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Executive summary

A major initiative for increasing personal savings has been underway in the United Kingdom since 2005. Every child born on or after 1 September 2002 has been given an investment account, called a Child Trust Fund (CTF), endowed with a modest government contribution. By building the savings capacities of families, it is intended that CTFs will give all children a financial asset to fund their transition to adult life. Indeed, government data indicate that the Child Trust Fund policy has been successfully launched and shows great promise for the future.

This paper sets out some of the early findings from the UK's experience of CTFs and highlights the key challenges for other countries that may be interested in implementing a national universal children's savings programme.

The operation of the Child Trust Fund account

Shortly after birth, every child in the UK receives a voucher from the government. The amount depends on the family's wealth, and ranges from £250 (US\$500)¹ to £500 (\$1,000) for children from less affluent families. The child's parents can then use this voucher to open a CTF account with a private sector provider. If the voucher is not used within 12 months of being issued, the government will automatically open an account on behalf of the child with a randomly chosen private sector provider.

At age 7, each child receives a further contribution from the government, which is known as a 'top-up': £250 for every child and a further £250 for children in low-income families. Parents, friends and family can make additional tax-free contributions to accounts of up to £1,200 (\$2,400) in total each year. The accounts mature when the child reaches 18 and there are no restrictions on how funds are spent. The balance is automatically rolled over into an accessible adult savings account. No withdrawals can be made before the child reaches 18.

Initial findings from the first few years of the CTF

Using official data from the first two-and-a-half years of the Child Trust Fund together with academic research, industry data, and original research, we are able to draw some initial conclusions about the early achievements of the CTF.

Initial parental involvement

- Parental engagement with the CTF is relatively high but could be improved.
- 75 per cent of accounts are opened by parents, which compares favorably with take-up of other similar financial products.
- Parents who fail to open an account are more likely to be on a low income, but this lack of engagement extends across the income distribution.

Impact on savings behaviour

- The initial government endowment encourages parents, family, and friends to make additional contributions, with private savings already equal to 55 per cent of the government's endowment.
- Positive effects on savings behaviour in family-opened CTFs – even among low-income households – are becoming evident: 30 per cent of accounts opened by parents have received additional private contributions.

Investing in shares

- Equity investing has proven popular and 80 per cent of all CTFs are 'stakeholder accounts' – invested in shares but subject to a cap on fees and 'lifestyling' to reduce risk as children get older.

1. This paper uses a conversion rate of £1 = US\$2 throughout.

The role of the private sector

- Participation by the private sector is extensive, with 100 organisations operating in the CTF market.
- This helps to broaden the availability of CTFs, but can make investment decisions difficult for some families.

Challenges ahead for the UK

Our research also indicates some areas for further development of the CTF policy. The first is the need to increase initial parental involvement and reduce the number of government-opened CTFs. Research indicates that the range of providers and variety of account types may be undermining participation, and points to the need for improvements in the provision of information to parents.

The second area for further development is to expand the number of CTFs receiving private contributions, particularly among lower-income families. One way to achieve this is through the direct matching of private contributions by the government, rather than relying on tax relief to incentivise saving. Evidence from the Saving Gateway in the UK and from workplace savings plans in the United States indicate the potential role for matching in increasing savings rates among low-income households.

Safeguards will be needed when applying matching to CTFs to ensure that low-income families do not prioritise saving for the future over immediate consumption on essential items. However, there is scope for matching to be an important enhancement to the Child Trust Fund policy which helps ensure all young people can benefit from having a sizeable pot of money to support their transition to adulthood.

1. Introduction

In recent years, the personal savings rate in the United States and other industrialised countries has fallen sharply, and it is now at a historically low level. This decline raises concerns about the ability of families to finance their long-term needs such as educating their children, buying a home, or enjoying a secure retirement. It also creates potential challenges for national economic prosperity. Further, there are concerns about ethnic and social class differences in homeownership rates and ownership of other assets in the US.

One promising initiative for increasing personal savings and reducing wealth inequalities has been underway in the UK since 2005 in the shape of an investment account called the Child Trust Fund (CTF). Every child born since September 2002 has a CTF opened on their behalf which is endowed with a modest government contribution. By building the savings capacities of families, the aim is that CTFs will give all children a financial asset to fund their transition to adult life.

