



# As More Households Rent, How Can We Encourage Them to Save?

By David Abromowitz and Sarah Edelman September 10, 2014

When it comes to building wealth, renting in general tends not to be a good strategy for saving. Renter households in the United States have a median net worth—the total value of what a household owns, minus what it owes—of about \$5,100.<sup>1</sup> By contrast, households that own homes have a median net worth of more than \$170,000.<sup>2</sup> Even renters with incomes comparable to their homeowner counterparts make fewer financial investments and have significantly less wealth.<sup>3</sup>

In the wake of the housing crisis and subsequent recession, more people are renting rather than owning homes. In many jurisdictions, renting is even more expensive than owning. Yet when a homeowner remits a monthly mortgage payment to their lender, a portion of that payment builds equity in the home, which belongs to the homeowner. When a renter pays monthly rent to a landlord, that money is gone for good.<sup>4</sup> The absence of this “forced savings” of a mortgage payment is one of the reasons renting families have only a small fraction of the savings cushion available to most homeowners.

Traditionally, home equity has accounted for a significant share of family wealth, especially for low-income families and families of color. In 2010, home equity comprised 62 percent of household net worth among African American households and 67 percent among Latino households.<sup>5</sup> It is important to ensure that every qualified household has the opportunity to build assets through homeownership if they choose. It is also critical to make it easier for those who are not able or interested in pursuing homeownership to accumulate savings.

Especially in the face of stagnant wages, it is an ever-increasing challenge to help renter households save.<sup>6</sup> If America is to continue as a land of widespread economic opportunity, it is critical to find ways to enable families who are renting to build assets.

Indeed, there are already a few promising models to help renters accumulate savings while they pay their monthly rent. In this issue brief, we provide information about programs that provide renters the opportunity to save and build wealth offered through the federal government, a nonprofit organization, and a for-profit company. We also

provide a review of behavioral economics fundamentals to help inform the conversation about designing effective programs to put renters on a path toward financial security.

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## The challenges of building savings while renting

The most recent snapshot of American households shows that the median renter household has virtually no cash savings. According to Harvard’s Joint Center for Housing Studies, renters have median cash savings of \$630 and the median renter net worth, including all assets, is just \$5,100. For homeowners, the cash savings cushion is 10 times as large as that of renters—\$6,400—and median net worth is almost 35 times as much—\$173,010.<sup>7</sup> In short, most renter households have neither a personal safety net nor a way to build assets for the future.

It is not easy to isolate the individual factors that explain this correlation between renting and relatively low savings. One factor may be the high percentage of income that most families pay for rent. Half of renters pay more than 30 percent of their gross household income for their housing, which classifies them as “cost-burdened” by housing costs, and represents a 12 percent increase since 2001.<sup>8</sup> Twenty-eight percent of renters pay more than half their income toward having a place to live, a roughly 8 percent increase since 2001.<sup>9</sup> African American and Latino households face even steeper rent burdens than the population as a whole: 35 percent of African American households and 31 percent of Latino households spend more than half of their income on rent.<sup>10</sup>

For many of these households, paying rent competes with paying for other basic needs. According to one analysis, lower-income families in unaffordable housing units spend “a third less on food, half as much on pensions and retirement, half as much on clothes, and three-quarters less on healthcare as families paying affordable shares of their incomes for housing.”<sup>11</sup>

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## Creating savings opportunities for renters: Existing models and emerging approaches

For families that rent, a well-designed savings program can provide the means to buy a home, invest in a small business, or send a child to college. In many cases, having the ability to save means the difference between being able to financially weather a job loss, an illness, or even a major car repair, instead of going into debt to cover these types of unexpected costs.<sup>12</sup> Ultimately, having savings can make the difference between a financial setback being a small, navigable bump in the road versus a trigger for longer-term dependence on governmental social safety net programs.

