How U.S. Households Steward Their Individual Retirement Account (IRA) Assets To and Through Retirement

by **Sarah Holden, Ph.D.** | *Investment Company Institute*

U.S. Households Rely on a Variety of Retirement Resources

When analyzing resources Americans have for retirement, it is important to consider the complementary components of the U.S. retirement system. One way to think about retirement resources is as a pyramid that has five layers. These five layers draw from government programs, accumulations earmarked for retirement and other savings: Social Security; homeownership; employer-sponsored retirement plans (private sector and government employer plans, including both defined benefit (DB) and defined contribution (DC) plans); individual retirement accounts (IRAs), including rollovers; and other assets (Figure 1). Households rely on the different components of the pyramid to different degrees.

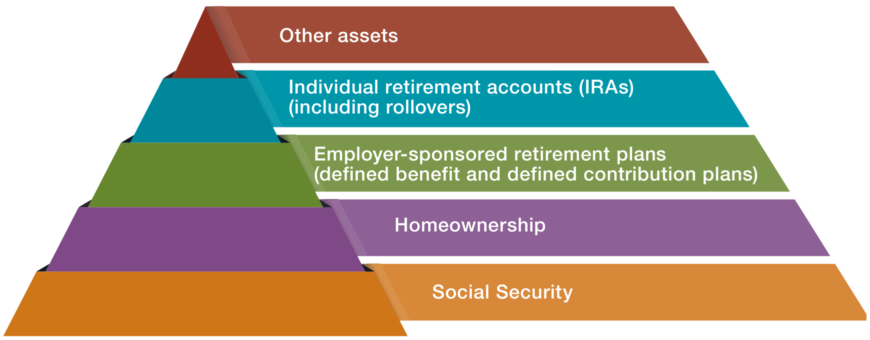
Social Security, the base of the U.S. retirement resource pyramid, often is the largest component of retiree income and the primary source of income for lower income retirees.[1] By design, Social Security is the primary means of support for retirees with low lifetime earnings and a substantial source of income for all retired workers. For individuals born in the 1960s who claim benefits at the age of 65, a Congressional Budget Office (CBO) analysis finds that mean first-year scheduled Social Security benefits will replace 83% of average inflation-indexed lifetime earnings for retired workers in the lowest 20% of households, ranked by lifetime household earnings, and 34% of earnings for the highest quintile.[2] When Social Security benefits are converted into an asset and added onto the balance sheet of

AT A GLANCE

- Traditional individual retirement accounts (IRAs) hold nearly $8 trillion in assets.
- Nearly 60% of households with traditional IRAs rolled over funds from employer-sponsored retirement plans into the accounts.
- Most U.S. households with traditional IRAs tend to preserve the accounts until they are required to take distributions.
- Retired households are more likely to use withdrawals from traditional IRAs to pay for living expenses than those that are not retired.

FIGURE 1

The Retirement Resource Pyramid

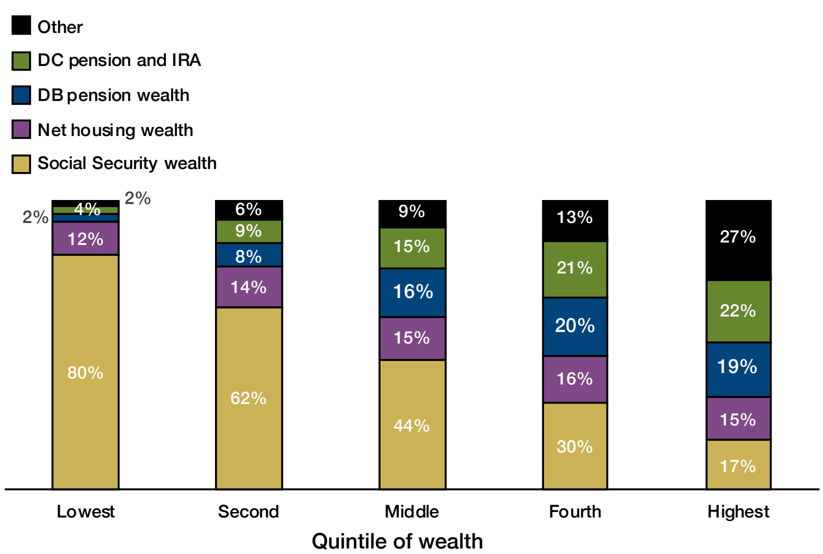


Source: Investment Company Institute, *Investment Company Fact Book.*

FIGURE 2

The Composition of Retirement Resources Varies by Household, Largely Influenced by the Design of Social Security

(Percentage of comprehensive wealth by wealth quintile, 2010)*



*Data represents households with at least one member aged 57 to 62 and excludes the top and bottom 1%.