Research suggests that the possession of a small pot of money in early adulthood is associated with improved chances later in life (Bynner and Paxton 2001). The CTF is designed to ensure that all children, regardless of their family background, have access to some assets at age 18. In the long term, it is hoped that this will contribute to reducing the large inequalities in wealth in the UK. By linking the CTF to school-based financial education programmes, the CTF is also designed to promote a savings habit from an early age and boost levels of financial capability.

This paper starts by explaining how the Child Fund Trust accounts work. We then summarise the main findings from data that cover the first two-and-a-half years of the policy, focusing on the impact on savings behaviour, parental engagement and the role of the private sector. We then highlight two of the major challenges as the CTF policy moves forward: increasing parental involvement and boosting savings rates among low-income families, in order to reduce the gap in final account values between children from higher- and lower-income families.

2. The Child Trust Fund account

Every child born in the UK on or after 1st September 2002 receives a voucher worth £250 (\$500) from the government, which parents can use to open a CTF account in their child's name.² Children from low-income households, where household income is less than £15,575 (\$31,150) in 2008/09, receive an additional £250. Nearly 30 per cent of children receive the full £500 (\$1,000) endowment (HMRC 2007a). Parents can open an account with a provider of their choice and all accounts are operated by private sector financial institutions. If a child's parents fail to use their voucher within 12 months, the government automatically opens an account for the child with a randomly chosen private sector provider.

All accounts receive an additional payment when the child turns 7, on the same basis as the initial endowment – £250 for all children and a further £250 for children from less affluent families. Additional contributions to accounts can be made by parents, family and friends up to a total value of £1,200 (\$2,400) each year. All interest earned on the account is tax-free. Account funds are locked up until children reach 18 years of age, at which point they may choose how to spend their accumulated savings; neither the government nor parents can impose any restrictions.

CTFs at a glance

- Government issues a voucher worth £250 (\$500) – or £500 (\$1,000) for low-income families – to every child at birth.
- When the child is seven, CTFs receive a second government contribution (or 'top-up') on the same basis as the initial endowment.
- Parents use the voucher to open a CTF at a private sector provider.
- Government opens CTFs for children whose parents do not use their voucher within 12 months.
- No tax is paid on interest.
- Additional contributions from parents, family and friends of £1,200 (\$2,400) are permitted each year.
- No withdrawals are available before age 18.
- Children have full access to CTF funds at age 18.
- All CTFs are automatically converted to an adult savings account at age 18, allowing for continued tax-free growth and unrestricted use of funds.
- The government promotes CTFs through media campaigns and coordinated financial literacy education in schools.

In order to promote the responsible use of CTF funds at age 18 and build financial capability among a new generation of CTF-owning children, the government has allocated £11.5 million (\$23 million) between 2008 and 2011 to fund an active financial education programme, including an inter-disciplinary 'Money Week' in schools to coincide with the second government contribution when children turn seven years old (HMRC 2007a). When a young person reaches 18, the CTF account is automatically converted into an accessible adult saving account, called an Individual Savings Account. This is designed to promote responsibility by encouraging young people to maintain a savings account, and avoids potential pitfalls that could come with presenting young people with a large sum of money at age 18.

Overall, the government currently spends around £240 million (\$480 million) annually on the CTF programme. This is expected to rise to £490 million (\$980 million) by 2012/13 as top-ups at age

2. This paper uses a conversion rate of £1 = US\$2 throughout.

seven are introduced from September 2009 (HMRC 2007b).

Although CTFs are initially funded through a government-issued voucher, the accounts themselves are available only through private sector financial institutions. There are three types of CTF account available to parents: cash, equity and stakeholder. The stakeholder account is equity-based with some key protections: a 'lifestyling' option means that funds are automatically transferred to less risky investments after the child reaches 13 and annual fees are capped at 1.5 per cent. All approved CTF providers must offer a stakeholder account and all government-opened accounts are stakeholder accounts.

