Ownership of Individual Retirement Accounts (IRAs) and Policy Options for Congress

John J. Topoleski
Analyst in Income Security

November 5, 2010

Congressional Research Service
7-5700
www.crs.gov
R41476

CRS Report for Congress
Prepared for Members and Committees of Congress

Summary

Preparing for financial security in retirement continues to be a concern of working Americans and policymakers. Although most Americans participate in the Social Security system, Social Security is likely to be only a part of income in retirement. A recent Gallup poll indicated that while 34% of working Americans expect Social Security to be a major source of retirement income, 45% of those polled expect private retirement savings accounts to be a major source of retirement income.

Since the 1920s, Congress has provided tax incentives to employers to sponsor pension plans for their workers. Recognizing that workers for companies that did not offer pension plans did not benefit from the incentives, in 1974, Congress permitted workers without pension plans to establish Individual Retirement Accounts (IRAs). IRAs are tax-advantaged savings accounts to encourage workers to save for retirement. Since 1974, eligibility for IRAs and the tax treatment of contributions to IRAs have changed. Currently, workers without pensions and workers with pensions whose income is under certain limits may make tax-deductible contributions to IRAs. Other workers may make non-deductible contributions. Since 1998, some workers have been able to make non-deductible contributions to Roth IRAs. Lump-sums from employer-sponsored pensions may be rolled-over into either traditional or Roth IRAs. Most of the funds in IRAs consist of rollover balances rather than the accumulation of contributions and investment earnings.

IRAs may be falling short of their goal of encouraging workers to save for retirement. While about one-half of working Americans participate in employer-sponsored pensions, only about one-third of working households in the United States owned an IRA in 2007. Although IRAs were originally intended for workers in employment without pension plans, IRA ownership rates are higher among households in which the head or spouse participates in a pension plan at work. Among households with pension coverage, 38.7% had an IRA in 2007. Among households without pension coverage, 25.5% had an IRA in 2007.

Analysis of the 2007 Survey of Consumer Finances from the Federal Reserve indicates that households that own IRAs tend to be older, wealthier, more educated, and have higher propensities to save than households that do not own IRAs. Although one-third of working households owned an IRA in 2007, relatively few households made a tax-deductible IRA contribution in 2007. Statistics of Income data from the Internal Revenue Service indicate that 2.3% of tax returns reported a tax-deductible IRA contribution in 2007. The percentage of taxpayers reporting tax-deductible IRA contributions was lower in 2007 than in any year since 1978. Both the percentage of taxpayers reporting tax-deductible IRA contributions in 2007 and the average amount of that contribution increased as taxpayers' reported income increased.

Although IRA ownership rates are lower among households without pension coverage, IRA ownership patterns are similar among households with and without pension coverage. For example, IRA ownership increases as households' income increases and IRA ownership rates are higher among households that own their homes compared with households than do not own their homes. Some policy proposals that supporters argue will increase IRA ownership rates and account balances include making the Retirement Savings Contributions Credit a refundable tax credit, adopting Automatic IRA proposals, increasing household financial literacy, and making the fees that financial institutions charge IRA owners more transparent.

Contents

Figures

Tables

Contacts

Introduction

Income in retirement comes from several sources. Most workers participate in the Social Security system, which pays retirement income as early as 62 years old. Retirement income security can also be provided by non-government sources, such as employer-sponsored pensions and participant-initiated retirement accounts. About half of the U.S. workforce participates in one or both of two kinds of employer-sponsored pensions.

The two kinds of employer-sponsored pensions are defined benefit (DB) and defined contribution (DC) pensions. DB pensions provide retirees with monthly benefits in which the amount is calculated using a formula based on the number of years of employment and final salary. DC pensions, of which the 401(k) plan is the most common, provide participants individual accounts in which contributions from individual employees—and often their employers—are placed in tax-advantaged accounts that accrue investment returns.[1] The accumulated contributions and investment earnings are then used for participants' retirement income. Although employers choose whether to offer DC plans, individual employees decide the contribution amounts (subject to an annual limit) and investment allocations of the contributions.

Over the past 30 years, fewer employers have been providing DB plans and instead have offered DC plans.[2] One consequence of this shift is that workers have had increasing responsibility for their retirement income security. Individual Retirement Accounts (IRAs) can play an important role by providing workers with tax-advantaged savings accounts in which to accumulate retirement savings.

Although enrollment in a DC or DB plan is contingent on employer sponsorship of such a plan, most individuals (or married couples) who have taxable compensation can establish and contribute to an IRA. Similar to 401(k) plans, IRAs are tax-advantaged accounts in which contributions and investment earnings accumulate, which are then used for retirement income. Depending on the type of IRA, contributions may be made on a pre- or post-tax basis and investment earnings are either tax-deferred or tax-free. [3]

This report provides an overview and a brief legislative history of IRAs, examines the tax-deductible contributions to traditional IRAs in 2007, analyzes the characteristics of households that have IRAs, and compares IRA owners who have pension coverage at work with those who do not have pension coverage. The report concludes with a discussion of some of the policy proposals that some suggest might increase IRA ownership rates among American households.

---

[1] 401(k) plans are offered by private sector employers. Other types of defined contribution retirement accounts include 403(b) plans offered by charitable and educational employers, 457 plans offered by state and local governments, and the Thrift Savings Plan (TSP) offered by the Federal government.

[2] For more information on this shift, see James Poterba, Steven Venti, and David A. Wise, "The Shift From Defined Benefit Pensions to 401(k) Plans and the Pension Assets of the Baby Boom Cohort," *Economics of Health and Mortality Special Feature: The Economics and Demography of Aging,* Proc. Natl. Acad. Sci., vol. 104 no. 33, (August 14, 2007), pp. 13238-13243, available at http://www.pnas.org/content/104/33/13238.full.

[3] More information on eligibility requirements for IRAs can be found in CRS Report RL34397, *Traditional and Roth Individual Retirement Accounts (IRAs): A Primer*, by John J. Topoleski. For more information on current laws on IRAs, see U.S. Congress, Joint Committee on Taxation, Present Law And Analysis Relating To Individual Retirement Arrangements, 110th Cong., 2nd sess., June 24, 2008, JCX-53-08.

Traditional IRAs, Roth IRAs, and Rollover IRAs

The two types of IRAs available to households in which either the head of the household or the spouse receives income from wages are traditional IRAs and Roth IRAs.[4] Traditional and Roth IRAs differ in their eligibility requirements and the tax treatment of contributions and withdrawals. Individuals can also rollover lump-sum retirement assets from an employer-sponsored pension or an IRA into a rollover IRA. Rollover IRAs may be either traditional IRAs, in which investment earnings continue to accumulate tax-deferred, or Roth IRAs, in which investment earnings continue to accumulate tax-free.

Traditional IRAs

Individuals with taxable compensation who are under the age of 70½ can contribute to traditional IRAs. Traditional IRAs have at least two tax advantages over accounts that do not receive tax advantages: (1) the tax-deductibility of contributions allows individuals to have larger yearly contributions than otherwise would be the case; and (2) the earnings grow tax-deferred.

Individuals may annually contribute the lesser of $5,000 or their taxable compensation to an IRA. Individuals aged 50 or older may make an additional $1,000 annual contribution.[5] Contributions to traditional IRAs are tax-deductible (up to the maximum contribution) for individuals who (1) are not covered by an employer-sponsored pension plan or (2) are covered by an employer-sponsored pension plan but have income under statutory limits.[6] In 2010, the phase out of the deduction begins at an Adjusted Gross Income (AGI) of $55,000 for single filers with pension coverage; at an AGI of $89,000 for married filers in which the head of the household has pension coverage; and at an AGI of $166,000 for married filers in which the head of the household does not have pension coverage but in which the spouse is covered by a pension plan. No deduction is allowed for AGI of $65,000 or more for single filers with pension coverage; $109,000 or more for married filers in which the head of the household has pension coverage; or $176,000 or more for married filers in which the head of the household does not have pension coverage but in which the spouse is covered by a pension plan.[7]

[4] Although individuals open traditional and Roth IRAs, employers may sponsor one of two kinds of IRA-based retirement plans: Simplified Employee Pension (SEP-IRAs) or Savings Incentive Match Plan for Employees (SIMPLE-IRA). Both kinds of employer-sponsored IRAs have higher contribution limits than traditional or Roth IRAs but are otherwise subject to many of regulations that govern IRAs. SEP- and SIMPLE-IRAs were created to allow employers to provide retirement accounts for their employees but without many of the regulatory requirements of 401(k) plans. For more information, see U.S. Government Accountability Office, *Individual Retirement Accounts: Government Could Encourage More Employers to Offer IRAs to Employees*, GAO-08-590, June 4, 2008.

