

# The missing link

Bringing emergency savings solutions to retirement plans

**With the passage of SECURE 2.0, new in-plan emergency savings solutions are on the horizon. What have the past five years of research taught us about the connection between short-term and long-term financial security? And how can 401(k) plans benefit from lessons learned?**

It was the shot heard round the financial security world. In 2017, a Federal Reserve report found that four in 10 Americans couldn't cover an unexpected \$400 expense<sup>1</sup> (Figure 1). In the years that followed, several organizations – including [BlackRock's Emergency Savings Initiative](#) – mobilized to identify the tools and opportunities people can use to help set aside money for the future.

**Figure 1: Americans struggle to cover emergency expenses**  
% with a savings buffer <\$400

All Americans	<b>39%</b>
Low-to-moderate income (LMI) households	<b>58%</b>
Hispanic LMI households	<b>70%</b>
Black LMI households	<b>72%</b>

Sources: Federal Reserve, Report on the Economic Well-Being of U.S. Households in 2017, 2018 and Commonwealth, Addressing Inequity.

Today, it's widely acknowledged that having a liquid savings buffer can help individuals stay on track for longer-term, retirement saving. After all, it's hard to save for tomorrow if you're worried about making ends meet today. The pandemic made that especially clear, and it's something policymakers are taking seriously, as evidenced by the inclusion of the Emergency Savings Act of 2022 in SECURE 2.0 – which would allow for in-plan emergency savings programs, as well as an employer match on workers' emergency savings contributions.

With the possibility of new in-plan emergency savings solutions on the horizon, we wanted to know:

**Just how big a buffer is needed to insulate long-term, retirement savings from short-term spending needs?**

**What is the risk that emergency savings “cannibalize” retirement plan contributions?**

**What best practices from emergency savings studies can be applied to retirement savings?**



**Robert Crothers**  
Head of Retirement Product & Strategy



**KC Boas**  
Head of Retirement Marketing

<sup>1</sup> Federal Reserve, Report on the Economic Well-Being of U.S. Households in 2017, 2018.

## What's the threshold?

The share of 401(k) participants taking loans or hardship withdrawals — about one in five in the past year<sup>2</sup> — has been in the headlines. It's hardly surprising, as rising inflation and interest rates have made it harder to keep up with the cost of living and more expensive to borrow money.

Research from Voya, as part of BlackRock's Emergency Savings Initiative, found that participants with inadequate emergency funds are 13 times more likely to take a hardship withdrawal than those with adequate savings.<sup>3</sup> The research is clear on this point: When people have a liquid savings pot that they can draw from to cover immediate expenses, they are less likely to raid their 401(k).

But the question of "how big a buffer people need" has been harder to answer. One study found that low-income households with at least \$1,000 in emergency savings were half as likely to draw on their workplace retirement

account to cover an emergency expense.<sup>4</sup> Another study — one funded by BlackRock's Emergency Savings Initiative — suggested that the figure is at least twice as high.<sup>5</sup>

Another way to approach this question would be to look at the size of hardship withdrawals people take. Bank of America's new 401(k) Participant Pulse report shows that the average participant hardship amount was \$4,700 (for the same period).<sup>6</sup>

Obviously, \$4,700 is significantly different than the suggested buffer of \$1,000 — \$2,000. Of course, \$4,700 is an average — and we'd be keen to see the median. It would also be useful to see the full distribution, cut by income level, as the \$1,000 — \$2,000 study was focused specifically on low-to-moderate income earners.

Still, when we consider that the number one reason cited for taking a hardship withdrawal is to pay off a credit card bill or debt,<sup>7</sup> it's clear that the link between short-term financial stability and long-term saving cannot be ignored.

## What's in SECURE 2.0?

When it comes to emergency savings, SECURE 2.0 has two main provisions: sidecar accounts and withdrawals. Both provisions are optional (can be offered at the discretion of the plan sponsor) and go into effect in 2024.

### What's a sidecar?

- Roth (after-tax) account that is tied to participant retirement accounts
- Contributions capped at \$2,500 (though asset earnings can exceed \$2,500) and count towards annual deferral limits
- May be invested in cash, interest bearing deposit accounts, and principal-protected assets
- Allows employers to auto-enroll participants at a contribution rate of up to 3%

- Withdrawals must be allowed at least once a month — at no charge for the first four withdrawals (after which, the participant may be charged a reasonable fee for subsequent withdrawals)
- Allows for a company match — which has to go straight into the retirement account (not the sidecar)

### What's changing with withdrawal rules?

- Participants would be allowed to withdraw up to \$1,000 a year from their retirement account for emergency purposes
- This must be repaid within 3 years before a subsequent withdrawal

<sup>2</sup> EBRI, "2023 Retirement Confidence Survey," 2023.

