

ASSET BUILDING PROGRAM

CHILDREN'S SAVINGS ACCOUNTS

Research, Practice, and Implications for Policy Design

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JUNE 2014

The American Dream is built upon the enduring values of equal opportunity and personal responsibility. Ensuring that this dream remains attainable depends upon America being able to promote these values among rising generations. Research and experience in the field consistently supports the thesis that children's savings accounts (CSAs) can provide a vehicle to support these objectives. These accounts can serve as a magnet for savings and investment from families and communities, and meaningfully promote increased savings, responsible financial behavior, and achievement that can facilitate the climb up the economic ladder. Previous CSA proposals have attracted the attention of policymakers across the political spectrum, and with renewed leadership, CSAs can be a foundational element of a bipartisan opportunity and economic mobility agenda. This paper will review the research foundations for this policy idea, describe the proliferation of recent policy efforts in diverse contexts, and consider some of the key policy design questions relevant for a federal policy effort.

Empirical Foundations

Recent research has confirmed that the presence of savings plays a key role in facilitating economic security and mobility.¹ Furthermore, this effect is especially pronounced in children. There is a significant relationship between a family having savings and the outcomes of their children in school and in life. Having access to savings

generally—and particularly in the child's name—are associated with a range of positive outcomes, including better academic performance, higher rates of college matriculation, and higher rates of college completion.² There is evidence that supports the idea that having savings improves the way children think about themselves and their future. It can help them set their sights on

¹ Urahn, Susan, Travis Plunkett, Erin Currier, Diana Elliott, Sarah Sattelmeyer, and Denise Wilson, 2013. "Moving On Up: Why Do Some Americans Leave the Bottom of the Economic Ladder, but Not Others?" Washington, DC: The Pew Charitable Trusts.

² Assets and Education Initiative, 2013. "Building Expectations, Delivering Results: Asset-Based Financial Aid and the Future of Higher Education." Lawrence, KS: Assets and Education Initiative.

higher achievement and change their behavior so they actually follow through.

Looking across generations, we see that having savings is an influential factor in achieving economic mobility. Research from the Pew Charitable Trusts has demonstrated that children of low-income, but high-saving parents are more likely to experience upward mobility than children of parents with lower savings. 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 over a generation. In contrast, roughly half (50 percent) of children raised by low-saving parents moved up from the bottom of the income distribution a generation later.³ This research supports the hypothesis that savings is a foundation for economic mobility and other asset building activities that can unfold across the life course. Other evidence confirms that families at the bottom of the income distribution whose children advanced up the income ladder had almost double the median wealth assets as those families whose children remained at the bottom of the earnings ladder in adulthood.⁴

Not only do savings promote economic stability and mobility, savings helps build a bridge to retirement security.⁵ Regardless of any changes to the Social Security program, families will need to

³ Cramer, Reid, Rourke O'Brien, Daniel Cooper, and Maria Luengo-Prado, 2009. "A Penny Saved is Mobility Earned: Advancing Economic Mobility Through Savings." Washington, D.C.: Economic Mobility Project, The Pew Charitable Trusts.

⁴ Ibid., 1.

⁵ Fellowes, Matt and Katy Willemin, 2013. "The Retirement Breach in Defined Contribution Plans: Sizes, Causes, and Solutions." Washington, DC: Hello Wallet.

build up their own assets to achieve peace of mind, and there are large advantages for making sure everyone has this opportunity and can begin the process as early as possible.

Nonetheless, millions of households, regardless of their income level, want to save but do not. Current policy rewards savers through preferential tax treatment, but this public support of private saving goes overwhelmingly to households at the top of the income distribution.⁶ Research clearly shows that households at all income levels can and will save when they have access to appropriate, safe, and easy-to-use products with the right incentives and support systems in place.⁷

A national, universal platform for children's saving could provide an infrastructure to help families accrue the savings that make a meaningful difference in the lives of children and improve their prospects for economic mobility. Such a policy would also create additional benefits by reinforcing a culture of savings, personal responsibility, and increased ownership and investment.