[5] The contribution limits are adjusted annually for inflation.

[6] Individuals are considered covered by a pension plan if contributions have been made to a defined contribution plan in the tax year or if they are eligible to participate in a defined benefit. Individuals are not considered covered by a pension plan if they are only covered under Social Security, Railroad Retirement, or if the only reason for their participation in a pension plan is because they are reservists or volunteer firefighters. See 26 U.S.C. 219(g) and IRS Publication 590, *Individual Retirement Arrangements (IRAs)*, available at http://www.irs.gov/publications/p590.

[7] IRS Publication 590, *Individual Retirement Arrangements (IRAs)*, has details on calculating the deductible amount of IRA contributions. It is available at http://www.irs.gov/publications/p590/ch01.html#en_US_publink1000230433.

Withdrawals from traditional IRAs, except for that part of a withdrawal that represents after-tax contributions, must be included in account holders' taxable income.[8] Congressional intent was that IRAs were to provide financial security in retirement and not be used for either pre-retirement expenses or as tax-free asset transfers to heirs. Most withdrawals from traditional IRAs before the account holder reaches the age of 59½ are subject to an additional 10% penalty tax, unless the reason for the withdrawal meets one of the exceptions found in 26 U.S.C. § 72(t).[9] In addition, account holders older than the age of 70½ must receive Required Minimum Distributions (RMDs). RMDs are withdrawals of a specified percentage of the IRA balances each year.[10]

Roth IRAs

Roth IRAs were authorized by the Taxpayer Relief Act of 1997 (P.L. 105-34). The key differences between traditional and Roth IRAs are that (1) contributions to Roth IRAs are not tax-deductible (thus the contributions are after-tax dollars) and (2) qualified distributions are not included in taxable income. The annual contribution limit to Roth IRAs is the lesser of $5,000 or the individual's taxable compensation.[11] Individuals aged 50 or older may make an additional $1,000 annual contribution. Contributions to Roth IRAs are permitted only by individuals with incomes under prescribed statutory limits, currently at $120,000 for single filers and $176,000 for joint filers. Because qualified distributions are tax-free, Roth IRAs have no RMD requirement.

Rollover IRAs

Rollovers are transfers of assets from one retirement plan to another retirement plan, often upon separation from an employer. Generally, individuals may rollover account balances from employer-sponsored pension plans into traditional or Roth IRAs upon separation from employment. Individuals may also rollover traditional IRA account balances to Roth IRAs. Rollovers not completed within 60 days are considered taxable distributions. Rollovers are considered neither distributions nor contributions. The amount of the rollover is not included in taxable income, is not subject to the contribution limits, nor subject to rules that govern early distributions. Rollovers can come from traditional IRAs or from employers' pension plans. Prior to 2010, rollovers into Roth IRAs were limited to individuals with incomes under specified limits[12]; these income limits were eliminated beginning in 2010.[13]

---

[8] Withdrawals that represent non-deductible contributions do not have to be included in income because doing so would subject the contributions to double taxation since income used to make non-deductable contributions is taxed when the income is earned.

[9] Some of the exceptions to the early withdrawal penalty include distributions for higher-education expenses, purchase of a first home, or if the individual becomes disabled. For more information, see CRS Report R40192, *Early Withdrawals and Required Minimum Distributions in Retirement Accounts: Issues for Congress*, by John J. Topoleski.

[10] The percentage is based on the individual's life expectancy according to IRS-approved mortality tables.

[11] While individuals may contribute to traditional IRAs, Roth IRAs, or both, an individual's total annual IRA contribution to all IRAs cannot exceed the lesser of $5,000 ($6,000 if aged 50 or older) or total taxable compensation.

[12] In 2009, individuals with Modified Adjusted Gross Income (for Roth IRA purposes) over $100,000 could not rollover amounts to Roth IRAs.

[13] These were eliminated by the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA, P.L. 109-222).

Legislative History of IRAs

IRAs were first authorized in 1974 by the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406) to encourage workers who did not have a pension plan at work to save for retirement. Prior to ERISA, Congress allowed self-employed individuals and their employees to make tax-deductible contributions to Keogh accounts for the purpose of providing for income in retirement.[14] Some Keogh plan features, such as imposing penalties for withdrawing funds before the account owner reached the age of 59½ or for failing to take required withdrawals after the age of 70½, were incorporated into the design of IRAs.

Table 1 lists the major IRA legislation since 1974 that has affected eligibility for and contributions to IRAs.

From 1974 to 1981, only individuals who were not covered by an employer-sponsored pension plan could establish and contribute to IRAs. From 1982 to 1986, all workers regardless of pension coverage could make tax-deductible IRA contributions (up to the annual limit). Because of the revenue loss to the U.S. Treasury, the Tax Reform Act of 1986 (P.L. 99-514) limited the tax deduction on IRA contributions to non-covered workers and to covered workers with incomes under $25,000.[15] Since 1986, workers without pension coverage and workers with pension coverage and who have incomes under prescribed limits can make tax-deductible IRA contributions (up to the annual limit) while covered workers who have incomes greater than the prescribed limits may make non-deductible contributions.

Annual Contribution Limits

The annual contribution limit was set at $1,500 in 1974 and was increased to $2,000 in 1982. The limit was increased to $3,000 in 2002, $4,000 in 2005, and has been annually inflation-adjusted for increases in the Consumer Price Index (CPI) since 2008. The contribution limit for 2010 is $5,000. Beginning in 2002, individuals aged 50 and older could make an additional annual $500 “catch up” contribution to their IRAs. This was increased to $1,000 beginning in 2006. From 1982 to 1996, a non-working spouse could annually contribute $250 to an IRA. Since 1997, the contribution limit for non-working spouses has been equal to the contribution limit for working spouses.[16]

[14] Keogh plans, also known as H.R. 10 plans, were established in 1962 by the Self-Employed Individuals Tax Retirement Act (P.L. 87-792) to encourage the owners of small businesses to establish retirement plans through the use of tax-deferred savings.

[15] The Office of Management and Budget (OMB) estimated the tax expenditure for IRA contributions in 1986 to be $19.6 billion ($39.1 billion in 2009 dollars). See *Budget of the United States Government, Fiscal Year 1986*, Office of Management and Budget. OMB estimated the tax expenditure for IRA contributions in 2009 to be $12.1 billion. See *Budget of the United States, Table 16–1. Estimates of Total Income Tax Expenditures for Fiscal Years 2009 - 2015* available at http://www.whitehouse.gov/sites/default/files/omb/budget/fy2011/assets/receipts.pdf.

[16] For example, a married household in which neither the head nor spouse has a pension plan at work could make a total tax-deductible contribution of $10,000 to their IRAs in 2010.

Tax-Deduction for Traditional IRA Contributions

From 1974 to 1981, workers covered by a pension plan at work were prohibited from making IRA contributions. From 1982 to 1986, workers covered by an employer-sponsored pension plan could make tax-deductible contributions up to the annual limit of $2,000 to an IRA. Since 1987, workers covered by a pension plan may deduct 100% of their IRA contribution only if their incomes are under statutory limits. The percentage of the contribution that may be deducted is gradually reduced from 100% to 0% for incomes that are $10,000 or $20,000 (depending on filing status) greater than the statutory limits. No deduction is available for taxpayers with income greater than the upper limit of the phase-out range.[17]

Since 1998, workers with taxable income under statutory limits could make contributions to Roth IRAs. The maximum contribution to a Roth IRA is phased out for persons with income greater than limits specified in statute.[18]

Table 1. Individual Retirement Accounts: Major Laws Affecting Eligibility and Contributions

Law	Major Provisions Affecting IRAs
Employee Retiree Income Security Act of 1974 (ERISA, P.L. 93-406)	Allowed workers without pensions to make up to $1,500 in annual deductible contributions. Workers with pension coverage were ineligible to open IRAs.
Economic Recovery Tax Act of 1981 (P.L. 97-34)	Extended IRA eligibility to individuals in covered employment.
	Raised the annual contribution limit to $2,000.
	Allowed non-working spouses to make annual IRA contributions up to $250.
Tax Reform Act of 1986 (P.L. 99-514)	Began to phase out the tax-deduction for contributions for single filers who have pension coverage at work and who made more than $25,000 per year or married filers who made more than $40,000.
Small Business Job Protection Act of 1996 (P.L. 104-188)	Raised the contribution limit for non-working spouses from $250 to $2,000.

