INSTITUTE FOR
FINANCIAL LITERACY

Proposed Rebates in 2008: How will Americans Spend Their Tax Rebate Checks?

A Report Published by the
Institute for Financial Literacy, Inc.
March 2008

Final Version

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Acknowledgments

The Board of Directors of the Institute for Financial Literacy, for their continued support of the mission of financial education, the many wonderful clients who even in their darkest financial hours were willing to participate in this research and those alumni and former clients who have successfully moved forward with their financial lives but saw the value in participating in this research. Also to the fine staff of the Institute who on a daily basis go above and beyond to help improve the financial literacy of those they serve.

Mission

The **Institute for Financial Literacy** is a 501(c)(3) nonprofit organization whose mission is to make effective financial literacy education available for all American adults.

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Executive Summary

The Institute for Financial Literacy is a non-profit financial literacy organization. The Institute's mission is to make effective financial literacy education available for all American adults. The Institute accomplishes its mission by developing financial literacy education materials, publishing the National Standards in Adult Financial Literacy Education, maintaining the Library of Personal Finance, administering the Center for Financial Certifications, hosting the Annual Conference on Financial Education and conducting research through the Center for Consumer Financial Research.

Findings

This report finds that:

- Most survey respondents intend to Pay Debt with their prospective tax rebate checks (48%).
- The second most common response was to place the funds into Regular Savings (22%).
- The third most common response was Buy Something at (13%).
- The fourth most common response was Other at (12%).
- Retirement Savings was the least popular answer at (4%).

Recommendations

- Further study should be conducted to determine why Americans are expressing such a significant preference for debt reduction at this time.
- The study results may be an early indication of the educational effectiveness of both the pre-filing bankruptcy Credit Counseling and the Bankruptcy Debtor Education and additional research should be conducted.
- The low preference for retirement savings options, even among those 40 years and older, is an alarming indicator and educators, academics, economists and policymakers should all take serious note of this data.

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Introduction

On January 28, 2008 the United States House of Representatives introduced H.R. 5140 known as the "Recovery Rebates and Economic Stimulus for the American People Act of 2008".[1] The next day the bill was passed and referred to the United States Senate for consideration. This bill eventually passed the Senate and was signed by the President of the United States.[2] Part of this bill amends the Internal Revenue Code to grant tax rebates of the lesser of net income tax liability or $600 to individual taxpayers ($1,200 for married taxpayers filing joint returns) and allows additional rebates of $300 for each child of an eligible taxpayer.[3]

The largest daily newspaper in Maine ran the following headline on January 29, 2008: "$600 rebate: save it, splurge, invest or go surfing?"[4] The Institute for Financial Literacy (IFL) was curious to know how Americans would answer this question.

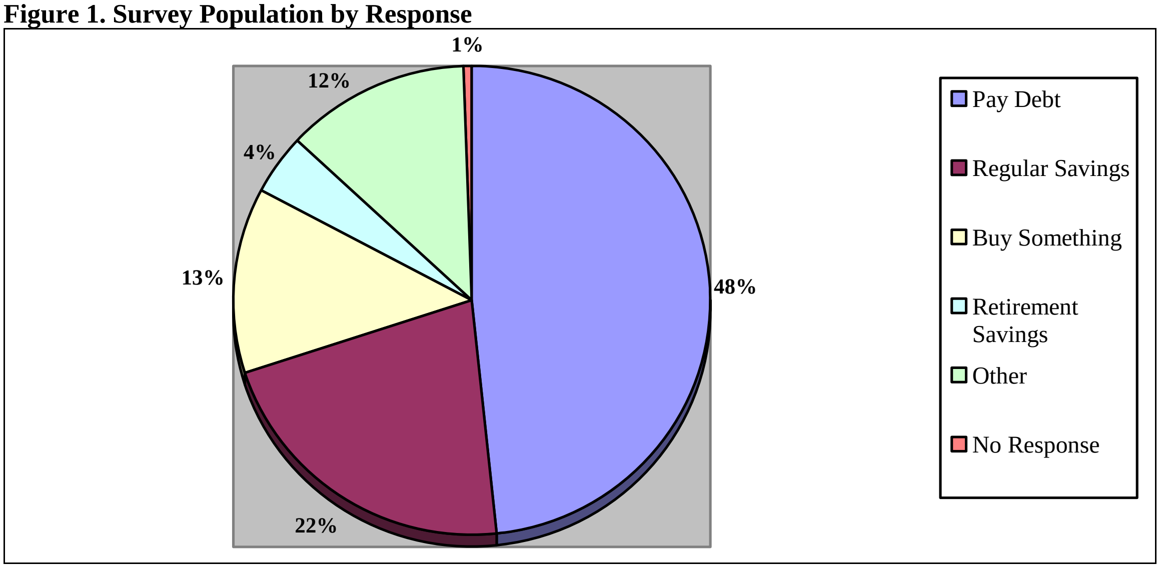
This paper reviews and analyzes survey and demographic data gathered from 949 participants during the period from January 29, 2008 through February 4, 2008. The question posed was "How will you spend the proposed Tax Rebate?" Survey participants were given one of five options to choose from: Buy Something, Pay Debt, Put it into Retirement Savings, Put it into Regular Savings, or Other. Demographic information was collected from survey participants in the categories of gender, age cohorts and geographic region.

