FIRST FOCUS
MAKING CHILDREN & FAMILIES THE PRIORITY

ENSURE EVERY CHILD HAS A LIFELONG SAVINGS ACCOUNT

by

Reid Cramer and **Elliot Schreur**,
New America

Building savings over the life course can be a key contributor to financial security and upward economic mobility. One of the most effective ways to trigger these outcomes is to start the process of saving as early as possible. Every child should be provided a savings account to serve as a vehicle to plan for their future.

Connecting children to savings accounts early on exposes them to the experience of saving, facilitates the delivery of basic financial education during the school years, and jumpstarts saving habits.[1] Successful demonstration projects show that children's savings accounts increase a sense of financial inclusion; promote financial literacy and fiscal prudence; protect against economic shocks; improve access to education; improve health and education outcomes; and help develop a future orientation.[2]

In the early 1990s, Michael Sherraden articulated the idea of giving all individuals tax-advantaged savings accounts at birth. Sherraden posited that programs like Aid to Families with Dependent Children (AFDC) and, later, Temporary Assistance for Needy Families (TANF), which provide income supports while actively discouraging saving, were not enough to help families climb out of poverty. What were needed to bring about a meaningful improvement in the long-term economic conditions of low-income families were asset-building policies like children's savings accounts (CSAs).[3] His assets-based perspective on the needs of American families in poverty helped drive the development of privately-funded national demonstration projects and a series of legislative proposals, including proposals for universal CSAs like the America Saving for Personal Investment, Retirement, and Education Act (the ASPIRE Act). These efforts have generated a series of insights that continue to inform policy development.

A successfully implemented national CSA policy would promote overall economic growth while providing a means for individual households to build assets, engage in meaningful financial education, and plan for a financially-secure future. This paper will introduce the central arguments for CSAs, provide examples of existing CSA efforts that can serve as models for broader CSA policies, and describe a proposal for a national system of CSAs.

The Case for Children's Savings Accounts

Research shows that the presence of savings plays a key role in facilitating financial security and economic mobility.[4] The positive effects of having savings are enhanced when families start saving early on for their children. Having access to savings generally – and particularly when the assets are in the child's own name – is associated with a range of positive outcomes throughout the lives of children, including better academic performance, higher rates of college matriculation, and higher rates of college completion.[5] Beyond these effects, evidence also suggests that there is a significant aspirational effect of having savings early in life. When children know that funds are available for college, they are more likely to embrace what William Elliott and others have called a "college-bound identity."[6] Having savings changes the way children think about themselves and their future and leads them to perceive that higher achievement is within their grasp.

Looking across generations, we see that having savings is an important factor in achieving economic mobility. Research from the Pew Charitable Trusts has shown that children of low-income – but high-saving – parents are more likely to experience upward mobility than children of low-income, low-saving parents. According to Pew's research of children raised in the bottom 25 percent of the income distribution, 71 percent of those with high-saving parents moved up from the bottom quartile over the course of a generation compared to only about 50 percent of children raised by low-saving parents.[7] These results show that saving for children today can do more than bestow positive benefits on a single lifetime; it can project the benefits of saving in the form of greater economic mobility into generations to come.

Not only do children's savings promote economic mobility, they build a bridge to retirement security. While Old-Age, Survivors, and Disability Insurance (Social Security) does play an important role in ensuring the retirement security of many Americans, outside of a massive expansion of this program, building individual assets for retirement will continue to be an essential part of families' lifelong financial planning. And starting to save early in life – even as early as childhood – is one of the best ways to achieve long-term financial goals.

Many families realize the wisdom of this advice: they want to save. But millions of families are placed at a disadvantage in their efforts to build savings by ineffective federal savings policy. Current policy rewards savers through preferential tax treatment, but this public support of private saving almost exclusively benefits households at the very top of the income distribution.[8] Households at all income levels can and will save if they have access to appropriate, safe, and easy-to-use products with the right incentives and support systems in place.[9]

A national, universal platform for children's savings could provide an infrastructure to help all families build the assets they need to increase their children's chances to financially succeed.

As a Pathway to Lifelong Saving and Asset Building

One of the primary justifications for creating a system of children's savings accounts is that it creates a pathway to the large-scale accumulation of assets. Savings built up over time can be deployed in a variety of productive ways that make a significant difference in people's lives. These include being able to pursue post-secondary education and training, saving up for a downpayment on a home, and saving for retirement security. These investments can provide returns that lead to greater economic stability, mobility, and prosperity for families.

Today, the federal government promotes asset building and long-term savings exclusively through the income tax code. These tax incentives do not reach the millions of lower-income families that have little or no income tax liability. A universal CSA system that includes everyone would be a major step towards remedying this policy failure. Low-income families already face significant barriers to saving, such as high housing costs, counterproductive public assistance eligibility rules that put a cap on assets, and simply having low incomes. Current federal savings policy must be changed so as to not exclude these families.