Source: Investment Company Institute tabulation derived from an updated Table 3 of Gustman, Steinmeier and Tabatabai, 2009.

near-retiree households, they represent a substantial share of household wealth, ranging from 80% of wealth for the lowest wealth quintile to 17% of wealth for the highest wealth quintile (Figure 2).[3]

For many near-retiree households, homeownership, the next layer of the pyramid, is the second most important retirement resource after Social Security. Older households are more likely to own their homes, more likely to own their homes without mortgage debt and, if they still have mortgages, more likely to have small mortgages relative to the value of their homes. Retired households typically access this resource simply by living in their homes rent-free. Housing wealth represents a relatively similar share of household wealth across the wealth distribution, ranging from 12% of wealth for the lowest wealth quintile to 16% of wealth for the fourth wealth quintile (Figure 2).

The next two layers of the retirement resource pyramid represent accumulations earmarked for retirement. Employer-sponsored retirement plans and IRAs are important resources for households across the wealth distribution. Complementing Social Security benefits are DB pension wealth and DC pension wealth and IRAs. These resources represent 6% of wealth for households in the lowest wealth quintile (who rely heavily on Social Security), 31% of wealth for the middle wealth quintile, and 41% of wealth for the highest wealth quintile (Figure 2).

In addition, some households have other assets, which include financial assets (such as bank deposits and investments through taxable accounts) and nonfinancial assets (such as business equity, investment real estate and second homes). These other assets play a large role in household wealth among higher wealth households (Figure 2).

Most Near-Retiree Households Have Retirement Assets to Manage

U.S. households have a variety of complementary retirement resources to help maintain their standard of living as they transition from work to retirement.[4] Analysis of *Survey of Consumer Finances* data finds that about eight in ten near-retiree households in 2016 had accrued benefits in employer-sponsored retirement plans—DB and DC plans sponsored by private sector and government employers—or IRAs (Figure 3). About seven in ten near-retiree households have DC plan account or IRA assets.

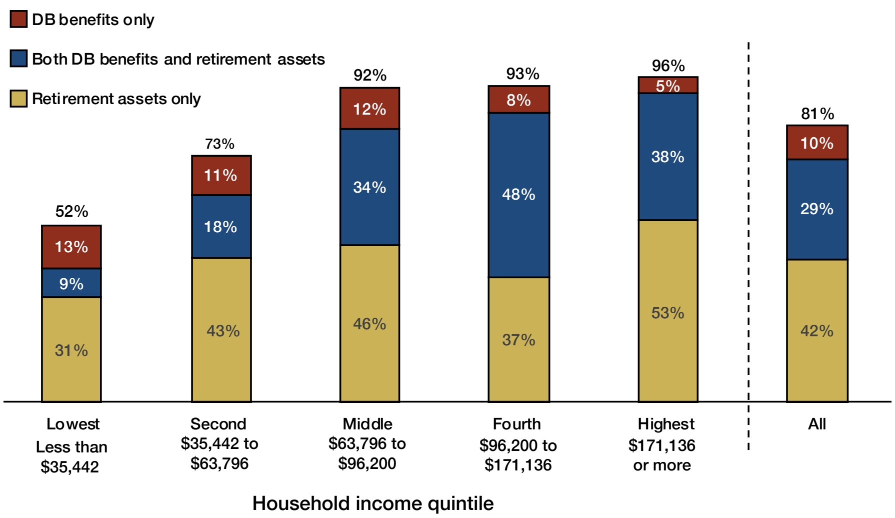
Near-retiree households have accumulated significant amounts in DC plan accounts and IRAs, and accumulations vary across the income distribution. Recalling the retirement resource pyramid, the distribution of retirement accumulations across households reflects the role of Social Security across households. Similarly, the amounts accumulated to supplement Social Security vary across households, ranging from an average of less than $100,000 in DC plan and IRA assets in the lowest two income quintiles to nearly $1 million among near-retiree households in the highest income quintile in 2016 (Figure 4).

