Investment Company Research – IRC Inc.

# IRAs in Americans' Retirement Preparedness

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## The Role of IRAs in Americans' Retirement Preparedness

### Key Findings

- **IRAs and employer-sponsored retirement plans are the two main types of tax-advantaged savings vehicles available to Americans:** About 70 percent of American households either have retirement plans through work or own IRAs.

- **Households that invest in IRAs can accumulate sizeable balances in these accounts:** In 2011, households that owned IRAs for 10 or more years and contributed to them in tax-year 2010 had average IRA assets of $148,000. By comparison, three-quarters of all U.S. households had total household financial assets of less than $126,000 in 2008.

- **Despite the boost IRAs can give to retirement savings, the majority of U.S. households currently do not take advantage of them:** Only 38 percent of U.S. households own IRAs. Furthermore, most households do not make annual contributions to IRAs. Less than two out of every 10 U.S. households contributed to IRAs in tax-year 2010, and very few eligible households made "catch-up" contributions.

### Retirement Savings is a Primary Financial Goal for Americans

Americans frequently rank preparing for retirement as one of their primary financial goals.1 In the United States, two main types of formal retirement savings arrangements are available to help individuals and families attain that goal: Individual Retirement Accounts (IRAs) and employer-sponsored retirement plans, which include traditional pension plans as well as defined contribution plans, such as 401(k) and 403(b) plans. This issue of *Fundamentals* summarizes the results of an ICR survey of Americans' use of IRAs.

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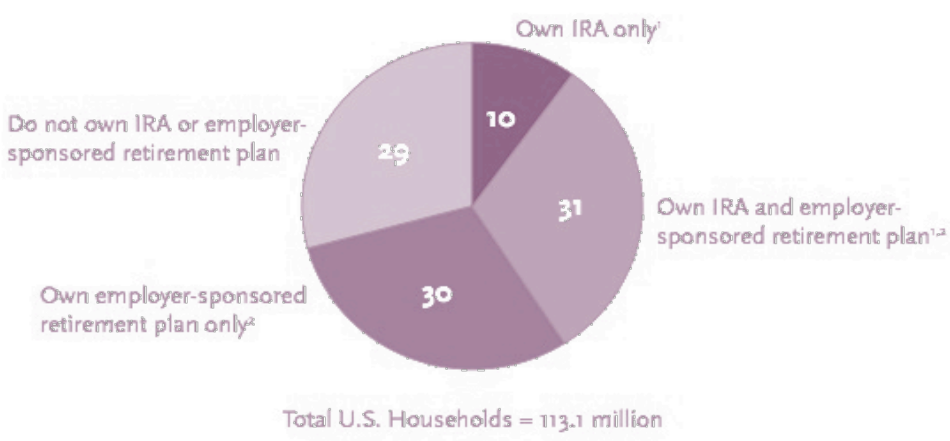
## About Four in 10 Households Own IRAs

About 70 percent of all U.S. households have some type of formal, tax-advantaged retirement savings (Figure 1). More than 60 percent have employer- sponsored retirement plans. Only 41 percent, or 46.8 million U.S. households, own IRAs (Figure 2), even though most households are eligible to make contributions to them. Households most frequently own traditional IRAs—the first type of IRA created by Congress. Roth IRAs are the second most frequently owned type of IRA, followed by employer-sponsored IRAs, which include SIMPLE IRAs, SEP IRAs, and SAR- SEP IRAs.