[17] See 26 U.S.C. § 219(g). The phase-out range is $10,000 for single filers with pension coverage and married filers in which the head of the household does not have pension coverage but in which the spouse is covered by a pension. For married filers in which the head has pension coverage and in which the spouse also has pension coverage, the phase-out range was increased from $10,000 to $20,000 beginning in 2007. The threshold at which phase-out for the deduction begins depends on the filing status and pension coverage of the taxpayer and the spouse's pension coverage. For single filers with pension coverage, the deduction phase-out began at $25,000 from 1987 to 1997; $30,000 in 1998; $31,000 in 1999; $32,000 in 2000; $33,000 in 2001; $34,000 in 2002; $40,000 in 2003; $45,000 in 2004; $50,000 in 2005 and 2006; $52,000 in 2007; $53,000 in 2008; $55,000 in 2009; and $56,000 in 2010. For married filers in which the head of the household has pension coverage, the deduction phase-out began at $40,000 from 1987 to 1997; $50,000 in 1998; $51,000 in 1999; $52,000 in 2000; $53,000 in 2001; $54,000 in 2002; $60,000 in 2003; $65,000 in 2004; $70,000 in 2005; $75,000 in 2006; $83,000 in 2007; $85,000 in 2008; and $89,000 in 2009 and 2010. For married filers in which the head does not have pension coverage but in which the spouse has pension coverage, the deduction phase-out began at $40,000 from 1987 to 1997; $150,000 from 1998 to 2006; $156,000 in 2007; $159,000 in 2008; $166,000 in 2009; and $167,000 in 2010.

[18] The phase-out range is $15,000 for single filers and $10,000 for taxpayers filing joint returns. For single files, the phase began at $95,000 from 1998 to 2006; $99,000 in 2007; $101,000 in 2008; $105,000 in 2009; and is $105,000 in 2010. For taxpayers filing joint returns, the phase out began at $150,000 from 1998 to 2006; $156,000 in 2007; $159,000 in 2008; $160,000 in 2009; and is $167,000 in 2010.

Law	Major Provisions Affecting IRAs
Taxpayer Relief Act of 1997 (TRA,P.L. 105-34)	Raised the threshold at which phase-out of the tax deduction for contributions begins: • *Single filers who have pension coverage at work*: $30,000 in 1998; $31,000 in 1999; $32,000 in 2000; $33,000 in 2001; $34,000 in 2002; $40,000 in 2003; $45,000 in 2004; and $50,000 after 2004. • *Married filers in which the head of the household has pension coverage and in which the spouse also has pension coverage*: $50,000 in 1998; $51,000 in 1999; $52,000 in 2000; $53,000 in 2001; $54,000 in 2002; $60,000 in 2003; $65,000 in 2004; $70,000 in 2005; $75,000 in 2006; $80,000 after 2006. • *Married filers in which the head of the household does not have pension coverage but in which the spouse has pension coverage*: $150,000. Increased the phase-out range for married filers who file a joint return from $10,000 to $20,000. Created the Roth IRA.
Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16)	Raised the contribution limit to $3,000 in 2002; $4,000 in 2005; and $5,000 in 2008. Allowed "catch-up" contributions: individuals aged 50 and older could make an additional yearly contribution of $500 from 2002 to 2005 and $1,000 in each year thereafter. Adjusted, based on increases in the Consumer Price Index (CPI) beginning in 2008, the following: the IRA contribution limits; the income threshold above which taxpayers may not claim a tax-deduction for traditional IRA contributions; and the income threshold above which taxpayers may not make Roth IRA contributions. Established the Retirement Savings Contributions Credit to encourage lower income workers to save for retirement.
Pension Protection Act of 2006 (P.L. 109-280)	Made permanent EGTRRA provisions establishing the Retirement Savings Contributions Credit and the adjustments in contribution limits and income thresholds for the Consumer Price Index.
Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222)	Removed income restriction on converting traditional IRAs to Roth IRAs beginning in 2010.

Source: Congressional Research Service (CRS).

Notes: Covered workers have either defined benefit or defined contribution pension plans provided through their workplace.

Tax-deductible IRA Contributions from 1974 to 2007

Less than 3% of taxpayers made tax-deductible IRA contributions in 2007. As a percentage of all tax returns filed, fewer tax returns had IRA deductions in 2006 and 2007 than in any year since 1977. **Figure 1** through **Figure 4** show historical tax-deductible IRA contributions.[19] **Figure 1**

[19] The data used in this report are from two sources: (1) Internal Revenue Service (IRS), Statistics of Income Division, Individual Income Tax Returns and (2) The Federal Reserve Board, Survey of Consumer Finances. The IRS publishes detailed tax data from Form 1040. IRS data for 1974 to 1983 is from *IRS Publication 75, Individual Income Tax Returns*; data for 1985 to 2007 is from *IRS publication 1304, Individual Income Tax Returns.* Data for 1990 to 2007 is (continued...)

shows the inflation-adjusted yearly amount of tax-deductible contributions to traditional IRAs from 1974 to 2007. **Figure 2** shows the inflation-adjusted average tax-deductible contribution. **Figure 3** and **Figure 4** show the number and percentage of taxpayers who made tax-deductible IRA contributions from 1974 to 2007. The total amount of IRA contributions was nearly twice as much in 1981 compared with 1975, although the average amount was more than 30% lower. The large increase in 1982 both in the number and percentage of returns reporting IRA contributions and the average amount of IRA contributions is a result of the Economic Recovery Tax Act of 1981 (P.L. 97-34), which extended eligibility for IRAs to workers with employer-sponsored pensions. The Tax Reform Act of 1986 (P.L. 99-514) that limited the eligibility for tax-deductible contributions beginning in 1987 sharply curtailed both the number of returns reporting IRA contributions and the average IRA contribution. This suggests that tax-deductible IRA contributions were largely made by workers with higher incomes and pension coverage.

The data suggest that since the mid-1990s some taxpayers have responded to changes in the contribution limit. The total and average value of IRA contributions generally declined from 1990 to 2001. Total tax-deductible IRA contributions were 46% lower in 2001 compared with 1990 and the average contribution was 16% lower. From 1987 to 2001, neither the income limit for eligibility for tax-deductible contributions nor the contribution limit was increased, although in real (inflation-adjusted) terms these limits were more than 25% lower in 2001 than in 1987. The 5.5% increase in average IRA contributions from 1996 to 1997 may be due to an increase in the contribution limit for non-working spouses from $250 to $2,000.

The increases in the contribution limit from $2,000 to $3,000 in 2002 and from $3,000 to $4,000 in 2005 were accompanied by increases in the average contribution. Interestingly, there was not a corresponding rise in the number of returns reporting an IRA contribution nor a rise in the percentage of returns reporting a contribution. This suggests that the response to these changes was among taxpayers who were already contributing near the contribution limit and increased the amount of their contributions. This is consistent with research that has shown that many individuals who make IRA contributions contribute close to the statutory limit.[20]

The introduction of Roth IRAs beginning in 1998 appears to have had no effect on the total amount of the contributions to traditional IRAs nor on the average traditional IRA tax-deductible contribution. Continuing the trend that began in 1990, both total and average IRA contributions were lower from 1998 to 2001, the first four years of the existence of Roth IRAs.[21] While it is possible that the decline in traditional IRA contributions over this period is as a result of taxpayers making Roth IRA contributions instead, a more likely explanation is that decline in traditional IRA contributions is a result of the decreased real value of the IRA contribution limit.

(...continued)

available online from *Table A: Selected Income and Tax Items for Selected Years (in Current and Constant Dollars)* available at[http://www.irs.gov/taxstats/indtaxstats/article/0,,id=134951,00.html#_tbla. The Survey of Consumer Finances (SCF) is a triennial survey conducted on behalf of the Board of Governors of the Federal Reserve and contains detailed information on U.S. household finances, such as the amount and types of assets owned, the amount and types of debt owed, and detailed demographic information on the head of the household and spouse. Each survey interviews different households to provide separate cross-sections of data. The SCF uses the household as the unit of analysis as assets such as homes and bank accounts are often jointly owned by married couples. Further information on the SCF is available in the codebook at http://www.federalreserve.gov/PUBS/oss/oss2/2007/codebk2007.txt.