As a Meaningful Opportunity for Financial Education

The incidence of account ownership and access provides an excellent opportunity for families to be exposed to the lessons of financial education. The opportunity to actively contribute to one's own account is a powerful tool for developing the habit of saving, a behavior linked to healthy personal financial management. Financial education is widely recognized as a necessary component of economic security. Regardless of income, families that have a poor understanding of personal finance have a harder time managing and holding on to their resources. A 2008 study on asset building among low-income families found that the benefits of asset ownership "might be raised significantly with the addition of expanded financial education, especially for low- and middle-income families."[11]

As a Promoter of Financial Inclusion

The lack of access to mainstream financial services is a primary source of economic insecurity for millions of American families. Costly alternatives, such as payday loans, refund anticipation loans, and pawn shops, often serve to strip away assets and savings rather than help families build them up. Broad access to children's savings accounts will not alone solve the unbanked and underbanked problem, but making universal CSAs a reality would offer an avenue for greater financial inclusion. First, these accounts could offer access to a long-term savings platform. Second, these accounts would represent an affordable and safe point of entry into the world of personal finance. Third, the accounts would have the potential to be linked to mainstream financial services. Creating access to low-cost and high-quality financial services is essential for reducing reliance on the higher-cost products that are currently used by many low- and moderate-income families.

Models for Policy

In recent years, there has been a proliferation of efforts at the state and local levels to expand opportunities for children to save. Philanthropic institutions have financed the development of pilot projects to model and study the impacts of these accounts. States and municipalities have observed the positive effects of these projects on children and families and have followed through with their own efforts. Taken together, these pilot programs, demonstration projects, and policies at the local and state levels have explored a range of approaches that have implications for a federal policy effort in the United States.

Saving for Education, Entrepreneurship and Downpayment (SEED)

The SEED initiative was a Children's Savings Account pilot project implemented in 12 states with almost 1,200 participants. SEED research results offer insights to inform the design of an inclusive system of CSAs. SEED research suggests that children in low-income families can and will save; that universal, automatic access to accounts is critical to success; and that CSAs promote positive behavioral and attitudinal changes in children.[12]

SEED for Oklahoma Kids

SEED OK is an outgrowth of SEED, designed to experimentally test the effect of CSAs. In 2007, SEED OK became the first randomized controlled trial of a universal and progressive CSA program in the country. Over 2,600 newborns were randomly assigned to either a treatment or control group. The treatment group was automatically enrolled in Oklahoma's 529 College Savings Plan and was provided with a $1,000 initial deposit. The SEED OK experiment demonstrated that automatic account opening is a highly successful strategy for inclusion of a full population, with 99.9 percent of treatment participants accepting Child Development Accounts (CDAs), a type of children's savings account, and holding them several years later. Follow-up research has found that SEED OK increased young children's social-emotional development as early as age four among families that have low education, low income, receive welfare benefits, and rent their homes.[13]

Kindergarten to College (K2C) San Francisco

In 2011, San Francisco launched the Kindergarten-to-College (K2C) program, which opened accounts for every kindergartner in the city's public schools. K2C accounts are opened with a $50 seed deposit. Parents and students can contribute up to $2,500 each year and earn matching funds on the first $100 of contributions each year in the ongoing program. An additional $100 is available for parents who sign up for automatic contributions. Children eligible for free or reduced price lunch can receive an additional $50 bonus. The funds are specifically reserved for expenses related to post-secondary education and are held in a special account administered in partnership with Citi Bank.[14]

Cuyahoga (OH) College Savings Program

In the fall of 2013, Cuyahoga County, Ohio launched its own College Savings Account Program, which provided savings accounts seeded with $100 each for 15,000 incoming kindergarten students. The program's organizers have stated that saving incentives will be made available, but no details have yet been offered about this aspect of the program. The funds are restricted for post-secondary educational expenses, though emergency withdrawals are allowed. Cuyahoga County holds the funds in a special account until disbursement.

The Alfond Challenge (Maine) and Nevada College Kick Start

In 2008, the Alfond Challenge, funded by the Harold Alfond Foundation, began offering $500 in a 529 college savings account to any parent of an infant in Maine who enrolls before the child's first birthday. The funds are reserved for post-secondary educational expenses, in accordance with the standard rules governing 529 programs. Any unused Alfond funds and earnings revert to the fund upon the child's 28th birthday. Between 2008 and 2013, this program used an opt-in model, but recently the Alfond Foundation announced that it would transition to an automatic-enrollment structure, offering an account to every child in the state.[15]

This past year, Nevada College Kick Start began a similar program offered to over 30,000 kindergartners in the state. The program automatically provides a 529 college savings account with the option for parents to opt out. Each 529 account is seeded with $50 and offers a potential lifetime total of $1,500 in matching funds.