3. Initial findings from the first few years

Although the UK was the first country to implement a universal child savings account, contemporary thinking about savings accounts for children originated in the US in the late 1980s (Sherraden 1991). More recently, discussion in the US has focused on historically low national and personal savings rates, as well as soaring college tuition costs, ethnic disparities in homeownership rates, and a generation of baby boomers who are, on the whole, unprepared for retirement. These long-term challenges will require long-term solutions.

A policy like the Child Trust Fund – with the potential to build significant financial assets and change savings behavior over time – should be of interest to policymakers in the US, who can learn from the UK's initial experience with CTFs. It should be recognised that the CTF policy has only been up and running since April 2005 and is still in its early days. Nevertheless, data is now available from the first two-and-a-half years which points to some significant successes and highlights areas for further development. In this section, we summarise the key findings from the first few years of the CTF policy.

Highlights from the first few years

- 3.35 million CTFs have been opened since 2005.
- 75 per cent of accounts were opened directly by families; the remaining 25 per cent were opened by government.
- Nearly 30 per cent of children have received an extra contribution based on their household income.
- The annual cost to the government is £240 million (\$480 million).
- Over 100 commercial organisations operate in the CTF market.
- The 'stakeholder' account, which is invested in equities and has a 1.5 per cent fee cap, is the most popular account type.

Initial parental engagement

The CTF is a universal policy because it endows all children born in the UK with an investment account held in their name. Of the vouchers issued to date which had expired by March 2008, 75 per cent have been used by parents to open an account (HMRC 2008a). The remaining 25 per cent were not used within 12 months and so the government opened an account on behalf of those children. Given the infancy of the CTF policy, this level of take-up compares well with other similar financial products.

Evidence from the US shows that take-up of financial products that offer favourable savings incentives rarely approaches 100 per cent. Studies of a popular workplace saving system – the 401(k) plan – have found that between 20 and 60 per cent of workers do not contribute enough to earn a full matching contribution from their employer, foregoing as much as six per cent of additional pay (Choi *et al* 2007). The literature on the Earned Income Tax Credit (EITC), a tax credit for low-income

workers in the US, reports take-up rates that hover around the 70 per cent mark (Dickert-Collins *et al* 2005). Evaluation of the Saver's Credit, a tax credit for pensions savings for low-income workers, also indicates that only 66 per cent of individuals who make qualifying contributions actually applied for the credit (*ibid*).

Official data from the UK shows that parents who do not use their voucher before it expires tend to be low-income, have larger families and are more likely to be single parents (HMRC 2007b) than those who do use the voucher. A third of families with incomes below £5,220 (\$10,440) failed to use their voucher, compared with 11 per cent of households with incomes between £30,000 and £40,000 (between \$60,000 and \$80,000). Only 60 per cent of families with five or more children used their vouchers, compared with 82 per cent of families with just one child. A third of single parents did not cash in their voucher, whereas this figure is only 18 per cent for couples.