[1] H.R.5140,110th Cong., 2d Sess. (2008)
[2] Pub Law 110-185 (2008)
[3] *See id*. at § 6428.
[4] Portland Press Herald, January 29, 2008 at 1.

This report finds that most survey respondents intend to Pay Debt with their prospective tax rebate checks 48% (459), followed by those intending to place the funds into Regular Savings 22% (205) with the third most common response being Buy Something at 13% (121). The Other category followed at 12% (117) and finally the Retirement Savings category choice was last at 4% (41).[5]

The chart below compares the tax rebates responses for the total population of the IFL survey.

Figure 1. Survey Population by Response



The following is the full paper for consideration with a demographic analysis looking at the respondents by gender, age and geographic location.

[5] Six respondents did not indicate their preference which was less than a 1% response rate.

Researching Organization

Institute for Financial Literacy

The mission of the Institute for Financial Literacy is to make effective financial literacy education available for all American adults. The Institute accomplishes its mission by working with organizations to incorporate financial education into their existing services. The Institute also provides direct delivery of financial counseling and education to the general public. As the national authority on adult financial education, the Institute advances professionalism and effectiveness in the field of financial literacy by setting the National Standards for Adult Financial Literacy Education™, hosting the Annual Conference on Financial Education™, maintaining the Library of Personal Finance™, administering the Center for Financial Certifications™ and conducting research through the Center for Consumer Financial Research™.

Center for Consumer Financial Research

Established as a division of the Institute for Financial Literacy in 2007, the mission of the Center for Consumer Financial Research is to expand and disseminate the body of independent, unbiased research within the field of financial literacy. The Center accomplishes this mission by objectively assessing the effectiveness of financial education efforts, researching consumer financial behavior and publishing its findings.

Background

The Institute, which was founded in 2002, expanded its mission with the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). BAPCPA incorporated a requirement that individuals must complete mandatory credit counseling in order to be eligible to file a consumer bankruptcy case under the bankruptcy code[6]. That section reads as follows: "an individual may not be a debtor under this title unless such individual has, during the 180-day period preceding the date of filing of the petition by such individual, received from an approved nonprofit budget

[6] Title 11 USC

and credit counseling agency described in section 111(a) an individual or group briefing (including a briefing conducted by telephone or on the Internet) that outlined the opportunities for available credit counseling and assisted such individual in performing a related budget analysis."[7]

In addition, the law requires certain debtors in the bankruptcy system to complete a mandatory financial management instructional course in order to receive a discharge of their debts.[8] A married couple filing a joint bankruptcy petition must each complete both the counseling and the education as a result of the law's application of these requirements to "individuals".[9]

The Institute was approved under section 111(a) to provide both the mandatory credit counseling and mandatory financial management instructional course in all 88 judicial districts covered by the United States Trustees Program and the six Bankruptcy Administrator[10] districts in the fall of 2005[11]. The Institute provides services in all districts by telephone and Internet as allowed in section 109(h)(1), as well as in person in its home district of Maine. It should be noted that the 94 judicial districts cover all 50 states as well as the US territories.