**Figure 1**

**Many U.S. Households Have Tax-Advantaged Retirement Savings**

*Percent of U.S. households with IRAs and employer-sponsored retirement plans, 2011*




*1IRAs include traditional IRAs, Roth IRAs, SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs.*
*2Employer-sponsored retirement plans include defined contribution and defined benefit retirement plans. sources: Investment Company Research and U.S. Bureau of the Census*


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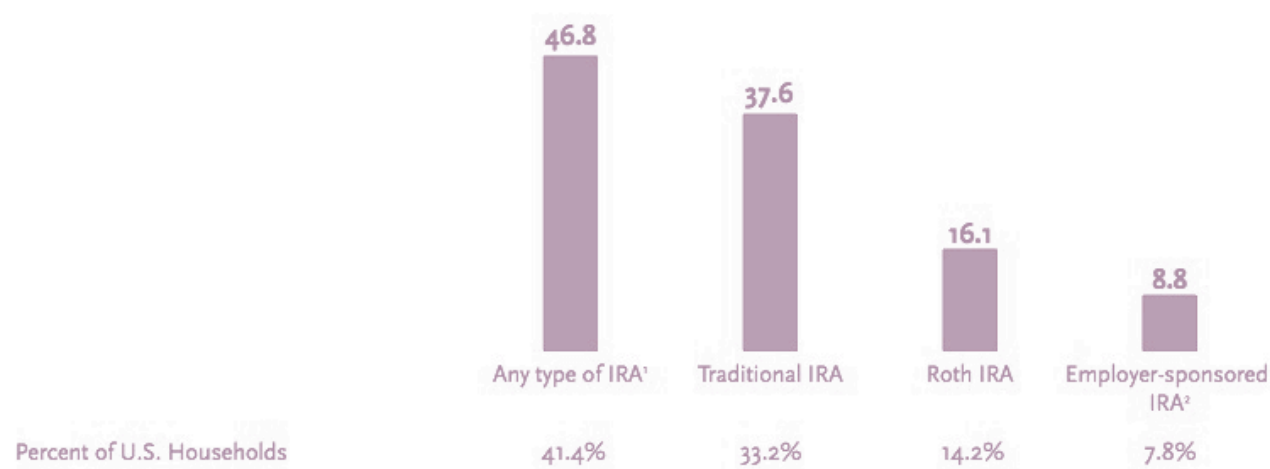
**Figure 2**

**Households Most Frequently Own Traditional IRAs**

*Millions of U.S. households owning IRAs, 2011*




*1Households may own more than one type of IRA.*
*2Employer-sponsored IRAs include SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs.*
*sources: Investment Company Research and U.S. Bureau of the Census*

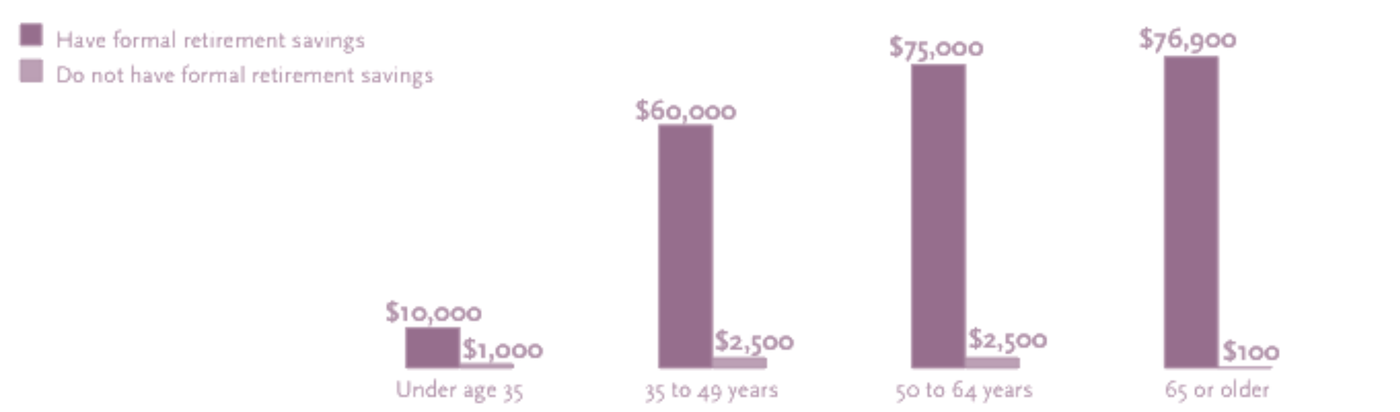
## Households With IRAs Have More Savings than Other Households

