INVESTING IN TOMORROW

helping families build savings and assets

federal policy brief

January 2016

For a low-income family, a day's wages might only fulfill today's basic needs: food, clothing and housing that may be temporary. But some families' daily struggle to support themselves leaves nothing for tomorrow. To help children realize their full potential, families need savings and assets, the currency of the future.

Assets — emergency savings, a college fund, homeownership — provide the financial stability a family needs to create a quilt of resources that turns children's dreams into plans. That quilt also serves as a security blanket of a family's own making. Without it, what should be a temporary difficulty — a flat tire, a sick child, an injury — can become a crisis with permanent consequences, including a lost job or impossibly large debts. Family financial stability can easily be undermined by such events, eroding prospects for self-sufficiency and long-term success.[1]

The Great Recession was devastating for U.S. families, causing a collective $16 trillion loss in net worth.[2] This loss disproportionately affected low-income families of color,[3] perpetuating a racial wealth gap even as the racial income gap has narrowed.[4] The median net worth of white households was more than 10 times greater than that of African-American or Latino families in 2013. While white families' net worth rose by 2 percent from 2010 to 2013, Latino and African-American families' net worth fell markedly — by 15 percent and 34 percent, respectively.[5] The typical white household has slightly more than one month's income in easily accessible savings, compared with just 12 days for the typical Latino household and only five for the typical

The Annie E. Casey Foundation is a private philanthropy that creates a brighter future for the nation's children by developing solutions to strengthen families, build paths to economic opportunity and transform struggling communities into safer and healthier places to live, work and grow.

Tracking and Protecting Family Assets

To properly gauge the effects of policies and practices on families' ability to build assets, we must have the right tools. Data on family assets are meager and difficult to access, particularly for various racial and ethnic groups. The federal government should explore better mechanisms to track that information, such as representative surveys for national and state use with questions on savings behavior and asset holdings or additional questions in the U.S. Census Bureau's American Community Survey.

We also need a good monitoring system to protect families from risky financial products. The Consumer Financial Protection Bureau — the only federal agency overseeing how such products and services affect consumers — is key in helping people navigate their options by issuing and enforcing rules to prevent high-cost, harmful practices.

African-American household.[6] These dramatic differences are especially troubling given the critical importance of assets as an engine of the American Dream — a dream that is, increasingly, unequally achieved.

An uneven financial foundation causes daily family stress that harms children's development and hinders their ability to grow into successful adults.[7] Childhood is a time to imagine and prepare for the future; poverty can eclipse that horizon. While increasing income is important to moving families out of poverty, building assets helps them become financially stable and open doors to opportunity.

Falling Behind: The Racial Wealth Gap

Throughout much of our country's history, the federal government has provided incentives to help families save and build assets. However, these policies — from retirement savings tax breaks to the home mortgage interest deduction — disproportionately benefit families with assets and do little for those with low incomes and minimal savings. This regressive pattern creates particular disadvantages for families of color, who are less likely to have savings or inherited resources.[8] A home, for example, is a primary driver of net worth, making homeownership an important milestone for many American families.[9] Yet systemic prejudice in zoning, building code enforcement, residential restrictions, mortgage practices and home insurance account for stark differences by race in homeownership and, therefore, net worth.[10] Although home values among households of color took a much harder hit during the recent recession, especially in some communities, home equity remains an essential long-term asset that all families should be able to access.

For these reasons, many people of color have a far greater hill to climb to build assets — affecting their prospects for generations. We cannot afford to continue these patterns, especially as people of color make up more of our population.[11] Family assets strongly correlate with indicators of child well-being — such as academic performance and self-esteem — and help children avoid negative consequences such as behavioral problems and teenage pregnancy.[12] Yet 47 percent of Americans cannot handle a $400 emergency[13] — the cost of replacing a car alternator, for example — let alone pay for college or a home. Nearly half of U.S. households could not subsist at the federal poverty level for three months if they suddenly lost their income, using experts' most basic measure of assets.[14] Not having savings exacts additional costs: Payday loans cost cash-strapped families $8.7 billion in interest and fees annually.[15] Without savings, Americans also cannot start new businesses that stimulate our economy. An analysis of federal data recently found the share of people younger than 30 owning private businesses at a 24-year low, in part due to their low savings rate.[16]

Smart policies can help reverse these trends and close the racial wealth gap by allowing more families to steadily build savings. We recommend four federal policy solutions to increase the financial stability of low-income families, especially those of color, through savings and home equity.