Consumers learn about the availability of approved providers from one of several sources. The bankruptcy clerks maintain lists of approved providers for their districts and distribute these lists to the general public upon request.[12] The Bankruptcy Administrators and the United States Trustees Program also maintain updated lists of approved providers

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[7] 11 USC sec. 109(h)(1)
[8] 11 USC sec 727(a)(11) and 1328 (g)(1)
[9] 11 USC 302
[10] The states of North Carolina and Alabama and their six respective judicial districts are not under the authority of the United States Trustees Program, but rather individual Bankruptcy Administrators (BA). Each BA has set its own approval process in place for the approving of a nonprofit budget and credit counseling agency as is required under section 111(a).
[11] The Institute for Financial Literacy has subsequently been re-approved as a provider for a one year period of time, as the initial approvals were for a six-month probationary period only.
[12] 11 USC sec. 111(a)

on their respective websites.[13] Consumers may also learn about the requirements and approved providers in their district during their initial consultation with an attorney.

Methodology

During these past weeks there has been great debate about both the economy and the impact the Recovery Rebates and Economic Stimulus for the American People Act of 2008 (or similar bills which may be introduced) will have. Yet with all the rhetoric there often is little comprehensive research regarding the demographics of individual consumers from a personal financial literacy perspective. The Institute recognized the importance of establishing a comprehensive, neutral research program to better understand these individuals and strives to accomplish this through its research papers published through its Center for Consumer Financial Research.

Development of Sample

Two distinct groups were surveyed. The first group consisted of clients currently receiving services from the Institute. The second group surveyed was Institute alumni (former clients).

Current Clients

Many of our current clients are contemplating bankruptcy and therefore seeking the credit counseling which is required prior to filing bankruptcy[14] or are already debtors in bankruptcy completing the mandatory financial management instructional course.[15]

[13] The United States Trustees Program website is located at www.usdoj.gov/ust. The six Bankruptcy Administrators maintain their own individual websites, but they can be accessed by a link maintained by the United States Courts at www.uscourts.gov .
[14] 111 U.S.C. 109(h)
[15] See note 6.

Institute Alumni

The Institute for Financial Literacy regularly communicates with former clients, referred to as alumni, through ongoing educational newsletters. Since many of these individuals are moving towards financial recovery and working towards their financial goals, it seemed an appropriate population to survey on this question. Additionally, the Institute works with non-bankruptcy clients, those adults who are simply seeking to better understand personal finance and utilize the Institute's other financial literacy educational offerings.

Data Collection Instrument

Current Clients

Clients must call to speak with a trained counselor to receive a certificate, which is then filed with the court for both the mandatory pre-filing credit counseling and the pre-discharge financial management instructional course. The opportunity to ask current clients to participate in this survey presented itself during these calls. All clients were given the option to not participate in the survey, or to not answer all questions in the survey. Counselors also explained that the information gathered would have no impact on the outcome of the counseling or education session. Once a client agreed to participate, the counselor collected the client's gender, age information, state of residence, and then asked the following question: "How will you spend the proposed Tax Rebate?" The counselor then read from a list of five choices: Buy Something, Pay Debt, Put it into Retirement Savings, Put it into Regular Savings, or Other. Clients' were asked to choose one option, and their answer was recorded. It was noted by Institute counseling staff that there was a high participation rate, though this was not statistically monitored due to the time constraints of this survey. Equally it should be noted that there was a relatively high degree of consumer awareness of the tax rebate issue and little background explanation had to be offered regarding the survey question.

The total population of Current Clients surveyed was 520 out of the total 949 participants, representing 55%.

Institute Alumni

The alumni were surveyed utilizing a third party online survey tool. The email accompanying the survey explained that the Institute for Financial Literacy was conducting research on the proposed tax rebate proposal and that their participation was voluntary and responses would be kept confidential. To comply with "anti-spam" laws a disclosure at the bottom of the email included an option for alumni to opt out of receiving future email surveys from the Institute.