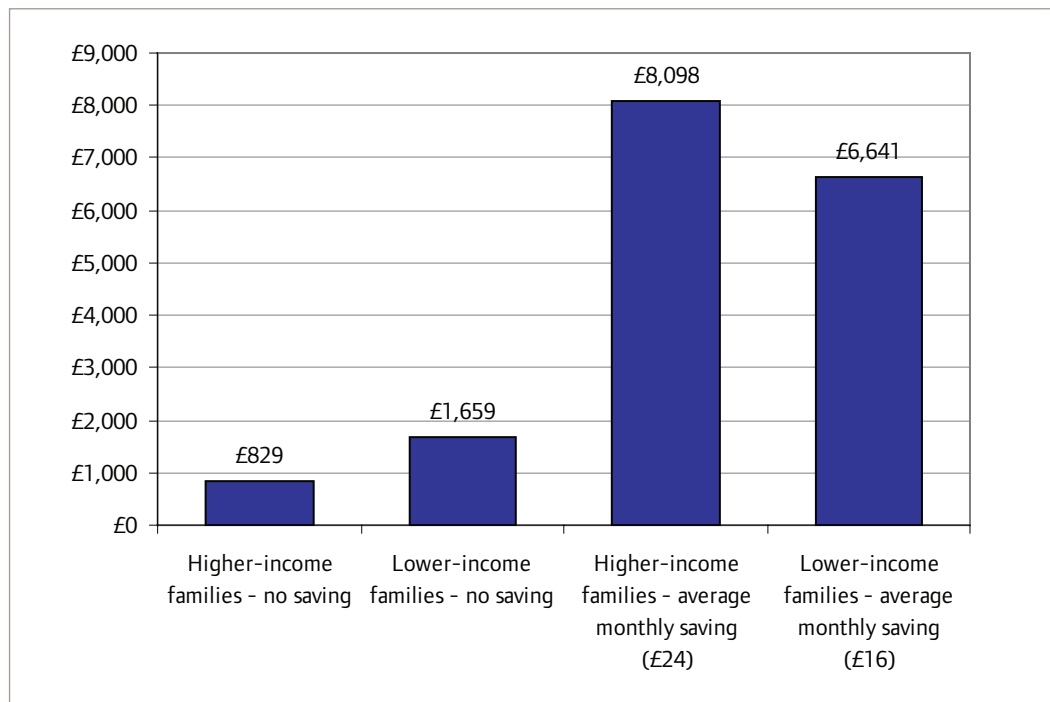
Disadvantaged families tend to experience greater levels of financial exclusion and may also face greater family and financial pressures which prevent them opening an account. However, this data also highlights the fact that the lack of initial parental engagement occurs across the income distribution and is not solely limited to disadvantaged families.

Investing in shares

Equity-based CTFs have proven to be the most popular option among parents. As Figure 1 shows, 80 per cent of all CTFs are stakeholder accounts (HMRC 2007b). This is partly because all government-opened accounts are stakeholder CTFs, but also reflects the high number of stakeholder accounts opened by parents. Three quarters of all family-opened accounts are stakeholder CTFs. As outlined above, stakeholder accounts are equity-based investments with safeguards, including a cap on fees and a move away from riskier shares once a child turns 13. Over the 18-year lifetime of a CTF, equity-based accounts are likely to produce higher returns than cash savings. Of the remaining CTF accounts, 18 per cent are held in cash accounts and three per cent of accounts are non-stakeholder equity-based CTFs (HMRC 2007b).

Figure 1: CTF account type for all children born in or before 2005/06

Source: HMRC 2007b



Impact of CTFs on account ownership and savings behaviour

Initial data suggests that CTFs have had a positive effect on account ownership among children and on savings behaviour among families. A major baseline survey carried out prior to the introduction of CTFs gives some indication of patterns of saving for children in the UK before 2005 (Kempson, Atkinson and Collard 2006). The study found that 69 per cent of children held some kind of savings or investments, primarily in the form of a cash savings account.³ The average account balance was £420 (\$840). The likelihood of a child having savings or investments varied greatly with household income. Only half of children living in households with a net monthly income of less than £1,000 (\$2,000) had any savings or investments, whereas over 80 per cent of children in households with a monthly income of between £2,000 and £2,999 (or between \$4,000 and \$5,998) held such products. Similarly, the average amount held in these accounts was £257 (\$514) for the first group, but double that for the second group (Kempson *et al* 2006).

Kempson *et al* (2006) also found that half of all children had received extra payments into their account since it was opened, and 43 per cent had received deposits in the last year. The average amount contributed in the previous 12 months was £180 (\$360). Again, children in lower-income families were much less likely to have had a deposit made in the last 12 months: just over a quarter (27 per cent) of children in households with a monthly income of less than £1,000 had received additional payments in the last year, compared with 56 per cent of children with a household income of between £2,000 and £2,999. Family income also had an effect on the amount of money being deposited, with children in the lower-income group receiving £120 (\$240) on average over 12 months, compared with £165 (\$330) for children in the higher-income group (*ibid*). The baseline survey did not collect data on how many accounts were receiving regular monthly contributions, which is generally felt to be one of the key tests of the success of the CTF policy.

