TABLE *of* EXPERTS *Series*

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Insights into RETIREMENT

The Discussion

Q: What's the most important thing an individual should consider when determining how much they will need for retirement? What's a key retirement planning step that many individuals overlook?

Lee Applebaum (Plan Sponsor Consultants): My biggest concern is longevity risk. To give you an example, a friend of mine's father died last year at the age of 107. To the end, he was mobile and active. This friend of mine is now in his mid-70s, has been retired for about 15 years, and has a good chance of living another 25 years. Had he not done proper planning years before, there's no way he could do it. You can't just make it up at the end. You need to plan at the beginning and know what your family health history is. To me, that is one of the single-most important factors to determine a beginning baseline of where to start.

Q: How have the recession and the current economic climate (low interest rates, etc.) impacted retirement planning strategies for Americans? How does the possibility that low interest rates will remain for an extended period of time impact retirement planning?

Applebaum: People now have to have a different vehicle to get some sort of yield for income. The problem with that is you end up having to move up the risk scale, and risk adverse people may not be comfortable doing that. When a client isn't comfortable with how their money is invested because they think it's too aggressive, they start making emotional decisions, and probably nine times out of ten those decisions will be wrong. They make kneejerk reactions today versus what they need in 15 or 20 years. I've seen a big effect from the rates being at zero, just erasing an entire asset class for people to invest in.

The problem is that the government inflation rate excludes so many things, like food and energy. While inflation is historically low today, I know my grocery bills and gas bills are higher than they were 10 years ago. It makes an impact.

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Q: What factors should you consider when determining which financial adviser or firm to hire? How have recent regulations about fees and disclosures impacted the process or what consumers should look for?

Applebaum: As a retirement plan advisor, being able to be a fiduciary on the plan is a huge advantage for the client, because they know that you're sitting on the same side of the table with them. I think that's a big plus. On the individual side, qualifications, references and designations are also important. A good place to start is to work with a CFP (Certified Financial Planner). It's hard to get, and it's somewhat selective. Even national magazines like Fortune and Money often recommend only working with a CFP as you have to have education, and specialized training. There are other specific retirement-plan designations as well. One of the biggest (and most exclusive) ones out there for retirement plan advisors is the AIFA, the Accredited Investment Fiduciary Analyst. It, like the CFP, requires education and training, but additionally, you must go through a due diligence process as well as a background check. I agree about working with a team. You need to look at not just the advisor but also the team that backs him/her up.

Q: How big of a role should tax considerations play in a retirement strategy? How can individuals find the right balance when it comes to their tax burden?

Applebaum: I agree that taxes have to play a role, but they can't play the only role. From the retirement plan side, a great example is you can now have a Roth 401(k), whereas a couple of years ago you they didn't even exist. So a decision to think about is if you're a 25-year-old employee, is it better to not get a pre-tax deduction for your 401(k) contribution today, and put your money into a Roth 401(k) having it grow for the rest of your life completely tax free? That's a tax decision you have to make now, versus taking a tax deduction up front to get a regular 401(k) contribution, but then in 20 or 30 years you pay the full amount of taxes on it when withdrawn. With a 25 or 30-year old, that could potentially be a huge difference in money. For a 50 or 60-year old, it may not be that big of a difference, if at all. So in an example like that, yes taxes should be a consideration

Q: Aside from conventional retirement plans (IRAs, 401(k) plans, etc.), what are some other options individuals can consider as they plan for retirement (annuities, insurance options, etc.)?

Applebaum: Life insurance is an important component in retirement planning. Most people have to have it, especially if you have young children. Long-term care is also an important issue. Most people are going to need some sort of long-term care at some point, so it's something that should be addressed.

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Q: What are some of the metrics individuals should use when trying to determine their retirement readiness? What tools does your company offer to help clients determine their readiness?

Applebaum: We have what we call a Plan Success Audit that we use to measure a retirement plan's health. What that does is it allows us to get plan level data to figure out the employee deferrals into the plan, how their investments are allocated, as well as how many employees of the company are currently participating. Studies have shown that you need to be deferring about 10 percent of your income into a retirement plan every year to be able to retire "on track." This is a way to see if your plan is doing the right thing, whether it's structured the right way. Can we do something a little bit different with the match that the company gives? Maybe change the numbers around to get people to defer more to max out a match to get closer to that number. Behavioral finance has shown that most employees contribute up to what the company will match, so if the company offers something like a $.50 on the dollar match up to 6%, then most employees set their deferral at 6%, and never change it. What if we change that to $.30 up to 10%? This way the company is still on the hook for no more than a 3% match, but many employees will increase their contribution to get the full match. We also use a Financial Wellness Campaign that's based on the input of individual participants into the plan, and they tell us, in effect, what's keeping them up at night. Once we get those individual answers, we can aggregate all those together and sit down with the business owner or the plan sponsor and customize a campaign to educate the employees to try to increase the deferrals into the plan. So it's kind of a top-down approach with the Plan Success Audit and a bottom-up approach with Financial Wellness. And by coming at it from both angles, we're addressing all needs from the company's

and the employees' standpoint. Another important tool that a lot of the better 401(k) vendors have is a retirement readiness status on the 401(k) website landing page. It will tell you for example that you're 80 percent on track to retire, or you're going to have $2,500 a month in retirement. That's more useful than saying that you're up 2 percent this quarter. Who really cares about this quarter when retirement is in 20 to 30 years? These web sites are sophisticated enough to give people a long-term look at things and help people focus on what they need to be focusing on, which is the long-term and not the short-term. It can also be designed to implement any changes to help them meet their retirement readiness goals.