Approximately 5,000 emails were sent out with a response rate of approximately 8.6%. This is considered a high participation rate for an internet survey.

The survey tool recorded the alumni responses and produced a final report for the Institute to analyze.

The total population of alumni surveyed was 429 out of the total 949 participants, representing 45%.

<u>Core Sample</u>

During this period of time a total of 949 surveys were gathered. The survey was conducted from January 29, 2008 until February 4, 2008.

<u>Protection of Confidentiality</u>

The Institute maintains a client confidentiality policy. Counselors are trained that all information, whether gathered for research or for the credit counseling or financial management instructional courses, is to be held in the strictest confidence. Counselors are provided a written confidentially statement to sign during their training.

The Institute only reports demographic information in the aggregate. Clients' names or other personal identifiers have been removed to protect clients' privacy.

Findings

<u>Survey Response-Overall</u>

This report finds that most survey respondents intend to Pay Debt with their prospective tax rebate checks 48% (459), followed by those intending to place the funds into Regular Savings 22% (205) with the third most common response being the Buy Something category at 13% (121). The Other category followed at 12% (117) and finally the Retirement Savings option at 4% (41)[16].

The following looks specifically at the respondents by gender, age and geographic location.

<u>Gender</u>

A total of 947 participants answered the gender question, a 99.8% response rate. Of these, 54% (506) indicated that they were female, while 46% (441) were male [17].

Females

When queried how they would spend their tax rebate, the majority of females, 48% (244), answered Pay Debt, while 23% (116) would put it into Regular Savings. The third most common response amongst females was Other at 13% (66) with 10% (52) indicating that they would Buy Something. Finally 5% (24) indicated that they would put their rebate checks into Retirement Savings with 1% (4) not responding to the question at all.

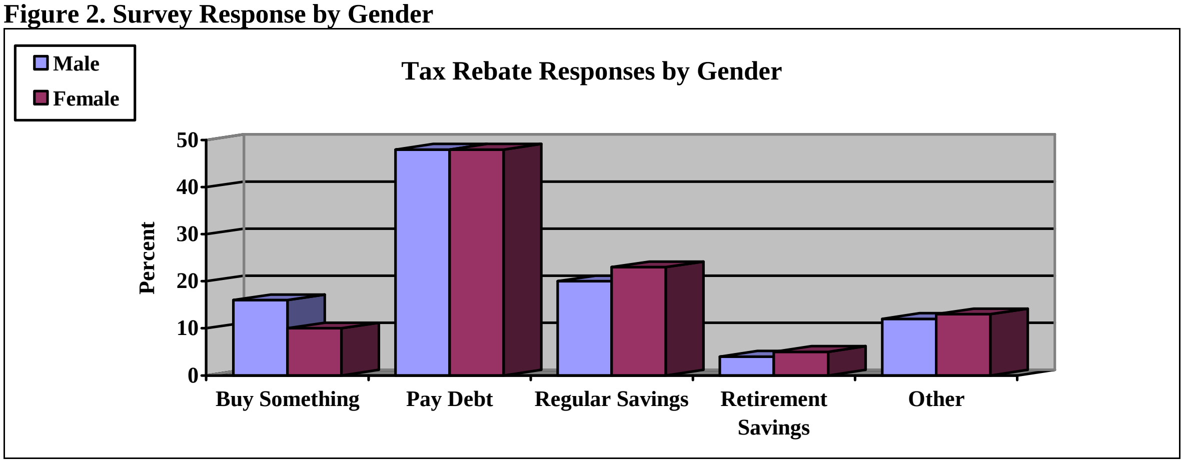
[16] Six respondents did not indicate their preference which was less than a 1% response rate.
[17] Two respondents did not indicate their gender which was less than a 1% response rate.

Males

When queried how they would spend their tax rebate, the majority of males, 48% (214), answered Pay Debt, while 20% (88) would put it into Regular Savings. The third most common response amongst males was Buy Something at 16% (69) with 12% (51) responding Other. Finally 4% (17) indicated that they would put their rebate checks into Retirement Savings with 1% (2) not responding to the question at all.