Even though the majority of children had some form of savings account, accounts that were long-term and that attracted regular monthly saving – two of the key features of CTFs – were uncommon. Just 10 per cent of children's savings accounts had any form of limited access, such as notice periods or restrictions on the number of withdrawals that could be made (Kempson *et al* 2006). Life insurance policies, which mature when a child reaches a certain age – usually 16, 18 or 21 – and therefore mirror an important feature of the CTF, were held by only six per cent of children (*ibid*). Furthermore, market research conducted by the financial services industry suggests that, prior to the introduction of CTFs, only 18 per cent of children had long-term accounts attracting regular monthly payments.⁴ The study by Kempson *et al* study also highlights the fact that 31 per cent of children had no savings or investment account at all before the introduction of the CTF.

Through the CTF policy, all children born since September 2002 now have a long-term savings account. By December 2007, 3.35 million CTF accounts had been opened in total (including accounts opened by parents and by HMRC). By April 2007, CTFs held assets worth £1.3 billion (\$2.6 billion), while the cost to the UK government has been approximately £856 million (\$1.7 billion) (HMRC 2007a). In other words, less than three years into the programme, private assets already equal 55 per cent of government contributions. This compares with 15 per cent at the same point in 2006 (HMRC 2006). Our conservative projections are that private assets will equal or exceed government's contribution some time in 2009, just as the age 7 payments begin. This indicates that there has been a substantial degree of parental participation in the policy.

Overall, 24 per cent of Child Trust Funds had received an additional contribution by April 2007. Among CTFs opened by parents (rather than by the government), this figure rises to 30 per cent (HMRC 2007b). As we would expect, the contribution rate varies with household income. Table 1 shows that only 21 per cent of accounts that received the initial government endowment of £500

3. This includes savings and investments held in a child's name as well as accounts which parents indicated were for their child but which were not necessarily in their child's name. Children did not always have access to the accounts.

4. From research carried out by the Children's Mutual.

(\$1,000) – which we identify as ‘lower-income’ accounts – had received additional private contributions by April 2007. This compares with 34 per cent of accounts opened by ‘higher-income’ households – those who were only entitled to the £250 (\$500) voucher.

Table 1 also shows that lower-income families tend to make smaller contributions to their children’s CTFs. Only 11 per cent of children from lower-income families had received more than £300 (\$600), compared with 28 per cent of higher-income families. For all CTFs, the additional contributions made by lower-income families are equal to a fifth of the contributions made by higher-income families. If we consider just those CTFs that receive additional contributions, lower-income families contribute 38 per cent as much as higher-income families.⁵ Previous research carried out by the authors in May 2006 found that where monthly deposits to CTFs were being made, accounts in higher-income families received an average of £24 (\$48) a month, compared with an average of £16 (\$32) a month in lower-income families.

Table 1. Additional contributions made to family-opened CTFs

	Percentage of accounts receiving any additional contribution	Total additional contributions (excluding initial government endowment) made to family-opened CTF accounts since account opening			
		Less than £100 (\$200)	£100 - £299 (\$200 - \$599)	£300 - £1,199 (\$600 - \$2,399)	£1,200 (\$2,400) or more
Families who received the £500 (\$1,000) endowment	21%	44%	44%	10%	1%
Families who received the £250 (\$500) endowment	34%	28%	44%	22%	6%

Source: Authors’ calculations based on data in HMRC 2007b

One of the original rationales for the CTF was its potential to promote a long-term, regular savings habit among parents and, eventually, children. The number of accounts that receive regular monthly payments via ‘Direct Debit’⁶ is therefore a good indicator of how successful this element of the policy has been. For this, we have to rely on industry data collected from a sub-sample of over two million CTF accounts (TISA 2008). These figures indicate that, by March 2008, 78 per cent of private contributions had been made through monthly Direct Debit, with the remainder being lump sum contributions averaging £472 (\$944) in total (TISA 2008). The level of contributions via Direct Debit has also shown an upward trend. In the 12 months before March 2008, the average monthly Direct Debit contribution increased from £20.65 to £21.43 (or from \$41.30 to \$42.86). Lump sum contributions also increased by 4.9 per cent from £386 to £472 (or from \$772 to \$944) (TISA 2008).

Although the amounts saved by lower-income families are likely to be smaller, one survey suggests that lower-income families are contributing a higher proportion of their incomes. Data from a major CTF provider reveal that, among families who make regular deposits, lower-income families are saving 1.1 per cent of their net monthly salary in their children’s CTFs, while higher-income families are only saving 0.6 per cent. The survey also found that both groups have increased the amount that they are saving into their children’s CTFs since April 2005 by between 8 and 9 per cent (Engage Mutual Assurance 2007).