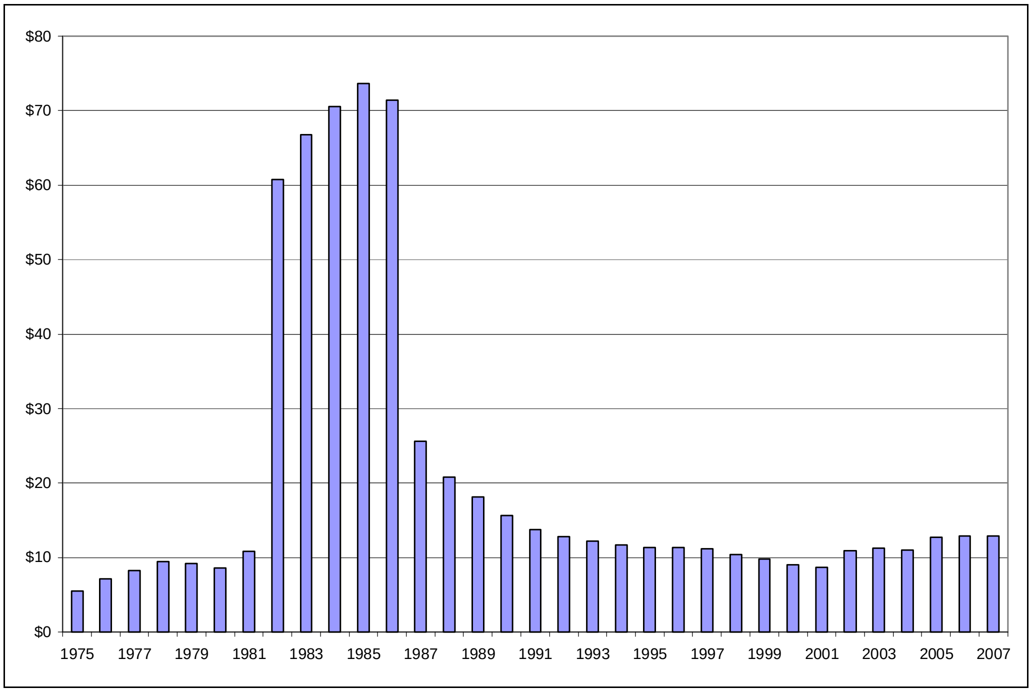
[20] See, for example, *The American Economic Review*, Vol. 84, No. 5 (Dec., 1994), “IRAs and Household Saving,” by William G. Gale and John Karl Scholz.

[21] The contribution limit for traditional IRAs remained unchanged over this period.

Roth IRA contributions were likely not a result of individuals shifting their contributions from traditional IRAs to Roth IRAs.

Figure 1. Total Value of Tax-Deductible Contributions to Traditional IRAs

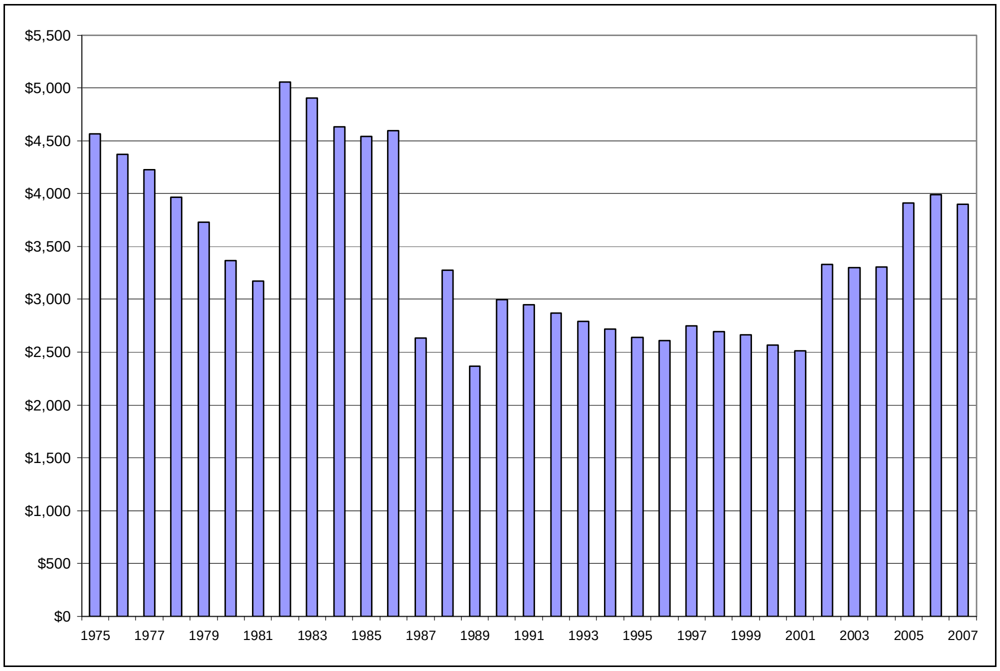
Calendar Years 1975 – 2007, Billions of 2007 Dollars



Source: CRS analysis of various years of *Statistics of Income* data from the Internal Revenue Service.

Figure 2. Average Value of Tax-Deductible Contributions to Traditional IRAs

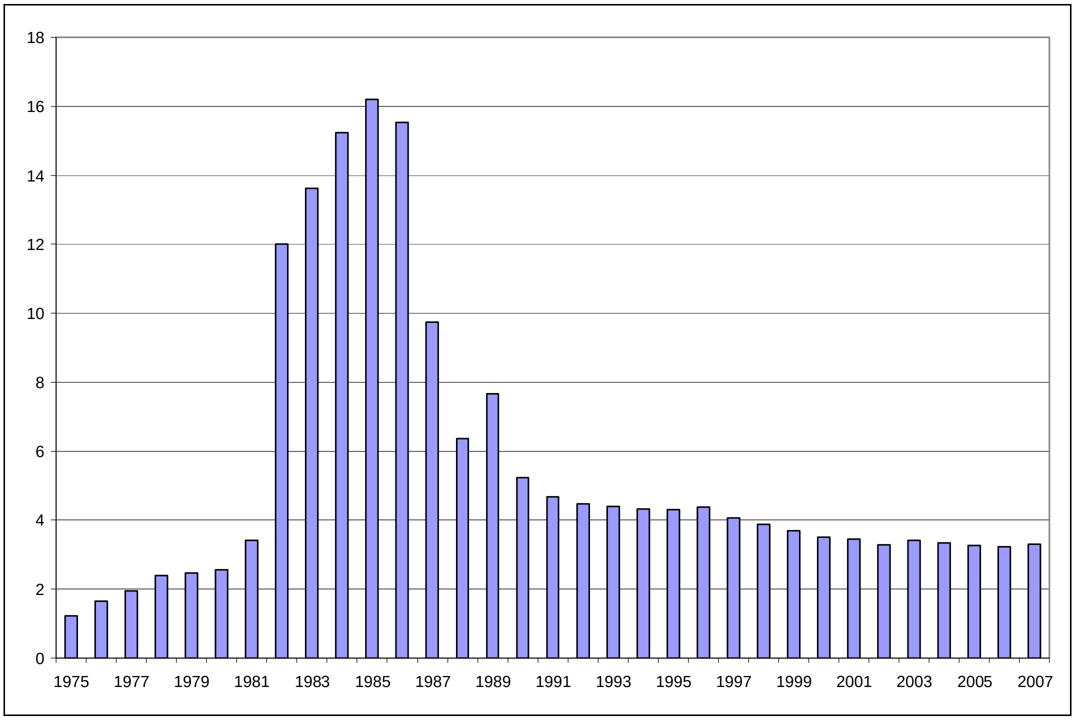
Calendar Years 1975 – 2007, Constant 2007 Dollars



Source: CRS analysis of various years *of Statistics of Income* data from Internal Revenue Service.

