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AutoSave:

A Proposal to Reverse America's Savings Decline and Make Savings Automatic, Flexible, and Inclusive

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SUMMARY

Last year the United States had a negative personal savings rate for the first time since the Great Depression, contributing to a historically low national saving rate. If low saving persists over an extended period of time, it will drain resources available for potentially productive investments, undermine economic growth and foster economic insecurity. Recent findings from the field of behavioral economics and institutional savings theory provide valuable insights into what it would take to turn America back into a saving nation. Specifically, the value of savings plans and default policies provides a constructive platform to facilitate savings. Savings plans bundle support structures that offer participants access to savings products and information, limited investment options, and low-cost administration. Default policies, such as direct deposit and automatic enrollment in savings plans, can be highly significant drivers of economic behavior. However, many Americans do not have access to these savings tools.

An alternative policy proposal, called AutoSave, would serve as a universal savings plan accessible to all workers. Under this plan, employers that make payroll deductions will be required to make deposits to the AutoSave system on behalf of their employees and the self-employed would be able to make deposits into the system at their discretion. Employers will shoulder no extra costs but will facilitate automatic deposits. AutoSave will offer a limited set of low-cost investment options, such as index funds, which would be administered by professional money managers. Money deposited in this system belongs to the individual and since deposits will be from after-tax dollars, normal tax rules apply. Individuals will have the flexibility to opt-out of the system or drawn down on their funds at any time. A default contribution rate can be set at 2% of pay. At this rate, someone earning $50,000 a year would have $1,000 diverted directly into savings, which could grow with responsible stewardship. Additional targeted incentives could be applied to encourage longer-term savings, but AutoSave would be designed to take advantage of one of the most tried and true savings techniques—inertia.

Key Features of AutoSave

- Automatic Participation in an Inclusive Savings Plan
- Freedom to Opt-Out of the Savings Plan
- Contributions via Direct Payroll Deductions
- Flexible Withdrawals to Meet Emergency and Other Needs
- Low-Cost Investment Choices
- Normal Tax Rules Apply

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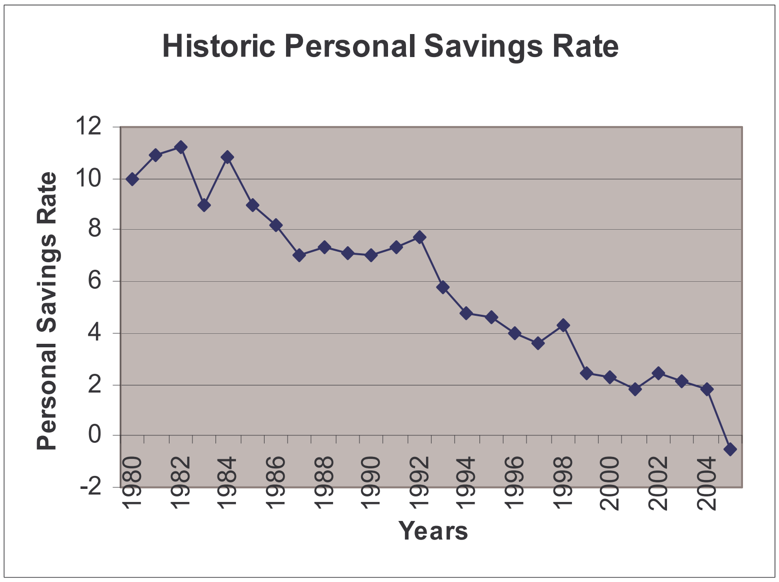
THE SAVINGS PROBLEM

Americans are failing to save. The Commerce Department has chronicled a startling decline in the personal savings rate, which is calculated by subtracting total personal outlays from disposable income. Over the last ten years the amount of unspent income has declined precipitously. Dropping from its historic average of about 9 percent, the personal saving rate for 2005 was negative and has remained in negative territory through the first two quarters of 2006.[2] In 2005 personal outlays exceeded disposable income by $42 billion, which can only happen if people spend money they have borrowed, sell existing assets, or draw down on their savings.[3] Some explain this decline by claiming people feel wealthier when they look at the value of their homes and stock portfolios, while others have questioned the validity of this "wealth effect" as stock prices have been flat in recent years and mortgage refinancings have drained off a substantial amount of housing equity.

