NEW Research

Improving the Saver’s Credit for Low- and Moderate-Income Workers

Webinar
October 12, 2017
Agenda

• Introductions
• Research Review
• Q&A
Webinar Logistics

- Attendees in listen only mode.
- Research, supporting materials at nirsonline.org.
- Questions welcome. Type question using “Question” function on control panel, and we will answer.
- Encourage distribution of information: @nirsonline #saverscredit
- Audio, technical issues during webinar, please call contact GoToWebinar at 1-800-263-6317.
- Recording & replay of webinar will be available.
Speakers

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Manager of Research
National Institute on Retirement Security

David C. John
Senior Strategic Policy Advisor
AARP
Why This Study?

- Saver’s Credit designed to incentivize retirement savings for low-to moderate-income workers.

- But, millions of low-to moderate-income individuals have been unable to use the credit, leaving the credit underutilized.

- Saver’s Credit should be improved to increase utilization and increase retirement security for workers.
Key Findings

1. Millions of low- & moderate-income workers unable to use Credit.

2. Credit is underutilized, even among those eligible to claim it.

3. Retirement plan coverage is key factor in Credit’s underutilization.

4. A series of changes would enable more of the credit’s target population to benefit from the Credit and build retirement savings.
Saver’s Credit: Background

• Due to the nature of the tax code, the distribution of retirement benefits is tilted towards higher earners.

• In 2001, as a way to level the playing field, Congress created the Saver’s Credit – a tax credit designed to encourage low- and moderate-income workers to saver for retirement.
Improving the Saver’s Credit for Low-and Moderate-Income Workers

Enacted in 2001, the Elective Deferrals and IRA Contributions by Certain Individuals tax credit is commonly referred to as the Saver’s Credit. As displayed in Table 1, Taxpayers with yearly incomes of less than $31,000 for single filers and $62,000 for married filers in 2017 can claim a credit of up to $1,000 for contributions to a qualified retirement plan or individual retirement account (IRA) if they have a tax liability.

As currently structured, the Saver’s Credit provides taxpayers who fall within its income limits with tax credits equal to 50 percent, 20 percent, or 10 percent on up to $2,000 of the amount individuals saved in a qualifying retirement account.

Taxpayers filing married or joint returns in 2017 with adjusted gross incomes under $37,000 a year can qualify for a 50 percent tax credit, while those with incomes between $37,001 and $40,000 a year qualify for a 20 percent credit, and those with incomes between $40,001 and $62,000 a year qualify for a 10 percent credit.

The Saver’s Credit evolved from a series of efforts in the late 1990s to expand retirement plan coverage among low- and moderate-income workers and to distribute tax-preferred retirement benefits more evenly along the income scale. It was first proposed in 2000, when the Treasury Department designed a refundable tax credit for low- and moderate-income savers earning at least $5,000 a year who contributed to a qualified defined contribution retirement savings account or a defined benefit pension plan. This expansive tax credit was designed to act like a matching contribution to the retirement account, and income-eligible workers would get the credit regardless of income tax liability (a refundable tax credit). In 2000, the Treasury Department estimated the proposal to cost $54 billion in tax revenue over 10 years.

Concerned by the potential cost of the proposal, as part of the Economic Growth and Tax Relief Reconciliation Act of 2001, Congress passed a nonrefundable version of the Saver’s Credit that was estimated to cost $10 billion in tax revenue. Initially, the credit was temporary and was to expire after five years. In addition, eligibility was based on income limits that were not indexed for inflation. Both of those features were changed by a provision in the Pension Protection Act of 2006 (PPA).

In spite of the legislation’s intended purpose, millions of low-to moderate-income people have been unable to use or have had to give up the credit.

Table 1: 2017 Saver’s Credit Income Eligibility and Credit Rates

<table>
<thead>
<tr>
<th>Credit Rate</th>
<th>Married Filing Jointly</th>
<th>Head of Household</th>
<th>All Other Filers*</th>
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<tbody>
<tr>
<td>50% of your contribution</td>
<td>AGI not more than $37,000</td>
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<td>more than $62,000</td>
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Source: Internal Revenue Service
Improving the Saver’s Credit for Low-and Moderate-Income Workers

B. Make It Easier To Claim The Saver’s Credit

Changes to the existing filing requirements would provide another opportunity for reform that could improve usability and ultimately foster more savings. Today, low- to moderate-income individuals and families must jump through two hoops in order to file for the Saver’s Credit. These two hoops are not required for other tax credits that target the same population. First, they must file a “long-form” 1040 or 1040A form—they cannot file a 1040EZ form. Second, they must also complete a Form 8880, which requires the filer to record the total amount of distributions received from his or her retirement plans for the prior three years.