Proliferation of Models

In recent years, there has been a proliferation of efforts to expand opportunities for children to

⁶ Cramer, Reid and Elliot Schreur, 2013. "Personal Savings and Tax Reform: Principles and Policy Proposals for Reforming the Tax Code." Washington, D.C.: New America Foundation.

⁷ Moore, Amanda, 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.

save. Philanthropic institutions have financed the development of pilot projects to model and study the impact of these accounts and saving opportunities. States and municipalities have followed these initiatives and deemed them promising enough to mount their own efforts. Outside of the United States, a number of children's savings policies have been developed and implemented at scale. Taken together, these pilot programs, demonstration projects, and policies at the local, state, and international levels have explored a range of approaches that have implications for a federal policy effort. Below is a short description of the legislative history of Children's Savings Account (CSA) proposals and some of the key initiatives that have been implemented in the field.

*Legislative History*⁸

KidSave. First offered in the late 1990's by Senator Bob Kerrey, KidSave would allow every American child to receive a loan of \$2,000 at birth from Social Security. Funds could be withdrawn only at retirement. In addition to the base loan, parents would be allowed to deposit up to \$500 annually in each child's account until he or she reaches the age of 19. The initial loan would have to be repaid starting at age 30. KidSave attracted diverse and bipartisan support, such as from Senators Judd Gregg, Charles Grassley, Daniel Patrick Moynihan and others.

PLUS Accounts. Proposed by Senator Jeff Sessions (R-AL) in 2006 but never introduced as legislation, Portable, Lifelong, Universal Savings (PLUS Accounts) would have automatically

created an account for each child. The account would have been seeded with a one-time \$1,000 contribution. Beginning January 1, 2009 individual PLUS accounts would be established for all working U.S. citizens under the age of 65 with a mandatory 1 percent of each worker's paycheck withheld pre-tax and automatically deposited into their account (workers could voluntarily contribute up to 10 percent). Employers would also be required to contribute at least 1 percent (and up to 10 percent) of earnings. No withdrawals from PLUS accounts could be made until the accountholder reached the age of 65, although there would be a loan program for pre-retirement uses.

Young Savers Accounts. Parents would be allowed to direct contributions to Roth IRA accounts for their children, not just for themselves. YSAs were introduced by Senator Max Baucus (D-MT) as part of the Savings Competitiveness Act of 2006, and a similar provision was introduced in July 2005 in the House by Rep. Connie Mack (R-FL) as part of the Lifetime Prosperity Act.

The ASPIRE Act. First introduced in 2004 by Senators Rick Santorum (R-PA) and Jon Corzine (D-NJ), The ASPIRE Act would create an account for all children at birth, seeded with \$500 and an additional deposit for children of low-income parents. Deposits would be capped at \$2,000 annually and grow tax-free. Matches would be available to low-income families, up to \$500 each year. In addition to retirement security objectives, funds would be available to pay for post-secondary education and first-time homeownership. The ASPIRE Act has been subsequently introduced in both the House and Senate with bipartisan supporters, including Senators Jim DeMint (R-SC) and Charles

⁸ Cramer, Reid, Alejandra Lopez-Fernandini, Lindsay Guge, Justin King, and Jamie Zimmerman, 2011. "The Assets Agenda 2011." Washington, D.C.: New America Foundation.

Schumer (D-NY) and Representatives Jim Cooper (D-TN) and Tom Petri (R-WI).

Research Pilots

Saving for Education, Entrepreneurship and Downpayment (SEED).⁹ The SEED initiative was a Child 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.

SEED for Oklahoma Kids.¹⁰ SEED OK is an outgrowth of SEED, designed to test CSAs rigorously. In 2007, SEED OK randomly assigned over 2,600 newborns in a treatment or control group. The participants assigned to the treatment group were automatically enrolled in Oklahoma's 529 College Savings Plan and were provided a \$1,000 initial deposit. SEED OK has demonstrated that automatic account opening is a highly successful strategy for inclusion of a full population, with 99.9 percent of treatment participants accepting CDAs (Child Development Accounts), a type of CSA, and holding them several years later. Follow-up research has found that SEED OK increased young children's social-

emotional development at age four among families that have low education, low income, receive welfare benefits, and rent their homes. This is a powerful finding, which confirms an impact of CSAs even among very young children.