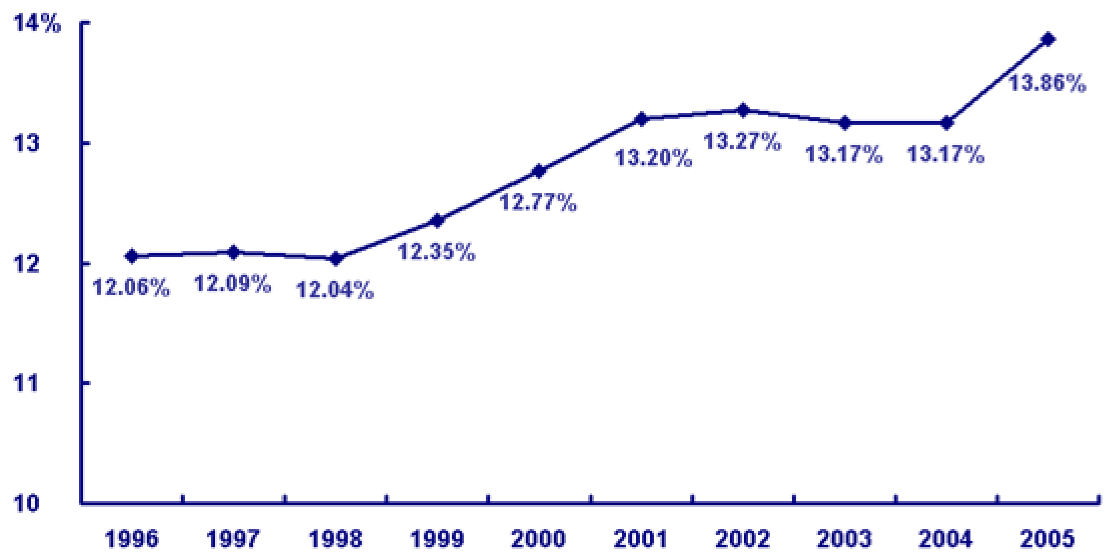


Source: Bureau of Economic Analysis, U.S. Department of Commerce.

The personal savings rate offers one perspective on the financial state of households in the aggregate, but other indicators reflect additional sources of economic insecurity. Last year consumer debt and personal bankruptcies were also at record levels. Personal bankruptcies have been steadily rising in recent years and in 2005 the number of consumers seeking relief from their debts through bankruptcy increased to 2.04 million.[4] Also, both business and household borrowing has increased since the mid-1990s, but household debt rose 11.7 percent in 2005, while business debt rose only 5.7 percent. This is a trend that has persisted over the last ten years as household debt has increased 121.7 percent compared to 73.1 percent for business debt.[5] Further, household debt as a percentage of disposable income has climbed over the same period, rising from 12.06 percent in 1996 to 13.86 percent in 2005; and recent data from the Federal Reserve's Survey of Consumer Finances shows that debt as a percentage of total assets now stands at 15 percent, up 3 percent from 2001.[6]

[2] Bureau of Economic Analysis (2006).
[3] Bureau of Economic Analysis (2006).
[4] This widely reported figure has been provided by Lundquist Consulting, an industry group that tracks bankruptcies. The 2005 level increased over 30% from the previous year as many filers sought to declare before the provisions of the new bankruptcy law took effect. Even without this surge, the number of personal bankruptcy filings was expected to reach an all-time high.
[5] Board of Governors of the Federal Reserve System (2006).
[6] Bucks et al. (2006).

Household Debt as a Percent of Disposable Income, 1996-2005



As measured by the household debt service ratio, an estimate of the ratio of debt payments to disposable personal income, including outstanding mortgage and consumer debt.

Source: Board of Governors of the Federal Reserve System.