U.S. retirees must make decisions surrounding the claiming of Social Security, the distribution of accumulations from DB plans,[5] the management of DC plan assets and distribu-

FIGURE 3

Near-Retiree Households Across All Income Groups Have Retirement Assets, DB Plan Benefits or Both

(Percentage of working households aged 55 to 64 by income quintile, 2016)



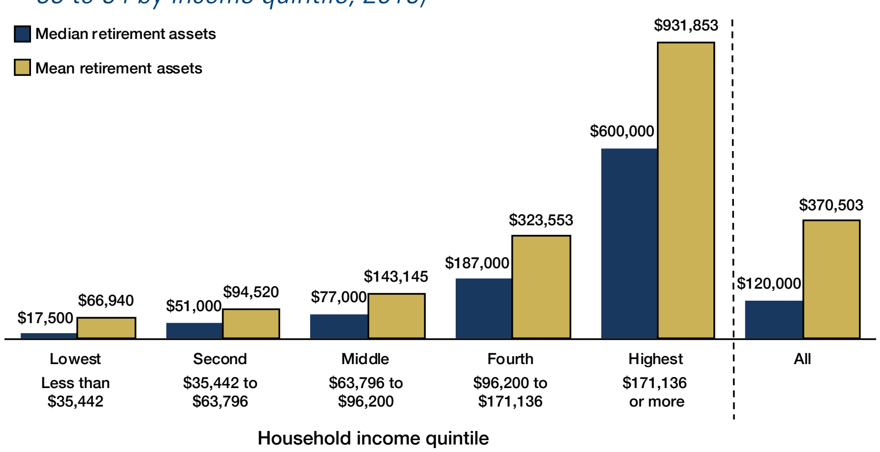
Note: Component percentages may not add up to the total due to rounding.

Source: Investment Company Institute tabulations of the Federal Reserve Board *2016 Survey of Consumer Finances.*

FIGURE 4

Near-Retiree Households' Retirement Assets Are Significant

(DC plan account and IRA assets for working households aged 55 to 64 by income quintile, 2016)

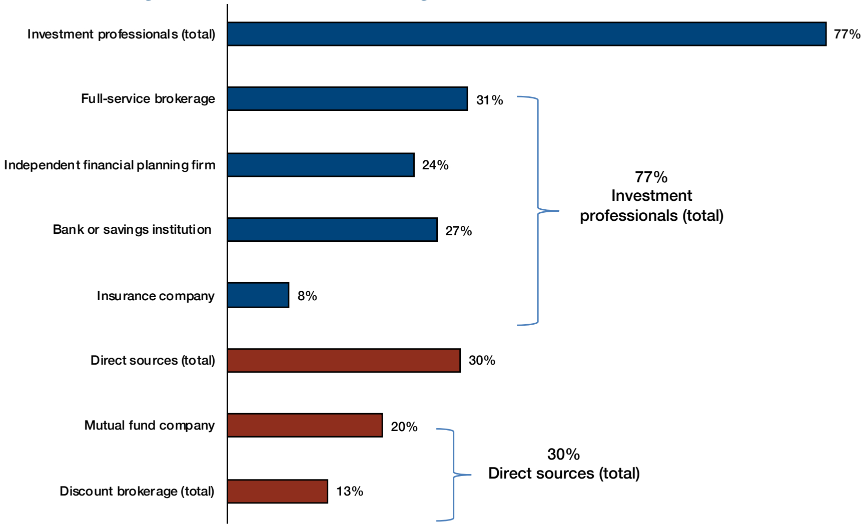


Source: Investment Company Institute tabulations of the Federal Reserve Board *2016 Survey of Consumer Finances.*

FIGURE 5

Traditional IRAs Are Held Through a Variety of Financial Institutions

(Percentage of households owning traditional IRAs, mid-2017)



Note: Multiple responses are included.

Source: Investment Company Institute *IRA Owners Survey;* see Holden and Schrass, 2017b.

tions,[6] and the management of IRAs. This article explores how investors in the most common type of IRA, the traditional IRA, manage their traditional IRAs to and through retirement.