State and Municipal Efforts

Kindergarten to College San Francisco.¹¹ In 2011, San Francisco launched the Kindergarten to College (K2C) program, which is opening 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 can earn matching funds on the first \$100 of contributions each year; 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 delivered in partnership with Citi Bank.

Cuyahoga County (OH) College Savings Account Program.¹² In the fall of 2013, Cuyahoga County, Ohio launched its own College Savings Account Program, opening accounts for 15,000 incoming kindergarten students, seeded with \$100 each. The plan's organizers have stated that saving incentives will eventually be made available, but no details have yet been offered. The funds are reserved for post-secondary educational expenses, though emergency withdrawals are allowed.

⁹ Sherraden, Michael and Julia Stevens (Editors), 2010. "Lessons from SEED: A National Demonstration of Child Development Accounts." St. Louis, MO: Center for Social Development, Washington University in St. Louis.

¹⁰ Beverly, Sondra, Margaret Clancy, and Michael Sherraden, 2014. "Testing Universal College Savings Accounts at Birth: Early Research from SEED for Oklahoma Kids." St. Louis, MO: Washington University, Center for Social Development.

¹¹ Phillips, Leigh and Anne Stuhldreher, 2011. "Kindergarten to College: A First-in-the-Nation Initiative to Set All Kindergartners on the Path to College." Washington, D.C.: New America Foundation.

¹² For more information, visit the website of the Cuyahoga County College Savings Account Program at: <http://collegesavings.cuyahogacounty.us/>.

Cuyahoga County holds the funds in a special account until disbursement.

The Alford Challenge (Maine)¹³ and Nevada College Kick Start.¹⁴ In 2008, the Alford Challenge, funded by the Alford 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 Alford funds and earnings revert to the fund upon the child's 28th birthday. This program has used an opt-in model, but low adoption rates have led the organizers to recently announce a shift to an automatic model. This past year, Nevada College Kick Start began offering over 30,000 kindergartners a 529 college savings account with a parental opt-out available. Each 529 account is seeded with \$50 and offers a potential lifetime total of \$1,500 in matching funds.

State 529 College Savings Accounts. 529 college savings plans are offered by every state to supporting children's savings for postsecondary education. Several states offer a combination of seed and matching deposits based on availability of funds for children meeting specified eligibility requirements, typically based on family income.¹⁵ The network of 529 state plans has important features as a potential platform or model for a national CSA program, including an existing

infrastructure and centralized administration.¹⁶ However, current take-up is limited. Less than 3 percent of parents have opened an account for their children. And since the tax benefits associated with these accounts benefit higher income families, it is not surprising that it is typically these families that make contributions.¹⁷ The postsecondary focus of 529 accounts is a major driver of parental efforts to save, but approximately one-third of high school graduates do not attend any college. Fee structures vary widely across and within state 529 account offerings, making costs difficult to ascertain.

International Examples

Canada.¹⁸ Canada leverages its Registered Education Savings Plan (RESP), similar to our 529 plans, to provide matched savings and seed deposits for lower-income parents through the Canada Education Savings Program (CESP). The program provides a universal matching grant of 20 percent, 30 percent, or 40 percent (up to \$7,200), depending on family income and the amount of contribution and low-income families are eligible for an additional \$2,000 grant.

¹³ Clancy, Margaret and Michael Sherraden, 2014. "Automatic Deposits for All at Birth: Maine's Harold Alford College Challenge." St. Louis, MO: Washington University, Center for Social Development.

¹⁴ For more information, visit the website of the Nevada College Kick Start at: <http://collegekickstart.nv.gov/>.

¹⁵ Ibid., 2.

¹⁶ Newville, David, 2010. "The Potential of Inclusive 529 College Savings Plans." Washington, D.C.: New America Foundation.