Rising consumer debt is a significant source of financial insecurity as families become especially vulnerable to rising interest rates and falling or stagnant incomes. When this is combined with low personal savings at the household level economic well-being is threatened in both the short and the long term. For instance, a recent study by the Center for Retirement Research at Boston College found that about half of current working-age households are at risk of seeing their standard of living fall in retirement as a result of low savings.[7]

Personal savings is one of the primary components of national savings, which takes into account the finances of the government and business sectors as well. Net national saving offers a fuller, macroeconomic picture of the amount or share of our resources available for building up the country through capital investment, and recently, the national saving picture has also been troubling.[8] This is because government borrowing from world capital markets has provided a growing share of the resources which are currently financing investment, and in a turn-around from the late 1990s, the government expects to run budget deficits into the foreseeable future. While short-term budget deficits may in some circumstances be beneficial to the economy, maintaining budget deficits over the long term cuts into net national savings and takes away resources that would be otherwise available for investment. The United States currently has the lowest national savings rate of any of the countries that make up the G-20. In 2003, the United States had a net national savings rate of 1.6 percent which is almost half that of the United Kingdom and well below Japan (5.0%), France (7.3%), and Saudi Arabia (25.3%).[9] Low national savings is poised to become an even greater problem as the population ages. According to the McKinsey Global Institute, savings rates in the largest developed economies are set to fall dramatically over the next two decades as median ages in Japan, the U.S., and Western Europe increase. Not only do people save less after they retire, but current workers in their prime earning years are saving at lower rates. McKinsey projects that household financial wealth

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[7] Center for Retirement Research (2006).
[8] See Gramlich (2005) for an informative discussion of the national savings issue.
[9] World Bank as reported by Johnson et al. (2006).

will be roughly $31 trillion, or 36 percent, less than it would have been had historical trends persisted in the world's major economies.[10]

New National Savings Rates (2003)
of Select Countries
(as a share of Gross National Product)

Argentina	10.6%	Italy	5.0%
Australia	3.6%	Japan	10.8%
Brazil	8.4%	Mexico	8.2%
Canada	7.5%	Russia	19.0%
China	38.6%	Saudi Arabia	25.3%
European Union	7.0%	South Africa	3.0%
France	7.3%	South Korea	19.2%
Germany	5.4%	Turkey	12.3%
India	15.2%	United Kingdom	2.9%
Indonesia	13.4%	United States	1.6%

Source: World Bank as reported by Johnson et.al. (2006).

THE CASE FOR SAVINGS

The combination of low personal savings and low net national saving is a perilous one. If low saving persists over an extended period of time, it will limit the resources available for investment, undermine economic growth and foster economic insecurity. Yet America used to be a nation of thrift. Historically, this did not mean being cheap or stingy; it referred to a quality of stewardship associated with wise spending that generates future wealth.

Saving was traditionally regarded as a virtuous activity because it was beneficial both individually and collectively. At the national level, savings creates pools of capital available for investment that promotes productivity and keeps interest rates low; and while it is theoretically possible for a society to over-save (as perhaps Asia is now), we are far from having that problem. At the household level, it is helpful to consider the wide range of reasons as to why households save. People save as a precaution to protect themselves against an unexpected loss of income; they save to smooth out their consumption over the life cycle to maintain their standard of living in retirement; and they save to pass along something to their kin. Accordingly the level of savings that would be considered "adequate" for any particular household may be difficult to predict as it is a function of individual preferences. Still, at a minimum, savings should be expected to be a primary component of retirement planning. Yet it is worth noting that savings can also be deployed productively over a shorter time horizon.

Savings that can be accessed on an emergency basis are an essential component of economic security. The lack of adequate emergency savings, for example, has been linked to the growth of high-cost loans and can undermine the asset accumulation process. The Consumer Federation of America conducted a series of surveys in 2004 and found that households had a median of five emergency expenditures throughout the previous year, with a total annual expense of $2,000.[11] These were often related to medical care or motor vehicle use. Respondents identified emergency savings as a prime cause of both financial worries and physical ailments. So, while savings policy has traditionally focused on retirement savings, many households would benefit from building up a pool of non-retirement, flexible savings that could be tapped in an emergency. Failure to weather these financial emergencies

[10] McKinsey Global Institute (2005).
[11] Consumer Federation of America (2005).

or save for other intermediate range purchases, such as a downpayment or school tuition, can make it much harder to save for the longer-term.

