how some other states use their lottery revenues to build things like stadiums (Washington) and landfills (Nebraska).

Nevertheless, the New Mexico Lottery still needs to identify a strategy to compensate for its impact on low-income New Mexicans. Establishing a statutory minimum of at least 31% of lottery revenues for beneficiaries would maximize revenues needed for the sustainability of lottery scholarships. It would also create a surplus that could be used to establish a modest, but more comprehensive IDA initiative. That would benefit precisely the people who are spending most heavily on lottery tickets.

These are complimentary goals because many IDA owners use the proceeds of their accounts for college tuition. IDA owners are not eligible for lottery scholarships since they are not coming directly from high school and lottery scholarships are not available to returning students. Thus, IDAs would compliment lottery scholarships by making college even more accessible to low-income students.

Governor Bill Richardson understands the need to address the New Mexico Lottery's regressiveness and to refine the lottery scholarship program. Last year, for example, the Governor tried to use about $2 million of lottery proceeds for need-based financial aid scholarships, "to make sure that every New Mexican has access." The Commission on Higher Education, however, rejected the Governor's proposal on fiscal grounds before it could be presented to the Legislature.

In sum, our proposal **1)** addresses the regressive nature of the New Mexico Lottery by adding an IDA component; **2)** ensures the sustainability of the lottery scholarship program, consistent with Senator Sanchez's original vision; and **3)** helps Governor Richardson to achieve his objective to make college more accessible to more working low-income New Mexicans without raising taxes.

CONCLUSION

If New Mexico is ever to break away from the same group of states that always rank at the top for poverty and the bottom for income, then we will need to adopt innovative strategies with proven track records for success. A good place to start would be with a statewide, state-supported IDA strategy.

New Mexico already has the capacity to achieve this. As we discussed earlier in this report, all the key players are in place—New Mexico's community colleges, the banking industry and the nonprofit sector. They could be brought together to create a model IDA statewide initiative.

For a more comprehensive IDA project to succeed, it will require financial support from state government. In the prior section, we identified the New Mexico Lottery as a logical and appropriate source of revenues to underwrite a state-supported IDA initiative. We explained how this could be done while enhancing the current lottery scholarships and at the same time addressing some of the most regressive aspects of the lottery.

This in turn will require the right type of political leadership, from both parties, in the same way that the GI Bill was a bipartisan effort.

The alternative is to continue what we are doing, crossing our collective fingers and hoping for the best while one in four of New Mexico's children grow up in poverty. The longer we wait to act, the more of those children we consign to life in poverty without any real hope of getting out.

State Public Welfare Expenditures Per Capita for 2003

State	Expenditure	State	Expenditure
Alaska	$2,025.92	Iowa	$950.17
New York	$2,024.44	Georgia	$928.94
Rhode Island	$1,646.44	North Carolina	$927.81
Minnesota	$1,558.16	New Hampshire	$919.98
Maine	$1,520.60	Maryland	$916.53
Vermont	$1,476.21	Delaware	$914.50
California	$1,366.84	Illinois	$907.47
Tennessee	$1,306.11	Michigan	$906.39
Pennsylvania	$1,300.24	Oklahoma	$906.25
Mississippi	$1,287.72	Wyoming	$887.37
New Mexico	$1,283.07	Indiana	$867.39
West Virginia	$1,231.71	Texas	$836.92
Kentucky	$1,205.46	Massachusetts	$824.44
South Carolina	$1,150.96	South Dakota	$812.57
Ohio	$1,095.29	New Jersey	$810.58
Connecticut	$1,085.57	Arizona	$803.41
Oregon	$1,071.28	Idaho	$799.28
Wisconsin	$1,053.93	Florida	$788.26
Nebraska	$1,041.68	Colorado	$756.95
North Dakota	$1,029.04	Utah	$747.60
Washington	$1,019.44	Montana	$722.89
Alabama	$1,006.17	Virginia	$710.79
Arkansas	$991.69	Kansas	$699.32
Missouri	$977.79	Louisiana	$623.11
Hawaii	$974.07	Nevada	$530.78

Source: U.S. Census Bureau, 2003.
http://www.census.gov/govs/www/state03.html

In the meantime, traditional welfare programs strain to meet demand, in spite of the fact that New Mexico is relatively generous in subsidizing those programs. As the accompanying chart demonstrates, New Mexico ranks 11th highest in state public welfare benefits per capita, even while we rank 46th in per capita income, according to the Census Bureau. New Mexico's population of age 65 and over is projected to more than double by 2030. As New Mexico's Baby Boomers begin to retire, it will become increasingly difficult to maintain those benefits at that level, while the need will likely grow.

New Mexico urgently needs policies that will create jobs through micro-enterprises, foster a better educated and trained work force and reduce welfare dependency. This is precisely where IDAs offer the greatest promise.

Naturally, there will be detractors. No doubt, some will complain that IDAs do not go far enough. Others will argue that IDAs subsidize pursuits of low-income people that would better be left to the free market. Here, we should recognize that both the state and federal government subsidize asset acquisition for the non-low-income with tax breaks and credits, including mortgage deductions, college savings plans, and retirement plans, totaling more than $200 billion annually. We are simply trying – on a much smaller scale – to extend these same asset-building opportunities to those low-income New Mexicans who are striving to enter the middle class.

Owning assets gives working, low-income New Mexicans a bigger stake in New Mexico's future and a better shot at realizing the American Dream. Any New Mexican willing to work hard and to commit to saving and investing deserves to have access to a college education, the opportunity to start a business, and the security of owning a home.

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State Statutes, Regulations, & Legislation

We reviewed 16 state IDA statutes, including all of the states listed on the chart on page 11. In addition, we reviewed lottery statutes for 41 states including the district of Columbia. Because of space limitations, we have not listed each one separately here.