IRAs Provide Consolidation Strategy, Investment Choices and Options for Comprehensive Advice

At year-end 2017, IRA assets totaled $9.2 trillion and were a significant component of the U.S. retirement system.[7] With nearly $8 trillion in assets, traditional IRAs were the most common, reflecting rollover activity as well as investment returns and contributions. Household survey data reveal that nearly six in ten U.S. households with traditional IRAs reported rollover activity from employer-sponsored retirement plans.[8] By these measures, traditional IRAs are very clearly a key component of Americans' retirement planning.

Households that want to set up traditional IRAs have a wide array of financial institutions available to them. Some households seek the assistance of investment professionals, while others go directly to mutual fund companies or discount brokers. Indeed, in mid-2017, 77% of traditional IRA–owning households held them through investment professionals, and 30% held them directly at mutual fund companies or discount brokers (Figure 5). Nearly one-third (31%) of traditional IRA–owning households held them through full-service brokerage firms, 27% held them through bank or savings institutions, and 24% held them through independent financial planning firms. One in five (20%) held their traditional IRAs through mutual fund companies, and 13% held them through discount brokers. Households may have multiple traditional IRAs and hold them through different financial services firms.

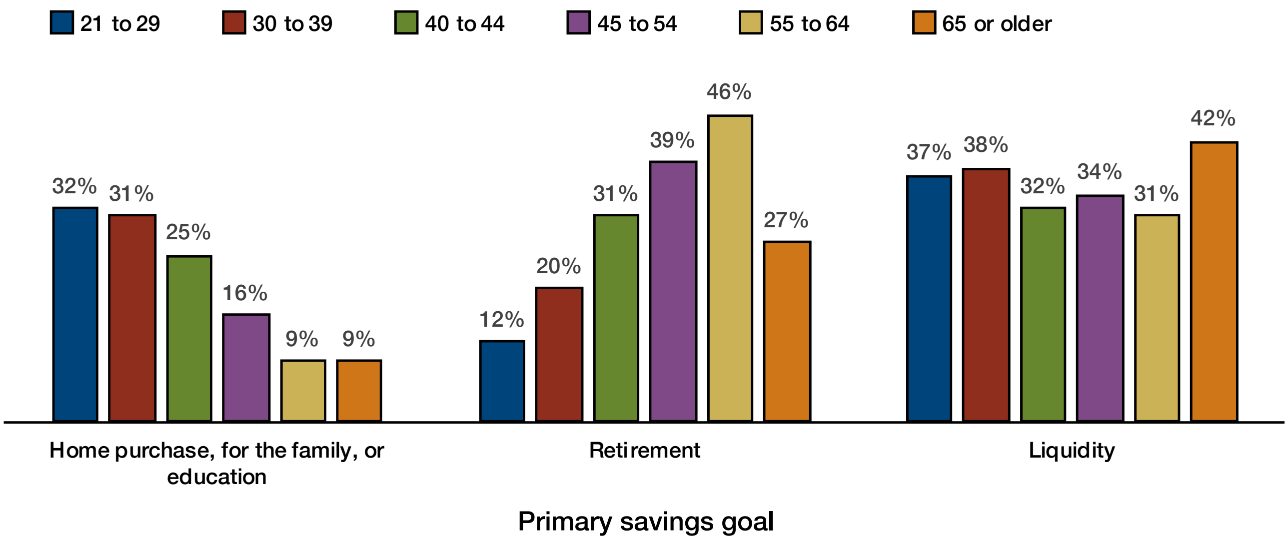
IRA Owners Often Have Strategies to Manage Income and Assets in Retirement

Retiree households have many decisions to make as they manage income and assets, and there are trade-offs and risks involved. Retiree households that are managing IRAs have to make decisions around rollovers,[9] contributions,[10] asset allocation,[11] and distributions or withdrawals. In addition, discussion often turns to the question of whether households should manage the IRA assets and determine withdrawals or annuitize some of their retirement balances.

A key factor influencing the demand for annuitization is the already high degree of existing annuitization for many U.S. households through Social Security, housing and DB pensions. Many households across all ages indicate that saving for liquidity or precautionary purposes is a financial goal of their households, and 42% of households aged 65 or older indicate that their primary savings goal is for liquidity (Figure 6). Thus, households are balancing the need for liquidity (e.g., to cover large expenditures—fixing the roof on the house, replacing

FIGURE 6

Older Households Often Indicate Need for Precautionary Saving
(Percentage of U.S. households by age of head of household, 2016)



Source: Investment Company Institute tabulations of the Federal Reserve Board *2016 Survey of Consumer Finances.*

a car, health expenses, emergencies) versus income flow in the context of their entire balance sheet and set of retirement resources.[12] Economic issues that arise when choosing to annuitize include:

- Risk in selecting a particular annuity provider
- Adverse selection in annuity markets
- Low interest rates, which reduce payments
- The range of complex products.