Not only are Americans failing to save, but our politicians are failing to respond. The savings incentives that policymakers have crafted are expensive, often wasteful, and generally ineffective. The problem is two-fold. First, it is higher-income households that receive the overwhelming majority of these annual subsidies, so these policies do not help those most in need of a boost. Second, these policies encourage deposits and asset shifting rather than reward new savings.[12] To make matters worse, regulations actually discourage savings by lower-income families. Eligibility for many public assistance programs, such as food stamps, TANF, and Medicaid, are linked to an asset test, so a family must deplete most their resources before qualifying for help.[13]

All told, our current savings policies are both upside down and backwards. More importantly, they are failing to actually promote savings. This policy failure is acutely revealed when comparing the negative personal savings rate to the $150 billion a year in tax subsidies that accrue to those contributing to 401(k) and IRA accounts, which have grown in recent years as the personal and national saving rate has fallen.[14]

From a macroeconomic perspective, it matters less whether it is high-wealth or low-wealth households that are doing the savings as long as enough is being set aside to finance the investment that supports economic growth. Yet high savings in the aggregate is not a guarantee of economic growth, and countries can borrow in the global capital markets as the U.S. has done. Still there may be limits to foreign borrowing over the long term, and demographic trends in many rapidly aging countries will reduce the availability of their savings to finance American consumption. Maintaining high productivity growth over the long term will undoubtedly require financing higher investment rates with domestic savings.[15]

Furthermore, in terms of social policy, the distribution of savings does matter. All families need savings to safeguard against unexpected events, invest in their future, and build up resources to use when their earnings decline in retirement. A great deal of the utility of savings is generated by their flexibility; they can be deployed strategically over time to maximize their effect, and increase economic well-being over the long-term. For many families, savings provide security as a buffer against income fluctuations; and for those families with low incomes, savings may make the difference between living in a constant state of anxiety about the next unanticipated expense or not. This is one of the more debilitating aspects of being poor because it undermines household stability and long-term planning. And for many people with low incomes and few resources, the value of savings is that they can be converted into assets that can help chart a path toward greater economic stability, which may be realized through homeownership or access to post-secondary education. In this sense, savings should be seen as an essential piece of an anti-poverty policy strategy, the first step in the asset building process.

The case for savings can be made at both the macro- and microeconomic level. Besides addressing the long-term federal budget outlook, increasing the rate at which households save is a necessary step to get our fiscal house in order and raise national saving. As this appears unlikely to happen on its own, public policy should be reconfigured to induce more people to save.

RECENT INSIGHTS INTO SAVINGS BEHAVIOR

Recent research from the field of behavioral economics and institutional savings theory provide valuable insights into what it would take to reverse America's saving decline and turn America into a saving nation.

[12] Bell et al. (2004).
[13] Parrish (2005).
[14] Cramer et al. (2006).
[15] McKinsey Global Institute (2005).

This growing body of work has focused on the intersection between policy and economic decision-making, and for several reasons proves to be a compelling area of research. First, policymakers are often faced with having to decide what to do when individuals fail to indicate a preference among a set of available options. Second, policymakers are interested in which particular policy choices will most effectively maximize public welfare or achieve a desired outcome. Most policy choices have a no-action default, so that a condition is imposed even when individuals do not state a particular preference. One robust finding is that economic decisions can be strongly influenced by the result of a "no-decision" which keeps someone in a default situation.[16] In other words, the existence of defaults in certain areas has been shown to have a large impact on the economic behavior of households.

In economic theory, individuals will rationally choose to maximize their utility subject to constraints. Even if they are not satisfied by the end result, individuals often stay in default situations. It may be because the perceived cost of action is high, the perceived benefit of action is low, or the effort to acquire the necessary information to make an informed choice is too great, but the status quo has proven to be a powerful force.[17]

One illuminating example of the potential impact of default policies is the case of organ donation. Two types of policies that generally govern organ donation in most countries: presumed consent and informed consent. An informed consent policy requires a person to choose to be a donor before they die and opt-in to the donor pool, while a presumed consent policy assumes people wish to be donors unless they state otherwise and opt-out. Nobody is required to become a donor but society has a vested interest in promoting organ donation. In recent decades a number of European countries have enacted opt-out policies consistent with presumed consent. This default appears to have a large effect: France, Poland, and Portugal have an effective consent percentage over three times that of Denmark, United Kingdom, and Germany.[18] It turns out that the majority of people in all of these countries do not choose to leave the situation where they are initially assigned. Several explanations might explain this observation, such as a taboo on thinking about death, anticipated regret about making the wrong choice, high cost of change (such as filing out paperwork), weak preferences, or the strong inclination to procrastinate. Whatever the reasons for why people decide to stay put, the end result is a divergence where the presumed consent countries achieve an outcome much closer to their desired policy goals.