In order to best assist low- and moderate-income taxpayers, the most important reform would be to allow eligible taxpayers to claim the Saver’s Credit on the 1040EZ form. Regardless of what other changes are made, this is an essential step toward increasing the number of eligible taxpayers who can claim the credit. A second important step would be to require the IRS to make the credit’s availability more prominent on all relevant tax forms. Additionally, employers that offer a retirement savings plan should include prominent information on the Saver’s Credit and its eligibility standards when employees sign up for the plan or are automatically enrolled in it.

Compared with filing for the Earned Income Tax Credit (EITC), which is also designed to benefit low- and moderate-income individuals, filing for the Saver’s Credit is significantly more complicated for a much smaller tax credit value. The EITC does not require the use of a long-form 1040 or 1040A and allows the individual to claim that credit using a 1040EZ. In addition, the EITC only requires taxpayers to file a short six-question worksheet rather than a separate form, with no look-back to previous years’ income required. Given these hoops, it is not surprising that in 2014, while 15.04 percent of taxpayers who were income eligible led for the EITC, only 5.33 percent of taxpayers who were income eligible led for the Saver’s Credit.

In order to improve utilization of the Saver’s Credit, its filing requirements should more closely mirror those of the EITC. In addition to being able to claim the Saver’s Credit on the 1040EZ form, individuals wishing to file for the Saver’s Credit should be able to complete a simple worksheet that asks their income, filing status, and retirement contributions and recent withdrawals in order to calculate their credit. By eliminating these hoops, many more individuals will be able to claim the Saver’s Credit and will be incentivized to save more for retirement.

Previously discussed features of the new mechanism, meanwhile, would eliminate the need for Form 8880, which includes information on withdrawals from retirement savings plans and is designed to prevent taxpayers from claiming the credit and then promptly withdrawing the qualifying savings. As discussed above, the need for such a look-back requirement could be eliminated if the Saver’s Credit were deposited directly into the retirement account and taxpayers were prevented from withdrawing it until a set age. Using a worksheet or having the credit directly deposited to the retirement account would serve as a substitute for the filing of Form 8880. The same type of withdrawal restrictions could also be imposed on personal contributions used to qualify for the Saver’s Credit, either permanently or for a set minimum period of time.

You are Eligible for the Saver’s Credit if:

- Age 18 and over
- Not a full-time student
- Are not claimed as a dependent on another filer’s return
- Make less than $31,000 if single, or $62,000 if married
- Make a retirement contribution to an Individual Retirement Account (IRA), 401(k), 403, or 457 plan.
- File a Federal Form 1040 or 1040A U.S. Individual Income Tax Return

Current Steps in Claiming the Saver’s Credit

1. **Save for Retirement.** Contribute to an IRA or a 401(k), 403(b), or 457 plan.

2. **Confirm You are Eligible: Income and Status.** You must make less than $62,000 if married and $31,000 if single.

3. **Prepare and File Your Taxes Using a “Long-Form” 1040 or 1040A.**

4. **Complete a Form 8880 to Calculate Amount of Saver’s Credit.**
Finding #1: Millions Of Low- And Moderate-Income Workers Are Unable To Use The Saver’s Credit

- Reasons include:
  - failure to contribute to a qualified retirement plan;
  - failure to file for the credit; or
  - insufficient tax liability

- These shortcomings, combined with a general lack of awareness of the credit among taxpayers, severely limits its use.
Finding #2: Saver’s Credit Underutilized, Even Among Those Who Are Eligible To Claim It

Figure 1: Percent of Returns Eligible Compared with Returns that Actually Claimed the Saver’s Credit, 2008 to 2013 Tax Years

Authors’ calculations provided by data from the Internal Revenue Service, Statistics of Income Division.
Finding #2: Saver’s Credit Underutilized, Even Among Those Who Are Eligible To Claim It

Figure 2: Average Amount of the Saver’s Credit, 2007 to 2014 Tax Years

Authors’ calculations provided by data from the Internal Revenue Service, Statistics of Income Division.
Finding #3: Retirement Plan Coverage Is A Key Factor In The Credit’s Underutilization

- A key reason for underutilization is that many low- to moderate-income taxpayers do not make a contribution to a retirement savings plan, because they are not offered one by their employer through payroll deduction.