Both employer-sponsored retirement plans and IRAs provide opportunities for U.S. workers to set aside assets for retirement in tax-advantaged vehicles. Households with this formal retirement savings arrangements typically have accumulated more financial assets than those who have not taken advantage of these accounts (Figure 3). In 2011, for example, median financial assets of households owning IRAs were six times greater than the financial assets of households that do not own IRAs (Figure 4).

**Figure 3**

**Households With Formal Retirement Savings1 Have Greater Total Financial Assets**

*Median total household financial assets, by age of head of household and formal retirement savings, 2011*




*1Formal retirement savings include IRAs, employer-sponsored retirement plans, or both.*
*source: Investment Company Research*

IRA owners typically exhibit the characteristics of individuals who are most likely to save. An individual's propensity to save increases with age, educational attainment, and income; and married people tend to save more than single people.3 Following this pattern, the financial decision makers of households with IRAs tend to be older and are more likely to be married, employed, and have college or postgraduate degrees than those without IRAs.

IRAs help households build their savings over time. For example, in 2011, households owning IRAs for less than five years had median IRA holdings of $7,000, while households owning IRAs for 20 years or more had median IRA holdings of $35,300 (Figure 5). Mean IRA holdings, while considerably higher than the median values, follow a similar pattern.


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Figure 4

## IRA Owners Are Typically Middle-Aged, Married, and Employed

*Characteristics of U.S. households, by ownership of IRAs, 2011*

| | Households Owning IRAs[1] | Households Not Owning IRAs |
|---|---|---|
| **Median Per Household** | | |
| Age of household sole or co-decisionmaker for investing | 52 years | 45 years |
| Household income | $70,000 | $34,000 |
| Household financial assets[2] | $150,000 | $25,000 |
| Household financial assets in IRAs | $30,000 | NA |
| Share of household financial assets in IRAs | 25% | NA |
| **Percent of Households** | | |
| Household sole or co-decisionmaker for investing: | | |
| Married | 62 | 44 |
| College or postgraduate degree | 59 | 28 |
| Employed full- or part-time | 71 | 62 |
| Retired from lifetime occupation | 26 | 25 |
| Household has defined contribution plan account or defined benefit plan coverage (total) | 73 | 51 |
| Defined contribution retirement plan account | 67 | 43 |
| Defined benefit plan coverage | 45 | 28 |

*NA=not applicable*
*1IRAs include traditional IRAs, Roth IRAs, SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs.*
*2Household financial assets include assets in employer-sponsored retirement plans but exclude primary residence.*
*note: Number of respondents varies. Data for households owning IRAs are from ICR's May 2011 survey of U.S. households owning IRAs. Data for households not owning IRAs are from ICR's June 2011 Mutual Fund Shareholder Tracking Survey.*
*source: Investment Company Research*

Even more striking is how effective IRAs can be in building assets over time for investors who make ongoing contributions. Among households that have owned IRAs for at least 10 years and contributed to them in tax-year 2010, the average IRA balance in 2011 was $148,000 and the median balance was $80,000. Most U.S. households have not saved nearly this much. According to the Federal Reserve Board's *2001 Survey of Consumer Finances*, three-quarters of all U.S. households have total financial assets below $100,000, including IRA assets.4

### Traditional IRAs' Rollover Feature Preserves Retirement Savings

Traditional IRAs were designed with a dual purpose: to provide individuals not covered by retirement plans at work with the opportunity to save for retirement, and to give retiring workers or individuals changing jobs a means to preserve the tax-advantaged status of employer-sponsored retirement plan assets by allowing transfers, or "rollovers," of plan balances into IRAs.