The chart below compares the tax rebates responses between males and females as a percentage.

Figure 2. Survey Response by Gender



Age

A total of 936 participants answered the age question, a 99% response rate. The age categories were broken down into the following categories; 20-29, 30-39, 40-49, 50-59, 60+.

Twenty Somethings

When queried, the 20-29 age cohort indicated they would primarily spend their tax rebate to Pay Debt 50% (43), while 27% (23) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 12% (10). Finally 4% (3)

indicated that they would put their rebate checks into Retirement Savings and 6% (5) indicated Other[18].

Thirty Somethings

When queried, the 30-39 age cohort indicated they would primarily spend their tax rebate to Pay Debt 50% (131), while 22% (58) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 15% (40). Finally 3% (7) indicated that they would put their rebate checks into Retirement Savings and 10% (27) indicated Other.

Forty Somethings

When queried, the 40-49 age cohort indicated they would primarily spend their tax rebate to Pay Debt 51% (136), while 21% (58) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 11% (30). Finally 4% (12) indicated that they would put their rebate checks into Retirement Savings and 13% (36) indicated Other[19].

Fifty Somethings

When queried, the 50-59 age cohort indicated they would primarily spend their tax rebate to Pay Debt 49% (94), while 19% (36) would put it into Regular Savings. The third most common response amongst this cohort was Other at 17% (33). Finally 9% (18) indicated that they would Buy Something and 6% (11) would put their rebate checks into Retirement Savings.

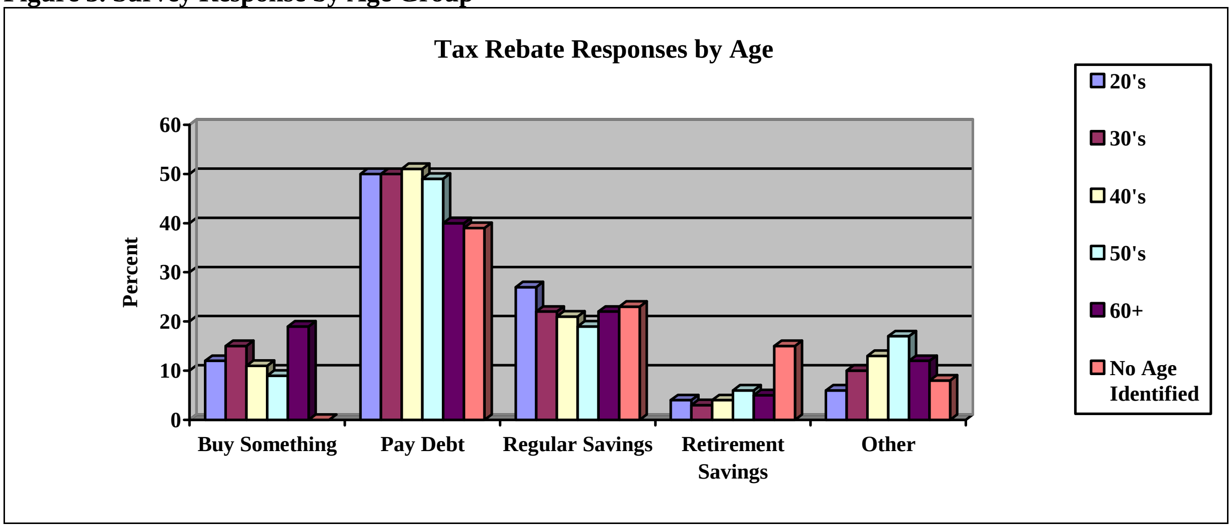
[18] One respondent did not indicate their preference which was less than a 1% response rate.
[19] One respondent did not indicate their preference which was less than a 1% response rate.

Sixty Plus

When queried, the 60+ age cohort indicated they would primarily spend their tax rebate to Pay Debt 40% (50), while 22% (27) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 19% (23). Finally 5% (6) indicated that they would put their rebate checks into Retirement Savings and 12% (15) indicated Other[20].

The chart below compares the tax rebates responses by age cohort as a percentage.