Percent of Private Sector Workers with Access to a Retirement Plan

Finding #3: Retirement Plan Coverage Is A Key Factor In The Credit’s Underutilization

• About 55 million workers between the ages of 18-64 lack access to an employer-sponsored retirement plan.

• Younger workers and minorities are most likely to work for an employer without a plan.
Finding #3: Retirement Plan Coverage Is A Key Factor In The Credit’s Underutilization

- Small business employees are especially at risk.

Percent of Employees with Access to an Employer Sponsored Plan

<table>
<thead>
<tr>
<th>Employer Type</th>
<th>Percent of Employees with Access</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employers with more than 100 employees</td>
<td>50.7%</td>
</tr>
<tr>
<td>Employers with 100 or fewer employees</td>
<td>49.3%</td>
</tr>
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Typical Small Business Employee Not Covered by a Plan

- Female
- Under 40
- A person of color
- Low and middle-income
- Single, not married

Source: NIRS analysis of U.S. Census Bureau’s Survey of Income and Program Participation 2008 Panel, Wave 11. (January 2012 - March 2012), universe limited to private, for-profit employees, aged 21-64.
Finding #4: A Series Of Changes Would Enable More To Benefit From The Credit And Build Savings

- As currently structured the Credit does not adequately help the low- and moderate-income individuals it was designed to assist. However, changes would enable more of the Credit’s population to benefit and build more retirement savings.

- The changes include:
  1. Making the Saver’s Credit a savings match;
  2. Making the Credit easier to claim;
  3. Increase eligibility to claim the Credit;
  4. Replacing cliff income limits with a gradual phase-out;
  5. Creating state tax benefits similar to the Credit.
Proposal A: Make the Saver’s Credit A Savings Match

- Eligible savers would receive a match equal to 50 percent of the amount they contributed during that tax year.

- It would be claimed through their tax return and would go directly into their retirement savings account.

- The match would remain in the account until the saver reaches retirement age.

- The match would phase out gradually for higher incomes.
Proposal A: Make the Saver’s Credit A Savings Match – A Case Study

- WISER developed the Appalachian Savings Project in Ohio and West Virginia.

- The Project simulated a refundable Saver’s Credit by providing participants with a 50% savings match.
Proposal B: Make It Easier To Claim The Saver’s Credit

• Filers must jump through two hoops to file for the Credit
  1. Must file a long-form 1040 or 1040A
  2. Must complete Form 8880, which requires a look-back of three years.

• We should allow filers to claim the Credit on the 1040EZ form.

• We should mirror the filing requirements of the EITC, eliminating the Form 8880 filing and lookback, and allow individuals to complete a worksheet to file for the Credit.
Proposal C: Increase The Percentage Of Workers Who Are Eligible To Receive The Credit

- Increase income limits so more people would be eligible for Credit.

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Source: Internal Revenue Service
Proposal D: Replace Cliff Income Limits With Gradual Phase-Out Of The Credit

- We should replace the three levels of credit based on exact-dollar income limits with one level that is phased out gradually.

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Source: Internal Revenue Service
Proposal E: Further Publicize The Saver’s Credit

• State-sponsored retirement savings plans for small businesses will increase the opportunity for a greater number of eligible save to file for the Saver’s Credit.

• All states should provide information to participants.
Proposal F: Create State Tax Benefits Similar To The Federal Tax Credit

- States could create additional tax benefits that would be both on top of the federal Saver’s Credit and linked to it such as:
  
  $ 529 college savings plans

- Maryland’s Long-Term Care Credit

- Indiana’s Unified Tax Credit for the Elderly

- Massachusetts’ Real Estate Tax Credit

- Montana’s Elderly Homeowner/Renter Credit
Conclusions

• Existing Saver’s Credit could do a better job helping the target population.

• Number of changes – especially matching – can increase Saver’s Credit’s utilization.

• Increased use of Saver’s Credit can increase savings and thus, reduce potential future costs of the states and the federal government.
Fact Sheet

How the Saver’s Tax Credit Can Boost Your Retirement Savings

The average retirement benefit from Social Security may not be enough to pay for your expenses during retirement. The federal government encourages low-income earners to save for retirement through a tax credit called the Saver’s Credit. It is a non-refundable tax credit for individuals who make under $30,750 or married couples who make under $61,500 a year. Only 25 percent of those eligible for the Saver’s Credit based on their income take advantage of the credit.

