THE DEMISE OF THE U.S. TREASURY'S myRA RETIREMENT PROGRAM: WHY IT FAILED

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ABSTRACT

In 2017 the U.S. Treasury announced the termination of its myRA program. This program, enacted during the Obama era in 2015, was designed to get more Americans to save for retirement. The program operated as a starter for a Roth IRA account for those individuals who did not have retirement plans at work. The program had automatic payroll deductions, no fees, no minimum balance, and virtually no risk with the funds being invested in Treasury debt. When a balance reached $15,000, then the savings rolled over into a private sector Roth IRA.

This paper explains why the program failed. To begin with, the program had few participants. A problem for participants was the low rate of return on Treasury debt. This type of retirement fund needs better returns over a long investment horizon. Unfortunately for the myRA program, potential participants can find private sector alternatives with better expected returns. In addition, the program had high management costs for the government. Taxpayers paid nearly $70 million in management costs since the date of launch and the government expected future costs to run $10 million per year. Unfortunately, the participants contributed only $34 million to their accounts. The result was a failed government program.

The main purpose of the program was to improve retirement income for seniors. But the government efforts on the myRA program were misguided. A basic analysis of the program's characteristics, with a comparison to the characteristics of market alternatives, reveals the inadequate design of the program. Unfortunately, the government wasted substantial funds administering this doomed program. Those government funds could have better gone to shoring up Social Security, an important program that provides retirement income for seniors. Social Security has solvency problems and needed the funds wasted on the myRA program.

INTRODUCTION

In 2017, the U.S. Treasury announced the termination of its myRA program. [1] This program, enacted during the Obama era in 2015, was designed to get more Americans to save for retirement. The program operated as a starter for a Roth IRA account for those individuals who did not have retirement plans at work. The program had automatic payroll deductions, no fees, no minimum balance, and virtually no risk with the funds being invested in Treasury debt. When a balance reached $15,000, then the savings rolled over into a private sector Roth IRA. [2]

This paper explains why the program failed. A basic analysis of the program's characteristics, with a comparison to the characteristics of market alternatives, reveals the inadequate design of the program.

LITERATURE REVIEW

Prior research has examined how investors can optimize their retirement planning. Investors need to select investments that are suitable for long term retirement planning. There can be a shortfall risk if investors choose highly conservative portfolios with low expected return. The investor then is at risk for having inadequate savings for retirement. This shortfall risk is often a neglected, or even omitted, part of the risk assessment of retirement investing. Leibowitz and Kogelman (1991) formally model asset allocation decisions subject to shortfall risk by considering investment horizon, minimum returns thresholds, and allowable probabilities that returns will fall below the minimum threshold. Their model indicates that even for short-term investment horizons as small as five years, optimal portfolio allocations should include equity components of at least 30%. For investors who are more risk tolerant, equity components may be as high as 85%. This suggests that portfolio allocations that exclude material equity components are likely to suffer from shortfall risk, especially for investors with longer investment time horizons. Smith and Gould (working paper) also model the shortfall risk problem and conclude that "for a variety of plausible assumptions about asset returns, investment strategies, and what constitutes shortfall, the minimum risk portfolio generally has between 50 and 70 percent stocks."

Several empirical studies suggest myopic risk management techniques expose investors to a high probability of shortfall risk because of the exaggerated focus on short-term portfolio volatility. For example, Spitzer and Singh (2008) examine shortfall risk by testing the effectiveness of target-date funds. They find that a simple 50/50 stock/bond portfolio unambiguously outperforms target-date funds that systematically move investors to funds that are more heavily weighted in bonds as those investors approach retirement. Haensly (2016) observes that even though TIPS are virtually risk free, a strategy relying heavily or solely on investing in TIPS for retirement typically fails to provide adequate retirement resources. He concludes that "significant shortfall risk exists for TIPS-only portfolios across a range of savings plans and securities selection rules." Therefore, strategies that rely solely, or heavily on interest-bearing securities with little or no capital gains potential are likely to subject an investor to retirement shortfall and should be avoided because they produce suboptimal outcomes.

THE CREATION OF THE myRA PROGRAM

The program was created to help citizens prepare for retirement. Financial planners have long urged citizens to start saving early for their retirements. With looming shortfalls in Social Security and Medicare, along with towering federal deficits, planners have encouraged citizens to exercise self-reliance in planning for their futures without undue reliance on shaky federal programs. Despite the presence of the traditional IRA, the Roth IRA, the 401 (k), the 403 (b), and traditional pensions, planners have found many citizens with insufficient savings for their old age. Some citizens have failed to take individual initiative. Other citizens have lacked employer-sponsored retirement plans.