Q: According to a 2013 Putnam study of retirement plan participants, only 61% are on target to replace their income. What solutions are you employing to assist plan sponsors overcome the three participant psychological barriers of inertia, loss aversion and myopia?

Applebaum: We are big proponents of trying to overcome that inertia; that's a big a problem with employees. They become eligible for the plan and they don't want to do anything, or maybe it's a bad time and they can't do it now. But a lot of times if they don't start now, they never will. If somebody has to be proactively involved and nothing happens, that inertia stays where it is. We think one of the best ways to overcome that is automatic enrollment. Force people to be in the plan. Let them choose not to be in the plan, rather than choosing to be in it. This is another example of how we use behavioral finance to improve retirement plans. Most of the time, when an employee is automatically enrolled into a 401k, they choose to stay, as opposed to opting out. A great example of the opting out vs. in advantage is organ donation. In Austria, it is assumed you will be an organ donor and you actually have to opt-out on your driver's license to not be an organ donor. They assume you're going to be one, unless you check a box. Because of this, Austria presently has about a 98 percent organ donation rate. Whereas in America we have to check the box (opt-in) to be a donor, and we only have about a 25 percent organ donation rate. Just that one process of checking a box is really hard for people to do for some reason. So using behavioral finance, having people automatically enrolled in the plan, most of the time they're going to stay there. I mentioned earlier the behavior of most employees is to contribute up to the maximum the company will match. Understanding this along with the auto enrollment concept can help to determine the appropriate auto-enroll amount. Many companies use a 3% auto enrollment rate, but we already discussed that the average employee needs to defer around 10% to retire successfully. This sets the employee up for failure in the future. Why not auto enroll an employee at a higher number, say 5% or 6% and design the plan to increase that 1% to 2% annually until they reach 10% or 12%? The increases can be designed to coincide with company raises as well. So understanding how an employee acts from a behavioral finance standpoint, we can work with the business owner to design a retirement plan that tackles these barriers head-on.

A small business owner could add a profit-sharing component, but there are also ways you can customize a profit sharing plan so you can make it a huge benefit for the business owner. So they get a much larger percentage of a contribution. The rank-and-file still gets money, but they don't all have to get the same percentage. You can structure it so the owners can put aside a substantial amount of money without bankrupting the company to do that.

Q: How does the possibility that Social Security and Medicare benefits will be reduced in the future impact retirement planning?

Applebaum: Take the whole Social Security issue and add on that pensions are really non-existent. So what's really happened is the onus has been placed on the individual more so than ever before. It's the individual's responsibility to take care of everything. That means they should take advantage of all resources possible, be it 401(k)'s, IRAs, taxable accounts, etc.. You need to put as much money as you can into these vehicles and enable it to grow over time. The problem is, they don't teach this stuff in school. Kids today are getting out of college with $50,000 in debt, and they don't have a clue about how to manage their money. So, we as parents need to start early educating our children. Maybe if a kid earns money babysitting or mowing grass, the parent could take part of that money and contribute it to a Roth IRA. If people could start early with their kids, teaching them how to save money for retirement, over their life they'll hopefully continue that discipline, and it will make it much easier for the next generation to retire.

Q: What can advisors do to help people avoid the mistake of taking on undue investment risk to achieve financial goals, or maintain cash flow in retirement?

Applebaum: Start a plan early. The earlier you do it, the easier it's going to be and the less any bumps in the road will hurt you. That to me is very important Hire somebody you trust who you feel comfortable working with. And make sure that everyone in the family works together.

Thank you for reading an excerpt from Table of Expert Series – Insights into Retirement. For the complete article, visit the Birmingham Business Journal website.

About the Contributor

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Lee Applebaum is a Senior Vice President with Plan Sponsor Consultants, a Michael M. Kane Company. Plan Sponsor Consultants is a full service independent retirement plan consulting firm, which has been recognized for their expertise, on a national scale, by magazines including Forbes, PlanSponsor, PlanAdviser and 401(K) Wire. Plan Sponsor Consultants was also a Finalist for the NAPA/ASPPA 2013 Advisor Leadership Team of the Year as well as a Finalist for PLANSPONSOR 2010 Advisor Team of the Year. Lee is a CERITFIED FINANCIAL PLANNER™ (CFP®) designee, a Chartered Retirement Planning Counselor (CRPC®), an Accredited Investment Fiduciary Analyst (AIFA®), and well as a Center for Fiduciary Excellence (CEFEX) Analyst. Lee is responsible for retirement plan development and servicing in the State of Alabama.

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