Figure 3. Number of Tax Returns with Tax-Deductible Contributions to Traditional IRAs

Calendar Years 1975 – 2007, Millions of Returns

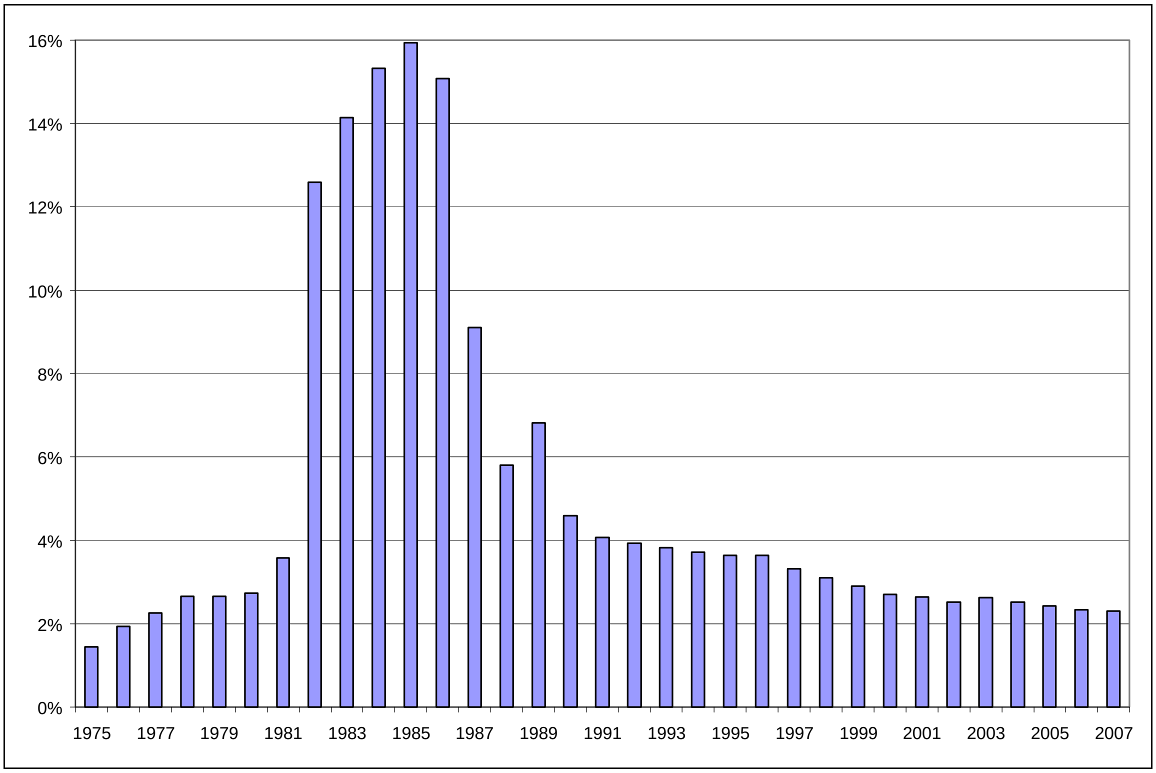


Source: CRS analysis of various years *of Statistics of Income* data from Internal Revenue Service.

Figure 4 shows that the percentage of taxpayers who make IRA contributions was highest in 1985 at 15.9%; declined sharply after 1986 as a result of the limitations on tax-deductible contributions by workers covered by a pension plan; and gradually declined from 1989 (4.7%) to 2007 (2.3%). Since 1999, less than 3% of tax returns each year reported tax-deductible contributions to traditional IRAs.

Figure 4. Percentage of Tax Returns with Tax-Deductible Contributions to Traditional IRAs

Calendar Years 1975 – 2007



Source: CRS analysis of various years *of Statistics of Income* data from Internal Revenue Service.

Contributions to Traditional IRAs in 2007

Although less than 3% of taxpayers made a tax-deductible contribution in 2007, the average contribution was $3,902, which suggests that many households made close to the maximum allowable contribution.[22] Contributions to traditional IRAs were disproportionately made by households with higher incomes. **Table 2** indicates that although households with Adjusted Gross Incomes of less than $50,000 in 2007 filed 65.6% of all federal income tax returns, these households accounted for 41.1% of households claiming deductions for IRA contributions and 32.0% of the total dollar amount of tax-deductible IRA contributions. Higher-income households

[22] Recent research indicates that the median contribution in 2008 was $3,300 to traditional IRAs and was $3,500 to Roth IRAs. See the Investment Company Institute's Research Fundamentals, *The Role of IRAs in U.S. Households' Savings for Retirement, 2009,* by Sarah Holden, available at http://www.ici.org/pdf/fm-v19n1.pdf.

have an incentive to make tax-deductible IRA contributions as they are in higher tax brackets and receive a greater benefit for each tax-deductible dollar contributed to a traditional IRA.[23] Both the percentage of households that made tax-deductible IRA contributions and the average IRA contribution amount increased with household income. Of the 93.8 million tax returns with incomes below $50,000, approximately 1.4 million (1.4%) claimed the IRA deduction whereas of the 29.7 million tax returns with incomes above $75,000, 1.2 million (4.1%) claimed the deduction.[24] The average IRA contribution among taxpayers with incomes above $100,000 was $5,440, which was more than twice the average IRA contribution among households with incomes below $25,000.

Table 2. Tax-Deductible IRA Contributions in 2007

	Adjusted Gross Income				
	Less than $25,000	**$25,000 to $49,999**	**$50,000 to $74,999**	**$75,000 to $99,999**	**$100,000 or more**
Number of Returns Filed (Thousands)	58,893.5	34,896.9	19,450.7	11,744.1	17,993.5
Number of Returns Reporting IRA Contributions (Thousands)	450.1	905.1	736.0	481.0	727.6
Percentage of Returns Reporting IRA Contributions	0.8%	2.6%	3.8%	4.1%	4.0%
Total IRA Contributions (Billions)	$1.2	$2.9	$2.9	$1.9	$4.0
Average IRA Deduction Per Return	$2,656	$3,225	$3,907	$4,010	$5,440

Source: CRS analysis of the Internal Revenue Service's *Statistics of Income* data.

Notes: Table reflects tax-deductible contributions to traditional IRAs only. Contributions to Roth IRAs and non-deductible contributions to traditional IRAs are not reported in the *Statistics of Income* data.

IRA Ownership and Account Balances in 2007

The Survey of Consumer Finances (SCF) indicates that 28.2 million (32.7%) working households owned an IRA in 2007. Among working households that had IRAs, 77.0% had a single IRA and 23.0% had more than one IRA.

Table 3 indicates that more working households had traditional IRAs in 2007 (15.9 million) than had Roth IRAs (10.2 million) or Rollover IRAs (9.4 million). [25] Roth IRAs have been popular.

[23] Households under certain income limits (single filers with incomes up to $27,750 or married filers with incomes up to $55,500) are eligible for the non-refundable Retirement Savings Contributions Credit of up to $1,000 per year. Approximately 5.9 million households received the credit in 2007, although the IRS data does not break down the numbers for contributions to IRAs versus contributions to DC plans. For more information, see CRS Report RS21795, *The Retirement Savings Tax Credit: A Fact Sheet*, by John J. Topoleski

[24] These percentages are calculated from data in **Table 2**. Approximately 93.8 million tax returns had incomes less than $50,000 in 2007. Among tax returns with incomes below $50,000, 1.4 million tax returns claimed the IRA deduction. Among tax returns with incomes of $75,000 or greater, 1.2 million tax returns claimed the IRA deduction.

[25] The Investment Company Institute (ICI) estimates that 37.7 million U.S. households (32.5%) owned a traditional (continued...)

Although Roth IRAs were authorized in 1997—23 years after traditional IRAs—**Table 3** shows that there were two-thirds as many Roth IRAs as traditional IRAs in 2007.[26] Because Roth IRAs have not had as long to accrue contributions and investment earnings, the median Roth IRA account balance was $10,000, which was 63% lower than the median account balance of traditional IRAs ($27,000).[27]

In 2007, IRA assets totaled $3.0 trillion. A plurality of IRA assets were held in Rollover IRAs. Rollover IRAs held $1.4 trillion in assets in 2007, which was 46.3% of all IRA assets; traditional IRAs held $1.3 trillion in assets in 2007, which was 43.7% of all IRA assets; and Roth IRAs held $306 billion in assets in 2007, which was 10.1% of all IRA assets. The median rollover IRA account balance was nearly twice as large as the median traditional IRA account balance and more than five times as large as the median Roth IRA account balance. This is likely because traditional and Roth IRAs consist mostly of yearly contributions whereas Rollover IRAs consist of large sums transferred from other retirement accounts, like 401(k) plans.