There is history behind the creation of the myRA program. Powell (2013) notes that policy experts have long favored automatic IRAs to help solve the problem of inadequate retirement savings. But their proposed laws have failed. The proposals would require employers to automatically enroll employees in IRAs unless the employees opted out. In 2009 the Treasury Department developed an alternative idea of R-bonds, or retirement bonds, to encourage savings. The R-bonds would have the characteristics of an IRA and be aimed at workers at firms that do not sponsor retirement plans, part-time employees who are not eligible for plans that their firms sponsor, and the self-employed or non-

employed. With the recent gridlock in Washington, an advantage of R-bonds was that they would not require congressional authorization. With R-bonds, the employee could arrange an automatic payroll deduction with no government fees for an investment in government bonds. The R-bond proposal was not adopted.

With the President's State of the Union address in 2014, the President seized on some of the fundamentals of the proposed R-bond program and named his new program the myRA program. Its purpose was to help millions of Americans build a nest egg.

The White House (2014) summarized the myRA as a simple, safe, and affordable starter savings account. The President directed the Department of the Treasury to create the program which would be offered through employers and would help millions of Americans begin to save for retirement. The program targeted Americans who did not have workplace retirement plans. The product functioned like a Roth IRA with no tax deduction but with tax free growth. The savers benefitted from principal protection since the account would never go down in value. Like all savings bonds, the account was backed by the U.S. government. Contributions could be withdrawn tax free at any time. Initial investments could be as low as $25 and contributions could be as low as $5 through easy payroll deductions. Savers could keep the same account when they changed jobs and could roll the balance into a private sector retirement account at any time. Savers earned the same variable interest rate as the federal employees' Thrift Savings Plan (TSP) Government Securities Investment Fund. The plan was available to millions of American who could earn up to $191,000 per year. Participants could save up to $15,000 in their accounts before transferring the balance to a Roth IRA.

OPERATION OF THE myRA PROGRAM

The designers of the program hoped for many participants. Unfortunately, these hopes were not realized. As of 2017, contributions to the program totaled only $34 million. [3] A problem for participants was the low rate of return on Treasury debt. This type of retirement fund needs better returns over a long investment horizon. Unfortunately for the myRA program, potential participants can find private sector alternatives with better expected returns. In addition, the program had high management costs for the government. Taxpayers paid nearly $70 million in management costs since the date of launch and the government expected future costs to run $10 million per year. [4] The result was a failed government program. In 2017 the U.S. Treasury announced the termination of the program.

ANALYSIS OF THE myRA PROGRAM

The program had some positive characteristics: low fees, guaranteed return, low minimum investment, and wide availability to millions of Americans. On the other hand, the program's return on investment was low. Inflation can eliminate much, if not all, of the growth potential. Over a long time horizon for accumulating savings for retirement, the worker who instead invests in a low-fee private Roth IRA with automatic monthly transfers can utilize investment funds that can deliver better expected rates of return.

Some competitive models can show why the program's low rate of return is an important drawback for the retirement saver even if there is high volatility in the market. The following models pit the program against a private sector Roth IRA. The competitive models utilize reasonable assumptions based on recent financial performance for the myRA investment and recent financial performance for possible Roth investments.

Under all models, the saver deposits $1,000 at the start of each year and the saver has a 40 year time horizon with 40 years serving as the time horizon for the saver's working years. In addition, under all models, the normal return for the myRA model with investment in its government fund is 1.5% per year with no fees while the normal return for a Roth IRA with a mix of stocks and bonds is 8% per year after Vanguard fees of .2%.

In the first model, assume a myRA account with annual deposits of $1,000 and a 1.5% growth rate per year for 40 years. The account would grow to a total of $55,082 at the end of 40 years. This first choice assumes the worker stays with the same investment choice with 1.5% growth even after graduating to a regular Roth IRA in year 14 when the account exceeds $15,000.

In a second model, assume this worker observes that when the myRA account exceeds $15,000 after 14 years, the worker then wants to invest in other choices and begins earning 8% in a regular Roth IRA for the next 26 years. The total comes to $202,341.

In the third model, assume a worker, from the start, uses a regular Roth IRA with an 8% return per year. The Roth IRA continues through year 40 and totals $279,781.

In the fourth model, assume that market volatility for stocks and bonds is important. Assume the Roth IRA, in a state of volatility, has no growth for the first 5 years and then has 8% growth for 35 years. The total comes to $260,029. For comparison, note that the myRA government account used in Model 1 has the advantage of eliminating the effects of market volatility due to its investment in stable government bonds. It again totals $55,082 at the end of 40 years, the same amount as shown in the first model even if the account operates in a market for stocks and bonds that is volatile in the fourth model.