Housing policy experts across the board have recognized the importance of savings for families that rent. The Aspen Institute created a proposal to create Home Accounts—savings accounts that would enable low- and moderate-income households to receive a government match of up to \$5,000 for a down payment on a home.<sup>13</sup> It is an approach that the Center for American Progress has supported in its own savings proposals.<sup>14</sup>

From the other side of the political spectrum, Joseph Gyourko, an adjunct scholar at the American Enterprise Institute, has proposed a savings program for aspiring homebuyers wherein the government would match, dollar for dollar, money set aside as savings until funds were amassed sufficient for a 10 percent down payment toward a house purchase.<sup>15</sup> Wall Street analyst Josh Rosner has recently called for such a program as well.<sup>16</sup>

While existing programs have not produced the reliable accumulation of assets that would significantly change the economic prospects of most renters, there are now some interesting efforts to move the needle by linking savings to a renter's monthly rent payments. Data from these programs will be extremely valuable in creating even more effective efforts in the future.

#### Federal: HUD's Family Self-Sufficiency program

Created by Congress in 1990,<sup>17</sup> the Department of Housing and Urban Development's, or HUD's, Family Self-Sufficiency, or FSS, program, is the largest and most well-known program using rent payments as a savings mechanism. Participants in FSS enter into a five-year agreement with their local public housing authority, or PHA. Most participants are holders of federal Housing Choice Vouchers, or HCVs, which pay the difference between 30 percent of a renter's monthly adjusted gross income and the market rent for a privately owned apartment. A smaller group of families living in public housing, where they pay 30 percent of their adjusted monthly gross income toward rent, participate as well.

Normally, when the income of a household receiving an HCV or living in public housing increases, so does the household's rent payment. Under the FSS program, however, while the renter pays a monthly amount commensurate with additional income, the actual rent payment remains the same while the newly added portion of the payment is set aside by the PHA in an escrow account. For example, if a renter's income rises by \$1,000 a year, the additional \$300 that would have gone toward rent instead goes into the savings escrow. Renters who complete the program, typically after five years, may then access the saved funds for any purpose.<sup>18</sup>

FSS has proven to be a powerful savings vehicle for many participating households. A 2011 HUD study of 181 FSS participants found that renters who graduated from the program ended up with, on average, more than \$5,000 in savings.<sup>19</sup> To complete the program successfully, a participant has to meet a set of pre-established program goals, including a requirement that the household is not receiving Temporary Assistance for Needy Families, or TANF, cash benefits and that the head of household maintain employment.

At the end of the four-year study, 24 percent of FSS participants graduated, 37 percent left the program without graduating, and 39 percent remained enrolled. According to HUD, most of the participants in the study who left the program early did so because they “did not comply with FSS rules or lost their voucher assistance ... [or] because family and work obligations made it difficult to sustain contact with the case manager.”<sup>20</sup> Administrative hurdles and socioeconomic challenges, such as a lack of good job opportunities, inadequate child care, and transportation problems, are the forces that most frequently undermined participants’ capacity to complete the program.<sup>21</sup>

Approximately 14 percent of public housing FSS graduates became homeowners after completing the program in 2011-2012.<sup>22</sup> Although households that exited the program forfeited their right to access the savings accumulating in escrow, these households, on average, had still each accumulated more than \$2,000 in theoretical savings.<sup>23</sup>

Due in large part to funding constraints, the FSS program has remained relatively modest in size.<sup>24</sup> According to HUD data reported by the Center for Housing Policy of the National Housing Conference,<sup>25</sup> there “were nearly 47,000 housing choice voucher-holders and more than 8,700 public housing renters participating in FSS as of March 2011” out of some 27 million renter households in the United States with annual income under \$50,000 at that time.<sup>26</sup> Nevertheless, the FSS program may be the largest rent-based savings program in the United States and has more than a 20-year history.

Overall, FSS data show a promising correlation between a savings mechanism linked to rent payment and notable increases in savings for lower-income households.<sup>27</sup> Bipartisan legislation was introduced in 2013 to expand the FSS program by streamlining administrative functions, providing more support services to better equip participants to succeed in the program, and allowing more families to participate. Unfortunately, the legislation has not advanced.<sup>28</sup>

### Nonprofit: Cornerstone Corporation for Shared Equity’s renter equity program

Cornerstone Corporation for Shared Equity, or CCSE, a nonprofit community development organization based in Cincinnati, Ohio, created an innovative renter equity system in 2000.<sup>29</sup> As described by CCSE: “Residents can earn up to \$4,137 in five years. After five years, residents are vested in the Cornerstone Renter Equity fund and can draw on their equity—with a maximum of \$10,000 being paid over 10 years.”<sup>30</sup>

Renters who enter a renter equity contract earn what is termed “equity credit” each time they fulfill one of the specified renter obligations.<sup>31</sup> After five years, renters can cash in their credits for any purpose. They have the flexibility to use their savings as they choose and can borrow against the earned credits even before the account is fully vested. CCSE allows participants to borrow up to one month’s rent at 0 percent interest in their first

year, which must be paid back over 12 months. They can borrow progressively more the longer they participate, up to a cap of 80 percent after five years.