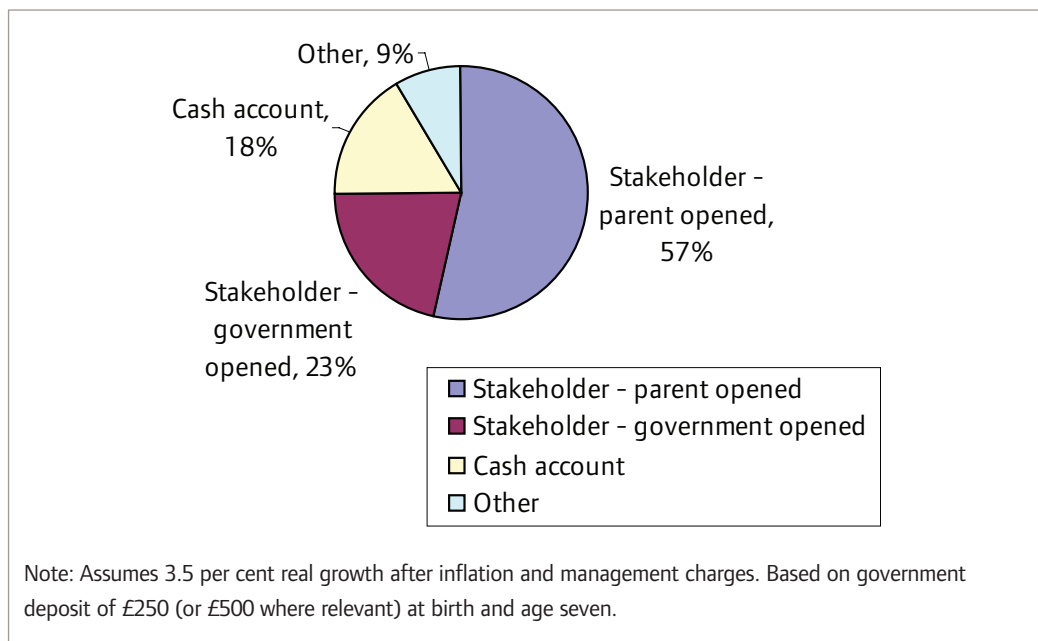
5. In this calculation, we assume that lower-income households contribute at the bottom quartile of each contribution classification and higher-income households contribute at the mid-range of each classification.

6. A Direct Debit is an instruction from a customer to their bank or building society authorising an organisation to collect an amount from their account. A Direct Debit can be set up so that a regular amount is automatically collected from a customer’s main account each month and transferred directly to a CTF. The US equivalent of a Direct Debit is an Automated Clearing House (ACH) transfer from a bank directly to a biller. The account owner initiates this transfer.

Additional private contributions are critical to the growth of CTFs. Figure 2 shows the value of a young person's CTF at age 18 under four different scenarios: a higher-income account⁷ with no extra deposits, a lower-income account with no extra deposits, a higher-income account with the average higher-income monthly direct debit of £24 (\$48), and a lower-income account with the average lower-income monthly direct debit of £16 (\$32).⁸ The difference between those accounts that attract regular saving and those that do not is considerable, and more significant than the difference between higher- and lower-income accounts with average amounts of monthly saving. Our calculations also find that if a higher-income family saved the maximum of £1,200 (\$2,400) each year, a young person's CTF would be worth £31,300 (\$62,600) at age 18.

Figure 2: Value of CTF accounts after 18 years under various scenarios

Source: Author's calculations



One particular area of concern is the rate of additional contributions among families who do not open their own CTF. Official data shows that only one per cent of government-opened accounts have received private contributions (HMRC 2007b). Where deposits have been made, they have almost all been worth less than £100 (\$200) in total (HMRC 2007b). While it is possible that these accounts will receive additional contributions later on – perhaps as family finances improve or the initial upheaval resulting from the arrival of a new baby starts to subside – this very low rate of contributions among government-opened accounts does highlight the relationship between initial parental engagement and the likelihood of families making additional contributions to a CTF.