In a variety of areas, it has been found that people tend to stay with the default situation. Beyond organ donation, the default option has been shown to make a difference in choosing providers of telecommunications, car insurance, utility service, and financial services.[19] Behavior economists and other academics in the field of social and cognitive psychology are exploring a range of hypotheses to explain the default effect.[20] By focusing on how humans process information within a broader social context, they expand our understanding of how people make decisions that impact their economic well-being.

For instance, contrary to the standard assumptions made in economics, Bertrand and colleagues note that the psychological carriers of value are gains and losses, not anticipated final states of wealth.[21] In reality, people are highly loss averse, meaning the loss associated with giving up something is greater than the gain associated with getting it. This generates a reluctance to depart from the status quo "because things that need to be renounced loom larger than those that are potentially gained."[22] Other cognitive principles at play include the observation that people compartmentalize financial matters into distinct budget categories, such as savings, rent, and play as well as into separate mental accounts, such as income, assets, and future income.[23] Yet people decide to consume from these accounts and categories differently, and it is more common for people to spend from their income than

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16 Bertrand et al. (2006), Beshears et al. (2005), Sunstein and Thaler (2003).
17 Gay (2005).
18 Johnson and Goldstein (2003).
19 Beshears et al. (2005).
20 Choi et al. (2005), Bertrand et al. (2006), Beshears et al. (2005).
21 Bertrand et al. (2006).
22 Bertrand et al. (2006).
23 Thaler (1999).

from their assets.[24] In general, this work has found that the local decision context is influential, and can contribute to an individual's propensity to plan, procrastinate, or exert self control. Of course, individual attitudes and preferences matter in predicting behavior but interestingly these "attitudes have better predictive validity in situations in which they are strongly activated and the link between attitude and behavior is readily apparent."[25] Therefore, while procrastination may be a powerful force, people may "choose" to remain where they are if they have not thought through the implications of doing so.

Applying these findings from behavioral economics and social psychology to public policy confirms that policy design matters a great deal. Achieving desired outcomes will depend upon how information and choices are presented, and excessive complexity will deter careful decision-making. Similarly, given the potentially pivotal role that defaults play, it is essential to establish the right ones. This is because the defaults can convey important information in and of themselves. McKenzie and colleagues have found that defaults are often interpreted as an implicit policy recommendation, and can be particularly influential with people that are uncertain of their preferences.[26] The wrong default can lead to sub-optimal resource allocations and policy outcomes.

One area where the effect of defaults has been scrutinized is retirement savings. Default policies, such as automatic enrollment in retirement plans and contributions from payroll deductions, has been shown to be highly significant drivers of savings activity. A frequently cited study by Madrian and Shea demonstrates that 401(k) participation is significantly higher in firms where employees are automatically signed-up than in firms where they have to choose to do so. This effect was greatest for lower-income employees. Madrian and Shea found that shifting to automatic enrollment raised participation among poorer workers from just over 10 percent to 80 percent.[27] Another study by Thaler and Benartzi suggest that people will save more if future savings are automatically tied to increased earnings.[28] They have proposed a savings scheme, which they call Save More Tomorrow, which automatically increases retirement contributions in conjunction with pay raises.[29] Thaler argues for the wisdom of policies based on libertarian paternalism, so that public policy can influence behavior in ways that increase welfare outcomes while respecting the individual's right to choose not to participate.

With respect to savings, there is an emerging consensus that finding the right defaults is the key to encouraging savings behavior. The wrong defaults or poorly-designed policies can dissuade people from saving. For example, if people are offered too many choices as to where to invest their funds, they may become afflicted with paralysis of choice. There clearly is an advantage to having an employer make payroll deductions, so the decision to save is not revisited every two weeks.