Figure 3. Survey Response by Age Group

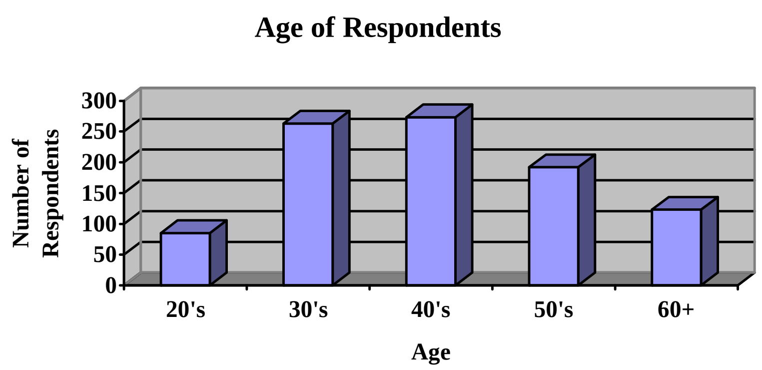


It's worth noting that a bell curve effect presents with the responses from the total population regarding their age. The Institute has seen this effect previously in its bankruptcy demographics research[21].

The chart below looks at the age cohorts of respondents and demonstrates this bell curve effect.

[20] Two respondents did not indicate their preference which was less than a 2% response rate.
[21] Linfield, Leslie E., *"Who Went Bankrupt in 2006? A Demographic Analysis of American Debtors" (May 2007).* Available at SSRN: http://ssrn.com/abstract=1084873

Figure 4. Survey Population by Age Group



What is of interest is that the US population does not demonstrate the same bell curve effect. Generally speaking the U.S. population is evenly distributed between 13-15% depending on the age cohort of the total population.[22]

Regions

Survey respondents were given the option of indicating which state they reside in. From this data the Institute was able to assign each participant to a geographic region. The regions used are by common and cultural usage and not assigned governmental units.[23] The six geographic regions are New England, Mid-Atlantic, the South, Midwest, the Southwest, and the West.

A total of 888 participants answered the state question, a 94% response rate.

New England

A total of 224 survey respondents indicated they resided in the New England region. When queried, New England residents indicated they would primarily spend their tax rebate to Pay Debt 51% (112), while 21% (47) would put it into Regular Savings. The third most common response amongst this cohort was Other at 15% (34). Finally 9% (20)

[22] Source: U.S. Census Bureau, 2006 American Community Survey 2006
[23] U.S. Department of State website http://usinfo.state.gov/infousa/life/geotravel/usa.usembassy.de/travel-regions.html

indicated that they would Buy Something and 4% (10) would put their rebate checks into Retirement Savings.[24]

Mid-Atlantic

A total of 136 survey respondents indicated they resided in the Mid-Atlantic region. When queried, Mid-Atlantic residents indicated they would primarily spend their tax rebate to Pay Debt 43% (59), while 26% (35) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 16% (22). Finally 5% (7) indicated that they would put their rebate checks into Retirement Savings and 9% (12) indicated Other[25].

The South

A total of 142 survey respondents indicated they resided in the Southern region. When queried, Southern residents indicated they would primarily spend their tax rebate to Pay Debt 45% (65), while 23% (32) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 14% (20). Finally 6% (8) indicated that they would put their rebate checks into Retirement Savings and 12% (17) indicated Other.

Midwest

A total of 174 survey respondents indicated they resided in the Mid-West region. When queried, Midwestern residents indicated they would primarily spend their tax rebate to Pay Debt 51% (88), while 22% (39) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 12% (21). Finally 3% (5) indicated that they would put their rebate checks into Retirement Savings and 11% (19) indicated Other[26].

[24] One respondent answered the state question but did not indicate their preference which was less than a 1% response rate.
[25] *Id.*
[26] Two respondents answered the state question but did not indicate their preference which was less than a 1% response rate.