Table 3. IRA Ownership Among Working Households in 2007

	Traditional IRA	Roth IRA	Rollover IRA
Number of households (millions)	15.9	10.2	9.4
Total assets (billions)	$1,327	$306	$1,406
Percentage of total IRA assets	43.7%	10.1%	46.3%
Average account balance	$83,661	$30,141	$149,490
Median account balance	$27,000	$10,000	$50,000

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Note: Percentages do not add to 100% due to rounding.

(...continued)

IRA in 2007 and 17.3 million households (14.9%) owned Roth IRAs in 2007. See *Appendix: Additional Data on IRA Ownership*, January 2010, available at http://www.ici.org/pdf/fm-v19n1_appendix.pdf. The ICI estimate does not separately classify rollover IRAs, it includes rollover IRAs as either traditional or Roth IRAs. ICI includes households in which neither the head of the household nor the spouse were working. This report focuses on IRA ownership among households in which either the head or the spouse were working at the time of the survey. Households in which neither the head of the household nor the spouse were working would not be able to contribute to either a traditional or Roth IRA. The SCF indicates that in 2007, of the 116 million working and non-working households in the United States, 35 million (30.31%) had a traditional IRA, Roth IRA, or Rollover IRA. Households in which neither the head of the households nor the spouse were working could still own IRAs as a result of contributions made in previous years.

[26] The analysis of data in this report emphasizes medians rather means or simple averages. The median is the middle value of a series of numbers, such that half the values are above the median and half are below the median. Many financial variables are skewed; that is, some individuals or households report very large values. In such cases, median values may be better representative of data series than average values; average values are influenced by a few very large values.

[27] Amounts in traditional and Roth accounts may not be directly comparable. Amounts withdrawn from traditional IRAs generally must be included in taxable income, so traditional IRA account balances generally overstate the amount available for spending after taxes are taken into account. Roth IRA withdrawals are not included in taxable income. Most Rollover IRAs are likely in taxable accounts, although some Rollover IRAs may be after-tax.

Most households that had traditional IRAs did not make taxable contributions to their IRAs in 2007. Although 15.9 million households had a traditional IRA in 2007, only 3.3 million tax returns reported tax-deductible contributions to traditional IRAs.[28]

IRAs and Pension Coverage

Although IRAs were authorized to encourage workers without pension coverage to save for retirement, IRA ownership is greater among households with pensions than among households without pensions. **Table 4** indicates that 38.7% of households with pension coverage had IRAs in 2007, compared with 25.3% of households without pension coverage. With regard to current policy, the data highlight that many individuals have not responded to the tax incentives designed to encourage IRA ownership among households without pension coverage.[29]

Table 4. Pension Plan Coverage and IRA Ownership Among Working Households in 2007

Household Has Pension		Household Does Not Have Pension	
Number with IRA (millions of households)	**Percentage**	**Number with IRA (millions of households)**	**Percentage**
18.3	38.7%	9.9	25.3%

Source: CRS analysis the 2007 Survey of Consumer Finances.

Note: Data is for households in which either the head of the household, the spouse, or both worked.

IRA Ownership and Firm Size

As **Table 5** shows, pension coverage increased with firm size in 2007. Among households with pension coverage, IRA ownership rates were highest in workplaces that had fewer than 20 employees. Small professional offices (e.g., medical practices and law firms) are more likely to offer pension plans than non-professional small businesses. These professionals (with high incomes and education levels) are also more likely to have IRAs. Among households without pension coverage (except for households that work in firms with 100—499 employees), about one-quarter own an IRA.

[28] IRS tax data are not available on the number of households that made non-deductible traditional IRA contributions, Roth IRA contributions, or Rollover IRA contributions.

[29] Individuals are considered covered by a pension plan if contributions have been made to a defined contribution plan in the tax year or if they are eligible to participate in a defined benefit plan. Individuals are not considered covered by a pension plan if they are only covered under Social Security, Railroad Retirement, or if the only reason for their participation in a pension plan is because they are reservists or volunteer firefighters. See 26 U.S.C. 219(g) and IRS Publication 590, Individual Retirement Arrangements (IRAs), available at http://www.irs.gov/publications/p590/ch01.html#en_US_publink1000230449.

Table 5. Pension Plan Coverage and IRA Ownership by Size of Employer, 2007

Size of Employer	Percentage of Households with Pension Coverage	Households with Pension Coverage		Households without Pension Coverage	
		Number with IRA (millions)	Percentage with IRA	Number with IRA (millions)	Percentage with IRA
Less than 20 employees	24.6%	2.8	48.1%	4.4	24.4%
20 - 99 employees	52.1%	2.3	35.0%	1.5	24.0%
100 - 499 employees	64.0%	2.6	33.5%	0.8	18.1%
500 or more employees	72.2%	9.2	35.9%	2.3	23.5%

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Notes: Size of employer is for head of household or spouse, whoever is working. If both head and spouse work, then size of employer is for person with larger IRA balance.

IRA Ownership and Industry of Workers

Table 6 shows that in 2007 pension plan coverage was highest among workers in the public sector and manufacturing industries and was lowest among workers in agriculture, mining, or construction industries. Among households without pension coverage, rates of IRA ownership varied considerably by industry. Households with workers in agriculture, mining, and construction industries had low rates of IRA ownership (11.3%) whereas about one-third (33.6%) of households with workers who worked in financial services had IRAs.

Table 6. Pension Plan Coverage and IRA Ownership by Industry, 2007

Industry of Employer	Percentage of Households with Pension Coverage	Households with Pension Coverage		Households without Pension Coverage	
		Number with IRAs (millions)	Percentage with IRAs	Number with IRAs (millions)	Percentage with IRAs
Agriculture, mining, or construction	34.2%	1.4	34.7%	0.9	11.3%
Trade	43.5%	1.9	33.2%	1.5	19.7%
Public sector	87.5%	1.8	36.0%	0.1	20.4%
Manufacturing and transportation	65.7%	9.6	36.5%	4.7	28.0%
Financial services	49.3%	2.3	46.2%	1.7	33.6%

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Notes: Industry of employer is for head of household or spouse, whoever is working. If both head and spouse work, then industry is for person with larger IRA balance.

The low IRA ownership rates among households without pension coverage and who worked in agriculture, mining, or construction may reflect the transient nature of these occupations, high-employee turnover, or lower education levels. The higher rates of IRA ownership for financial services workers may be a result of greater education level or that these workers are likely to be more knowledgeable about the benefits of IRAs than workers in other industry groups. This suggests a potentially important role for financial literacy efforts. Increasing workers' knowledge of financial matters and helping workers improve financial decision-making skills may increase IRA ownership.

IRA Ownership, Pension Coverage, and Household Financial Characteristics

Table 7 shows financial characteristics (median dollar amounts) for households with and without IRAs and with and without pension coverage. Households that had both pension coverage and IRAs were the wealthiest group in the measures of median retirement assets, total assets, and net worth. This group also had higher median debt than the other groups. Households with IRAs (whether or not they had pensions) were wealthier than those without IRAs. For example, among households with pension coverage, those with IRAs had median net worth that was four times larger than households without IRAs ($411,000 versus $100,150). The gap was even larger among households without pension coverage, as those with IRAs had median net worth that was more than 16 times the net worth of households without IRAs ($339,540 versus $20,560).[30]

Table 7. Financial Characteristics of Households by Pension Coverage and IRA Ownership in 2007

Median Dollar Amounts

	Households with Pension Coverage		Households without Pension Coverage	
	Have IRA	Do not Have IRA	Have IRA	Do not Have IRA
Non-IRA retirement assets	$40,000	$12,000	$0	$0
Total retirement assets	$105,000	$12,000	$38,000	$0
Total assets	$602,800	$223,970	$484,300	$47,980
Debt	$135,000	$78,400	$72,000	$14,000
Net worth	$411,000	$100,150	$339,540	$20,560

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Demographic Characteristics and IRA Ownership

Table 8 provides a demographic breakdown of IRA owners, grouped by their pension coverage. In nearly every category, IRA ownership was higher among households with pension coverage.

[30] Non-IRA retirement assets are mainly 401(k) and other thrift accounts. Total assets are financial assets and non-financial assets. Financial assets are mainly saving and checking account, stocks, bonds, and savings bonds. Non-financial assets are mainly housing, vehicles, and business interests.

The exceptions were among households with incomes between $50,000 and $75,000; households with incomes greater than $100,000; and households in which the head of the household is aged 70 or older.