Towards a National Children's Savings Account Policy

All Americans should have the opportunity to build assets. But in order to make saving feasible for many low- and middle-income families, the saving process must be supported by the right set of incentives and institutional structures. The ASPIRE Act (America Saving for Personal Investment, Retirement, and Education), introduced with bipartisan support in four consecutive Congresses between 2004 and 2010, represents a promising proposal to bring this aspiration to reality.[16]

As generally envisioned throughout its several iterations, the ASPIRE Act would offer a seeded account to every child born in America. The original seed amount would be based on a progressive sliding scale that increases in inverse proportion to family income, meaning that lower-income families start with a larger seed amount. Additionally, the accounts would include a progressive incentive structure for subsequent contributions in order to encourage families to make routine contributions to the account throughout the child's life. Contributions would be after tax and would be limited each year to a reasonable amount such as $2,000. Earnings would grow tax-free. Funds would be automatically held in default investment plans like the federal government's Thrift Savings Plan (TSP), but account custodians would have the option to transfer the funds to other investment options. Eventually, upon maturation, the funds could be used for restricted purposes such as paying for post-secondary education, buying a home, and serving as a source of income in retirement.

Default accounts would be administered by an entity similar to the Federal Retirement Thrift Investment Board that oversees the Thrift Savings Plan (TSP). The TSP has low administrative fees and a limited but diverse set of investment options. Under the ASPIRE Act, participants would be free to roll their accounts out of the default TSP-like investment and into one managed by a private financial institution. Accounts would also be supported with financial education services that would be available to both accountholders and their families.[17]

This system of CSAs proposed in the ASPIRE Act would provide a meaningful saving opportunity to the millions of American families that cannot take advantage of the federal government's regressive, opt-in savings-policy regime based solely on income-tax incentives. The current upside-down tax incentives for saving provide the greatest incentive to the highest earners, but no incentive for the roughly half of American households at the bottom of the income ladder who have no income tax liability to offset.[18] Moreover, the nearly exclusive focus of federal policy on building assets for use during retirement, and its neglect of saving for all other purposes, distorts rational saving behavior. Creating opportunities to save for other purposes over the life course, such as education, homeownership, entrepreneurship, or financial emergencies, is a necessary step for families to build a solid bridge to retirement.[19]

Families currently have very few options to save on behalf of their children in an incentivized vehicle. One example that does exist is the 529 College Savings Plan, but these plans are almost exclusively utilized by high-income families. Indeed, less than 3 percent of U.S. families make use of these plans.[20] CSAs, as envisioned in the ASPIRE Act, represent an opportunity to buck the trend of the nearly uninterrupted pattern of inequitable government policies that concentrate the benefits of saving in the wealthiest families. A universal, progressive system of CSAs would broaden opportunities to save by specifically targeting disadvantaged families who need more help in building assets, thereby turning at least some upside-down saving incentives right-side up. Yet although this system of CSAs would provide a much-needed counterweight to existing federal policies by establishing meaningful saving incentives specifically targeted at low-income families, it would not categorically exclude any child because of her family's income. The universal approach of the ASPIRE Act would automatically offer the same opportunities to all families, regardless of income or existing saving habits, in order to bring about a cultural shift towards savings, ownership, and prudent financial decision-making.

A new savings infrastructure, like the one the ASPIRE Act would create, should automatically provide a vehicle for saving with targeted and accessible incentives to every child in America.

Creating an opportunity for every child to save and build assets over her lifetime is a concept whose time has come. It is a concept that draws upon the enduring American values of individual responsibility and equal opportunity. Previous proposals have attracted the attention of policymakers from across the political spectrum, and with renewed leadership, it is a concept that could be a foundational element of a bipartisan economic mobility agenda.

Reviving an economy capable of producing long-term sustainable growth will require both increased saving and investment. But this change in Americans' approach to finances will not happen by itself. We need a CSA policy that will provide the right set of incentives, institutions, and vehicles to support saving. Recently implemented CSA programs at the state and local levels have demonstrated how a system of children's savings accounts could be the centerpiece of such an effort. Not only would CSAs empower people to start saving early, CSAs would also encourage positive behavioral changes, increase financial knowledge, and facilitate greater financial inclusion. These changes would provide the foundation for a more financially secure and economically mobile America and create a more vibrant economy whose benefits accrue to all Americans.

Reid Cramer is director and Elliot Schreur is a policy analyst in the Asset Building Program at New America, a non-partisan policy institute based in Washington, DC.