We also have gained an appreciation from an emerging institutional theory of saving that saving doesn't occur in a vacuum.[30] Rather, savings is directly facilitated by institutions and a set of structured mechanisms. These mechanisms are intentionally designed to support savings, banking, and investing activities; they include a wide range of policies, products, and services that shape the opportunities, constraints, and consequences of savings.[31] From this perspective, an individual's savings behavior is a function of both individual characteristics and the institutional context in which they act. Sherraden and his colleagues describe how institutions promote savings by providing information, creating access to incentives, facilitating participation, and offering protection against risk.[32] In practice these characteristics work in tandem rather than isolation, and they are often bundled together.

[24] Bertrand et al. (2006).
[25] Bertrand et al. (2006).
[26] McKenzie et al. (2006).
[27] Madrian and Shea (2001).
[28] Thaler and Benartzi (2004).
[29] Thaler and Benartzi (2004).
[30] Sherraden (1991); Sherraden et al. (2004).
[31] Sherraden et al. (2004).
[32] A detailed presentation of the institutional constructs that affect savings are included in Sherraden et al. (2004). These constructs include: (1) access; (2) information; (3) incentives; (4) facilitation; (5) expectations; (6) restrictions; and (7) security.

More relevant to this discussion is that these institutional characteristics are largely supported by public policies which encourage institutions in both the public and private sector to construct savings platforms; these platforms are best understood as savings plans.

Evidence abounds that savings does indeed work best when it is nested within a savings plan, such as a 401(k).[33] These plans encourage savings behavior in a variety of ways: they offer participants access to savings products and information, limited investment options, low-cost administrative fees, and direct deposit. The plan structure is also conducive to making sure that people allocate their contributions to investment vehicles that are appropriate to their stage of the lifecycle or risk-return profile. Individuals retain control over many decisions while participating in a plan, including how much to contribute and how it should be allocated, but once some of these decisions are made they can be carried out automatically until preferences change.

In sum, savings plans offer the best opportunity to establish default policies that can maximize savings performance. One of the characteristics of our current savings problem is that not enough Americans have access to them.

POLICY IMPLICATIONS

Any large scale savings policy which is designed to reverse America's savings decline should build on the power of default policies and savings plans. This has led many to support the enactment of more automatic enrollment of workers in their firm's 401(k) plans when offered. Scholars from the Brookings Institution have outlined additional design features that could increase savings, such as the automatic escalation of contributions over time and automatic investment in balanced, diversified, and low-cost index funds.[34]

It's certainly a good idea to establish a default policy where one has to "opt-out" of these savings plans, but it would be a great idea to ensure that everyone has access to this type of savings plan in the first place since about half of employers do not offer their employees access to a retirement plan.[35] The United Kingdom and New Zealand are currently taking just this approach, and pursuing reforms to their pension systems that would require employers to automatically enroll their employees in a voluntary pension plan that is designed to augment government-provided retirement benefits.[36] Earlier this year, the United Kingdom released a white paper detailing their intentions to support a system of personal accounts within a savings plan structure which would include automatic enrollment, the right to opt-out, and mandatory employer contributions equal to 3 percent of wages.[37]

In the U.S., an ambitious proposal has been made by Mark Iwry of the Brookings Institution and David John of the Heritage Foundation to dramatically expand private pension coverage by combining the employer payroll functions with the existing Individual Retirement Account (IRA) vehicle.[38] Their Automatic IRA proposal would offer employers a tax credit to offset the costs of making regular payroll deposit available to those employees who are not eligible for a plan.[39] These accounts would be supported by a savings plan structure and would potentially fill a large gap in retirement savings, particularly for households with fewer resources and lower incomes. Not only does this population often work for employers that do not offer retirement plans, but they are also unable to benefit from the many savings incentives, such as tax deferments for IRAs, Keogh Plans and employee pension plans.

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[33] Beshears et al. (2005), Madrian and Shea (2001), Choi et al. (2005), Thaler and Benartzi (2004).
[34] Gale et al. (2005).
[35] Iwry and John (2006) report that among the 153 million workers in 2004, over 71 million worked for an employer that did not offer a retirement plan, and another 17 million did not participate in their employer's plan.
[36] Iwry (2006).
[37] Department for Work and Pensions (2006).
[38] Iwry and John (2006).
[39] Iwry and John (2006).