Income

IRA ownership increased with income for both households with and without pension coverage although households with pension coverage did not have higher IRA ownership rates in all income groups. Within income groups, there is not a clear pattern of IRA ownership between households with and without pension coverage. Households without pension coverage had higher IRA ownership rates than households with pension coverage in two income groups: households with incomes from $50,000 to $75,000 and households with incomes greater than $100,000. At least two factors might explain the higher IRA ownership rate for households with incomes greater than $100,000 and without pension coverage: (1) the positive correlation between IRA ownership and income and (2) all of these households were eligible for a tax deduction for their contributions because they did not have pension coverage and were likely in the highest income tax brackets, which means they received larger per-dollar tax benefits for each dollar of IRA contribution compared to lower income households.

Age

The 2007 Survey of Consumer Finances data show that for both households with and without pension coverage IRA ownership increased with age until age 70. Households in which the head was aged 70 or older had lower rates of IRA ownership than those aged 60 to 69.[31] The difference between rates of IRA ownership decreased as the age of the head of the household increased. Among households in which the head was under the age of 30, the rate of IRA ownership was 10.8 percentage points lower for households without pension coverage (22.5% compared with 10.7%). By comparison, among households in which the head was aged 60 to 69, the rate of IRA ownership was 1.9 percentage points lower for households without pensions (50.0% compared with 48.1%).

Education

IRA ownership rates were lower among households in which the head of the household did not have a college degree. The difference was particularly large among households without pensions: the rate of IRA ownership for households without pension coverage and in which the head had some college education was less than half the IRA ownership rate for households without pension coverage but in which the head had a college degree (23.8% versus 47.9%). This may indicate a willingness to trade current income for larger future income, as college students generally forgo at least some current income while anticipating higher income in the future. Contributing to an IRA is a similar decision, as IRA owners forgo current income in exchange for larger income in retirement.

[31] This difference may not be surprising given that the sample excludes households where neither the head nor spouse were working. Most households in which the head is aged 70 or older were retired and therefore not included in tabulations for this report.

Race and Ethnicity

The IRA ownership rate was 32.4% among households without pension coverage in which the head of the household was white, 7.3% among households that did not have pension coverage and in which the head was African-American, and 6.1% among households that did not have pension coverage and in which the head was Hispanic. Some of these groups may be particularly economically vulnerable, as they likely have few assets and may need to rely on Social Security for most of their retirement income.[32] The IRA ownership rate was 37.4% among households that did not have pension coverage and in which the head was Asian, Pacific-Islander, American Indian, or another race.[33]

Homeownership

IRA ownership rates were higher among homeowners than non-homeowners. Low IRA ownership rates among non-homeowners (17.9% for non-homeowners with pensions and 10.6% for non-homeowners without pensions) may reflect several factors. Homeownership rates increase as household income and age increase. In addition, homeownership may be a proxy for long-term planning or higher levels of financial literacy, both of which are associated with higher IRA ownership rates.

Marital Status

Married households had higher IRA ownership rates than single households, although the difference was not as pronounced among households without pension coverage. Among households without pension coverage, 26.9% of married households had IRAs in 2007, while 23.5% of single male households had IRAs and 22.5% of single female households had IRAs. It is interesting to note that IRA ownership rates were only one percentage point higher among single male households compared with single female households.

---

[32] Analysis of the SCF indicates that median net worth in 2007 was $163,000 among households in which the head of the household was white, and $17,100 (89.5% lower) among households in which the head was African-American, $21,010 (87.1% lower) among households in which the head was Hispanic, and $156,000 (4.3% lower) among households in which the head was not white, African-American, or Hispanic.

[33] For its public release, the SCF combines Asian, Pacific-Islander, American Indian, and other races into one category.

Table 8. Demographic Characteristics of IRA Owners

	Households with Pensions		Households without Pensions	
	Number of Households (millions)	Percentage with IRAs	Number of Households (millions)	Percentage with IRAs
Income				
< $50,000	2.2	17.6%	3.2	13.2%
$50,000 - 75,000	3.1	28.0%	2.2	32.8%
$75,001 - $100,000	3.7	45.1%	1.2	36.4%
> $100,000	9.4	59.4%	3.4	63.5%
Age				
20 – 29	1.1	22.5%	0.9	10.7%
30 – 39	3.2	30.4%	1.5	17.0%
40 – 49	5.5	40.0%	2.1	23.6%
50 – 59	6.0	46.7%	2.2	34.9%
60 – 69	2.2	50.0%	2.3	48.1%
70 and older	0.3	32.2%	0.9	45.3%
Education				
High school or less	3.1	20.5%	2.8	13.6%
Some college	4.1	34.9%	2.2	23.8%
Finished college	6.2	48.6%	2.8	47.9%
Graduate school	4.9	64.2%	2.1	57.3%
Head of household is				
White	15.5	43.4%	8.6	32.4%
African-American	1.0	18.7%	0.4	7.3%
Hispanic	0.7	20.0%	0.4	6.1%
Asian, Pacific-Islander, American Indian, or other	1.1	40.1%	0.6	37.4%
Household owns home	16.6	43.9%	8.2	36.2%
Household does not own home	1.7	17.9%	1.7	10.6%
Marital status of household				
Married	14.1	41.3%	6.5	26.9%
Single male	1.8	35.5%	1.4	23.5%
Single female	2.4	29.6%	2.1	22.5%

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Note: The Survey of Consumer Finances reports age, education, and racial / ethnic category for the head of the household. Income is reported for the entire household.

Saver Characteristics and IRA Ownership

Individuals vary in their preferences for saving. Some individuals may be quite willing to give up current consumption in order to receive higher consumption in the future. Other individuals may be less willing to make this trade-off. Individuals who have a high preference for saving may be more likely to own IRAs. **Table 9** presents IRA ownership rates in combination with factors that indicate attitudes toward saving. The Survey of Consumer Finances asks respondents a number of questions to elicit their attitudes toward saving. The answers might provide insight into saving propensities, which might be an important factor in determining which households own IRAs. Three questions in the survey related to saver type: (1) the household's most important reason for saving, (2) the most important time period in planning the family's spending and saving, and (3) the amount of shopping around to find the best terms when making saving and investment decisions.

Among both households with and without pension coverage, households that have higher propensities to save have higher IRA ownership rates. Among households without pension coverage, IRA ownership rates increase substantially as households increase their savings horizon from less than one year to a savings horizon of two to 10 years (from 12.3% to 31.0%), and as households increase the amount of shopping the household engages in when making saving decisions from little shopping to a moderate amount of shopping (from 18.0% to 28.5%). This suggests that efforts to increase financial literacy among less financially literate households may lead to higher IRA ownership rates.

Table 9. Saver Type Characteristics of IRA Owners, 2007

	Households with Pensions		Households without Pensions	
	Number of Households (millions)	**Percentage with IRAs**	**Number of Households (millions)**	**Percentage with IRAs**
Retirement is not primary reason for saving	7.3	29.9%	5.3	18.7%
Retirement is primary reason for saving	11.0	48.0%	4.6	42.9%
Savings horizon: 1 year or less	2.9	24.5%	1.8	12.3%
Savings horizon: 2 to 10 years	10.5	39.7%	6.2	31.0%
Savings horizon: More than 10 years	4.9	53.9%	1.8	44.9%
Household does little shopping when making savings decisions	4.6	32.0%	2.4	18.0%
Household does moderate shopping when making savings decisions	6.2	37.8%	3.8	28.5%
Household does a great deal of shopping when making savings decisions	7.5	45.2%	3.7	29.5%

Source: CRS analysis of the 2007 Survey of Consumer Finances.

Policy Options

Analysis of the data presented in this report suggests that pension plan coverage is an important factor for determining whether a household owns an IRA. IRA ownership is not as widespread among households without pension coverage, yet these are the households that IRAs are targeted to help. In fact, IRA ownership rates are more than 50% higher among households with pension coverage compared with households without any pension coverage. Households with neither IRAs nor pensions are about 34% of all working households and disproportionately represent economically vulnerable populations, such as lower-income, less-educated, and minority households. Some policymakers have expressed concern that many workers have inadequate savings for retirement. Half of the working households with neither pension coverage nor IRAs have net worth less than $20,560. In some cases, these workers may have less wealth than they anticipated to enjoy retirement. Some of these households may have to rely on public assistance to meet their basic needs. To formulate more effective retirement savings policies, policymakers need to be aware of how IRA ownership is affected by factors such as pension coverage, education, income, and behavior (e.g., saver characteristics).