¹⁷ "Higher Education: A Small Percentage of Families Save in 529 Plans," U.S. Government Accountability Office, GAO-13-64, December 2012.

¹⁸ "Formative Evaluation of the Additional Canada Education Savings Grant and Canada Learning Bond," Evaluation Directorate, Strategic Policy and Research Branch, Human Resources and Skills Development Canada, SP-951-05-10E, November 2009.

The United Kingdom.¹⁹ The United Kingdom launched the Child Trust Fund in 2005, and awarded £250 vouchers for parents to open accounts for children born between 2002 and 2005. Children from low-income households received an additional £250. Parents use the voucher that they receive to open an account with a private sector provider. When the child reaches seven years old, the government issues a second voucher for every child on the same terms as the first. Interest accrued in the fund is paid tax-free and parents/relatives/friends can collectively deposit up to £1,200 per year. The account cannot be accessed until the child reaches age 18, upon which point they have full and unrestricted access to the fund. The CTF was closed to new children in 2010, but existing accounts provide a rich base for research and insight.

Policy Design Considerations

Learnings from these experiences in the field can help refine federal policy efforts. Choices in policy design features will impact program costs, scope, and ultimately outcomes. Effectively delivering CSAs at scale will depend upon how policy addresses several foundational issues, such as participation, intended uses, and account features.

Participation: Universal or Targeted, Automatic or Voluntary

Families currently can voluntarily elect to save on behalf of their children in a variety of vehicles, including in 529 College Savings Plans. But, for a variety of reasons, it is mostly families with higher incomes that take advantage of these opportunities. CSAs represent an opportunity to

interrupt intergenerational patterns of financial disadvantage, as well as promote a shared cultural commitment to saving. Some previous examples of CSAs have specifically targeted disadvantaged families. However, it is not just lower-income families that find it difficult to save in today's America. As mentioned above, less than 3 percent of families currently save in a 529 or Coverdell Education Savings Account. A universal approach would seamlessly offer the same opportunities to all families, regardless of income or existing savings habits and most effectively foster a cultural change in favor of savings, ownership, and prudent financial decision-making.

CSAs represent an opportunity to interrupt intergenerational patterns of financial disadvantage, as well as promote a shared cultural commitment to saving.

Universal account ownership would also provide a foundation for integrating meaningful financial education into the educational system. Research suggests that financial education is most effective when delivered in connection to an actual account with money in it.²⁰ A universal approach to CSA implementation can be facilitated through automatic enrollment to maximize participation. Until recently, Maine, for example, offered a \$500 initial contribution to their 529 plan for all children born in the state. However, parents were required to voluntarily opt in to participate in the program. As a consequence, initial take-up has been substantially lower than expected (39

¹⁹ For more information, visit the website of the United Kingdom's Child Trust Fund at: <https://www.gov.uk/child-trust-funds/overview>.

²⁰ Baker, Christi and Doug Dylla, 2007. "Analyzing the Relationship Between Account Ownership and Financial Education." Washington, D.C.: New America Foundation.

percent).²¹ Sponsors of the program recently announced that the accounts would switch to an opt-out model. This is consistent with the experience in San Francisco’s Kindergarten to College (K2C) program and the SEED OK research project, which open accounts automatically for all children involved. Even though parents are given the option to choose to opt-out, these efforts have a nearly universal take-up rate. If this is the goal of a national policy, a series of common actions by parents or guardians can be used to trigger an account opening on behalf of the child. These include the issuance of a Social Security card, the application for a birth certification, or enrollment in primary school, among other events.

Allowed Uses

The earliest CSA proposals, such as KidSave, focused on retirement security objectives. However, recent experience in the field strongly supports a more flexible approach. Accounts restricted to retirement depress large-scale participation because the extended time horizon between action and benefit is too great for many people. Similarly, even though many families view these accounts as most valuable for educational objectives, accounts that are singularly focused on education may present little value for those who do not pursue higher education.