Recommendations: Helping All Families Achieve Financial Stability

Promoting savings for a lifetime is the surest way to enable low-income families to build assets. Improving their prospects means undoing generations of unfair practices and making up for decades of foregone returns — and requires a combination of small, achievable steps and bold vision. We therefore recommend several incremental policy changes to help families develop savings habits and access more sophisticated financial products over time. To incentivize savings from birth, we outline a more ambitious proposal to promote opportunity for children and significantly narrow the racial wealth gap.

Provide Portable, Safe Accounts for Retirement and Emergency Savings

Saving for the future is extremely difficult for workers with low wages, who may not have workplace retirement plans.[17] The new My Retirement Account (*my*RA) can help make long-term saving a habit.[18] Employers can voluntarily establish these no-fee starter accounts, which are invested in government savings bonds that eliminate the risk of losing principal. Once the balance reaches $15,000, the funds must roll over to another retirement account.

Because *my*RAs are funded with after-tax dollars, participants can withdraw contributions without penalty for emergencies. While these accounts are now widely available, Congress should make *my*RAs permanently accessible through workplaces and banks and increase awareness about them. Employers without other retirement plans should consider automatically enrolling employees in *my*RAs. While these funds alone are not sufficient for retirement, businesses and government should incentivize rolling them over into vehicles that allow workers to grow a larger nest egg.

An analysis of *my*RA indicates its adoption and expansion could narrow the racial wealth gap. If everyone eligible saved the maximum, *my*RA could reduce the black-white wealth gap by 5 percent and the Latino-white gap by 7 percent, this analysis suggests. Modest participation and savings rates could still increase assets and racial equity.[19]

Raise Asset Limits for Public Benefit Programs

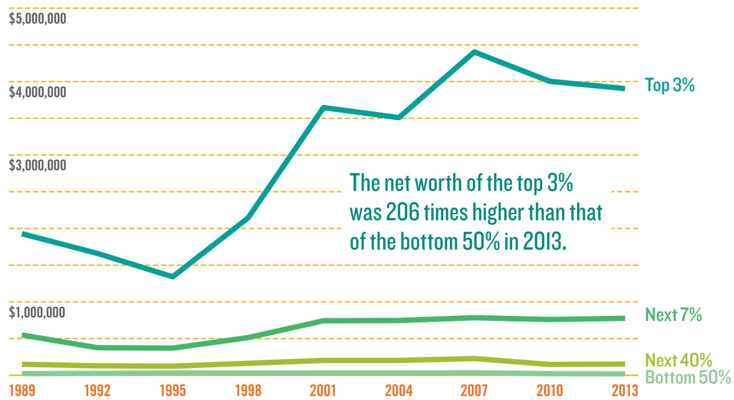
Although government policies seek to strengthen economic security for low-income families, they include asset limits that generally discourage savings among those who most need them — participants in public programs, such as Temporary Assistance for Needy Families (TANF). Depending on the state, $1,000 in savings may disqualify a participant for TANF.[20] Without being able to increase earnings and savings, families will continue their reliance on these programs.

Federal policy should permit program participants to have at least $12,125 in savings — the equivalent of three months' income for a low-income family of four.[21] Allowing this level of savings — recommended in case of sudden income loss[22] — will help families weather financial crises while enabling them to save for education, retirement or a home. This new floor would not restrict states from having higher limits or eliminating them entirely. States that have removed limits for public benefits have not seen participation increase; in Ohio and Virginia, TANF caseloads decreased.[23] Programs also should

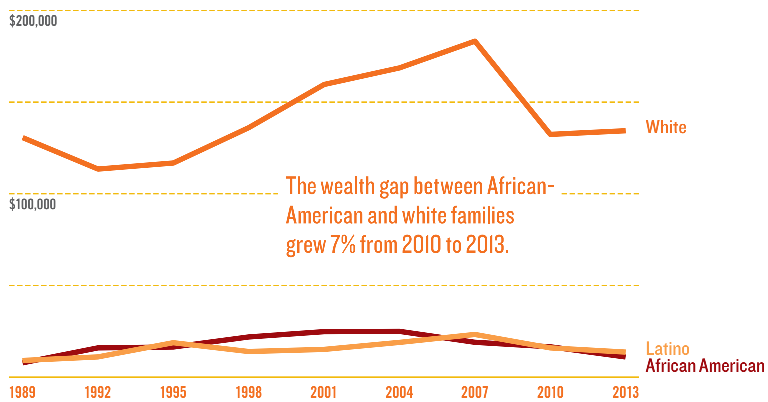
Median Net Worth of U.S. Families by Income and Race

Dramatic differences in family net worth by race, ethnicity and income have persisted for decades. In 2013, the median net worth of white households was more than 10 times that of African-American or Latino families. While white families' net worth rose slightly after the recession, Latino and African-American families' net worth fell markedly.