In addition to these economic factors, behavioral factors also may be at play. Individuals may downplay the lifelong income stream because it occurs in the future and gets discounted in their minds (*present bias*), or they may hesitate to annuitize for fear that they will die young (*loss aversion*).[13]

Within the context of managing the entire retirement resource pyramid, it is possible to examine how households manage the IRA component of their balance sheets. Generally, traditional IRA–owning households research decisions, have strategies in place and tap their IRAs in measured ways.

Retirement Strategies for Managing Income and Assets

More than two-thirds (69%) of traditional IRA–owning households in mid-2017 said they have a strategy for managing income and assets in retirement. Households typically conduct research and/or seek advice when building their retirement income and asset-management strategies, which typically have several components. Three-quarters (75%) of traditional IRA–owning households with a strategy consulted a professional financial advisor when creating the strategy, with 66% indicating that a professional financial advisor was their primary source.[14] Some households conducted research online: More than one-quarter (27%) used a website to help create their retirement income and asset-management strategy, with 10% saying website information was a primary source. More than one-quarter (27%) consulted with friends or family, 24% consulted written materials (e.g., a

TABLE I

Strategies for Managing Income and Assets in Retirement Have Many Components
(Percentage of traditional IRA–owning households that indicated they have a strategy for managing income and assets in retirement, mid-2017)

		Age of head of household*			
	All	Younger than 35	35 to 49	50 to 64	65 or older
Review asset allocation	71%	64%	77%	70%	70%
Develop a retirement income plan	65%	62%	63%	71%	62%
Determine retirement expenses	66%	54%	57%	73%	69%
Set aside emergency funds	60%	79%	64%	63%	48%
Determine when to take Social Security benefits	53%	33%	40%	67%	53%
Review insurance policies	50%	53%	57%	51%	42%
Other	2%	0%	2%	2%	3%

*Age is based on the age of the sole or co-decision maker for household saving and investing.

Note: Multiple responses are included; 70% of traditional IRA–owning households that indicated they have a strategy for managing income and assets in retirement took three or more steps in developing their strategy.

Source: Investment Company Institute *IRA Owners Survey;* see Holden and Schrass, 2017b.

book or article in a magazine or newspaper) and 9% used a financial software package to build their retirement income and asset-management strategy.

Traditional IRA–owning households with a strategy for managing their income and assets in retirement typically reported that their strategy had multiple components.[15] In mid-2017, 71% of these households reviewed their asset allocation, with households aged 35 to 49 more likely to indicate they had completed this step (77%) compared with other age groups (Table I). Nearly two-thirds (65%) developed a retirement income plan as part of their strategy, with households in their 50s or early 60s the most likely to have done this step; more than seven in ten (71%) traditional IRA–owning households aged 50 to 64 with a strategy had developed a retirement income plan. Two-thirds (66%) of households with a strategy for managing their income and assets in retirement determined their retirement expenses, with households aged 50 or older more likely to have done so than those younger than 50. Three in five (60%) set aside emergency funds, and the youngest households were the most likely to have done this step (79% of households younger than 35). Half of households with a strategy reviewed their insurance policies. More than half (53%) determined when to take Social Security benefits, with households aged 50 or older more likely to have done so compared with households younger than 50.