**Figure 5**

**IRA Assets Increase With Length of Ownership**

*Median and mean household financial assets in IRAs, by length of ownership, 2011*


*source: Investment Company Research*

The rollover feature has helped many Americans sustain their retirement savings. In 2008, households transferred about $300 billion from employer- sponsored retirement plans to IRAs.5 In 2011, more than 16 million U.S. households, or 43 percent of all U.S. households owning traditional IRAs, had traditional IRAs that included rollover assets. During their most recent rollovers, the vast majority of these households transferred their entire retirement plan balances into traditional IRAs.

The rollover feature is especially beneficial to individuals who change jobs during their careers or leave the work force for reasons other than retirement. In 2011, nearly two-thirds of households with traditional IRAs that include rollover assets said their rollovers were due to jobs changes, lay-offs, or employment terminations. About one-third conducted rollovers at retirement.

A comparison of the traditional IRA assets of households that have and have not conducted rollovers demonstrates the positive effect of the rollover feature on retirement savings. Median traditional IRA holdings that include rollovers were $50,000 in 2011, while median traditional IRA holdings that did not include rollovers were $20,000 (Figure 6)

**Figure 6**

**Traditional IRAs Preserve Assets from Employer-Sponsored Retirement Plans**

*Traditional IRA assets, by employer-sponsored retirement plan rollover activity, 2011*

| | Traditional IRA Includes Rollover from Employer-Sponsored Retirement Plan[1] | Traditional IRA Does Not Include Rollover from Employer-Sponsored Retirement Plan[2] |
|---|---|---|
| **Traditional IRA Assets** | | |
| Mean | $107,000 | $46,500 |
| Median | $50,000 | $20,000 |
| **Household Financial Assets[3]** | | |
| Mean | $325,000 | $257,200 |
| Median | $200,000 | $146,000 |

*1Forty-three percent of households owning traditional IRAs have traditional IRAs that include rollovers from employer-sponsored retirement plans.*
*2Fifty-seven percent of households owning traditional IRAs have traditional IRAs that do not include rollovers from employer-sponsored retirement plans.*
*3Household financial assets include assets in employer-sponsored retirement plans but exclude primary residence.*
*source: Investment Company Research*

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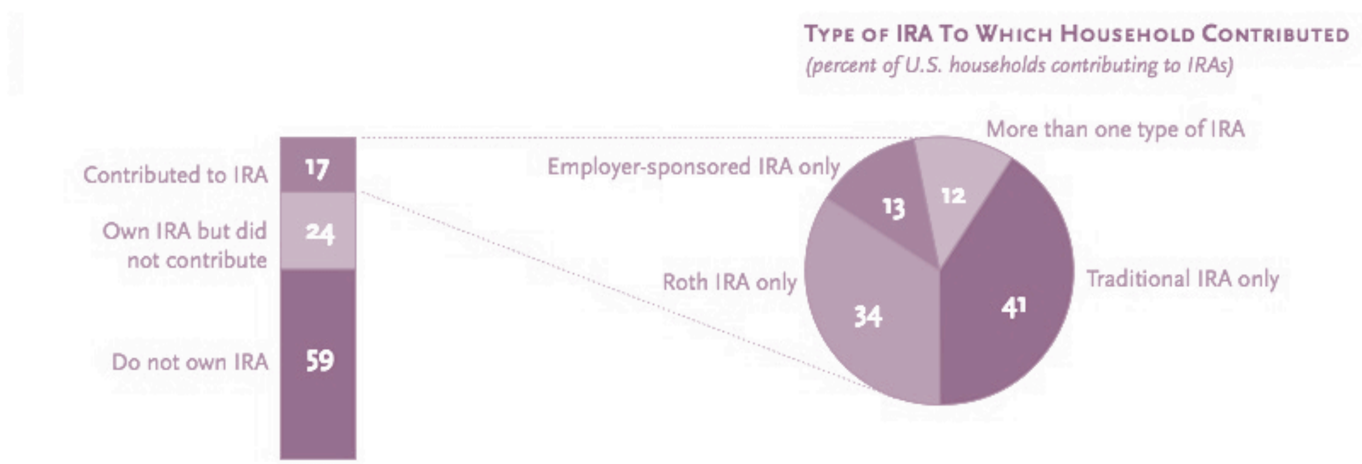
## Most Households Do Not Contribute to IRAs