NET WORTH OF FAMILIES BY INCOME (MEDIAN)



NET WORTH OF FAMILIES BY RACE (MEDIAN)



SOURCE Marin Economic Consulting analysis of the Federal Reserve Board's Survey of Consumer Finances, 1989–2013.

NOTE Income categories, which vary annually, are based on the Federal Reserve Board's Survey of Consumer Finances. For example, in 2013, half of U.S. families (bottom 50 percent) had incomes of $45,000 or less. Forty percent had incomes between $45,001 and $150,000. Seven percent had incomes between $150,001 and $300,000. The top 3 percent of families had incomes exceeding $300,000.

let families keep assets that provide safe and adequate transportation and housing as they work to move off public assistance and become self-sufficient.

Expand Access to Homeownership

Federal policy should help low-income families move toward purchasing a home, increasing net worth and creating more stable communities.[26] While lawmakers can broadly promote homeownership through tax and housing policy, they also should bolster one promising underused option.[27] The U.S. Department of Housing and Urban Development's (HUD) voluntary Family Self-Sufficiency (FSS) program helps individuals with housing vouchers and those living in public housing increase income, build assets and improve financial stability, including saving for a home. Through the program, an escrow account is established for participants. As their earnings rise, they pay more rent, but the amount of each increase is deposited in their accounts monthly over five years.[28]

FSS serves nearly 70,000 households — a fraction of the more than 3 million eligible — mostly participating in the housing-voucher program. Congress has temporarily expanded FSS to include project-based Section 8 housing participants,[29] making it available to another 1.2 million families. This eligibility should be made permanent, and widely promoted.

In addition, HUD should experiment with new approaches to allow all families entering subsidized housing to increase savings along with earnings. Small pilot projects are underway in Massachusetts and Oregon.[30] The Alaska Housing Finance Corporation plans to match up to $1,500 in savings for participants completing FSS and a financial literacy course.[31]

Build Savings From Birth

Assets are best built over time to leverage the power of compounding interest. To ensure every child has savings, the federal government should create universal savings accounts, seeded with modest deposits, from the moment a child is born. This would foster college enrollment with the dollars the accounts would generate for education and manifest our belief in every child's potential.

Bipartisan legislation proposed in 2009, for example, would have provided a $500 deposit for all children, with $500 more for kids in low-income families. Research suggests a savings account can change children's behavior and make it substantially more likely they will attend college.[32]

Several states have versions of these accounts, often using 529 programs and contributing through direct starter funds or tax incentives. In an Oklahoma pilot, a group of young people received an Oklahoma College Savings Plan 529 account with a seed deposit of $1,000, along with $100 deposits to open separate 529 accounts. In early results, the group receiving the incentive deposits was 16 times more likely to have opened private 529s than peers in a control group.[33]

The federal government should provide these accounts for every child. Federal funds should seed each account, with larger deposits for infants in low-income families with minimal savings. At age 18, a young person could use the money for tuition or training, a business or a home.

An analysis of this ambitious policy indicates it could have a profound effect on the racial wealth gap among young adult households. Depending on funding and participation, these accounts could reduce the racial wealth gap by about 20 to 80 percent, while raising the wealth levels of all groups.[34] While costly, this investment in children could reduce dependence on public benefits, increase consumer buying power, boost investment in businesses and homes — and move our country to greater equity.

Conclusion

Investing in families allows families to invest in themselves — to imagine and confidently act upon opportunities for their children while cushioning against the financial setbacks that inevitably arise. We should equip all families to take on this responsibility. Doing so will not just help individuals along the road to opportunity. It will increase the stability of whole communities by creating committed homeowners and a workforce with the education and training required for many of today's well-paying jobs, truly building a solid foundation for our nation's future.

The Role of States

While changes in federal policies can provide equal access to savings and credit on a broad scale, states are important in making those policies work. States should:

- cap interest rates on products such as payday loans, lines of credit, refund anticipation checks and short-term mortgages. States also should target opportunistic credit repair organizations or banks authorizing these products and protect consumers from repeated rollovers of small-dollar loans that can balloon into unmanageable debt.[24]

- open 529 savings accounts, which help families save for college, for all children born in the state, partnering with financial institutions, individuals or philanthropies to seed them. States might match savings with federal funds, as Pennsylvania has done.[25]

- authorize prize-linked savings products to encourage savings with a chance to win a large prize. Although federal legislation permits states to allow financial institutions to offer these accounts, only 15 states do.

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ENDNOTES and more resources, including an analysis of the impact of our recommendations on the racial wealth gap, available at www.aecf.org.

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