The role of the private sector

The financial services industry has made good on its commitment to the CTF policy by creating a new product and supporting systems for millions of accounts within a very short period of time. CTFs are widely available from a range of mainstream and specialist financial institutions and there are currently over 100 organisations involved in the CTF market (HMRC 2007a).

For most companies, the profit margins associated with delivering CTFs in the short term will be small. In fact, some financial institutions initially decided not to enter the market as they felt the CTF would not be a worthwhile addition to their portfolios (Kempson *et al* 2006). However, many financial services providers recognised the medium- to long-term potential of CTFs. Where CTFs are a central

7. For the purposes of this section, we define a lower-income account as one that received the full £500 government endowment, and a higher-income account as one that received the £250 endowment.

8. These figures are from research carried out by the authors in May 2006 with providers covering 60 per cent of the market.

element of their product portfolio, providers recognised the need to focus on attracting a substantial share of the CTF market and maximising the proportion of accounts receiving additional contributions (Kempson *et al* 2006).

For others, offering a CTF product is an important means of attracting and retaining customers, and can also be a potential driver for increased take-up of other financial products (Kempson *et al* 2006). This is particularly true for some retail banks, which do not heavily market CTFs but offer them to ensure they do not have to turn away new business. There is also some anecdotal evidence that financial services providers are increasing their range of savings products aimed at children who are too old to qualify for CTFs (information from discussions with HM Treasury officials). This indicates that the industry is reacting positively to the CTF policy and using it to stimulate a more widespread growth in children's savings.

The financial services industry has created a variety of arrangements for offering and servicing CTFs. Organisations that wish to offer their own CTF product must be registered as an approved provider with HM Revenue and Customs, the government department with responsibility for the CTF policy. Organisations can also sell CTFs that are managed by approved providers and these organisations are known as distributors. There are currently over 40 approved providers and over 70 distributors, and the majority of distributors have a direct relationship with a single approved provider (HMRC 2008b).

Over two-thirds of approved providers are building societies, friendly societies, credit unions, and other mutual financial institutions⁹ (HMRC 2008b). Mutual financial institutions have traditionally been major providers of children's savings products in the UK, so it is not surprising that they have dominated the CTF market. They also tend to have longer-term profit horizons, which are more in line with the longer-term returns from CTFs. However, mainstream banks, given their extensive branch networks, also have an important role in the CTF market, particularly as distributors. Non-financial companies including supermarkets and mainstream retailers also act as distributors, which further increases the availability of accounts, especially for families who may not be familiar with mainstream financial institutions.

4. Challenges ahead for the UK

After only two years, the UK's Child Trust Fund policy has demonstrated some solid results. There are, however, some important areas that will require further development. In this section, we focus on two challenges that are likely to be of particular interest to policymakers in the US and elsewhere: increasing parental involvement from the very beginning; and increasing the rate and level of private contributions, especially in lower-income families.

Increasing parental involvement

The evidence presented above highlights the importance of parental engagement for the CTF policy to be successful in endowing every young person with a sizeable asset when they reach 18. When parents are not engaged from the very beginning, they are very unlikely to make any additional contributions, at least in the first few years. Accounts that do not receive regular additional payments will have a low value when they mature. This points to two challenges: increasing the initial involvement of parents so that more families open their own CTF account; and increasing parental engagement throughout the life of an account.

Research conducted by Kempson *et al* (2006) as part of their baseline survey at the inception of the CTF shows that 99 per cent of parents intended to open a CTF account for their child. Yet we know

9. Mutual financial institutions, including building societies and credit unions, are owned by their customers, whereas banks and insurance companies are owned by shareholders.

that only 75 per cent of parents actually go on to open an account, which points to a significant gap between parents' intentions and actions. Qualitative evidence from focus groups conducted with parents indicates that the variety of account types and large number of providers may be undermining participation (ibid, Prabhakar 2006). Parents have reported feeling overwhelmed by the choice of providers and the amount of time it takes to make a proper assessment of accounts and providers, particularly given the time constraints on parents with a new baby (Prabhakar 2006).