Notes

1. Reid Cramer and David Newville, 2009, "Children's Savings Accounts: The Case for Creating a Lifelong Savings Platform at Birth as a Foundation for a 'Save-and-Invest' Economy," Washington, D.C.: New America Foundation.
2. Edward Scanlon and Deborah Adams, 2005, "In-Depth Interviews with SEED Youth: Profiles of Participants in a Pilot Study," Working Paper 05-25, St. Louis, MO: Center for Social Development, Washington University in St. Louis.
3. Michael Sherraden, 1991, *Assets and the Poor*, New York: M.E. Sharp.
4. Pew Charitable Trusts, 2013, "Moving On Up: Why Do Some Americans Leave the Bottom of the Economic Ladder, but Not Others?" Washington, D.C.: Pew Charitable Trusts.
5. Assets and Education Initiative, 2013, "Building Expectations, Delivering Results: Asset-Based Financial Aid and the Future of Higher Education," in William Elliott, ed., Biannual report on the assets and education field, Lawrence, KS: Assets and Education Initiative (AEDI).
6. William Elliott, 2012, "We Save, We Go to College: Creating a Financial Stake in College," Washington, D.C.: New America Foundation.
7. Pew Charitable Trusts, 2013, "Moving On Up: Why Do Some Americans Leave the Bottom of the Economic Ladder, but Not Others?" Washington, D.C.: Pew Charitable Trusts.
8. Reid Cramer and Elliot Schreur, 2013, "Personal Savings and Tax Reform: Principles and Policy Proposals for Reforming the Tax Code," Washington, D.C.: New America Foundation.
9. Amanda Moore, Sondra Beverly, Michael Sherraden, Margaret Sherraden, Lissa Johnson, and Mark Schreiner, 2001, "Saving and Asset-Accumulation Strategies Used by Low-Income Individuals," St. Louis, MO: Center for Social Development, Washington University in St. Louis.
10. Robert I. Lerman and Signe-Mary McKernan, 2008, "Benefits and Consequences of Holding Assets," in Signe-Mary McKernan and Michael Sherraden, eds., Asset Building and Low-Income Families, Washington, D.C.: The Urban Institute Press, 175-206.
11. For more information, see Lisa Reyes Mason, Yunju Nam, Margaret Clancy, Vernon Loke, and Youngmi Kim, 2009, "SEED Account Monitoring Research: Participants, Savings, and Accumulation," St. Louis, MO: Center for Social Development, Washington University in St. Louis.
12. For more information, see Yunju Nam, Youngmi Kim, Margaret Clancy, Robert Zager, and Michael Sherraden, 2011, "Do Child Development Accounts Promote Account Holding, Saving, and Asset Accumulation for Children's Future?: Evidence from a Statewide Randomized Experiment," CSD Working Papers No. 11-33, St. Louis, MO: Center for Social Development, Washington University in St. Louis.

13. For more information, see Leigh Phillips and Anne Stuhldreher, 2011, "Kindergarten to College (K2C): A First-in-the-Nation Initiative to Set All Kindergartners on the Path to College," Washington, D.C.: New America Foundation.
14. For more information, see Margaret Clancy and Michael Sherraden, 2014, "Automatic Deposits for All at Birth: Maine's Harold Alfond College Challenge," CSD Policy Report 14-05, St. Louis, MO: Center for Social Development.
15. The ASPIRE Act was introduced in the 108th Congress by Representatives Ford, English, Kennedy, and Petri as H.R. 4939 and by Senators Santorum and Corzine as S. 2751; it was introduced in the 109th Congress by Representatives Ford, English, Kennedy, Grace Napolitano, Platts, and Bill Shuster as H.R. 1767 and by Senators Santorum, Corzine, Demine, and Schumer as S. 868; it was introduced in the 110th Congress by Representatives Cooper, Emanuel, English, Lofgren, and Petri as H.R. 3740 and by Senator Schumer as S. 3557; and it was introduced in the 111th Congress by Representatives Kennedy, Cooper, Petri, Tsongas, Capuano, and Barbara Lee as H.R. 4682 and by Senators Schumer and Dodd as S. 3577.
16. For more details about the ASPIRE Act, see Reid Cramer, 2009, "The ASPIRE Act of 2009: Questions and Answers," Washington, D.C.: New America Foundation.
17. Reid Cramer and Elliot Schreur, 2013, "Personal Savings and Tax Reform: Principles and Policy Proposals for Reforming the Tax Code," Washington, D.C.: New America Foundation.
18. For a more complete statement of the importance of supporting a savings continuum, whereby families can build long-term assets while meeting short-term savings needs, see Reid Cramer, Justin King, Elliot Schreur, and Aleta Sprague, 2014, "Solving the Retirement Puzzle: The Potential of myRAs to Build a Personal Safety Net," Washington, D.C.: New America Foundation.
19. Government Accountability Office, 2012, "A Small Percentage of Families Save in 529 Plans," Washington, D.C.: Government Accountability Office.