CCSE acts as the owner and developer of the rental housing—offering third-party management as well—and the renter equity system is funded by management and development fees as well as foundation support. The renter equity partnership has contributed to high occupancy rates, with an average of 96 percent,<sup>32</sup> thereby cutting down on turnover costs for CCSE. Cornerstone’s property-management costs, even after considering the cost of the renter equity credits, are on par with similar Low-Income Housing Tax Credit properties in the community.<sup>33</sup>

In a recent independent study, the Corporation for Enterprise Development, a nonprofit helping moderate- and low-income families build assets, found both social and financial benefits associated with the renter equity program. The study concludes, “Cornerstone renters are earning equity and that participation in the property management system appears to have had a positive impact on renters’ lives in terms of their physical and financial security, their optimism about the future and their ties with the surrounding community.”<sup>34</sup>

The Cornerstone renter equity system so far has remained small, serving 51 renters in 2012.<sup>35</sup> Cornerstone’s unique approach offers renters the opportunity to build equity, live in affordable rental units with high-quality property management, and help make decisions about building management. Such an approach requires a well-trained and highly dedicated staff. With hopes of bringing this unique model to scale, Margery Spinney, the founder of CCSE, recently established an organization called Renting Partnerships to provide renters, developers, and property managers with the tools and support they need to effectively develop, administer, and sustain a renter equity exchange model.<sup>36</sup>

#### For-profit: Waypoint’s earning credit for paying rent

Waypoint Homes, or simply Waypoint, is a private real estate company active in buying and rehabilitating distressed single-family homes, many formerly foreclosed, and offering them for rent.<sup>37</sup> Waypoint promotes what it calls a Lease Plus Rewards program. This program gives renters the chance to earn so-called “Waypoints” for paying rent on time, keeping the unit well maintained, renewing their lease, and taking a financial literacy class.<sup>38</sup> They can then redeem these points for cash back. The program is open to Waypoint renters who have signed two-year leases with Waypoint, which currently represents about half of Waypoint’s residents.

Waypoint’s adoption of such a program suggests that for-profit landlords can realize positive economic benefits from a program that links rent payments to savings. Under the Waypoint program, the renter is not required to make any additional contribution

beyond paying full rent on time. Waypoint may have particular motivations to offer such a program due to its business focus on scattered-site, single-family rentals. For example, requiring participants to sign a lease for 24 months rather than the typical 12 months, Waypoint may be able to realize substantial costs savings through reducing vacancy periods. Waypoint also may benefit from branding their approach as “reinventing renting,” which may help attract both renters and investors.<sup>39</sup>

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## Designing an effective renter savings programs

Over the past 20 years, researchers in behavioral economics have explored in great detail the motivations for, and obstacles to, saving by consumers. While researchers do not agree on a single list of characteristics that savers share, this body of literature highlights factors that influence whether putting aside money is more or less likely to occur. These characteristics include future orientation, inertia, information, access to institutional opportunities, and sufficient financial resources. In particular, consumers are more likely to save—and to save more—when they have access to a structured savings plan that is easy to understand and where deposits occur automatically.

While a full review of the behavioral economics literature is beyond the scope of this issue brief, a few key points are useful in considering the design of an effective savings structure for renters.

### *Make saving automatic*

Current savings behavior tends to require the ability to visualize and plan for the future along with the willpower to stick to a savings program. Even for those with such skills, exigencies of daily life and circumstances often prevent or disrupt savings, particularly for households where income barely covers basic living expenses.

However, researchers show that the experience of starting a savings plan and accumulating even modest assets can help individuals change their behaviors or ways of thinking.<sup>40</sup> As they save, they become more confident about the future and develop a greater commitment to savings.