Evidence from the US demonstrates that complexity and lack of good quality information can have a negative impact on participation in savings programmes. The experience of 401(k) plans has shown that too much choice paralyses many would-be savers. Many 401(k) plans are now adopting default features with automatic contribution rates and investment options in order to reduce the need for individual savers to make complicated investment decisions.

Further research into the particular barriers to parental participation in the CTF may be useful. In particular, if the choice of providers is a major stumbling block, simplifying communications about providers might prove helpful. If, instead, too many parents are inhibited by the choice of investment options at a given provider, there may be a case for enabling providers to designate one option – such as the stakeholder account – as the default.

It should also be remembered that a new baby puts significant emotional and financial strain on families. Some families may not be in a position to engage with their child's CTF in the early years, but this could change as the child gets older. This suggests that the CTF needs to maintain a high profile among parents throughout their child's lifetime and this is one of the potential benefits of the top-up at age seven. Keeping the CTF 'live' in the minds of parents is important for all families, but those families who were not involved in the initial account opening will need specific targeting to encourage them to reengage with the policy. Government, the financial services industry and community organisations can all have a role in this.

Increasing account equity

Ensuring that all young people can benefit from owning assets as they make the transition to adulthood is one of the key pillars of the CTF policy. Yet the evidence presented above suggests that there could be significant differences in the value of CTF assets to which young people have access at the age of 18. To a large extent, this simply reflects existing inequalities in wealth ownership in the UK. However, there is scope for the CTF policy to reduce these pre-existing inequalities by increasing the savings rate among lower-income families in particular. This could also have the added benefit of embedding a savings habit more widely among less affluent households.

One option for boosting the additional contributions made by lower-income families and achieving greater account equity across the income distribution is the use of matched savings. Matched savings plans work by offering a direct match from the government for any private contribution. They can be more effective than savings incentives based on tax relief because a direct match is easier to understand. Lower-income families also benefit less from tax relief on savings. In the UK, the government has recently announced its intention to roll out the Saving Gateway, a matched savings plan for all low-income families, after a number of successful pilots. However, a matched savings plan for CTF contributions could prove expensive. There are also concerns about the potential for matched CTF contributions to distort parental financial decisions to the detriment of children – that is, matching may encourage low-income parents to prioritise saving for the future over immediate consumption, potentially leading to greater levels of child poverty. However, some of these concerns can be overcome by setting the match at a reasonable level and setting a relatively low limit on the amount that the government will match.

The US experience with matched savings may provide some empirical support for such a policy. Matching is common in the US and has proven to be an important incentive in stimulating private saving and changing savings behaviour over the long-term. For example, matching is a very popular feature throughout the private pension system in the US. The US has also tested matched savings plans among low-income families through experiments with Individual Development Accounts (IDAs),

which provide matching dollars to reward personal savings toward a home, small business or education. Matched IDA programmes for homeownership have been successful even in high-cost housing markets like San Francisco.

Evaluations of the American Dream Demonstration show that this matched savings programme has had a significant positive impact on home ownership. Among participants – all of whom had an average household income of under \$18,000 – homeownership rates increased by 14 per cent compared to non-participants, with an even greater impact on African-American participants (Mills *et al* 2004). H&R Block – a US company offering tax preparation and other financial services to primarily low- and moderate-income households – found that more customers contributed to a retirement savings plan when a higher match was offered, and that these customers also tended to have higher savings rates than those offered a lower match or no match at all (Duflo *et al* 2005). This success has shown that there is both capacity and interest among low-income families to save in a more structured way and that matching contributions can provide a catalyst for saving.

5. Conclusion

The Child Trust Fund policy in the UK has had a very successful launch. An extensive private sector infrastructure is in place, and over 3 million new accounts have been created. Some 75 per cent of families are redeeming their vouchers, choosing a private provider and making investment decisions. Some 30 per cent of accounts opened by parents are receiving private contributions.

The UK has demonstrated the potential of a universal child savings account, funded with a modest government contribution and delivered through the private sector, to change family savings behavior significantly. Further development around the issues of parental engagement and increasing savings rates among lower income families could help to ensure the CTF enables all children to build an asset to support their transition to adulthood.

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