The Southwest

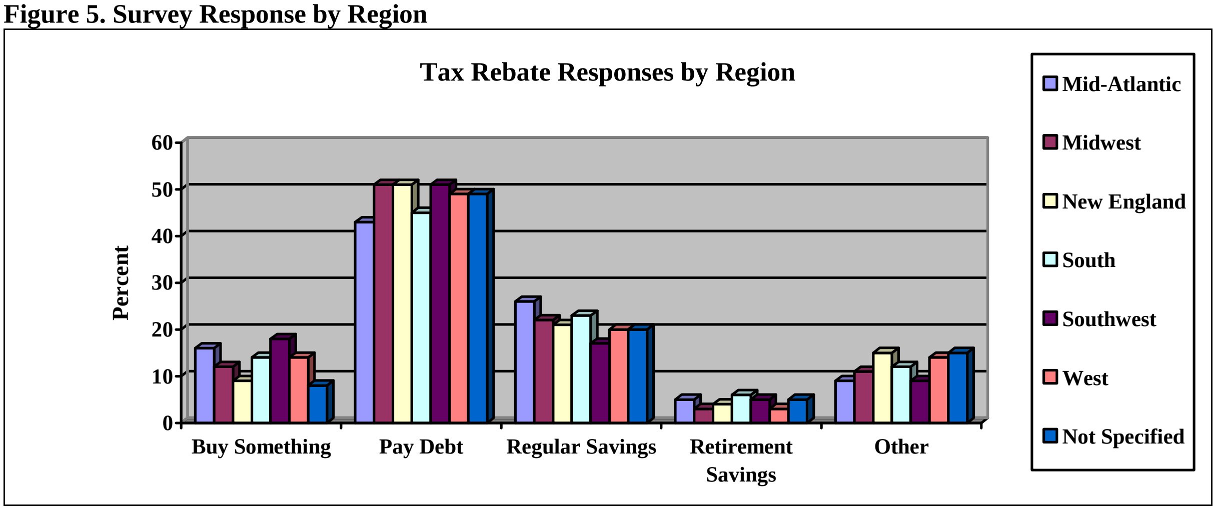
A total of 87 survey respondents indicated they resided in the Southwest region. When queried, Southwestern residents indicated they would primarily spend their tax rebate to Pay Debt 51% (44), while 17% (15) would put it into Regular Savings. The third most common response amongst this cohort was Buy Something at 18% (16). Finally 5% (4) indicated that they would put their rebate checks into Retirement Savings and 9% (8) indicated Other.

The West

A total of 125 survey respondents indicated they resided in the Western region. When queried, Western residents indicated they would primarily spend their tax rebate to Pay Debt 49% (61), while 20% (25) would put it into Regular Savings. The third most common response amongst this cohort was Other at 14% (18). Finally 3% (4) indicated that they would put their rebate checks into Retirement Savings and 14% (17) indicated Buy Something.

The chart below compares the tax rebates responses by region as a percentage.

Figure 5. Survey Response by Region



Discussion

When the largest daily newspaper in Maine ran the headline "$600 rebate: save it, splurge, invest or go surfing?"[27], the Institute for Financial Literacy could not anticipate how Americans would answer.

Paying Debt

That a majority of current clients stated they would apply their tax rebates towards paying debt is not surprising. Many of these individuals are in the throes of financial difficulty and would no doubt prefer to meet their contractual obligations then seek redress in the bankruptcy court. What we at the Institute found surprising however was the similarity of response from the alumni cohort. The responses were so similar, in fact, that it made little difference to break out the data between the two populations when analyzing the responses by specifics of gender, age and geographic region. Yet we must ask why. Why would the alumni population, the majority of whom have already received their redress by the bankruptcy courts, indicate that their first choice would be to apply their tax rebate to pay debt?

This result of a preference to pay debt was also reflected in one informal internet poll and accompanying article[28] as well as an unpublished survey.[29]

The Institute for Financial Literacy is recommending that further study be conducted to determine why Americans are expressing such a significant preference for debt reduction at this time. Though the mission of the Institute for Financial Literacy is one of financial education, it also understands that there are economic factors both micro and macro that impact the national economy. This question is well beyond the scope of this organization's capacity to research. It is our hope that this paper will help seed that discussion.

