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Asset allocation and asset location: household evidence from the survey of consumer finances

Daniel Bergstresser [a], James Poterba [b] [c]

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Abstract

The rapid growth of assets in self-directed tax-deferred retirement accounts has generated a new set of financial decisions for many households. In addition to deciding which assets to hold, the traditional choice among bonds, stocks, and other investment classes, households with substantial assets in both taxable and tax-deferred accounts (TDA) must now decide where to hold them. This paper uses data from the Survey of Consumer Finances to assess how many households have enough assets in both taxable and tax-deferred accounts to face significant asset location choices. It also investigates the asset location decisions these households make. In 2001, 49% of households had at least some assets in a tax-deferred account, and more than 11 million households had at least US$25,000 in both a taxable and a tax-deferred account. Asset allocation inside and outside tax-deferred accounts is quite similar, with about 70% of assets in each location invested in equity securities. Roughly two thirds of households with financial assets in both taxable and tax-deferred accounts hold portfolios that are tax efficient. Most of the other third could reduce their taxes by relocating heavily taxed fixed income assets to their tax-deferred account. For more than half of the households that hold apparently tax-inefficient portfolios, however, a shift of less than US$10,000 in financial assets would eliminate tax inefficiency.

Keywords

Asset allocation; Asset location; Survey of consumer finances