To achieve the dual advantages of generating savings and sustained savings behavior, there are benefits in aligning accounts with the goals of the families who own them.²² Some programs,

notably the UK Child Trust Fund, allow the account holder unrestricted access to funds once the accountholders reach the age of 18. Other programs have made it a principle that the use of funds should be restricted to activities that are likely to boost the well-being of the beneficiary, as public funds are invested in the accounts. Past versions of CSA proposals in the US have targeted post-secondary education, home-ownership, and a secure retirement as eligible uses for the funds. Entrepreneurship has also been considered as a possible use.

Savings Platform and Account Features

The choice of savings platform has large implications for this type of policy effort. The initial seed deposit may vary in size, but will always play an important role in anchoring the account and providing the resources to support the infrastructure.²³ Regardless of the size of the initial deposit (which might range from \$50 to \$2,000), these accounts will start small. Small value accounts can be expensive to manage, and increase the costs of the policy to both the accountholders and the public sector. There are significant advantages to supporting these accounts within a savings plan structure, similar to 401(k)s or 529 College Savings plans, such as low-cost administration, outreach and education, diversified investments, and centralized accounting. While individual investors often see their return erode as a result of high administrative costs, savings plans can take advantage of economies of scale and keep these costs down, passing along the savings to their participants. Maybe more importantly, the plan

²¹ Ibid., 13.

²² Xiao, Jing J. and Franziska E. Noring, 1994. “Perceived Saving Motives and Hierarchical Financial Needs.” *Financial Counseling and Planning*, Volume 5, 1994: 25-45.

²³ Beverly, Sondra G., and Michael Sherraden, 1999. “Institutional determinants of saving: Implications for low-income households and public policy.” *Journal of Socio-Economics*, 28:457-473.

structure has the potential to establish a set of default settings and other practices that maximize returns; these include automatic enrollment, direct deposit and payroll deduction, and linking rising contributions to increases in earnings.

To achieve the dual advantages of generating savings and sustained savings behavior, there are benefits in aligning accounts with the goals of the families who own them.

For successful adoption and use of accounts, participants will need widely available and easy-to-use options to interact with their accounts. Depending on the savings platform, there are myriad investment and management options for saved funds. One promising approach is to require accounts to remain within a national or regional savings plan until they reach a certain dollar threshold, such as \$15,000, at which time the accounts could be rolled out to another financial institution. Regardless of where the accounts will be held, rules will be required to govern contributions, withdrawals, and other consumer protections.

Savings Incentives

A CSA policy that is universal and automatic will eliminate many significant barriers to saving. However, such an account does not begin the development of the savings habit on its own. Incentives to save can make a critical difference in encouraging families to make the short-term sacrifices that lead to better long-term outcomes, especially for families on the lower end of the income ladder.²⁴ In addition to promoting the

²⁴ Ibid.

savings habit, these incentives help to build bigger balances.

The U.S. government has traditionally promoted savings by providing tax benefits for saving, such as deductions for contributions or tax-free earnings. CSAs may benefit from similar tax treatment. However, research in the field shows us that additional incentives will likely be needed to engage struggling families. Matching contributions on an annual basis could engage families with limited resources and accelerate asset accumulation by providing an accessible incentive to save. Matches could take the form of direct transfers from the U.S. Treasury or as a refundable credit, such as the EITC, Child Tax Credit, or a special CSA credit, that would be deposited directly into the account.

There is room for creativity in designing incentives. K2C, for example, offers \$100 for families who sign up for automatic deposits or save in six consecutive months to promote building a savings habit. Incentives for school-aged children could also include meeting certain academic performance measures, a practice known as “Conditional Cash Transfers.” The incentives could be universal, progressive, and/or conditional. They could be delivered at account opening, throughout the life of the account, or when the money is accessed and used. The type, extent, and structure of incentives not only affect the level and distribution of program costs, but also the attractiveness of the program to potential participants.

Concurrent Policy Considerations

Successful implementation of a national CSA policy is contingent upon both the design of the CSA itself as well as the coordination of CSAs with intersecting policies.