[27] See note 3.
[28] Randy Duermyer, Poll: What Would You Do with a Tax Rebate?, About.com, January 23, 2006
[29] Survey results were published in a press release by International Council of Shopping Centers on behalf UBS Securities February 6, 2008.

Regular Savings

As an organizations whose mission is to make effective financial literacy education available for all American adults, we take interest in the survey respondents' second preferred option for their tax rebates: Regular Savings. A component of both the financial counseling and financial education is a discussion regarding the importance of savings. Both savings for emergency expenditures and financial goal setting are topics discussed with Institute clients (as with many clients seeking services from other providers approved under BAPCPA). Conventional wisdom and prudent fiscal money management suggests that adults should set aside 10% of their gross earnings into savings. The national savings rate is published quarterly. In the past twenty years this number has eroded from a positive number of approximately 7.5% to a negative number which has been the case since the second quarter of 2005.[30] What we find interesting is that despite this national trend, 22% of the survey respondents would place these funds into regular savings.

At the Institute for Financial Literacy we posit that this may be an early indication of the educational effectiveness of both the pre-filing bankruptcy credit counseling and the pre-discharge financial management instructional course (also known as debtor education). In its report published in April 2007 on the pre-filing credit counseling, the United States Government Accountability Office (GAO) recommended that the United States Trustee Program develop the capability to track and analyze the outcomes of the pre-filing credit counseling requirement[31]. Additionally, the National Endowment for Financial Education (NEFE) introduced a financial education evaluation toolkit in June 2007. These guidelines assist financial organizations in measuring the effectiveness of their financial literacy efforts. The Institute believes that this large percentage of survey respondents (in light of the fact that national savings rates that are so low) who indicate that they intend to put their rebate into savings may be an early indicator of the educational effectiveness of both the pre-filing bankruptcy credit counseling and the pre-

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[30] Source: Department of Commerce, Bureau of Economic Analysis as reported by the Federal Reserve
[31] *BANKRUPTCY REFORM Value of Credit Counseling Requirement Is Not Clear*, April 2007 GAO-07-203

discharge financial management instructional course as all of the respondents had received counseling and/or education.

The Institute would strongly recommend the continued study of the effectiveness of both pre-filing bankruptcy credit counseling and the pre-discharge debtor education courses. The Institute would also recommend that these analyses be performed internally by both those who provide the services using tools developed by the financial literacy education community and externally by the regulatory and academic communities.

Retirement Savings

It should be noted that Institute for Financial Literacy staff members were greatly surprised by our findings regarding the next discussion point, Retirement Savings. When survey participants were given the five choices on how to use the proposed tax rebate checks, Retirement Savings was their last choice regardless of their gender, age, or geographic location. Surprisingly, those in the 20 year old cohort came in statistically at the same rate as those in the 40 year old cohort (4%).

Age Bell Curve

Survey respondents also demonstrated a noticeable bell curve around age with the top of the bell curve being the 40 year old cohort, a phenomenon that has presented in other research the Institute has published on bankruptcy demographics. The cautionary tale here is that this is an aging population who, when presented with a potential windfall, are not thinking about their future retirement needs. What does this mean? The Institute would recommend that the financial literacy education community take notice and redouble its education effort around retirement planning[32]. The Institute would further recommend that the academic and economics communities conduct further research to better understand why this result presented. Policy makers should be aware of this issue and understand the potential impact it will have as this population reaches eligibility for Social Security benefits. If they have not properly planned for their retirement years they

[32]See National Standards for Adult Financial Literacy Education, www.financiallit.org

may find themselves relying on a system that was not designed to be their sole source of retirement income.

Conclusion

In January, when Congress introduced the "Recovery Rebates and Economic Stimulus for the American People Act of 2008," there were questions as to exactly how Americans would spend their proposed rebate checks. We will not know for sure until those checks begin to be mailed out in approximately May 2008 and Americans actually begin to cash and spend them. However, as the above paper has shown, we now know how 949 Americans intend to spent theirs. The Institute for Financial Literacy submits this paper respectfully in the hope that additional discussion and research will come forth in the areas of financial literacy education and economics.