An issue for policymakers is how to encourage workers to better prepare for retirement, particularly when they may have other, more immediate financial concerns. Retirement security is often thought of as a three-legged stool: Social Security, private savings, and employer-provided pensions. Although participation in Social Security is mandatory for most workers, the other legs have traditionally been voluntary, though encouraged through tax incentives. For example, employer contributions to pension plans are a tax-deductible expense; participants' contributions to defined contribution plans are not included in current taxable income; contributions to traditional IRAs may be tax-deductible; and qualified distributions from Roth IRAs are not taxed. Current tax incentives, however, may not be effective for some target populations. Several policy proposals have been suggested to help workers better prepare for retirement.

Changing the Retirement Savings Contributions Credit

The Retirement Savings Contributions Credit (the Saver's Credit) is an additional incentive to encourage lower-income households to save for retirement.[34] This non-refundable tax credit of up to $1,000 was authorized by the Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16) for eligible individuals who contribute to an IRA or an employer-sponsored retirement plan. The credit is available to single filers with incomes up to $27,750 and married filers with incomes up to $55,500. IRS data indicates that 5.9 million households received the Saver's Credit in 2007 and that the average amount of the credit received was $167. **Table 10** indicates that the credit may not be widely used: 5.9% of households with Adjusted Gross Incomes under $50,000 claimed the Saver's Credit in 2007.

[34] For more information see CRS Report RS21795, *The Retirement Savings Tax Credit: A Fact Sheet*, by John J. Topoleski.

Table 10. Retirement Savings Contributions Credit Use In 2007

Adjusted Gross Income	Number of Tax Returns With Saver's Credit (thousands)	Percentage of Tax Returns in AGI Group With Saver's Credit	Average (Mean) Saver's Credit Amount
Less than $10,000	30.5	0.1%	$74
$10,000 to $19,999	945.6	4.1%	$162
$20,000 to $29,999	2,042.6	10.8%	$173
$30,000 to $39,999	1,427.0	9.7%	$168
$40,000 to $49,999	1,126.5	10.1%	$159
$50,000 to $74,999	290.0	1.5%	$171

Source: Internal Revenue Service, *Statistics of Income* data.

Note: No returns with Adjusted Gross Income greater than $75,000 claimed the Saver's Credit in 2007.

Several factors may limit the effectiveness of the Saver's Credit: (1) it is non-refundable, so households with little or no tax liability receive little or no benefit; (2) it is not available to individuals who file their taxes using form 1040EZ; and (3) the credit may be used by individuals who would have made retirement plan contributions in the absence of the credit. Thus, not all retirement plan contributions tied to the credit are "new" contributions.[35]

Adopting Automatic IRAs

Because current tax and other incentives have not substantially increased voluntary participation in the retirement savings system, some policymakers believe that IRA ownership rates could be raised through increased access to retirement accounts. One of the challenges is determining how to comprehensively provide retirement accounts to workers who do not have employer-sponsored pension plans. The success of automatic enrollment in 401(k) plans has prompted calls for an automatic enrollment program for IRAs.[36]

The Automatic IRA (Auto IRA) is a proposal for increasing workers' access to retirement accounts.[37] Under such proposals, employers above a certain size that have been in business a certain number of years and that do not offer a pension plan would be required to establish IRAs for their employees. The employer would direct a specified percentage of each employee's pay into the IRA. Eligible employees would automatically be enrolled by their employers in the Auto IRA program, but could opt-out of participation or change the amount of their contribution. Employers could, but would not be required to, match their employees' contributions.

[35] In the 111th Congress, Rep. Earl Pomeroy introduced H.R. 1961, the Savings for American Families' Future Act of 2009, and Sen. Kirsten Gillibrand introduced S. 3090. These bills would expand eligibility for the Saver's Credit and make the credit refundable. In addition, H.R. 1961 would double the amount of the tax credit if the credit is paid directly into a retirement account.

[36] In automatic enrollment defined contribution plans, new employees are deemed to be participating in the pension plan, so eligible participants must opt-out rather than opt-in to the plan. Participation may include employee and employer contributions to the account.

[37] In the 111th Congress, Sen. Jeff Bingaman introduced S. 3760, the Automatic IRA Act of 2010, which would provide for Auto IRAs. Rep. Richard Neal introduced companion legislation, H.R. 6099. Further background on the Auto IRA proposal can be found in *Pursuing Universal Retirement Security Through Automatic IRAs*, by J. Mark Irwy and David C. John, available at http://www.brookings.edu/papers/2009/07_automatic_ira_iwry.aspx.

Although approximately 39.1 million households work for employers that do not offer pension plans (about 50% of U.S. working households), not all of these households would be covered by Auto IRAs. Some households might work for employers that are small enough to be exempt from offering Auto IRAs or some households might not meet job tenure requirements.[38]

An Auto IRA program for most workers without pension coverage could be costly to implement and administer, as millions of individual accounts would likely need to be processed. One goal of Auto IRA proponents is to minimize employers' administrative burdens and fiduciary obligations. For example, there may be questions about which default investments are appropriate for workers that do not make active participation decisions. In addition, Auto IRAs would provide IRAs to some workers who already have traditional or Roth IRAs. Among households that do not have an employer-sponsored pension plan, and therefore would be potentially eligible for the Auto IRA, 25.3% already own IRAs. While individuals could opt out of the Auto IRA, the possibility exists that some individuals may inadvertently exceed the yearly IRA contribution limit. The tax penalty is 6% of amount of the excess contribution.[39] The Treasury Inspector General for Tax Administration noted that noncompliance with IRA contribution limits is an area of concern and that the IRS has inadequate procedures to ensure compliance. It is estimated that 146,976 taxpayers exceeded the contribution limit in 2007.[40]

Improving Financial Literacy

Efforts to improve financial literacy may increase IRA contributions and ownership rates by increasing knowledge of the benefits of IRAs, the Saver's Credit, and the option to have federal income tax refunds deposited directly to IRAs. Many government agencies, non-profit groups, and for-profit companies have ongoing campaigns aimed at improving financial literacy (for example, increasing awareness of credit card fees). In particular, some of these efforts focus on the importance of saving for retirement.[41]

Increasing Fee Transparency

Small differences in the amount of fees that financial institutions charge for managing IRAs can yield large differences in the account balances at retirement. Some policymakers have expressed concern regarding the fees that financial institutions charge 401(k) plan participants. Legislation has been introduced that would increase 401(k) plan sponsors' and participants' awareness of the fees that they pay.[42] However, legislation to increase fee transparency for IRA owners has not been introduced. The Department of Labor recently issued an interim final rule that would require

[38] The SCF indicates that 10.4 million households worked for an employer that had less than 10 employees and did not offer a pension plan in 2007.

[39] If the excess contribution is withdrawn by the due date of the tax return, the 6% tax penalty does not apply.

[40] For more information, see Treasury Inspector General for Tax Administration, A Service-wide Strategy Is Needed to Address Growing Noncompliance With Individual Retirement Account Contribution and Distribution Requirements, available at http://www.treas.gov/tigta/auditreports/2010reports/201040043fr.pdf.

[41] For more information, see NBER Working Paper No. 13824, *Household Saving Behavior: The Role of Financial Literacy, Information, and Financial Education Programs*, by Annamaria Lusardi, available at http://www.nber.org/papers/w13824.

[42] More information is available in CRS Report RL34678, *Fee Disclosure in Defined Contribution Retirement Plans: Background and Legislation*, by John J. Topoleski.

greater transparency of fees paid in 401(k) plans.[43] The final rule specifically excludes IRAs, noting that IRA owners are solely responsible for managing their accounts and that IRA fee disclosure requirements could be quite costly. One difference between IRAs and 401(k) plans is that IRA owners have complete control over the choice of the financial institution and investments. However, individuals may find the decisions associated with opening and maintaining IRAs complicated and perhaps overwhelming. This suggests that opportunities may exist for financial institutions to charge higher fees than necessary. A direct comparison of IRA and 401(k) fees is not possible because of the different structures of the plans. IRAs are likely administratively costly, as each separate account requires separate record keeping, whereas 401(k) plan administrators can take advantage of economies of scale.

Author Contact Information

John J. Topoleski
Analyst in Income Security
jtopoleski@crs.loc.gov, 7-2290

[43] See Department of Labor, Employee Benefits Security Administration, "Reasonable Contract or Arrangement Under Section 408(b)(2)—Fee Disclosure," Federal Register, vol. 75, no. 136 (July 16, 2010), pp. 41600-41638.