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Roth IRAs Most Often Created by Contributions

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Roth IRA Investors Persistent, Responsive to Tax Rule Changes

Washington, DC, June 30, 2014 - Contributions are the predominant way investors open Roth individual retirement accounts (IRAs), according to a new Investment Company Institute (ICI) examination of Roth IRA data. In 2012, more than seven in 10 new Roth IRAs were opened exclusively with contributions—in sharp contrast to traditional IRAs, which largely are created through rollovers from employer-sponsored retirement plans.

The report, "The IRA Investor Profile: Roth IRA Investors' Activity, 2007–2012," analyzes contributions, conversions, rollovers, withdrawals, asset allocations, and account balances of two populations of Roth IRA investors: 2.5 million "consistent" Roth IRA investors (those with accounts in every year between 2007 and 2012); and a snapshot of 5.1 million Roth IRA investors at year-end 2012. The report is based on The IRA Investor Database™, a joint project by ICI and the Securities Industry and Financial Markets Association (SIFMA). The database has information on 15.5 million IRA investors at year-end 2012, of which 68 percent hold traditional IRAs, 33 percent hold Roth IRAs, and 14 percent hold employer-sponsored IRAs, with some holding more than one type of IRA. Roth IRAs mainly differ from traditional IRAs in their tax treatment. With a Roth IRA, taxes are paid up front on contributions and conversions, and withdrawals generally are tax-free in retirement. With traditional IRAs, contributions may be tax-deductible, and withdrawals are taxed.

"The use of Roth IRAs has grown significantly since their introduction in the late 1990s and they have become an important tool for Americans to save for retirement," said Sarah Holden, ICI senior director of retirement and investor research. "The availability of both traditional and Roth IRAs provides flexibility for households to manage the timing of taxation of their retirement accumulations."

Roth IRA Investors Are Consistent Contributors

In recent years, nearly $20 billion of contributions has flowed into Roth IRAs each year. In any given year, more than three in 10 Roth IRA investors make contributions to their accounts. In 2012, 30.3 percent of Roth IRA investors aged 18 or older contributed, and more than four in 10 investors who contributed did so at the legal limit. Roth IRA investors also persisted in their contribution activity year to year. For example, more than two-thirds of investors who contributed at the limit in tax year 2011 did so again in tax year 2012.

Roth IRA Investors Are Responsive to Tax Rule Changes

While few Roth IRAs in a typical year are created through conversions from other qualified retirement assets, Roth IRA conversion activity tended to shift in direct response to tax rule changes. For example, in 2010, when income limits on conversions were lifted and taxpayers could choose to spread out taxes on conversions made in 2010 over the next two years, one-third of new Roth IRAs were opened only with conversions. In 2010, more than 5 percent of Roth IRA investors made conversions into their Roth IRAs, compared with less than 2 percent in 2008 and 2009. Conversion activity shrank when the special tax payment option expired, but is still higher than before 2010: in 2012, 2.6 percent of Roth IRA investors had conversions into their Roth IRAs.

Rollovers to and Withdrawals from Roth IRAs Are Rare

In recent years, only about one in 10 new Roth IRAs were created through rollovers. This is a stark difference from traditional IRAs, which are created largely through rollovers (nearly nine in 10 new traditional IRAs in 2012 were opened only with rollovers).

Overall, fewer than one in 25 Roth IRA investors took withdrawals in 2012. In contrast to traditional IRAs, which require investors aged 70½ or older to take required minimum distributions (RMDs), Roth IRAs do not require RMDs during the account holder’s lifetime. As a result, withdrawal activity is much lower among Roth IRA investors and varies much less by age, compared with traditional IRA investors.