First, attention should be given to removing savings disincentives within public assistance eligibility rules and existing financial aid policies that could undermine the intent and impact of any proactive savings policy. Treatment of different types of savings and assets, including 529s, vary among programs and states. For example, the Supplemental Nutrition Assistance Program (formerly food stamps) has eliminated 529s from consideration when determining program eligibility, but many states still include them when calculating eligibility for TANF.²⁵ These asset limits create barriers, both real and perceived, that inhibit saving among low-income families. Programs such as Kindergarten to College use a custodial account structure where the City and County of San Francisco own the account, rather than the students or their families, exempting their savings from consideration in the application process. These workarounds are costly to administer and create confusion among participating families. Legislation authorizing the creation of a national CSA policy will need to categorically exclude resources in these accounts from counting toward these asset limits.

Like public assistance programs, the Free Application For Student Aid (FAFSA, the form which allows students and parents to determine their eligibility for federal student aid) considers both income and assets when determining the Expected Family Contribution, which is the basis for calculating aid. This can create the perception that savings will reduce the amount of financial assistance a student is awarded and similarly

²⁵ For more information about individual asset limits in federal means tested programs, the New America Foundation maintains a visual database at: <http://assetlimits.newamerica.net/>.

create a disincentive to save as well as to apply for assistance, believing that even a very small amount of savings will disqualify them from aid.²⁶

Incentives to save can make a critical difference in encouraging families to make the short-term sacrifices that lead to better long-term outcomes.

Putting in place a hard figure, under which any savings will not count against a family for financial aid purposes, would allow families to feel comfortable saving long before the FAFSA needs to be completed. As part of its effort to simplify the process of aid determination, the Obama Administration has proposed eliminating any financial question that could not be prepopulated with IRS data, including six of the most onerous questions related to income and assets.²⁷ The Administration would, instead, replace those questions with just one question asking if the family owned more than \$250,000 in assets, outside of excluded assets such as their home and retirement accounts. This move would be expected to have negligible cost compared to the benefit of simplification. The Administration

²⁶ Dynarksi, Susan and Judith Scott-Clayton, 2007. "College Grants on a Postcard: A Proposal for Simple and Predictable Student Aid." Washington, D.C.: Hamilton Project Discussion Paper No. 1, 2007.

²⁷ Executive Office of the President; Council of Economic Advisers; National Economic Council, 2009. "Simplifying Student Aid: The Case for an Easier, Faster, and More Accurate FAFSA." Washington, D.C.: Executive Office of the President; Council of Economic Advisers; National Economic Council.

reports that in the 2007-2008 school year, only 4 percent of financial aid applicants had more than \$150,000 in assets.

Additionally, an effective policy will maximize opportunities for families to connect with and contribute to CSAs. To that end, CSAs should be designed to leverage the resources and incentives to save that are already built in to the tax filling process. Every year, around 27 million households file for the Earned Income Tax Credit, a credit that boosts the value of work for low-wage earners by offering an additional subsidy for every dollar in earned income. In 2013, the average value of the EITC was \$2,335 per household with a potential maximum of \$6,044.²⁸ Both the number of families that engage in this process and the significance of the resources they receive make the tax time moment a powerful savings opportunity. Recent research of interventions to boost saving of tax refunds

either through behavioral mechanisms, such as defaulting a portion of the refund into a savings product, or by facilitating account opening or offering a direct match incentive, have demonstrated success and could be applied to using the tax filing process as a mechanism to build CSA balances.²⁹

Conclusion

While there are many decision points and policy issues to consider when designing a national system of Children's Savings Accounts, these issues are the primary building blocks for creating an effective and impactful policy effort. To be successful, policymakers need to consider the consequences of these choices on program costs and benefits. Utilizing existing program data and evaluating the interaction of the preferred design choices at scale can help build a model that is successful, manageable, and sustainable.

²⁸ Figure reported by the IRS and obtained online at: <http://www.eitc.irs.gov/EITC-Central/abouteitc>.

²⁹ Black, Rachel and Elliot Schreur, 2014. "Connecting Tax Time to Financial Security: Designing Public Policy with Evidence from the Field." Washington, DC: New America Foundation.

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