While these policies and policy proposals recognize the need for ensuring that families have access to and are automatically included within savings plans, they focus on retirement savings and do not address the need for flexible savings. As part of their proposal to dramatically alter the tax treatment of savings, the Bush Administration has proposed creating a flexible savings account. These Lifetime Savings Accounts would provide tax-free earnings on contributions up to $5,000 a year which could be withdrawn for any purpose. This proposal, made in successive Budget proposals since 2003, has not received much Congressional support. Its ultimate impact would be regressive since the majority of benefits would accrue to higher income households that could use such accounts to shelter existing assets.[40] Still, the proposal is significant as one of the first proposals to direct public subsidies to support flexible savings not tied to retirement. One of the primary drawbacks of the LSA approach is that the accounts were not supported by a plan structure. In order to reserve our savings decline, we could establish a national savings plan that would serve as the ultimate default.

AUTOSAVE: MAKING SAVINGS AUTOMATIC AND FLEXIBLE

This national savings plan could be called AutoSave, and if it builds on what we have learned from recent research, it could make the process of savings easy, accessible, and productive. Here's how it would work.

AutoSave would serve as a universal savings plan for all workers and would use the power of money as well as direct deposit to maximize savings performance. Any employer that makes payroll deductions would be required to make deposits to the AutoSave system on behalf of their employees, and self-employed workers would be able to make deposits into the AutoSave system at their discretion. Working Americans would not be required to participate; they could opt-out if they choose. But workers would not have to elect to participate either. The AutoSave system would assume you are in unless you state a preference to get out.

Employers would shoulder no extra costs but would facilitate automatic deposits. This approach would build on the existing capacities of existing firms that use electronic fund transfers to manage their payroll and withhold taxes. Many firms currently employ third-party firms to perform these services. Any firm that withholds taxes would be required to make deposits to the AutoSave system on behalf of their employees.

Money deposited in this system would belong to the individuals and since deposits would be from after-tax dollars, normal tax rules apply. Each individual could withdraw funds whenever they want for any purpose, it's their money, and they will have the flexibility to opt-out of the system altogether at any time if they choose. A default contribution rate could be set at 2 percent of pay but can be changed by the employee at any time. At this rate, someone earning $50,000 a year would have $1,000 diverted directly into savings every year. Over time, steady contributions and sustained earnings would build up account balances. For example, maintaining this savings rate over ten years could produce, with modest returns, over $15,000 (or $45,000 if allowed to grow over twenty years). These funds could be tapped at any time, but AutoSave would be designed to take advantage of one of the most tried and true savings techniques—inertia.

Once money is placed into the AutoSave system, participants would have a range of investment choices. AutoSave would offer a limited set of low-cost investment options, such as index funds, which could be administered by professional money managers. Similar to many 401(k) plans and the government's own Thrift Savings Plan that it offers to its employees, these funds could track different sections of the market, such as the S&P 500, International markets, or small cap firms[41]. It would also include a lower risk fund tied to government

[40] Burman et al. (2003).

[41] The Thrift Savings Plan (TSP) is a government-sponsored retirement savings and investment plan, which offers the same type of savings and tax benefits that many private corporations offer their employees. The TSP was established by Congress in 1986 to provide retirement income; it is a defined contribution plan that accrues assets based on participant contributions and the financial performance of invested contributions.

bonds, as currently offered by the TreasuryDirect program which facilitates the electronic purchase of securities directly from the U.S. government.

Initially there may be restrictions on where smaller deposits are held but ultimately, individuals would have a choice about where their money is invested among these options. For those who don't actively choose, a default setting could be established so savings opportunities are not lost unnecessarily. What is most essential is that money is diverted automatically into the AutoSave system that would provide every working American access to a savings plan

For the individual, it would be advantageous to have access to a portable savings plan, not tied to the employer. Employers could, if they choose, educate their employees about the benefits of savings, how the system works, and even provide additional incentives to save. Since there would be a public benefit from increased savings, especially by workers with lower incomes, the public sector could support targeted incentives. For example, savers with low-incomes could be eligible for a match if they keep their money invested for an extended length of time. This innovative approach would reinforce savings behavior and provide additional resources to those that would benefit from building up their savings the most.

