EBRI FAST Facts
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Losing Ground Safely: Small IRAs' Large Stake in Money

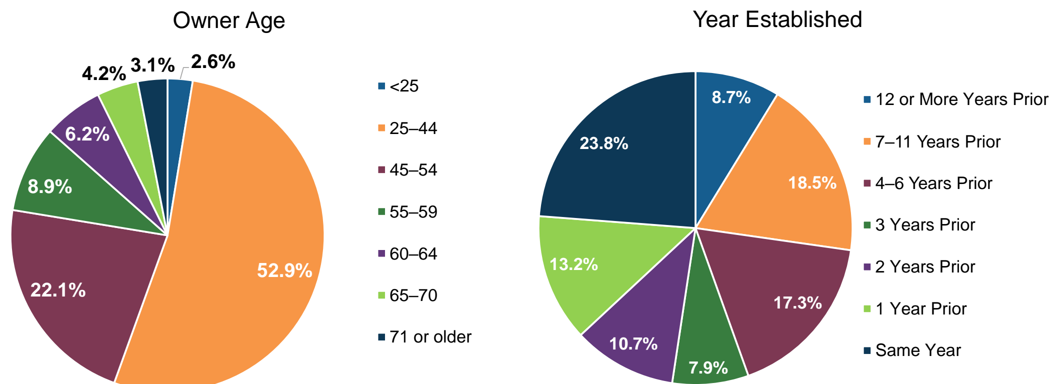
A key finding in the Employee Benefit Research Institute's (EBRI's) annual analysis of individual retirement accounts (IRAs) from the EBRI IRA Database is that extreme asset allocations are common. Namely, 28.6 percent of IRAs in the database had more than 90 percent in equities, and 24.4 percent had less than 10 percent in equities.[1]

One extreme allocation of particular note can be attributed to a safe harbor regulation. In 2005, the Department of Labor (DOL) issued regulations that — with respect to automatic force-outs of employment-based retirement plans with values of $1,000 up to $5,000 to IRAs — a fiduciary is deemed to have satisfied his or her fiduciary duties under section 404(a) of ERISA so long as the designated IRA provider of the automatic IRA, among other things, limits the initial investment choice of the IRA to those products designed to preserve principal and provide a reasonable rate of return.[2]

The result has been that a significant percentage of small IRAs are found to be invested 100 percent in money in Rollover IRAs.[3] This is true even though many had 100 percent allocations to balanced or target-date funds in their 401(k) plan. Diversified asset allocation funds are, of course, the safe harbor default for automatic enrollment arrangements in defined contribution plans.

EBRI's analysis finds that the safe harbor default affects many investors for long periods of time. Looking more closely at the data from the EBRI IRA Database, over one-fifth (22.7 percent) of Traditional Rollover IRAs had balances of less than $5,000 — not an insignificant share of all Traditional Rollover IRAs. Furthermore, 55.6 percent of the owners of Traditional Rollover IRAs with balances of $1,000 up to $5,000 were ages 44 or younger, and 27.2 percent of these accounts were at least seven years old (established seven or more years prior to the analysis year of the accounts) (Figure 1). Therefore, a majority of these accounts belong to younger individuals with many years until retirement, and many have been around for a significant number of years.

Figure 1
Owner Age and Year Account Was Established
Traditional Rollover IRAs with balances of $1,000–$5,000



Source: EBRI IRA Database (accounts as of 2016).

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To this latter point, three-fourths or more of accounts of those ages 25 to 29 that were established 7–11 years prior to the analysis year were 100 percent allocated to money. More than 85 percent of those established in the same year as the analysis year were fully invested in money (Figure 2).

Figure 2
Percentage of Traditional Rollover IRAs With Balances of $1,000–$5,000 With 100% Allocated to Money Assets

Owner Age and Time Account Was Established

Owner Age	Established 7–11 Years Prior	Established in Same Year
25–29	76.3%	85.7%
30–34	78.8%	87.6%
35–39	74.9%	89.0%

Source: EBRI IRA Database (accounts as of 2016).

Again, keep in mind that one of the main reasons that IRA assets are defaulted into money investments is so that principle can be preserved until the accountholder makes a proactive decision about the assets, such as consolidating them with other accounts or making a new asset allocation decision based on individuals' specific goals and risk tolerance. However, the evidence shows that these proactive decisions are not happening. As such, the assets remain in money for long periods of time. In the current interest rate environment, resulting returns, in many cases, may not even outpace the reasonable fees that cover the administration of the accounts.

These results have important implications for these small accounts. It cannot be assumed that owners of these accounts will take some action with these accounts to better address their retirement security. Therefore, some improvements are called for, such as promoting or helping with the consolidation of these accounts with other tax-preferred accounts such as 401(k) plans or reevaluating the default asset allocation for automatic rollovers.

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[1] See Craig Copeland, "EBRI IRA Database: IRA Balances, Contributions, Rollovers, Withdrawals, and Asset Allocation, 2017 Update," *EBRI Issue Brief*, no. 513 (Employee Benefit Research Institute, September 17, 2020) for the most recent analysis from the database.

[2] Sections 411(a)(11) and 417(e) of the Internal Revenue Code permit plans qualified under § 401(a) to include provisions allowing for the immediate distribution of a separating participant's benefit without such participant's consent where the present value of the nonforfeitable accrued benefit is less than $5,000. The DOL safe harbor pertains to this section of the Code.

[3] See Craig Copeland, "Comparing Asset Allocation Before and After a Rollover from 401(k) Plans to Individual Retirement Accounts," *EBRI Issue Brief*, no. 495 (Employee Benefit Research Institute, November 7, 2019).

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