



## Improving Financial Security Through Emergency Savings

The Emergency Savings Act of 2022 (S. 4310) would facilitate convenient and affordable access to workplace short-term savings accounts that would improve financial security by promoting emergency savings and reducing retirement account leakage.

### ISSUE

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Americans need to increase their personal savings so that they are better positioned to handle emergencies and major purchases, as nearly 40% report they would struggle to cover an unplanned \$400 expense. Most workers have the option to put aside savings in a bank account of their own, but far too many fail to do so. Insufficient short-term savings can lead households to draw down their retirement savings prematurely and, in turn, incur costly taxes and penalties. While dipping into retirement savings might help address an immediate financial squeeze, it jeopardizes long-term financial security as Americans plan for retirement.

### SOLUTION

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Payroll-deduction emergency savings can provide relief. As a workplace benefit, these plans allow employees to select a portion of each paycheck to deposit into an emergency account, similar to and alongside their 401(k) election. But in the case of these accounts, workers can access the funds quickly and penalty-free at any time. Some employers have already begun offering short-term savings accounts on an opt-in basis, but participation remains low. Given the power of automatic enrollment in workplace retirement savings plans—which has shown to dramatically increase plan participation—lawmakers have an opportunity to replicate this successful policy to help workers save for short-term emergencies. Clearing barriers that currently prevent employers from automatically enrolling their employees in these accounts can provide an avenue for businesses to build financial resiliency within their workforce and help more American households prepare for the unexpected.

# POLICY

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The legislation would provide retirement plan sponsors (e.g., employers) the option to automatically enroll their workers into after-tax short-term savings accounts that would reside in the 401(k) alongside their tax-advantaged retirement account. Specifically, the bill would allow for automatic enrollment by clarifying rules around state wage garnishment laws, Know Your Customer requirements, and default investments. Employees could always opt out or withdraw their funds from the emergency savings account penalty-free at any time.

- Account balances could be funded by any combination of employee or employer contributions.
  - Plan sponsors could automatically enroll workers at up to 3% of pay. Participants could adjust those contributions at any time.
  - Employer contributions would be treated as compensation.
- Emergency savings accounts would have no minimum balance requirements, have a maximum account balance that does not exceed \$2,500 (after which contributions would stop or be invested in retirement savings), and be readily available to individuals with limited withdrawal restrictions. Plan sponsors could set lower maximum account balances.
- Employee contributions (up to the maximum account balance on an annual basis) would be considered elective deferrals, meaning that employers would be required to match those contributions into the retirement account in the same way as they would participant contributions to retirement accounts. This also means that increased participation would help employers with their 401(k) nondiscrimination testing.
- At the discretion of the plan sponsor, funds would either go into a simple interest-bearing account or an investment that prioritizes principal protection. Investment flexibility and account growth are not the purposes of these accounts.
- When switching jobs, participants could roll their emergency savings account into a Roth defined contribution account or a Roth IRA. This would encourage additional retirement savings and reduce leakage out of emergency savings accounts.
- Emergency savings accounts would be covered by a modified version of ERISA regulations with fewer requirements.