Although IRAs can help Americans build their retirement savings, the majority of U.S. households do not contribute to them. In tax-year 2010, only 15 percent of all U.S. households made IRA contributions (Figure 7). Because there are many more traditional IRA owners than owners of other types of IRAs, contributors to traditional IRAs represent the largest share of all households making IRA contributions.

When contributions to IRAs are examined by the type of IRA owned, however, traditional IRA owners are less likely than owners of other types of IRAs to

**Figure 7**

**Few Households Contribute to IRA**




*sources: Investment Company Research and U.S. Bureau of the Census*

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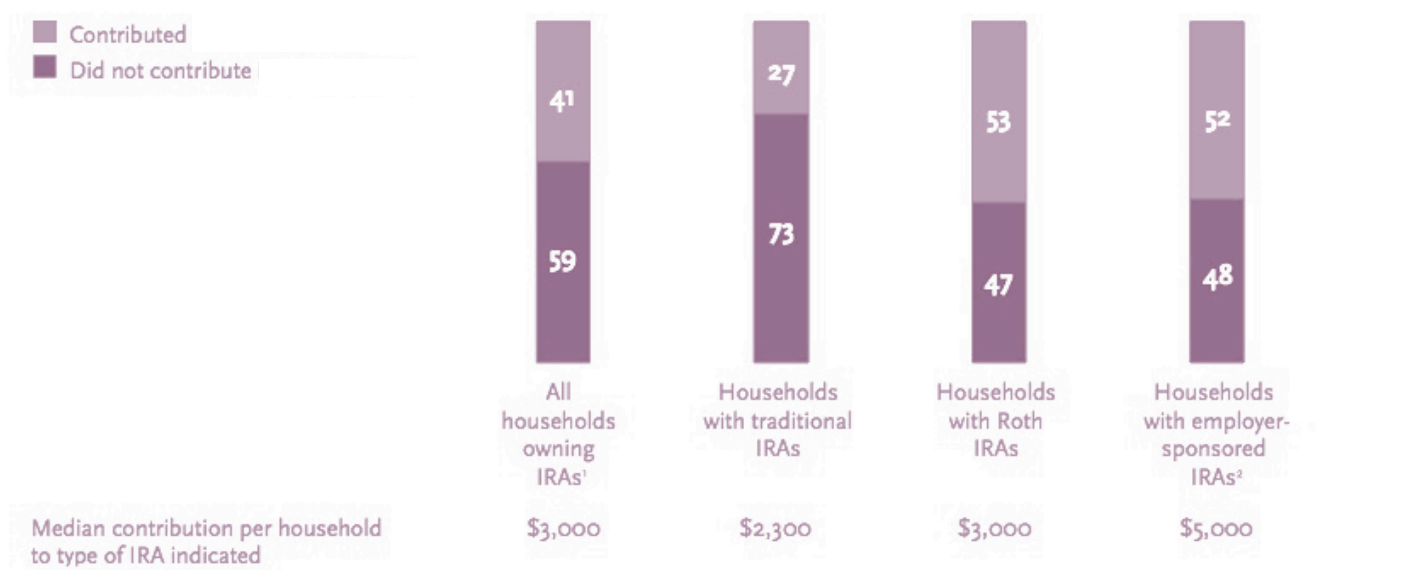
make contributions. For example, more than half of households owning Roth IRAs or employer-sponsored IRAs contributed to these IRAs in tax-year 2010 (Figure 8). In contrast, only 27 percent of traditional IRA-owning households contributed to their traditional IRAs in tax-year 2010. The lower contribution rate to traditional IRAs is likely due to tax deductibility restrictions.