Savings practices may also be shaped by a degree of “inertia” in our behavior—that is to say, once a choice is made it requires a motivation to make a change.<sup>41</sup> For example, in one classic study, the university retirement plan TIAA-CREF found that when employees were automatically enrolled in a savings plan and had to “opt-out” to stop saving, participation rates of new employees increased from 49 percent to 86 percent.<sup>42</sup>

### *Matched-savings programs can make saving more productive*

Not surprisingly, research shows that when there are tangible, short-term financial rewards for saving, saving becomes more attractive to consumers.<sup>43</sup> Matched-savings programs

offered through employers, local governments, and nonprofits, for example, have grown in popularity over the past decade and some programs have had stellar results. Matched-savings programs typically combine monetary savings incentives and financial education to help households set and meet savings goals. While no comprehensive study exists to show the nationwide footprint of matched-savings programs, millions of Americans of all income levels already benefit from matching programs.<sup>44</sup>

#### *Consumers are more likely to use easy-to-use programs*

In a study of a program operated by the mega tax preparation firm H&R Block that offers matches of individual retirement account, or IRA, contributions to tax filers, researchers found that a user-friendly and easy-to-understand program is more likely to resonate with consumers.<sup>45</sup> In that study, consumers chose the IRA-matching program at far greater rates than the Saver's Credit—a tax credit for low- and moderate-income taxpayers who make retirement contributions to an IRA, 401(k), or any other government-recognized retirement account—even though the Saver's Credit offered a more generous financial incentive, because the match was available to virtually all tax filers and was simpler.<sup>46</sup> The study points to the value of clear messaging and the importance of having a professional walk the consumer through the program. The Cornerstone program described in the previous section also shows the benefit of continually engaging with participants to encourage savings.

#### *Consumers may save more when they experience short-term rewards for saving*

Researchers at the University of North Carolina at Chapel Hill Center for Community Capital studied participation rates in the \$aveNYC program, a matched-savings program offered to low-income New Yorkers, and determined rewarding behavior sooner rather than later may help increase participation. According to the study, \$aveNYC was highly effective: about 70 percent of participants successfully completed the one-year program in 2010 with average savings contribution of \$700.<sup>47</sup> The researchers found that as participants neared the one-year completion date, their risk for withdrawing from the program decreased.<sup>48</sup> They said the finding suggests that participants are more likely to stay in the program when their goal is in sight and therefore might be more likely to stay in the program longer if there are opportunities for shorter-term savings' goals.

The four insights described above strongly suggest that it is worth exploring the feasibility of a program in which landlords match a deposit into savings made by a renter as part of an automatic monthly rent payment. But what would provide an incentive for landlords to make a matching payment? For some, it might be enough that such a program require the renter to make this automatic payment, as that will enable the landlord to receive the rent on time and electronically. Or, if the renter were allowed to access the account for short-term emergencies, it could help decrease the likelihood of failure to pay rent. It is also possible that the government at the local, state, or federal level could provide tax incentives to the landlord or even provide the savings match.

Key to any effective program would be assurances that landlords will not raise the monthly rent in order to cover the cost of the savings contribution. Additionally, strong consumer protections would have to be in place to ensure that the new savings initiatives are safe and reliable for consumers. Other questions that arise include whether to make such a program available only to renters below a certain income level, and whether some type of special savings account would need to be created. If there were to be a federal or state match, there is the question of whether the program could work with existing savings programs such as individual development accounts, or IDAs, or the federal Saver's Credit, or whether new savings vehicles would be needed.

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## Conclusion

As more families rent rather than own homes, it is critical to ramp up the policy discussion about how to make it easier for renters to build wealth. There are promising renter savings programs underway that deserve greater attention and further development from Congress, agencies, states and localities, and landlords themselves. To be effective, a renter savings program should employ as many as possible of the features that tend to increase savings, including an automatic contribution, simple design, matching or other financial incentives, and ongoing support for participants.

More research is needed to understand the long-term economic benefit of existing programs. Moreover, additional research is needed to determine whether and how to bring renter savings programs to scale. A small matched-savings pilot among renters living in buildings managed by for-profit landlords might be one way to help us better understand the benefits of this approach—including the property-management cost savings such a program might yield—and the challenges.

Creating a system to boost savings among renters is an essential part of creating a stable and financially secure middle class. The good news is that some work is already underway to provide low- and middle-income families with savings tools. If our nation is to make any headway in the widening gap between rich and poor, communities and policymakers must redouble these efforts.

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## Endnotes

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