In the fifth model, assume that volatility is even more pronounced. Now assume a Roth IRA has no growth for the first 5 years and then experiences a sudden 50% drop in the market that comes just after the deposit early in year 6 with no growth for the rest of the year. From there, the account has 8% growth. The total for the Roth comes to $212,387. For comparison, note that the myRA government account used in Model 1 has the advantage of eliminating the effects of market volatility. It again totals $55,082 at the end of 40 years, the same amount as shown in the first model.

In the sixth model, assume high volatility operates to the advantage of the saver. Now assume a Roth IRA has 20% growth for the first three years. From there, the account has 8% growth for 37 years. The total for the Roth comes to $294,645. For comparison, note that the myRA government account used in Model 1, despite a volatile market in this sixth model, would again total $55,082 at the end of 40 years, the same amount as shown in the first model.

In the seventh model, assume high volatility both helps and hurts the saver. Now assume a Roth IRA has 20% growth for the first three years and a sudden 50% drop in the market at the start of year 10 that occurs just after the early deposit for that year with no growth for the rest of the year. From there, the account has 8% growth. The total for the Roth comes to $202,114. For comparison, note that the myRA government account used in Model 1, despite a volatile market in this seventh model, would again total $55,082 at the end of 40 years, the same amount as shown in the first model. Table 1 summarizes the results for the seven models.

Table 1: Comparison of Seven Models

Model Number	Comments	Future Value of Account
1	myRA type of account with no equities for 40 years	$55,082
2	myRA account for 14 years followed by Roth IRA with mix of stocks and bonds for 26 years	$202,341
3	Roth IRA with steady returns	$279,781
4	Roth IRA with unfavorable volatility	$260,029
5	Roth IRA with unfavorable, intense volatility	$212,387
6	Roth IRA with favorable volatility	$294,645
7	Roth IRA with mixed, intense volatility	$202,114

DISCUSSION

Among all the models, Model1has the lowest total at $55,082 after 40 years despite its advantages of low fees and low volatility. Its low average return dooms this model to the lowest performance.

Model 2 matches Model 1 for 14 years until the point at which the account graduates to a regular Roth IRA. At that point, the saver earns regular Roth IRA returns for 26 more years. The total becomes $202,341 which exceeds Model 1 by $147,259, or 367%.

Model 3 uses a regular Roth IRA return for the entire 40 years. It totals $279,781 which exceeds Model 2 by $77,440 or 38%. These results show the first 14 years are important to the size of the accounts despite similar types of investments over the final 26 years.

Model 4 addresses investor fear of volatility. The “myRA” type of investment eliminates volatility by using government bonds. But even with the first 5 years in Model 4 producing no overall return due to volatility in a Roth IRA, the remaining 35 years of normal Roth IRA growth is enough to produce a total of $260,029. The penalty for volatility is not enough for the Roth IRA to lose this competition. The Roth IRA in model 4 exceeds Model 1 by $204,947 or 472%. The Roth IRA in model 4 also defeats Model 2.

Model 5 makes the volatility even more severe with 5 years of no growth for the Roth IRA followed by a sudden 50% drop in the market. Nevertheless, the Roth IRA in model 5 still defeats Model 1. Model 6 shows high volatility that operates to the advantage of the saver. The Roth IRA in model 6 then defeats Model 1 by a wide margin. Model 7 shows high volatility that both helps and hurts the saver. The Roth IRA in model 7 again defeats Model 1.

In summary, the myRA type of investment seems to be a weak savings vehicle. Under numerous plausible scenarios, the saver would be better off arranging for a regular Roth IRA despite the myRA having the advantages of lower fees and less volatility. The better growth rate for the Roth IRA overwhelms the myRA in the long run even with penalties against the Roth IRA for volatility and fees. The myRA program seems to be an ineffective tool for solving the problem of inadequate retirement savings for lower income individuals.

CONCLUSION

When the myRA program was introduced, it was hailed as a way to help lower income individuals fund their retirements. But an analysis of the program's characteristics shows that the program was a weak savings vehicle. Private sector alternatives appear to be superior savings vehicles even after adjusting for volatility and fees. Nevertheless, Social Security is an important program for this type of lower income saver. Social Security was created to provide an essential level of retirement income for those without adequate retirement savings. Social Security is highly progressive in the sense that it provides a higher return to the lower income worker than the high income worker. It seems government funds lost on the myRA program might have been better spent on shoring up Social Security.

FOOTNOTES

[1] Brandon (2017)
[2] White House (2014)
[3] Ebeling (2017)
[4] Ebeling (2017)

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