In addition, the typical household contribution to each type of IRA varies, partly because IRA contribution limits are not uniform. The median contribution among households contributing to Roth IRAs was $4,500 in tax-year 2010, while the typical contribution to traditional IRAs was $3,300 per household. For employer-sponsored IRAs, which generally have higher contribution limits, the median household contribution was $5,000.

**Figure 8**

**Contribution Activity to Roth, Employer-Sponsored IRAs Outpaces Contribution Activity to Traditional IRAs**

*Percent of households owning each type of IRA, by contribution status in tax-year 2011*




*1IRAs include traditional IRAs, Roth IRAs, SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs.*
*2Employer-sponsored IRAs include SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs.*
*source: Investment Company Research*

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## Notes

[1] See "Recent Changes in U.S. Family Finances: Evidence from the 1998 and 2001 Survey of Consumer Finances," *Federal Reserve Bulletin,* January 2003, p. 6 (www.federalreserve.gov/ pubs/bulletin/2003/0103lead.pdf) and Investment Company Research Research Series, *Profile of Mutual Fund Shareholders,* 2010, p. 10 (www.ICR.org/pdf/rpt_profile04.pdf).

[2] Data presented in this issue of *Fundamentals* on the number and percentage of households owning IRAs are based on an annual survey conducted in June 2011 of 3,000 randomly selected, representative U.S. households (the standard error for the total sample is ± 1.8 percentage points at the 95 percent confidence level). The demographic and financial characteristics of IRA owners are derived from a separate May 2011 survey of 595 randomly selected, representative U.S. households owning IRAs, including traditional IRAs, Roth IRAs, SIMPLE IRAs, SEP IRAs, and SAR-SEP IRAs (the standard error for the total sample is ± 4.0 percentage points at the 95 percent confidence level). IRA ownership does not include ownership of Coverdell Education Savings Accounts (formerly called Education IRAs). Additional data on household ownership of IRAs are available in an Appendix on ICR's website (www.ICR.org/pdf/ fmv15n1_appendix.pdf). For a brief history of IRAs and a discussion of the various features of different IRA types, see Sarah Holden, Kathy Ireland, Vicky Leonard-Chambers, and Michael Bogdan, "The Individual Retirement Account at Age 30: A Retrospective," *ICR Perspective,* Vol. 11, No. 1, February 2011 (www.ICR.org/pdf/per11-01.pdf) (to be referenced as ICR (February 2011) in the remainder of this publication). For the rules governing IRAs, see IRS *Publication 590, Individual Retirement Arrangements* (www.irs.gov/pub/ irs-pdf/p590.pdf) (to be referenced as IRS *Publication 590* in the remainder of this publication).

[3] See ICR (February 2011) for a discussion of the relationship between demographic characteristics and the propensity to save.

[4] Federal Reserve Board, *2001 Survey of Consumer Finances,* tabulations by ICR.

[5] See Figure A8 in "Appendix: Additional Data on Mutual Funds and the U.S. Retirement Market in 2010," *ICR Fundamentals,* Vol. 14, No. 4A, August 2011 (www.ICR.org/pdf/fm-v14n4_ appendix.pdf ).

[6] Roth IRAs are not eligible for direct rollovers from employer- sponsored retirement plan accounts (see IRS *Publication 590).* See the online appendix for additional data on households with IRAs that include rollover assets.

[7] Households that may make catch-up contributions to Roth IRAs are those with incomes within the limits to contribute to a Roth IRA and in which a household member is age 50 or older (see IRS *Publication 590).*

[8] Households that may make catch-up contributions to traditional IRAs are those in which a household member is at least age 50 but less than 701⁄2 years old (see IRS *Publication 590).* Some of these households may be ineligible to make deductible contributions to traditional IRAs.

[9] Data exclude households that closed and no longer own traditional IRAs.

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