<sup>3</sup> Voya Financial, "Retirement at Risk: Building Financial Resiliency With an Emergency Savings Fund," 2021.

<sup>4</sup> DCI Retirement Research Center & Commonwealth, "Emergency Savings Features That Work for Employees Earning Low to Moderate Incomes," 2021.

<sup>5</sup> Workers with significant emergency savings (>\$2,000) are half as likely to tap into retirement savings. DCI Retirement Research Center & Commonwealth, "Research Conducted Over Last 18 Months Highlights Key Role of Recordkeepers in Employee Emergency Savings," 2021.

<sup>6</sup> Report tracks more than 3 million 401(k) plan participants. Bank of America, "401(k) Participant Pulse," 2023.

<sup>7</sup> EBRI, "2023 Retirement Confidence Survey," 2023.

## Are we trading one problem for another?

Healthy skepticism would lead one to wonder: If money is tight, does an emergency savings program discourage or decrease employee contributions to traditional retirement accounts? If so, it could leave people worse off by sabotaging their ability to take advantage of compounding. Over the past four years, BlackRock's Emergency Savings Initiative has sought to investigate this very concern.

The Initiative first considered worker preferences. In recent years, employers have seen increased demand for workplace benefits, including tools to manage financial goals now and in the future. In fact, one study found that nearly a third of individuals would be more likely to start contributing (or contribute more) to a retirement account if it was paired with an emergency savings option.<sup>8</sup>

The Initiative also launched pilot programs, designed to test this theory. UPS, which converted its 401(k) after-tax option into an emergency savings solution, was a prime example. In this case, employees who increased their after-tax contribution rate (for emergency savings) were about twice as likely to also have increased their pre-tax contribution rate (for retirement).<sup>9</sup>

Across the pond, the research organization NEST Insight partnered with UK employers to introduce an emergency savings program that linked directly to payroll. One group was offered an automatic version of the program (with the ability to opt-out), while the other group was presented with a version of the program that required them to opt in. In both groups, participation rates in the traditional retirement plan held steady.<sup>10</sup>

## What can we adapt?

Looking across the 43 projects led by the Initiative, there are at least three relevant takeaways for retirement plans.

First, emergency savings programs and traditional retirement plans can pair well together. Across the various experiments, we found that those with emergency savings were more than 70% more likely to contribute to their retirement plan.<sup>11</sup>

Second, auto-features remain tried and true. Across the board, interventions that were automatic (opt-out) saw a median uptake rate that was four times higher than interventions in which people had to proactively take action to start saving.<sup>12</sup>

Third, timing matters — when it comes to behavioral nudges. In a paycheck-splitting experiment (workers could choose to divert part of their paycheck to an emergency savings fund), we tested the relative impact of receiving a reminder notification three days before payday, on payday (but for their next paycheck), and not at all. The results underscored that nudges have a powerful effect. Those who received the early reminder were 4 times more likely to turn on the feature than the control group; and those who received a day-of reminder were 3.4 times more likely to participate.

As the emergency savings provisions of SECURE 2.0 go into effect, employers will have the option to provide new opportunities for employees to save — for today and tomorrow. In navigating this new frontier, employers may want to consider the body of research that exists around these programs. For a more in-depth look at case studies and findings, refer to the [Emergency Savings Initiative Impact and Learnings Report](#).

<sup>8</sup> Commonwealth and SaverLife, "Low-to Moderate-income Household Perceptions on the Relationship Between Emergency Savings and Retirement Savings," 2022.

<sup>9</sup> Versus those who made no changes. BlackRock, "BlackRock's Emergency Savings Initiative Impact and Learning Report 2019-2022," 2023.

<sup>10</sup> Nest Insight, "Does Payroll Autosave Support Employees to Get Started with Saving?" 2022.

<sup>11</sup> DCIIRA Retirement Research Center & Commonwealth, "Emergency Savings Features That Work for Employees Earning Low to Moderate Incomes," 2021.

<sup>12</sup> 43% versus just 10%. BlackRock, "BlackRock's Emergency Savings Initiative Impact and Learning Report 2019-2022," 2023.

## Another note from abroad...

In the UK, BlackRock funded a separate, four-year pilot program with NEST Insight, a UK public benefit research unit set up by the Nest pension scheme to find ways to support low-to-moderate income workers to be financially secure today and into retirement. Called “Jars,” the savings tool added a linked rainy-day account to a retirement account. People had to opt-in to begin saving in the rainy-day account and any amount in excess then went to the retirement account.

While it was offered to 80,000 workers across the UK, only 1-2% elected to sign up. Among those who did opt-in, however, the median emergency savings balance had reached £384 — or nearly \$500 — within the first year. Given the difficulty many Americans would face in coping with a \$400 emergency expense (see above), the impact of this program is powerful. Still, the uptake was quite small — an important reminder of the effectiveness of auto-features.

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