AutoSave would require that a centrally-administered account management system is created. There are many ways to design this type of system, with various roles filled by the private, non-profit and public sectors. These roles include an oversight and policy board, a rule maker, an account manager (holder), an investment manager, a record keeper, and a distributor of funds. Many of the divisions of responsibility could be worked out during an extended policy design process. But the ultimate goal of the policy is to construct a savings system that would accessible to all. Right now, many of our savings policies leave out large chunks of the population, whether they are those without employers that offer 401(k) plans or those without high enough incomes to take advantage of the associated tax preferences. If saving and asset building policies are to matter to those currently neglected, they must be made inclusive. This means policy must be delivered in the form of a savings plan, which offers features that can enhance savings behavior and investment performance, such as low-cost administration, outreach and education, diversified investments, and centralized accounting.

Key Features of AutoSave

- Automatic Participation in an Inclusive Savings Plan
- Freedom to Opt-Out of the Savings Plan
- Contributions via Direct Payroll Deductions
- Flexible Withdrawals to Meet Emergency and Other Needs
- Low-Cost Investment Choices
- Normal Tax Rules Apply

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

An array of detailed policy issues will need to be addressed to move this idea forward. These include:

- How to handle employers that do not use electronic payroll systems
- How fiduciary responsibility is handled
- Additional savings incentives that could be incorporated into the system
- Cost implications for constructing the system and supporting these additional savings incentives

The public sector is currently expanding its expertise in many of these areas. In addition to the Thrift Savings Plan, there is a growing body of experience associated with state-run 529 college savings plans. AutoSave could build on these valuables lessons. A well-designed AutoSave plan would strive to emulate the success of the Thrift Savings Plan, which meets its members' needs by combining investor choice with responsible stewardship, a combination from which more Americans would benefit

THE CASE FOR AUTOSAVE

While previous savings proposals have been developed in the context of promoting retirement security, the AutoSave plan focuses on pre-retirement savings because it is often the investments made throughout the life course that best enhance security during the retirement years. For some, AutoSave can be used to build up savings for key asset building purchases, such as buying a home, paying for an education, or starting a business. For others, the AutoSave system will provide a means to generate resources that can be drawn down at the discretion of each participant. This flexibility will be a valuable means to respond to an emergency, such as the loss of income or unexpected expense. The AutoSave plan is not designed to replace other retirement security policies, such as the call for access to a universal 401(k) savings plan, but for many households, waiting to deploy their savings until retirement may be too late.

Given the strains on the federal budget and the imperative to jumpstart a savings campaign, it makes sense to scrap the expensive and ineffective tax subsidies, remove asset tests for the poor, and replace them with a saving plan structure that is truly universal and accessible to all.

Too much attention in savings policy has been given to those in the upper reaches of the income scale, and this clearly has not served the public well. Citibank economist Ajay Kapur has coined the term plutonomy to explain how the very well-off are the drivers of economic demand and most likely responsible for the collapsing savings rate.[42] Over time he shows how the greater the share of income in the top 1 percent, the lower the savings rate has been.[43] This finding undermines the claims for extending tax cuts for wealthier households, since they appear inclined to just plow the savings into more consumption. A better approach to savings would be to restructure our public policies to promote real savings and ensure that benefits flow to those who actually save rather than just move assets around. The greatest bang-for-the-buck strategy will target those with fewer resources, as evidence shows this is the group that responds more readily to such inducements and are the households that would benefit the most from building up their stock of assets.[44]

Addressing our national savings problem will require an increase in the rate of savings at the household level, up and down the income scale. Given the current state of consumption in America and the powerful messages to increase it no matter what the costs, this appears unlikely to happen on its own. Americans know how to consume, but need to learn once again how to save. More than an educational campaign will be required. Rather than just telling Americans to save more, a flexible platform that facilitates the direct deposit of earnings into specific savings vehicles, making the process easy and accessible.

The key point is that everyone will benefit if we not only increase savings in the aggregate but raise the extent to which most American households save. Democratizing savings will provide a valuable pool of resources for working families and contribute to the national pool at the same time. The innovation of AutoSave is the establishment of just such a structure. It would not only provide an inclusive platform open to all working Americans, but would serve a giant teaching tool, highlighting the best practices for a revived savings nation.

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[42] Kapur (2006).
[43] Kapur (2006).
[44] Gale et al. (2006).

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