How Does the Saver’s Credit Work?

The Saver’s Credit can reduce the amount of taxes you owe by 10% of the federal government tax you save for retirement. Individuals who make less than $30,750 a year, and who save for retirement, can receive a credit of up to $1,000 on their federal income taxes. Married couples who file together and make less than $61,500 a year, can receive up to $2,000 tax credit on their federal income taxes. The Saver’s Credit can be worth 10 to 50 percent of the amount that you saved for retirement during the year. See the chart at the bottom of the page to find out how much your credit can be.

In order to be eligible for the Saver’s Credit, you or your spouse must contribute to a retirement plan and meet other requirements. See the checklist at the right for a list of other requirements and which retirement plans are eligible.

The Credit is non-refundable, meaning that it can only decrease the amount of federal taxes that you owe and cannot provide a refund. However, the Saver’s Credit can be combined with other tax credits that can provide a refund, such as the Earned Income Tax Credit (EITC).

2016 SAVERS CREDIT

<table>
<thead>
<tr>
<th>CREDIT RATE</th>
<th>MARRIED FILING JOINTLY</th>
<th>HEAD OF HOUSEHOLD</th>
<th>SINGLE</th>
</tr>
</thead>
<tbody>
<tr>
<td>50% of your contribution</td>
<td>Income is less than $15,000</td>
<td>Income is less than $12,775</td>
<td>Income is less than $18,750</td>
</tr>
<tr>
<td>20% of your contribution</td>
<td>$15,001 – $30,000</td>
<td>$12,776 – $30,000</td>
<td>$18,751 – $42,000</td>
</tr>
<tr>
<td>10% of your contribution</td>
<td>$30,001 – $45,000</td>
<td>$30,001 – $46,125</td>
<td>$42,001 – $54,000</td>
</tr>
<tr>
<td>1% of your contribution</td>
<td>more than $45,000</td>
<td>more than $46,125</td>
<td>more than $54,000</td>
</tr>
</tbody>
</table>

Meet Tanya

Tanya is a single administrative assistant working in California who makes $25,000 a year. She contributes $1,250 or 5% of her salary to an IRA.

Because her income is over $20,000 the chart on the first page indicates Tanya will receive a 10% credit or $125 in other federal income taxes when she files for the Saver’s Credit because of her retirement contribution.

Meet Luis and Christina

Luis and Christina are married and file their taxes together. Luis is a plumber in Maryland and earns $15,000 a year. Christina is not employed.

Luis contributes $1,500 to an IRA.

The chart on the first page tells us Luis and Christina could receive a 50% tax credit or $750 because of Luis’s IRA contribution when they file for the Saver’s Credit on their federal tax form.

Meet Aiden and Mia

Aiden and Mia file their taxes together and have two children. Together, their income is $30,000. Mia is a private school teacher and Aiden works part-time.

Mia contributed $1,000 to a retirement savings account through work, which makes Mia eligible for up to 50% of $450 Saver’s Credit, and the couple has a $6,438 credit from the EITC. They owe $108 in taxes and can claim the Additional Child Tax Credit.

By following the SAVERS Credit to the S40 in taxes that they owe, they reduce taxes to zero. Now their full $1,000 Saver’s Credit is paid to Mia and Aiden as refunds because it isn’t reduced by the IAS in taxes that they owed.

2016 Taxes Owed

Adjusted Savings Credit + S40 = S400

10% EITC = $6,438

Mia and Aiden’s REDUCED = $6,548

How to File for the Saver’s Credit

1. Save for Retirement. Contribute to a retirement plan! See the Requirements of the Saver’s Credit on page one for eligible plan types.

2. Confirm your Income. In order to claim the Saver’s Credit, you must make less than $61,500 if married and $30,750 if single.

3. Prepare your Taxes. Consider using a tax preparer such as VITA or AARP to assist you in preparing your taxes.

4. File a “Long-Form” 1040. To take advantage of the Saver’s Credit, you must file the use the Form 1040 or 1040A. You cannot use Form 1040EZ.

5. File a Form 8880. You will need to fill out and file this form to calculate the amount of the Saver’s Credit.
Questions?

National Institute on Retirement Security
www.nirsonline.org