IRA Withdrawals Are Retirement-Related, Researched and Measured

IRA Withdrawals Are Infrequent

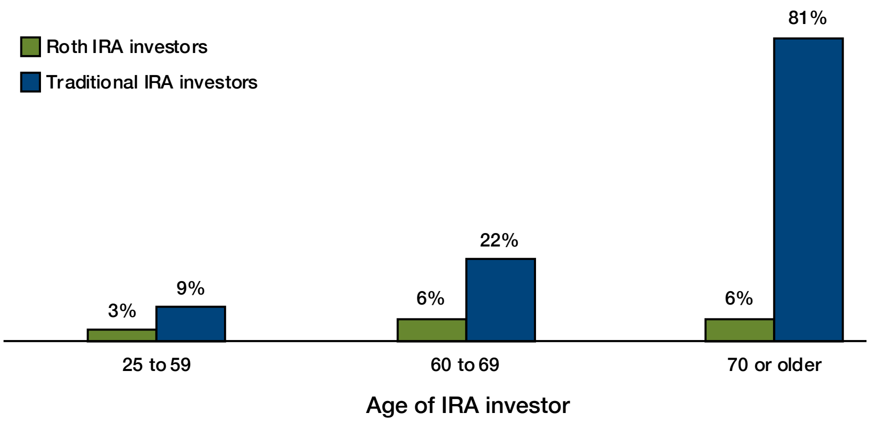
Few households withdraw money from their IRAs in any given year. A traditional IRA withdrawal taken by an individual prior to the age of 59½ generally is subject to a 10% penalty on the taxable portion of the withdrawal (in addition to the federal, state and local income taxes that may be due). Taxpayers older than 59½ but younger than 70½ may take withdrawals without penalty but generally are not required to do so. Traditional IRA owners aged 70½ or older are required to withdraw an annual amount based on life expectancy or pay a penalty for failing to do so; these withdrawals are called *required minimum distributions* (RMDs). Households with inherited IRAs also generally are required to take distributions. Roth IRA investors only face RMDs if the Roth IRA is inherited.

Against this backdrop of rules, traditional IRA withdrawals are rare among younger taxpayers and pick up when RMD rules kick in, while Roth IRA withdrawals are infrequent across all age groups. For example, only 3% of Roth IRA investors aged 25 to 59 and 9% of traditional IRA investors aged 25 to 59 took withdrawals in 2015 (Figure 7).[16] For ages when penalties don't apply, there is a slight increase in withdrawal activity, though only among a minority of IRA investors. But, as RMDs begin to take effect, 81% of traditional IRA investors aged 70 or older had withdrawals.

FIGURE 7

Traditional IRA Investors Are Heavily Affected by RMDs

(Percentage of IRA investors with withdrawals by type of IRA and investor age, 2015)



Note: The samples are 5.5 million Roth IRA investors aged 25 or older at year-end 2015 and 11.5 million traditional IRA investors aged 25 or older at year-end 2015.

Source: The IRA Investor Database™; see Holden and Schrass, 2017a.

IRA Withdrawals Are Mostly Retirement-Related

Household survey data tell us that traditional IRA withdrawals tend to be taken by retired households and often in consultation with an advisor or Internal Revenue Service (IRS) rules. More than one-quarter (26%) of households owning traditional IRAs in mid-2017 reported taking withdrawals from these IRAs in tax year 2016.[17] Among households taking traditional IRA withdrawals in tax year 2016, 81% reported that someone in the household was retired from their lifetime occupation. Nevertheless, nearly half (48%) of retired households owning traditional IRAs in mid-2017 did not take withdrawals in tax year 2016.

Withdrawal Amounts Tend to Be Based on Life Expectancy

The most common withdrawal amounts from traditional IRAs were taken to fulfill RMDs, which are based on remaining life expectancy. More than seven in ten (71%) households owning traditional IRAs in mid-2017 and making withdrawals in tax year 2016 calculated their withdrawal amount based on the RMD rule.[18] Another 9% reported a scheduled withdrawal amount, either as a percentage of the account or a regular dollar amount, and another 2% reported the withdrawal amount was based on life expectancy. Only 15% of traditional IRA–owning households taking withdrawals reported they withdrew lump sums based on needs in tax year 2016. Thus, overall, 82% of households taking traditional IRA withdrawals used a measured or planned approach to managing tapping their traditional IRAs.

Traditional IRA–owning households that took withdrawals in tax year 2016 usually consulted outside sources to determine the amount of the withdrawal.[19] Nearly two-thirds (64%) consulted a professional financial advisor to determine the amount to withdraw. Almost one-third (32%) consulted Internal Revenue Service (IRS) rules or publications. Less than one-tenth used a website (7%) or financial software (6%) when figuring out how much to withdraw.

Traditional IRA Withdrawals Are Used for a Variety of Expenses

After determining the timing and amount of the traditional IRA withdrawal, the final question to consider is the use of the amounts withdrawn. The use of traditional IRA withdrawals varies between households that are in retirement and those that are not. Among households in which either the head of household or spouse was retired in mid-2017, 43% reported using at least some of their traditional IRA withdrawals to pay for living expenses in tax year 2016. In contrast, only 21% of nonretired households with withdrawals used some or all of the withdrawal to cover living expenses.

Nearly two in five (39%) retired households that took traditional IRA withdrawals reinvested or saved at least some of the withdrawal amount into another account, in part reflecting households with RMDs.[20] Nearly one-fifth (18%) of retired households with withdrawals reported using at least some of their withdrawals for home purchase, repair or remodeling, and 11% reported using their withdrawals for health care expenses. Only 5% of retired households with withdrawals used their withdrawals for emergencies, in contrast with 22% of nonretired households with withdrawals. These patterns of use highlight the stewardship of traditional IRA assets to and through retirement.

Conclusion

U.S. households have a variety of retirement resources that are designed to complement each other to help maintain a standard of living as people transition from work to retirement. About eight in ten near-retiree households have DB plan benefits, DC plan accounts or IRAs. In a series of financial decisions that involve tradeoffs and balancing multiple retirement resources and financial goals, households are responsible for managing assets and income in retirement, which necessitates a holistic approach and recognition of tradeoffs.

IRA assets have grown to $9.2 trillion, and traditional IRAs are the most common type of IRAs, reflecting rollover activity from employer-sponsored plans as well as contributions. Only 26% of traditional IRA–owning households in mid-2017 had taken withdrawals in the prior tax year, but 71% of households taking those withdrawals calculated the amount based on IRS RMD rules. More than eight in ten (81%) traditional IRA–owning households with withdrawals were retired. Household survey data clearly point out that IRA investors often seek advice and research decisions involving their IRAs, typically within the context of an overall retirement asset and income strategy. Survey, tax and administrative data all indicate that households tend to steward their IRA assets to and through retirement with deliberate and measured tapping of their balances.

The views expressed are those of the author.

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Endnotes

1. See Brady and Bogdan (2016) and Brady et al. (2017).
2. See Congressional Budget Office (2017).
3. Gustman, Steinmeier and Tabatabai (2009) create an augmented household balance sheet that converts the future value of Social Security benefits and defined benefit (DB) plans into an asset on the household's balance sheet.
4. For recent research analyzing Internal Revenue Service (IRS) Statistics of Income tax data on the income replacement experience of workers transitioning into retirement (claiming Social Security), see Brady et al. (2017).
5. For an analysis of how distribution decisions vary with DB plan design, see Banerjee (2013).
6. Utkus and Young (2018) find that the majority of defined contribution (DC) plan accumulations are preserved when participants change jobs or retire.
7. See Investment Company Institute (ICI) (2018).
8. See Holden and Schrass (2017b).
9. In mid-2017, 57% of traditional IRA–owning households reported they had rollovers in their traditional IRAs; see Holden and Schrass (2017b). Analysis of data collected from financial services firms that provide the recordkeeping function for IRAs finds that while fewer than one in ten traditional IRA investors made rollovers in any given year, among traditional IRA investors with an account balance at year-end 2015, more than half had a rollover at some point between 2007 and 2015 (see Holden and Bass (2017)).
10. Almost half (46%) of traditional IRA–owning households with rollovers also had contributed to their traditional IRAs; see Holden and Schrass (2017b).
11. For the variation in asset allocation by age among traditional IRA investors, see Holden and Bass (2017). For variation in the asset allocation by age among Roth IRA investors, see Holden and Schrass (2017a).
12. Furthermore, individuals may have bequest motives.
13. See Madrian (2014).
14. These data are based on the ICI *IRA Owners Survey*; see Holden and Schrass (2017b).
15. Seventy percent of traditional IRA–owning households with a strategy took three or more steps in developing their strategy. See Holden and Schrass (2017b).
16. Both IRS Statistics of Income analysis of tax data (see IRS Statistics of Income (2018)) and analysis of data collected from financial services firms that provide the recordkeeping function for IRAs (see Holden and Schrass (2017a) and Holden and Bass (2017)) find similar patterns of withdrawal activity.
17. These data are based on the ICI *IRA Owners Survey;* see Holden and Schrass (2017b).
18. Ibid.
19. Ibid.
20. Ibid.

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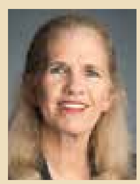

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